AUDIT REPORT

CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
BUREAU OF MANAGEMENT AUDIT
WILLIAM C. THOMPSON, JR., COMPTROLLER

Audit Report on
Department of Education Controls over Universal Pre-Kindergarten Payments to Non-Public Schools in Regions 6 and 7

MD05-072A

March 21, 2007

THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, N.Y. 10007-2341

WILLIAM C. THOMPSON, JR.
COMPTROLLER

To the Citizens of the City of New York

Ladies and Gentlemen:

In accordance with the Comptroller's responsibilities contained in Chapter 5, § 93, of the New York City Charter, my office has conducted an audit to determine whether the Department of Education (DOE) has adequate controls over Universal Pre-Kindergarten payments to non-public schools in Regions 6 and 7.

DOE contracts with non-public schools to provide comprehensive early-childhood education to children who become four years of age by December 31 of the school year in which they enroll. We audit programs such as this to ensure that City funds are used effectively, efficiently, and in the best interest of the public.

The results of our audit, which are presented in this report, have been discussed with DOE officials, and their comments have been considered in the preparation of this report.

I trust that this report contains information that is of interest to you. If you have any questions concerning this report, please e-mail my audit bureau at audit@comptroller.nyc.gov or telephone my office at 212-669-3747.

Very truly yours,

William C. Thompson, Jr.

WCT/ec

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AUDIT REPORT IN BRIEF

This audit covers Universal Pre-Kindergarten (UPK) payments to non-public schools authorized by the Regional Operation Center (ROC) in Staten Island. This ROC provides UPK support to non-public schools in parts of Brooklyn that are in Region 6 and all non-public schools in Staten Island and the parts of Brooklyn that are in Region 7. This audit determined whether the Department of Education (DOE) has adequate controls over UPK payments to non-public schools in Regions 6 and 7.

Audit Findings and Conclusions

DOE does not have adequate internal controls over UPK payments to non-public schools in Regions 6 and 7. This is because DOE has not developed formal fiscal review procedures for the ROCs to follow when monitoring and assessing the UPK programs in the schools. As a result, a total of $377,621 (12 percent) of the $3.2 million in UPK payments made by DOE in Fiscal Years 2004 and 2005 to the schools in our sample represents overpayments and other inappropriate payments to the schools that should be recouped, as follows:

- DOE overpaid six schools in our sample $141,055 in UPK funds by not adhering to the method of calculating UPK payments stated in the DOE contract.
- Three schools in our sample had unspent UPK funds totaling $82,321 that should have been recouped by DOE.
- A total of $97,586 of the $305,727 Other Than Personal Service (OTPS) expenditures reviewed in our sample lacked adequate supporting documentation.
- Of the $208,141 in OTPS expenditures that had supporting documentation, $56,659 was questionable since the expenditures were either not related to the UPK program or not reasonable.

In addition there were questionable bank statement activities totaling $407,322 for five of the schools in our sample. There were also issues regarding the use of UPK funds for: bonuses to teachers at one of the schools; building rental costs between related parties; and private sanitation service. Moreover, at one of the schools in our sample—Children's Playhouse—there were numerous internal control inadequacies that increase the potential for fraud.

Although DOE does not have adequate internal controls over UPK payments to non-public schools in Regions 6 and 7, we did note that the number of children did not decline by that needed for a full class for any of the schools. DOE did not pay any of the schools twice for the same student. The attendance information for each child contained on the attendance invoices corresponded to the attendance information contained on the Daily Attendance Cards in our sample. The schools properly deposited all funds received for the UPK program. In addition, at our unannounced observations class size did not exceed 20 children, and all UPK educational employees were bona fide.

Audit Recommendations

Based on our findings, we make 24 recommendations, including the following. DOE officials should:

- Develop and implement written fiscal review procedures for the ROCs to follow and monitor when assessing the UPK program. These procedures should include the steps that the ROCs will take to ensure that non-public schools comply with their contracts and the DOE *Expenditure Guide.*

- Recoup the UPK overpayments made during Fiscal Year 2005 to the six schools in our sample.

- Recoup the $97,586 identified in this audit as expenditures that are not supported by the records of the non-public schools we cited.

- Recoup the $56,659 identified in the audit as expenditures that were either not related to the UPK program or were not reasonable for the non-public schools we cited.

- Investigate the questionable bank activities totaling $407,322 that we cited, and if warranted, recoup the moneys.

- Investigate the conditions we cited at Children's Playhouse and, depending on the results of the investigation, consider terminating its UPK contract.

DOE Response

In their response, DOE officials generally did not agree with the audit's findings and recommendations. Nevertheless, DOE has taken steps to correct many of the issues identified in the report and to enhance the monitoring of the fiscal activities of the UPK program.

INTRODUCTION

Background

The New York City Department of Education (DOE) provides education to children from pre-kindergarten to 12th grade within 10 Regions. Each Region has a Learning Support Center that includes an instructional leadership team and a Parent Support Office. The instructional leadership teams provide professional development and assessment. In addition, there are six Regional Operation Centers (ROCs) covering all 10 Regions that provide fiscal support to schools and programs. The ROCs also determine whether contract expenditures are appropriate and children are receiving contracted services. This audit covers Universal Pre-Kindergarten (UPK) payments to non-public schools authorized by the ROC in Staten Island. This ROC provides support to non-public schools in parts of Brooklyn that are in Region 6 and all non-public schools in Staten Island and the parts of Brooklyn that are in Region 7. (It should be noted that the focus of this audit did not include determining the adequacy of the instructional support and professional development provided to these schools by the instructional leadership teams for the UPK program or the quality of the UPK services provided by the schools to the children.)

In 1997, the New York State Legislature enacted laws under Chapter 436 and provided funding to create a UPK program for children who become four years of age by December 31 of the school year in which they enroll, at no charge to parents. The UPK program was designed to provide comprehensive early-childhood education experiences to children through nurturing environments and curricula that promote creative expression and cognitive, linguistic, physical, cultural, and social development.

The Regions are responsible for monitoring and assessing the UPK program, which can be offered in non-public schools—such as community-based, early childhood organizations—as well as in public schools. Eligible non-public schools are licensed by the New York City Department of Health and Mental Hygiene and may become providers of UPK services. DOE selects the non-public schools to provide UPK services through a Request for Proposal (RFP) process, which it reviews according to prescribed evaluation criteria, site visits, the needs of the communities, and available funding.

DOE and each of the non-public schools enter into a three-year UPK contract. According to the contract, the amount payable each school year is referred to as the adjusted annual contract amount and is based on the number of children registered and attending as of the last school day in October (this number cannot be more than the estimated number of children specified in the contract), multiplied by the cost per child. The cost per child varies from one school to another and is based on information presented in the RFPs and on the operating needs of the schools to run the UPK program. The establishment and approval of the cost per child is a collaboration of the Learning Support Centers and the ROCs. The cost per child, on average, is approximately $3,100 per child.

According to the UPK contracts, a mid-year review of the reported number of children registered and attending as of the last school day in October should be conducted in February. If the number of children has declined by the number needed for a full class (according to the individual Classroom Utilization Form), DOE is to reduce the adjusted annual contract amount accordingly.[1] However, if the number of children has declined by less than that needed for a full class, DOE is not required, but may, reduce the adjusted annual contract amount.

The UPK program requires the non-public schools to provide two and one-half hours of instruction each day, five days a week. For the school year, a minimum of 176 days must be designated as UPK instructional days (when classes are in session), and four days must be designated as professional development days for the UPK staff (when classes are not in session). The maximum UPK class size is 20 children. Classes that have either 19 or 20 children must have one certified head teacher and two paraprofessionals, such as assistant teachers and teacher aides. Classes that have 18 or fewer children must have one certified head teacher and one paraprofessional.

As part of their contract with DOE, non-public schools must maintain records and documents in sufficient detail to support all claims for payment against the UPK program. They are also required to prepare and submit to the ROCs a UPK Mid-Year Expenditure Form and an End-of-Year Expenditure Form listing actual UPK expenditures—salaries, facility costs, equipment, consultants, maintenance and repairs, instructional supplies, transportation, and meals or snacks. The Contract Administration Officers of the ROCs stated that they review Mid-Year Expenditure Forms and End-of-Year Expenditure Forms to ensure that the actual UPK expenditures reported do not exceed budgeted UPK expenditures. They do not ask the schools to submit accompanying documentation, but ask the schools to retain the documentation on site for audit purposes. The schools may face disallowances if, upon audit, supporting documentation is lacking or inadequate.

In addition, each month, a designated official (usually an Educational Director) at each of the schools is to prepare attendance invoices (which include the total number of instructional days every child in a class was in attendance for the previous month), certify their legitimacy, and submit them to the overseeing regional instructional leadership team to be reviewed and approved. The information from the invoices is then relayed to the appropriate ROC so that the ROC can authorize and enter payment information in the school system's Financial Accounting Management Information System (FAMIS) and payments can be generated.

The initial DOE payment to non-public schools operating UPK programs is made in September of each school year and is for 20 percent of the annual contract's estimated amount. Then, for each of the months starting from November and ending in May, the schools receive 10 percent of their adjusted annual contract amount. (If the adjusted annual contract amount is less than the annual contract's estimated amount, DOE is to adjust the monthly payments accordingly.) The remaining 10 percent of the adjusted annual contract amount is paid in two installments—five percent is paid in June, and the second five percent, which is usually paid in

[1] Each school is required to submit a Classroom Utilization Form to DOE to be included with its contract that lists the following: the number of UPK classes (and corresponding class numbers), the number of children in each class, the start and end time for each class (class hours), and the ratio between children and teachers.

July or August, is not made until the schools submit all required end-of-year documentation to DOE.

During Fiscal Year 2004, DOE had UPK contracts with 583 non-public schools to provide services to an estimated 30,967 children at an estimated total cost of $97,317,114. In Regions 6 and 7 specifically, DOE had UPK contracts with 183 non-public schools to provide services to an estimated 9,043 children at an estimated total cost of $28,332,694.

Objective

The objective of the audit was to determine whether DOE has adequate controls over UPK payments to non-public schools in Regions 6 and 7.

Scope and Methodology

The audit scope period was Fiscal Year 2004 through Fiscal Year 2005 (July 1, 2003, through June 30, 2005).

To obtain an understanding of how the Regions monitor and assess the UPK program, we spoke and corresponded via e-mail with Learning Support Center officials responsible for the instructional review process as well as with ROC officials responsible for the fiscal review process. Specifically, we spoke with the Director of DOE's Office of Early Childhood Education and her Regional 6 and 7 Early Childhood Education Directors; the Deputy Administrator and the UPK program Supervisor of the Division of Financial Operations; the Directors and Contract Administration Officers of the ROCs responsible for Regions 1 and 2, Regions 4 and 5, Regions 6 and 7, and Regions 9 and 10. In addition, we spoke with DOE's Deputy Auditor General of the Office of Auditor General (OAG).

To obtain an understanding of UPK services and goals and what is expected of non-public schools, we reviewed:

- a standard contract between DOE and each of the non-public schools;
- an October 8, 2004 letter sent by OAG to each of the non-public schools outlining key provisions of DOE's UPK contract;
- *New York City Pre-kindergarten Programs—Setting High Standards*;
- *Implementing the UPK Program in New York City*; and
- *NYC Universal Pre-Kindergarten Frequently Asked Questions.*

To understand the regulations governing the UPK program, we reviewed §3602-e of the New York State Education Law of 1997 and Title 8, §151-1, of the New York City Administrative Code. Finally, to obtain an understanding of the guidelines used in determining whether UPK expenditures are to be reimbursed by DOE, we reviewed the DOE *Expenditure Guide for Programs Receiving UPK Funding* (*Expenditure Guide*).

Information obtained from our interviews and various documents was evaluated to assess whether DOE had internal controls as they relate to our audit objective. We also determined whether DOE's instructional and fiscal UPK review processes had written procedures and policies. If so, an assessment was conducted to determine whether the written procedures and policies were adequate.

DOE provided an Excel spreadsheet with the data pertaining to the 583 non-public schools that had contracts to provide UPK services during Fiscal Year 2004. To assess the reliability of the data, we obtained a listing (updated as of October 2003) from DOE's Web site of the schools that had contracts to provide UPK services. The listing was compared to the Excel spreadsheet provided to us by DOE; minor differences were found. Since these differences were minor, we concluded that the data was reliable and that we had the entire population of schools that had UPK contracts.

Thereafter, the data was sorted first by borough and then by estimated annual contract amount to determine the number of schools within each borough that had estimated annual contract amounts above $100,000—the judgmental dollar limit we chose for survey-sample selection. We then randomly selected one school from each of the five boroughs for our survey sample.

Originally, the scope of our audit included non-public schools providing UPK services within all 10 Regions throughout the five boroughs. However, we decided to reduce the scope of our audit in the interests of audit timeliness based on our limited testing of the Fiscal Year 2004 documents for the five schools in our survey sample. Thus, we narrowed our scope to focus on only two Regions—Regions 6 and 7. We selected these two Regions, whose expenditures are monitored by the ROC in Staten Island, since they had the greatest number of schools (183) with UPK contracts during Fiscal Year 2004.

Our analysis of the data received from DOE found that there were 183 schools in Regions 6 and 7 with annual contracts totaling an estimated $28,332,694 for an estimated 9,043 children. Next, it was determined that there were 18 schools within Regions 6 and 7 that had annual contract amounts estimated at more than $300,000. We judgmentally decided to select an additional eight schools for our fieldwork sample from these 18 schools for detailed testing of Fiscal Year 2005 documentation. In total, our sample selection included 10 schools in Regions 6 and 7 with annual contracts totaling an estimated $3,473,525 for an estimated 1,015 children—this included the eight schools from our fieldwork sample and two schools from our survey sample that we included since they were part of Regions 6 and 7.[2] (There were three schools selected in the survey that were not part of Regions 6 and 7 and were excluded from our analysis for purposes of this audit.)

[2] The following are the 10 schools selected, by Region:
Region 6: Brooklyn Institute for Children; CYCLE Day Care Center; and Bryan's Educational Center.
Region 7: Our Saviour's Lutheran Preschool; Smart Start Early Childhood Center; Gan Day Care Center; Children's Playhouse; Jewish Community Center of Staten Island; Staten Island YMCA Nursery School; and Building Blocks Preschool.

To assess the reliability of the data obtained from DOE on the Excel spreadsheet for the 10 schools from Regions 6 and 7 with UPK contracts, we obtained the actual UPK contracts for each of these schools and also obtained information from the City's Vendor Information Exchange System (VENDEX). We then compared the estimated annual contract amount, estimated number of children, and cost per child from these contracts and VENDEX to the Excel spreadsheet provided to us by DOE and found minor differences. Since these differences were minor, we concluded that the data for the 10 schools in our sample was reliable.

We verified that DOE's contracts with the 10 selected schools were registered with the Comptroller's Office by reviewing the Comptroller's Office Omnibus Automated Image Storage and Information System and VENDEX.

DOE could not provide all of the documentation necessary for us to conduct certain tests for one of the eight schools selected for detailed testing. Specifically, we were not provided with Daily Attendance Cards, UPK program expenditure documentation, and bank-related activity documentation. We felt no need to select another school for detailed testing since our reduced sample was still reasonable (7 out of 18).[3]

We obtained for Fiscal Years 2004 and 2005 the monthly Invoice/Attendance Forms for Contracted Providers (attendance invoices)—which summarize the monthly attendance of each child—submitted monthly to DOE's instructional teams by the 10 schools for each of their classes. We determined whether DOE correctly paid the 10 schools based on the number of children that were registered and attending as of DOE's cut-off date—either the last school day in October or the last school day of the third week in November, depending on which date the schools had the largest number of children.[4] (The schools received $3.2 million in UPK payments for Fiscal Years 2004 and 2005.)[5] To do so, we reviewed the attendance invoices for October and November 2003 and 2004 for each of the schools in our sample and added up the number of children listed as registered and attending as of the last school day in October and the last school day of the third week in November. (For the two survey schools, we reviewed the October and November 2003 and 2004 attendance invoices; for the eight fieldwork schools, we reviewed the October and November 2004 attendance invoices.) Next, we determined which of the two dates had the largest number of children (noting that this number could not be more than the contracts' estimated number of children) and multiplied this number by the cost per child stipulated in the contracts. We compared the amount that we determined should have been paid

[3] The Brooklyn Institute for Children did not submit to DOE its end-of-year documentation, such as its End-of-Year Expenditure Form, Daily Attendance Cards, and an updated Department of Health and Mental Hygiene permit. DOE made several attempts to obtain this documentation, to no avail, through letters to officials of this school. As a result, DOE withheld the June and final UPK payments. DOE officials informed us that they later terminated this school's contract.

[4] The contract between DOE and each of the schools states that payment is based on the number of children registered and attending as of the last school day in October. However, DOE extended the cut-off date to the last school day of the third week in November and allowed the schools to use either the October or November date, depending on the date that had the greater number of children.

[5] The two survey schools received $331,920 for Fiscal Years 2004 and 2005 and the eight fieldwork schools received $2,824,613 for Fiscal Year 2005 for a total of approximately $3.2 million.

to the schools to the amount that DOE actually paid to them, as reflected in the print-outs from FAMIS.

For the following tests, we reviewed Fiscal Year 2004 UPK program expenditure documentation, bank-related activity documentation, and attendance records for the two schools from our survey sample. We reviewed Fiscal Year 2005 documentation for the eight schools from our fieldwork sample.

For each of the 10 schools, we compared the number of children registered and attending as of DOE's cut-off date to the number of children registered and attending, as listed on the February, March, and April attendance invoices. Our purpose was to determine whether there was a decrease in the number of children in attendance during the middle and end of the school year and assessed whether this number declined by that needed for a full class. If so, we determined whether DOE reduced the adjusted annual contract amounts accordingly, as required by the UPK contract.

We determined whether any of the 10 schools in our sample had more than one UPK class. If so, for each of these schools, we compared the names and child identification numbers listed on the monthly attendance invoices for each of their classes during the three months of February, March, and April, and checked for duplicates. Our purpose was to determine whether DOE paid these schools twice for the same student.

We then obtained DOE's Approved Daily Attendance Cards (Daily Attendance Cards)—which list the daily attendance of each child for the whole school year on one card—submitted to DOE at the end of the fiscal year for nine of the 10 schools in our sample. (One of the 10 schools in our sample did not submit the Daily Attendance Cards to DOE, and thus we were unable to analyze daily attendance information for this school.) For these nine schools, we determined whether the attendance information for each child contained on the attendance invoices corresponded to the attendance information contained on the Daily Attendance Cards for the months of February, March, and April.

We requested from DOE a print-out from its Automate the Schools system (ATS) of all children registered with DOE during the fiscal year at the sampled schools.[6] We compared the names and child identification numbers of children to the names and child identification numbers listed on the attendance invoices for February, March, and April to determine whether all children attending the UPK classes were registered with DOE.

We conducted unannounced observations during March, May, November, and December 2005, and January through April 2006 of nine of the 10 schools in our sample that had a UPK contract (and visited each of the 12 sites affiliated with these schools) and interviewed the officials to gain an understanding of the operation of their UPK programs and their responsibilities in relation to DOE. We did not conduct an observation for the remaining school in our sample since this school had no UPK contract at the time of our visit. Therefore, we were

[6] We requested, but did not receive, the ATS printout for Building Blocks Preschool; therefore, we did not include this school in our analysis in determining whether children were registered with DOE.

unable to meet with any of the teachers at this school, observe classes, or obtain any documentation relating to its UPK program expenditures and bank-related activities.

We also observed each UPK classroom and counted the number of children to determine whether the class size was 20 or fewer children, and whether the required number of teachers was present in the classrooms. We also asked to see photo identification—such as a New York State Driver's License—of all the Educational Directors, head teachers, assistant teachers, and teacher aides. The names on the photo identifications were compared to the names obtained from the fiscal year End-of-Year Expenditure Forms that listed all UPK educational employees to determine whether the educational employees recorded on these forms were bona fide. For the UPK educational employees recorded on the forms who were not present at our visits, we asked for the personnel folders and reviewed them for any evidence that the employees were bona fide—such as photo identification, college degrees, teaching certificates, or background investigations. At the end of the visits, we obtained the attendance records and compared the number of children marked present to the number of students we counted.

To determine whether expenditures incurred by nine of the schools were reasonable and related to the operations of the UPK program, we selected the five largest Other Than Personal Service (OTPS) expenditures for each of the schools from the End-of-Year Expenditure Forms, which totaled $305,727 out of a total of $329,900 selected OTPS expenditures made by those nine schools during the fiscal year.[7] Then, during our unannounced observations, we requested and reviewed supporting documentation for the chosen OTPS expenditures, such as itemized invoices indicating the purchased items, receipts, and written agreements for consultant services. We also observed the location of any equipment purchased to check whether the items were used for the UPK program.

To determine whether each of the nine schools properly deposited all funds received for the UPK program, we obtained the bank statements for the period September (the first month that UPK payments were received by schools) through August (the last month that UPK payments were received by schools) and traced the payments made by DOE, as reflected on the print-outs from FAMIS, to the bank statements. We also noted whether there were any activities—such as cash withdrawals, checks issued, ATM debit card purchases, and transfers—with unusually high dollar amounts. If so, we requested justification and supporting documentation from the schools to indicate that the activities were legitimate, necessary, and related to the UPK program.

The results of the above tests, which were not projected to all UPK payments to all participating non-public schools, provided us a reasonable basis to determine whether DOE has adequate controls over payments to non-public schools in Regions 6 and 7.

This audit was conducted in accordance with generally accepted government auditing standards (GAGAS) and included tests of the records and other auditing procedures considered

[7] This test was targeted to focus on specific OTPS expenditures totaling $329,900 that due to their variability represented higher risk. We did not test facility costs, meals, and snacks, totaling $414,033 (total OTPS expenditures were $743,933) since these expenditures were constant.

necessary. This audit was performed in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

<u>Discussion of Audit Results</u>

The matters covered in this report were discussed with DOE officials during and at the conclusion of this audit. A preliminary draft report was sent to DOE officials and was discussed at an exit conference held on October 17, 2006. On December 8, 2006, we submitted a draft report to DOE officials with a request for comments. We received written comments from DOE on January 31, 2007. In their response, DOE officials generally did not agree with the audit's findings and recommendations. Nevertheless, they stated that DOE has taken steps to correct many of the issues identified in the report and to enhance the monitoring of the fiscal activities of the UPK program. DOE officials stated:

> "Although the DOE has taken significant steps in the area of creating fiscal controls around its programmatic collaborations with private UPK program providers, we acknowledge that there is a place for constructive recommendations for improvement. Admittedly, as raised in the Report, changes in payment policy to providers to assist them with covering fixed expenses should have been in writing and applied consistently across Regions. We further thank the Comptroller for bringing to our attention opportunities, albeit limited, that had been overlooked for recoupment of funds paid to providers."

The response indicates that DOE has either already recouped or will recoup a total of $51,717 in UPK funds that we identified as inappropriate payments. DOE officials also stated that they are investigating the conditions at Children's Playhouse and have already performed steps necessary to improving the school's performance; they agree that approvals for bonus payments from UPK funds must be in writing, as stated in the DOE *Expenditure Guide*; they are working with the non-public schools to ensure that those engaging in related-party rental agreements request and receive DOE approval in writing; and DOE issued a written directive to non-public schools notifying them of their eligibility to receive free services from the New York City Department of Sanitation and the procedures for obtaining these services.

However, DOE officials also stated:

> "Nevertheless . . . the relatively narrow scope of audit . . . and apparent zeal to attach dollars to relatively minor compliance findings, render many of the audit findings and the recommendations that flow from them only marginally relevant.
>
> "We are concerned that, despite its narrow focus on only ten UPK program providers in just two Regions, the Report invites conjecture about the DOE's controls over UPK payments overall."

The report is quite clear that the objective of the audit was to determine whether DOE has adequate internal controls over UPK payments to non-public schools in Regions 6 and 7. We selected Regions 6 and 7 because they had the greatest number of non-public schools (183) with UPK contracts during Fiscal Year 2004. In total, our sample selection included 10 schools with annual contracts totaling an estimated $3,473,525. It should be noted that the focus of the audit did not include determining the quality of UPK services provided to children. Our report's overall conclusion that DOE does not have adequate internal controls over UPK payments to non-public schools relates only to the schools in Regions 6 and 7. We did not conclude that DOE has inadequate controls "over UPK payments overall."

We disagree with DOE's assertion that the report's findings are "minor" and "marginally relevant." For most of the 10 schools in our sample, we found overpayments and other, inappropriate payments totaling $377,621 as well as questionable bank statement activities totaling $407,322. Given the fact that there are 183 non-public UPK schools in Regions 6 and 7 alone and a total of 583 in all Regions, our findings may well signal a source of potentially large savings. It has been reported elsewhere that DOE has contracted with a consulting firm to identify $200 million in school system savings. (One of its recommendations resulted in DOE's recent cutbacks to the city's yellow school bus routes that it hopes will save up to $12 million a year.) Indeed, it would seem that the substantial cost (estimated at $97 million) of the UPK program in non-public schools alone would compel DOE to reconsider the matters discussed herein and the position it took in its response. We believe that such a reexamination would result in positive changes to the UPK program as a whole.

DOE officials further stated:

> "The audit team conducted only the most superficial group interviews of managers of central offices that play key roles in providing guidance to and oversight for UPK program providers. And, while the managers brought to the auditors' attention during the exit conference and in conversations thereafter that the audit team had not obtained a complete picture of existing controls over UPK payments, the auditors did not seek to address this legitimate concern by conducting interviews before issuing the Report."

DOE's assertion that we did not interview officials extensively about the UPK program is not true. The Deputy Auditor General of OAG arranged for us to meet with officials from three areas to understand the program—the Office of Early Childhood Education, the ROCs, and the Division of Financial Operations. On September 23, 2004, the first formal meeting took place that included officials from these three areas and the Deputy Auditor General. The meeting afforded us an understanding of the responsibilities of the officials and their respective offices. Throughout the audit process, we conducted additional interviews, had discussions by telephone, and corresponded by e-mail with many officials responsible for instructional and fiscal reviews of the UPK program. Further, on various occasions, we discussed many of the audit's concerns with the Contract Administration Officers of the ROCs responsible for Regions 6 and 7 and with officials of the OAG, seeking clarification when needed.

Regarding DOE's efforts to establish a system of controls over the UPK program, officials further stated:

> "DOE managers were available, but were not asked to define their largely successful efforts to create an overarching structure of controls under which the Regions and their private partners implement collaborative UPK programs. . . . Our sustained efforts directed at programmatic and fiscal training for UPK program providers and Regional managers; updating published expenditure guidelines and responses to questions that derive from training and fieldwork; revising contracts; and enhancing financial reporting tools should more than meet the auditors' monitoring standards.
>
> "We suggest that had time been spent actually interviewing knowledgeable DOE managers, a more accurate picture of the DOE's internal controls would have emerged. Having recognized independently of the instant audit that improvements in the monitoring process can and should be made, DOE managers representing responsible central and Regional operations have been engaged in ongoing analysis of the process that has led to appropriate changes and enhancements, including an additional contract and fiscal compliance training program aimed at both Regional managers and providers."

First, as we state above, DOE's assertion that we did not interview knowledgeable DOE managers is incorrect. Second, we cannot comment on the success of DOE's efforts to establish programmatic controls over the UPK program since that was not the objective of our audit. However, concerning *fiscal* controls, the issues we uncover in this audit indicate that efforts in that area have been largely unsuccessful, at least in regard to the UPK program in Regions 6 and 7. Third, the DOE response is contradictory when it asserts that the agency's training, guidelines and reporting tools "more than meet the auditors' monitoring standards," yet later states that DOE recognized improvements should have been made in the monitoring process. Finally, DOE claims that it recognized, independent of this audit, that improvements were needed in its fiscal monitoring of the UPK program. However, other than the solicitation of private audit firms to conduct audits of the UPK program, it has provided no evidence to indicate that the additional changes or enhancements discussed or implemented by DOE officials occurred prior to our notifying them during the course of this audit of the conditions we uncovered.

The full text of the DOE response is included as an addendum to this report.

FINDINGS AND RECOMMENDATIONS

DOE does not have adequate internal controls over UPK payments to non-public schools in Regions 6 and 7. DOE has a fiduciary responsibility to ensure that all of these funds are used appropriately—for the provision of early childhood education to children—and in accordance with the respective contracts. Many of the issues would have been avoided had DOE developed formal fiscal review procedures for the ROCs to follow when monitoring and assessing the UPK program in the schools. A total of $377,621 (12 percent) of the $3.2 million in UPK payments made by DOE in Fiscal Years 2004 and 2005 to the schools in our sample represents overpayments and other inappropriate payments to the schools that should be recouped. We also noted an additional $407,322 in questionable bank statement activities, such as, cash withdrawals, checks issued, and transfers. The major findings (which are discussed in greater detail in the following sections of the report) are as follows:

- DOE overpaid six schools in our sample $141,055 in UPK funds by not adhering to the method of calculating UPK payments stated in the DOE contract. This resulted in DOE paying for more children than were registered and attending the schools as of DOE's cut-off date.

- Three schools in our sample had unspent UPK funds totaling $82,321 (out of $1,275,813 received in Fiscal Year 2005) that should have been recouped by DOE.

- A total of $97,586 (32 percent) of the $305,727 OTPS expenditures reviewed in our sample lacked adequate supporting documentation. Moreover, $66,955 (69 percent) of expenditures with inadequate documentation were for consulting services that were never approved in advance by the Region, as required.

- Of the $208,141 in OTPS expenditures that had supporting documentation, $56,659 (27 percent) was questionable since the expenditures were either not related to the UPK program or not reasonable. In addition, $13,812 (7 percent) was incorrectly classified on the End-of-Year Expenditure Forms.

The following table summarizes the overpayments and other inappropriate payments to the schools totaling approximately $377,621 that should be recouped.

Table I

Summary of DOE Overpayments and
Other Inappropriate Payments

Category	Amount
Overpayment to six schools in our sample caused by not adhering to the method of calculating UPK payments stated in the DOE contract	$ 141,055
Unspent UPK funds	$ 82,321
OTPS expenditures that lacked adequate supporting documentation	$ 97,586
Questionable expenditures	$ 56,659
Total	**$ 377,621**

In addition, there were questionable bank statement activities, such as, cash withdrawals, checks issued, and transfers, totaling $407,322 for five of the schools in our sample. There were also issues regarding the questionable use of UPK funds for: bonuses to teachers at one of the schools; building rental costs between related parties; and private sanitation service.

Moreover, at one of the schools in our sample—Children's Playhouse—we found numerous internal control problems that increase the potential for fraud. There was no segregation of duties for the ordering, authorizing, paying, and recording of goods and services—the Executive Director-owner, herself, performed all of these functions; record-keeping practices were inadequate; of the $346,528 in UPK funds received during Fiscal Year 2005, $93,525 (27 percent) was used for administrative expenses; of the total administrative expenses, (69 percent) was spent solely on the Executive Director-owner's salary;[8] the required number of teachers was not present in two of the classrooms; the number of children we counted did not match the number of children marked present on the attendance records—in some cases it was above while in other cases it was below; in one of the UPK classrooms, the number of three-year-old children exceeded the number of four-year-old children, a practice not allowed by DOE since the UPK program is designed for four-year-old children.[9]

Although DOE does not have adequate internal controls over UPK payments to non-public schools in Regions 6 and 7 to ensure that the funds are used for the intended purposes, we did note that the number of children between DOE's cut-off date and the middle and end of the school year did not decline by that needed for a full class for any of the schools; thus DOE did not have to make any adjustments to payments. DOE did not pay any of the schools twice for the same student. The attendance information for each child contained on the attendance invoices corresponded to the attendance information contained on the Daily Attendance Cards in our sample. Generally, the children listed on the attendance invoices in our sample were listed in ATS and therefore were registered with DOE. The schools properly deposited all funds received for the UPK program. In addition, at our unannounced observations: class size did not exceed 20 children; and all UPK educational employees were bona fide.

DOE Has Not Developed Formal Fiscal Review Procedures For the ROCs to Follow when Monitoring UPK Payments

DOE has not developed, and therefore cannot enforce, any formal fiscal review procedures for the ROCs to follow when monitoring and assessing the UPK program. The lack of such procedures has led to ROC officials' not having a clear understanding of their responsibilities nor of the steps necessary to ensure that schools are adhering to their UPK contracts or the DOE *Expenditure Guide*. As a result, DOE did not have controls in place to identify that some of the schools: did not spend all of their UPK funds received from DOE (the balance of which should have been recouped by DOE); had unsupported and questionable expenditures; had questionable bank

[8] As required by DOE, administrative expenses are not to exceed 10 percent of total UPK Program contract costs.

[9] Schools can combine the two age groups providing the number of three-year-olds in the classroom is at a minimum and does not exceed the number of four-year-olds.

statement activities; incorrectly classified their expenditures; and operated with a lack of segregation of duties and poor record-keeping.

According to ROC officials, the procedures they follow are contained in the contract between DOE and the schools. However, the contract merely contains the general guidelines for the schools and DOE to follow; it does not contain any detailed procedures which would be necessary for DOE or the schools to clearly understand and carry out their responsibilities.

For example, the contract states that the schools are to “maintain books, records, documents, and other evidence in sufficient detail to support all claims against the UPK program, including those that have been made on a cost allocation basis.” The October 8, 2004 letter sent by OAG to each of the schools outlining the key provisions from DOE’s contract states, “UPK transactions should be recorded in a general ledger (hardcopy or software programs) in a manner that is separate from other programs or personal transactions.” Further, ROC officials have informed us that they expect the schools to obtain the *Expenditure Guide* from DOE’s Web site and follow the guidelines of the *Expenditure Guide* which explain the types of expenses that constitute appropriate UPK program expenditures.

However, neither the contract, nor the outline of the key provisions of the contract, nor the DOE *Expenditure Guide* details the steps that the ROCs should follow in assessing whether the schools are in fact maintaining adequate books, such as a general ledger, in accordance with the OAG letter; records, such as invoices, in accordance with the contract; and incurring expenditures that are reasonable and related to the operations of the UPK program, in accordance with the DOE *Expenditure Guide*. By having formal fiscal review procedures, ROC officials would clearly know how and when to review documentation at the schools, and the criteria to measure schools’ fiscal performance. In the absence of formal procedures, officials may not be consistently working together to ensure that the UPK program is operating as intended.

ROC officials have stated that they do not ask the schools to submit any documentation to support actual expenditures reported on the Mid-Year Expenditure Forms and End-of-Year Expenditure Forms. They ask only that the schools retain the documentation on site for audit purposes. We questioned whether DOE ever conducts UPK audits of non-public schools. DOE’s Deputy Auditor General stated that OAG does not routinely conduct UPK audits of non-public schools, but conducts audits somewhat routinely of non-public schools that have special education children as part of their UPK program or that have many complaints made against them. DOE has not conducted audits for any of the 10 schools in our sample.

Learning Support Center officials responsible for the instructional review of the UPK program, however, make visits to the non-public schools at least once a year to evaluate them from an educational standpoint. We noted that for the 10 schools in our sample, the instructional teams made visits to the schools at least once during the school year reviewed and used a detailed checklist. However, there are no corresponding ROC teams to make visits to the schools to evaluate their UPK financial practices. DOE should ensure that the ROCs periodically visit these non-public schools and review the financial records to ensure that schools are in compliance with their DOE contract and that all expenditures are legitimate in accordance with the DOE *Expenditure Guide*.

DOE Response: "None of the documents cited was intended by the DOE to serve as a step-by-step guide to the *Regional Operational Centers* . . . for monitoring the program. Instead, and more logically, the documents are intended to serve as a statement of the *providers'* obligations (contract) and as guidance in operating the UPK program (contract and *Expenditure Guide*). The ROCs are expected to be thoroughly familiar with the contracts and fiscal guidelines and to work with the OAG and the audit firms retained by the OAG to review providers' fiscal and key contract provision compliance." (Emphasis in original.)

Auditor Comment: It appears that DOE has missed our point. We realize that the contracts and DOE *Expenditure Guide* were not intended by DOE to serve as a step-by-step guide for the ROCs to follow when monitoring the UPK program. Therefore, in the absence of such a guide, DOE should develop formal fiscal review procedures for the ROCs to follow. Formal fiscal procedures would provide the means by which ROC officials involved in the UPK program would gain a clear understanding of their responsibilities in monitoring UPK payments to the non-public schools.

Although DOE's response states that the ROCs are expected to be thoroughly familiar with the contract and DOE *Expenditure Guide*, our audit report has noted many issues of non-compliance regarding these documents that the ROC in Staten Island failed to notice. Therefore, we repeat our recommendation that DOE should develop and implement written fiscal review procedures for the ROCs to follow when monitoring and assessing the UPK program.

Recommendation

DOE should:

1. Develop and implement written fiscal review procedures for the ROCs to follow when monitoring and assessing the UPK program. These procedures should include the steps that the ROCs will take to ensure that non-public schools comply with their contracts and the DOE *Expenditure Guide*. For example, DOE should ensure that the ROCs periodically visit the non-public schools and review the financial records.

***DOE Response*:** "The DOE, through the OAG and private audit firms engaged specifically for this purpose, have trained Regional programmatic and operational staff and made available to them in hardcopy and on the website a work plan for auditing and conducting contract compliance reviews of UPK program providers. Further, the Regions have participated in training offered to providers in meeting fiscal responsibilities and have received auditors' assistance in analyzing expenditure reports submitted by providers. Further, during this current school year, the UPK monitoring program was expanded to include provider contract and fiscal compliance surveys and more drilled-down training opportunities for providers that required additional assistance."

Auditor Comment: In its response, DOE refers to a "work plan for auditing and conducting contract compliance reviews of UPK program providers." At the beginning of the audit, we obtained from DOE's Web site a work plan developed by OAG specifically for audit firms retained by DOE—not ROCs—to use when conducting their audits of UPK programs. However, this work plan is not adequate for the ROCs to use to conduct their routine fiscal monitoring of the schools. For example, there are no tests designed in the work plan to ensure that: UPK expenditures are made in accordance with the DOE *Expenditure Guide*—in fact, there is no mention about the DOE *Expenditure Guide* at all; End-of-Year Expenditure Forms are reviewed to verify that actual UPK expenditures reported do not exceed budgeted UPK expenditures and that actual DOE payments do not exceed actual expenditures; and DOE payments to schools are made in accordance with the payment method stated in the contract. We should note that DOE did not provide evidence that DOE or the audit firms conducted any audits for any of the 10 schools in our sample nor any other schools operating UPK programs.

DOE's response further states that it has made a work plan available in hard copy and on the Web site not only to the audit firms but to the Regional programmatic and operational staff. Since DOE's work plan was originally intended only for audit firms, we checked DOE's Web site to determine whether DOE has in fact revised the work plan to include detailed steps for use not only by audit firms but by the ROCs, to ensure that non-public schools comply with their contracts and the DOE *Expenditure Guide.* However, we did not find such a work plan.

Therefore, we continue to believe that it is in DOE's best interest to develop, distribute, and implement written fiscal review procedures for the ROCs to follow since DOE has a fiduciary responsibility to ensure that all UPK funds are used appropriately. Formal fiscal review procedures and standardized criteria would ensure that monitoring and evaluations of non-public-school fiscal performance take place and are consistent.

2. Develop and implement written procedures for the schools to follow and/or rewrite its contracts.

DOE Response: "The DOE considers [this recommendation] 'implemented'. **. . .** Providers already have been directed to comply with the *Expenditure Guide*; have been given further instructive guidance in the published *Frequently Asked Questions*; and have been provided with training materials and written self-assessments in the form of surveys.

"The further recommendation that we consider rewriting our UPK contracts, presumably for the purpose of offering 'written procedures for the schools to follow' is so vague as to thwart practical implementation. Our response is that the UPK contracts . . . provide a clear statement of obligations, among which are to expend UPK funds exclusively for the benefit of the program, maintain appropriate books and records, and make those records available for audit or other inspection."

***Auditor Comment*:** While the DOE *Expenditure Guide* and *Frequently Asked Questions* are important documents for the schools to follow, they are not comprehensive enough to help the schools understand all of their responsibilities in the UPK program. The DOE

Expenditure Guide is merely a document that explains the types of expenses that constitute appropriate UPK program expenditures, while *Frequently Asked Questions* is a document intended for schools that seek information about applying for and operating a UPK program. DOE needs to develop procedures that detail what is expected of the schools, including but not limited to: End-of-Year Expenditure Forms, supporting documentation for expenses, attendance records, calculations of payments they are to receive, record-keeping practices, and segregation of duties.

In addition, based upon the audit's findings, it is apparent to us that the non-public schools were either not aware of the DOE *Expenditure Guide* and/or *Frequently Asked Questions*, or chose not to follow these documents. For example, schools had unspent UPK funds; had unsupported and questionable expenditures; incorrectly classified their expenditures; and operated with a lack of segregation of duties and poor record-keeping.

DOE Overpaid Schools $141,055 in UPK Funds

DOE overpaid six (60 percent) of the 10 schools in our sample a total of $141,055 in UPK funds during Fiscal Year 2005 by paying for more children than were registered and attending the schools as of DOE's cut-off date.

As stated previously, the amount payable each school year (the adjusted annual contract amount) is based on the number of children registered and attending as of the last school day in October. However, DOE extended the cut-off date to the last school day of the third week in November and allowed the schools to use either the October or November date, depending on which date had the largest number of children.

Based on the attendance invoices for October and November 2003 and 2004 for each of the 10 schools in our sample, we determined the amount that should have been paid to each school and compared it to the amount that DOE actually paid, as reflected in the print-outs from FAMIS.

Table II, following, details for each of the six schools the Fiscal Year 2005 UPK payments that DOE should have made compared to the payments that DOE made and which resulted in overpayments totaling $141,055.

Table II

Six Sampled Schools That Were Overpaid
Fiscal Year 2005

(A) School	(B) Cost Per Child In Contract	(C) Estimated # of Children in Contract	(D) # of Children Auditors Calculated (Based on the Greater of the Two Days)	(D) Auditors Calculation (B x D)	(E) # of Children DOE Calculated	(F) Amount that DOE Paid (B x E)	(G) Amount DOE Overpaid (F – D)
CYCLE Day Care Center	$3,450	100	85	$293,250	100	$345,000	$51,750
Children's Playhouse	$3,332	108	93	$309,876	104	$346,528	$36,652
Smart Start Early Childhood Center	$3,904	81	74	$288,896	81	$316,224	$27,328
Jewish Community Center of Staten Island	$3,400	132	120	$408,000	132	$426,360 *	$18,360
Gan Day Care Center	$3,511	99	98	$344,078	99	$347,589	$3,511
Our Saviour's Lutheran Preschool	$3,454	88	87	$300,498	88	$303,952	$3,454
Total				$1,944,598		$2,085,653	**$141,055**

* DOE based its payments on 132 children and determined that $448,800 (132 x $3,400) was to be paid. However, DOE only paid $426,360.

We spoke with DOE officials for Regions 6 and 7 to inquire about the overpayments. They stated that during Fiscal Year 2005 a "10 percent shortfall allowance" (allowance) was used for determining payments, and based on this allowance, they stated that none of the schools we cited had overpayments. Officials further stated that if the number of children registered and attending as of DOE's cut-off date fell below the estimated number of children stated in the contract, then Regions 6 and 7 would pay the schools based on the reported number of children plus 10 percent of the estimated number of children. They gave as an example Children's Playhouse, which it was estimated would serve 108 children. However, the number of children registered and attending as of DOE's cut-off date was 93. By factoring in the allowance, Children's Playhouse was able to be paid for 104 children—93 children plus 11 (10 percent of the estimated number of children of 108).

We asked DOE officials for any written guidelines that they might have regarding how UPK payments should be made since their assertion of the existence of an allowance was contrary to anything stated in the UPK contract. Officials stated that they have not developed any written guidelines; however, they provided us with copies of e-mails dated January 13 and 14, 2005.

The e-mails indicated that there had been some discussion among all of the Regions and the Office of Contract Management concerning the possibility of changing the method, as stated in the contract, for determining the number of children to use when calculating UPK payments. The e-mails further indicated that the officials from Regions 6 and 7 took it upon themselves to adopt what the e-mails termed an “unwritten rule” concerning an allowance, since no new policy was ever formally established. In one of the e-mails, a DOE official indicated that this unwritten rule should not be expanded to the other Regions since these Regions do not use an allowance when determining UPK payments, but strictly follow the terms stated in the contract.

Thus, it appears from the e-mails that the alleged allowance has been used only by Regions 6 and 7. If DOE wanted to factor in such an allowance, then all of its UPK contracts with the schools should have been amended to reflect this allowance. At the very least, there should have been written guidelines governing the altered method for calculating UPK payments. It should be noted, however, that if DOE were to formally institute this allowance, it could have the unintended effect of discouraging schools from meeting the estimated target number, since they would be paid the same amount if they fell as much as 10 percent below the target.

> ***DOE Response***: “To further reinforce the incentives for providers to meet their target enrollment numbers, the DOE will issue a written statement to the Regions clarifying a policy that where a provider does not meet its enrollment estimate, the next year the starting point for setting the estimated number of available UPK seats should be reduced to reflect the prior year’s shortfall.”

Even though Regions 6 and 7 officials have their own informal procedures for calculating UPK payments using an allowance, they do not enforce even these procedures since this allowance was not always applied. For example, CYCLE Day Care Center was estimated to have 100 children. However, it actually had 85 children as of DOE’s cut-off date. By applying DOE’s informal allowance, DOE should have paid the school for 95 children—85 children plus 10 (10 percent of the estimated number of 100 children). However, DOE paid CYCLE Day Care Center for the estimated number of 100 children. When we questioned DOE officials about this, they asserted that they calculated the number of children as of DOE’s cut-off date to be 92 and not 85—as we determined—and factored in the allowance, which brought the number of children up to 100. Our review revealed that DOE officials had included seven children in their total of 92 who should not have been included—five children who never showed up at the school, one child who was discharged before DOE’s cut-off date (on October 22, 2004), and one child who was registered and attended after DOE’s cut-off date (on November 22, 2004).

Furthermore, we noted that not all of the schools were aware of an allowance. For example, the Chief Financial Officer (CFO) at the Jewish Community Center of Staten Island (JCC) reported actual expenditures for only 120 children when an allowance would have enabled her to report actual expenditures for 132 children. The CFO stated that she was not aware of an allowance and that as far as she knew, UPK payments are based on the number of children registered and attending as of either the October or November date, depending on which date had the largest number of children. She stated that for her school, the number of children was 120. She noted that when she prepared her End-of-Year Expenditure Form for Fiscal Year 2005, she specifically ensured that the expenditures reported as incurred totaled $408,000 (120 children multiplied by $3,400).

However, DOE officials based their payments to JCC on 132 children and determined that $448,800 was to be paid, but actually made payments of $426,360—resulting in an overpayment of $18,360 ($426,360 minus $408,000). The CFO provided us a letter dated December 15, 2005, from Region 7, which stated that approximately $18,000 was going to be deducted in equal installments from the November 2005 through June 2006 UPK payments to correct the overpayment that had been made. Since DOE officials initially asserted that because of the use of the allowance, no overpayments were made to any of the six schools that we cited as having been overpaid, we did not understand why they ultimately decided to recoup moneys from JCC.

Since DOE's allowance for calculating UPK payments during Fiscal Year 2005 was not formally written, approved, or communicated to all schools, we did not consider it an official policy change. Therefore, we have not changed our calculations or findings. (It should be noted that officials for Regions 6 and 7 informed us that they have been instructed not to apply the informal allowance to payments made during Fiscal Year 2006 for schools still operating under contracts that have not expired as of June 30, 2005.)

DOE officials stated that the contract section on the method of calculating UPK payments has been formally modified, starting with contracts being entered into for the period July 1, 2005, through June 30, 2008. According to the modified and rather complex method, DOE is still required to determine the number of children registered and attending a school as of DOE's cut-off date. However, the amount to be paid to the school will be based on specific rates set by DOE, depending on whether the number of children is five percent fewer than the estimated number of children, more than five percent fewer than the estimated number of children, or more than thirty percent fewer than the estimated number of children.

We determined whether, as of March 2006, DOE correctly calculated payments for the five schools in our sample that have entered into new contracts with DOE for the period July 1, 2005, through June 30, 2008. Payments were not calculated correctly for two of the five schools. As of March 2006, DOE overpaid CYCLE Day Care Center by $2,100 and underpaid Smart Start Early Childhood Center by approximately $593. Although these incorrect payments are not as significant as those we found during Fiscal Year 2005 for the 10 schools in our sample, errors in payments are still being made by using the modified method of calculating payments.

Recommendations

DOE officials should:

3. Ensure that they adhere to the provisions of the UPK contracts with non-public schools when determining payments. If the method for determining payments changes, then the contracts need to be amended. In addition, there should be written guidelines governing the calculation of the payments.

DOE Response: "In order to maintain availability of providers and the quality of the UPK program, the DOE determined in FY 2004/2005 that the best interests of the students were served by allowing a margin of ten percent above the number of students on register.

"If the question were whether it would have been better to formalize and consistently apply the margin policy at the time it was effected, the DOE would answer 'yes.' However, if the question posed, instead, were whether the DOE violated the law of contracts or its obligations to safeguard public funds, we stand on the action that was taken."

Auditor Comment: A contract is a legally binding agreement that contains specific, agreed-upon terms. It appears that DOE considers the UPK contract merely a suggestion rather than a binding document, since the terms regarding the calculation of UPK payments stated in the contract were not followed. Regions 6 and 7 officials took it upon themselves to adopt a "10 percent shortfall allowance," and did not even apply it to all contracts within the two Regions. In its response, DOE states "the best interests of the students were served by allowing a margin of ten percent above the number of students on register." However, if this was DOE policy, then DOE should have amended all UPK contracts within all Regions to reflect it, which would have ensured that the margin was formally and consistently applied, as even DOE acknowledges in its response. In the future, DOE should ensure that it adheres to the provisions of the UPK contracts when determining payments. Moreover, DOE should develop written guidelines governing the method of calculating UPK payments, and the guidelines should be distributed to all ROCs and schools so that all personnel are aware of the method and can apply it consistently.

4. Recoup the UPK overpayments made during Fiscal Year 2005 to the six schools in our sample.

DOE Response: "*The DOE did not overpay UPK program providers $141,055. The DOE's payments to the audited UPK providers were consistent with a policy in effect at the time, but for one case of an overpayment of $17,250, which will be recouped by the close of School Year 2006/2007*. [Italics in original.]

"We are steadfast in our position that the payment policy was appropriate as applied and have recomputed the auditors' numbers using the ten percent margin for each of the six schools. Based on our calculations, we reject the Report's recommendation for recoupment in large part. In five cases the number of students for whom payment was made fell within the ten percent range. However, we identified an overpayment in the case of CYCLE Day Care in the amount of $17,250."

Auditor Comment: We stand by our recommendation that DOE recoup the overpayments made to the six schools since the payments were not made in accordance with the terms of the UPK contract and since we did not consider the informal "10 percent shortfall allowance" an official policy change. In fact, it appeared that even DOE was uncertain about the allowance when an Office of Contract Management official stated in an e-mail that the unwritten rule concerning the allowance as applied by Regions 6 and 7 should not be expanded to the other Regions and added that the other Regions do not use an allowance, but rather strictly follow the terms of the UPK contract when determining UPK payments.

5. Make adjustments for the incorrect payments made as of March 2006 to CYCLE Day Care Center and Smart Start Early Childhood Center based on the new contract payment terms for the period July 1, 2005, through June 30, 2008.

***DOE Response:* "**In the case of CYCLE Day Care, the auditors calculated an overpayment of $2,100; Smart Start Early Childhood Center, according to the auditors, was underpaid $593.

"OAG performed its own calculations based on payments made by the end of the school year and official enrollment data for each school. It was determined that CYCLE Day Care received payments for exactly the 81 students on register as of the official close of register date (November 18, 2005); no adjustments were required; and no overpayment was made by the DOE. OAG's calculations with respect to Smart Start Early Childhood Center identified an underpayment in the amount of $1,185."

Auditor Comment: DOE's calculation regarding CYCLE Day Care is incorrect. In a footnote in its response, DOE claims that it obtained the number of registered students from ATS. However, attendance invoices (which are the source for the student registration figures reported in ATS) showed that there were 77, not 81, students registered at CYCLE Day Care as of November 18, 2005.

With regards to Smart Start, we calculated an underpayment of $593 as of March 2006. DOE calculated an underpayment of $1,185 as of the end of the school year. Due to the timing difference, the calculations would be different. However, we cannot determine whether DOE's calculation is correct because DOE did not state the number of students used in its calculation and we did not have the payment history information for Smart Start subsequent to March 2006.

DOE Failed to Recoup $82,321 in Unspent UPK Funds

Three of the nine schools in our sample received adjusted annual contract payments totaling $1,275,813 during our audit period, but reported to DOE expenditures of only $1,193,492 on the End-of-Year Expenditure Forms, resulting in $82,321 of UPK funds unspent, which should have been recouped by DOE. Specifically, Gan Day Care Center, Smart Start Early Childhood Center, and the Staten Island YMCA Nursery School received payments of $347,589, $316,224, and $612,000, respectively, during Fiscal Year 2005. However, expenditures reported to DOE by these schools totaled $299,560, $304,563, and $589,369, respectively, resulting in $48,029, $11,661, and $22,631 in unspent UPK funds for each of these schools.

According to the contract between DOE and each of the schools, if it is determined by the Region that a school has not expended its funds, the amounts not expended are to be recouped. The contract further states that the Region is to first notify the school in writing of its findings and allow 10 days for a response. Then, the Region is to review the response and make a determination about the actions that should be taken.

We spoke to the Contract Administration Officer for Region 7 about the unspent UPK funds. After a quick review of the UPK receipts and expenditures for the three schools, he agreed with our figures and noted that there were indeed unspent UPK funds that were not uncovered by DOE officials. He agreed to investigate the situation by discussing it with his staff and contacting the schools and would recoup the moneys.

As part of the contract between DOE and the non-public schools, the End-of-Year Expenditure Forms are to be submitted to the ROCs for review at the end of the school year. The Contract Administration Officers of the ROCs are required to review them to ensure that the actual UPK expenditures reported do not exceed budgeted UPK expenditures and also that the schools are expending all of the funds received. We question whether the ROCs are reviewing these forms as required since DOE officials were not aware of these discrepancies until we brought them to their attention.

At the exit conference, DOE officials stated that they have recouped the $22,631 in unspent UPK funds from the Staten Island YMCA Nursery School. (They subsequently provided us evidence of this recoupment.)

DOE officials further stated that for Smart Start Early Childhood Center, we did not have the revised End-of-Year Expenditure Form for Fiscal Year 2005, which they provided to us after the exit conference. This revised form, which was undated, shows that Smart Start spent $36,818 more than what was received from DOE for the UPK program. It is interesting to note that the revised form shows $36,818 as “In Kind Contributions” made by the Administrative and Educational Directors, which was never reported to DOE on the version of the End-of-Year Expenditure Form that we reviewed. It should be noted that we had discussed the overpayment totaling $11,661 with the Contract Administration Officer for Region 7 on May 16, 2006—almost one year after the form was required to be submitted. At that time, the Contract Administration Officer confirmed that we had the correct expenditure figures as reported by

Smart Start. He did not mention a revised End-of-Year Expenditure Form. Accordingly, we were unable to determine the legitimacy of the expenditures listed on the revised report.

DOE Response: "For reasons having to do with the difficulty of making a legible copy [of the revised signed and dated End-of-Year Expenditure Form] that could be faxed to the auditors, the OAG manager asked for and received from the Region a clean electronic version of the revised End-of-Year Expenditure Report that had also been submitted to the Region by the school in August 2005. Since that version of the expenditure report had been submitted electronically, it did not bear a dated signature. However, that was the version submitted electronically to the auditors by the OAG manager, and we apologize for any confusion that might have caused."

Auditor Comment: We question the validity of Smart Start's revised End-of-Year Expenditure Form. As stated previously in the report, DOE's Contract Administration Officer for Region 7 confirmed on May 16, 2006, that we had obtained the correct expenditure figures, as reported by Smart Start, and agreed that there were indeed unspent funds. The official did not mention a revised End-of-Year Expenditure Form. In addition, we conducted an unannounced visit to Smart Start on November 15, 2005. On that date, we requested supporting documentation for the five sampled OTPS expenditures that we chose from the Fiscal Year 2005 End-of-Year Expenditure Form. If in fact Smart Start had submitted a revised End-of-Year Expenditure Form in August 2005, as was stated in DOE's response, then we question why officials at Smart Start did not inform us of this during our unannounced visit or during the audit.

For example, we requested all of the supporting documentation for the expenditure "office/janitorial supplies" that totaled $2,422 on the Fiscal Year 2005 End-of-Year Expenditure Form. Not once during our discussions with officials at Smart Start were we informed that this number was incorrect. However, the revised End-of-Year Expenditure Form shows that the expenditure "office/janitorial supplies" was revised to $5,422—an increase of exactly $3,000. In another example, the revised End-of-Year Expenditure Form shows that the expenditure "instructional supplies" was revised to $6,897 from $3,947; however, Smart Start was not even able to supply documentation to support the entire $3,947 worth of expenditures, let alone the $6,897. (It should be noted that, in total, four of the five OTPS expenditures chosen in our sample were revised by Smart Start.)

With regards to Gan Day Care Center, DOE officials stated that salary and wage expenditures on the End-of-Year Expenditure Form were reported on a cash basis rather than on an accrual basis, as required by DOE. Therefore, according to DOE officials, the discrepancy did not indicate unspent funds by Gan Day Care Center but rather a reporting error. DOE subsequently had Gan Day Care Center prepare a revised End-of-Year Expenditure Form, which DOE provided to us, listing the salary and wage expenditures on the accrual basis and showing now that Gan Day Care Center had only $75 in unspent UPK funds. (DOE did not provide us with any documentation to support the revised figures, so we were unable to verify the reported error.) DOE officials also provided us with evidence that this amount was recouped.

Recommendations

DOE officials should:

6. Examine the revised End-of-Year Expenditure Forms submitted by Smart Start Early Childhood Center and Gan Day Care Center and verify that the reported expenditures are proper and adequately supported.

DOE Response: Regarding Gan Day Care Center, DOE officials responded, "The Gan Day Care Center End-of-Year Expenditure Form, as originally submitted, reported expenditures on a cash, rather than an accrual basis as required by the DOE. That misunderstanding substantially impacted the amount of expenses reported in the staff salary cost category, since Gan Day Care Center was permitted to—and did—pay its staff over a twelve-month period despite that the UPK program operated over ten months.

"The OAG, using the accrual basis method, determined that the twelve-month payments correctly represented the amount that should have been reported as salary expense. These calculations however have identified an unexpended balance of $75, which we have recouped."

Auditor Comment: In its response, DOE officials did not specifically address the part of the recommendation to examine the revised End-of-Year Expenditure Form submitted by Smart Start Early Childhood Center. DOE officials stated in the response that the End-of-Year Expenditure Form had been revised by Smart Start and was submitted to DOE in August 2005. However, DOE did not indicate whether the revised figures were traced back to the supporting documentation. Therefore, we repeat our recommendation that DOE officials examine the revised End-of-Year Expenditure Form submitted by Smart Start Early Childhood Center and verify that the reported expenditures are proper and adequately supported.

7. After examination, recoup any remaining unspent UPK funds for the schools cited.

DOE Response: *"The DOE . . . disputes the finding in large part and calculates unspent UPK funds in the total sum of $22,706. (Staten Island YMCA: $22,631; Gan Day Care Center: $75).* [Italics in original.]

"Preliminarily, the DOE acknowledges that the Staten Island YMCA in fact reported unexpended funds of $22,631. Those funds have been recouped in full as of this date. . . . But for that sum, and a $75 unexpended balance attributable to Gan Day Care Center, we dispute the finding."

Auditor Comment: While we are pleased that DOE officials have recouped $22,706 in unspent UPK funds, we continue to urge DOE to examine the revised End-of-Year Expenditure Form submitted by Smart Start Early Childhood Center and verify that the reported expenditures are proper and adequately supported. Then, if necessary, recoup any unspent funds.

OTPS Expenditure Issues

Expenditures Totaling $97,586 Lacked Adequate Supporting Documentation

Our review of the $305,727 in OTPS expenditures for the nine schools in our sample revealed a total of $97,586 (32 percent) that lacked adequate supporting documentation for such expenditures as consulting services, instructional and office or janitorial supplies, minor maintenance and repairs, and miscellaneous purchases. Therefore, we were unable to determine whether the expenditures were related and reasonable to the operations of the UPK program. Moreover, $66,955 (69 percent) of the expenditures with inadequate documentation were for consulting services, such as accounting and music instruction, provided at six of our sampled schools that were never approved in advance by the Region, as required.

The DOE *Expenditure Guide* states that all purchases must be supported with: itemized invoices indicating items purchased, date of purchase, and date of payment; and canceled checks. Invoices must be annotated to specifically identify the UPK purchases. In addition, credit card receipts must specifically identify the items purchased. The *Expenditure Guide* further states that costs associated with consulting services must be approved in advance by the Region, before hiring, and the Region may require bidding. Adequate documentation for consulting services includes, but is not limited to, a consultant's resume, a written contract that includes the specific services to be provided, the charge per day, service dates, and assigned work sites. In addition, the documentation should include the number of days actually worked, dates worked, work site, and if applicable, sign-in sheets for each service date and number of service hours performed.

Table III, following, shows for each of the nine schools in our sample the total OTPS expenditures sampled and the total amount and percentage that lacked adequate supporting documentation.

Table III

<u>Total OTPS Expenditures Sampled That Lacked Adequate Supporting Documentation For Each of the Nine Schools Sampled</u>

(A) School	(B) Total OTPS Expenditures Sampled	(C) Total OTPS Expenditures Unsupported	(D) Percentage of OTPS Expenditures Unsupported (C/B)
CYCLE Day Care Center	$28,617	$23,260	81%
Gan Day Care Center	$48,541	$24,223	50%
Children's Playhouse	$20,387	$ 7,185	35%
Our Saviour's Lutheran Preschool	$40,864	$13,026	32%
Building Blocks Preschool	$ 5,782	$ 1,588	27%
Smart Start Early Childhood Center	$20,261	$ 5,367	26%
Staten Island YMCA Nursery School	$90,065	$20,972	23%
Jewish Community Center of Staten Island	$41,348	$ 1,840	4%
Bryan's Educational Center	$ 9,862	$ 125	1%
Total	**$305,727**	**$97,586**	**32%**

Some examples of OTPS expenditures that lacked adequate supporting documentation include payments of $851 to the Director of Our Saviour's Lutheran Preschool for reimbursement of minor maintenance and repairs, $70 to the arts and crafts teacher of Gan Day Care Center for instructional supplies, and $822 to Lakeshore Learning Materials and $1,032 to Abram and Co. Publishers by the Staten Island YMCA Nursery School for instructional supplies.

At the exit conference, an auditor from OAG informed us that she had contacted the schools we cited to try to obtain the supporting documentation that was lacking. Immediately following the exit conference, she supplied us with the documentation she obtained. Upon our review, we found that this documentation was the same as that we had already obtained from the schools and that we had deemed inadequate. For example, most of the documentation provided to us by the OAG auditor was for consulting services and not all of the following documentation was present—as required by the DOE *Expenditure Guide:*

- approval in advance by the Region;
- bidding, if required by the Region;
- consultant's resume;
- written contract that includes the specific services to be provided;
- charge per day, service dates, and assigned work sites; and

- number of days actually worked, dates worked, work site, and if applicable, sign-in sheets for each service date and number of service hours performed.

Accordingly, our finding remains unchanged.

DOE Response: "We believe that within the finding's monetary 'disallowance' are numerous situations involving consulting services where the providers presented to the audit team satisfactory documentation of service and expense, but were unable to produce written approvals by the Region and/or bids. The audit team deemed each 'flaw' fatal to the transaction, referencing the section in the UPK *Expenditure Guide* that speaks to bids and the Region's pre-approval for consulting services, and refusing to accept the OAG and Region's position that if consulting services are identified in the budget, and that budget is approved, the approval satisfies the *Expenditure Guide*.

"We posed the question internally whether, if a tested transaction meets the cost principle of 'reasonable and necessary' and was supported, the DOE would be seeking recoupment from the providers simply because approval [for consulting services] had not been apparent from a separate writing or bids were not sought. We have concluded that we would not."

Auditor Comment: DOE's own *Expenditure Guide* provided the criteria we used to evaluate whether there was appropriate documentation for UPK purchases. It specifically requires six documents—DOE approvals, bids, written contracts, resumes, lists of service dates, and attendance records—necessary as support for consulting service expenditures. We merely applied DOE's own criteria. In most instances, the consulting services we reviewed lacked more than one of the required documents. As an example, for the Staten Island YMCA, the only documentation provided to us was an e-mail dated May 7, 2005, from the consultant to the YMCA detailing all of the payments that had already been made by the YMCA to the consultant up until that date. We should note that DOE officials attempted to obtain additional documentation from the school after we brought this matter to their attention, but they too were able to supply us only a copy of the same e-mail. Nevertheless, DOE accepted this e-mail as adequate supporting documentation for this expense which totaled $15,552.

Recommendations

DOE officials should:

8. Recoup the $97,586 identified in this audit as expenditures that are not supported by the records of the non-public schools we cited.

DOE Response: "*The DOE agrees that, to date, three providers* [CYCLE Day Care Center $12,510, Our Saviour's Lutheran Preschool $6,710, and the Staten Island YMCA $17,191] *have not submitted to the audit team or the OAG documentation adequately supporting total expenditures of $36,411; in those cases, the OAG will either pursue documentation or seek recoupment, as appropriate.* [Italics in original.]

"OAG using the audit team's work papers and additional information provided during meetings with the auditors, performed an analysis of the items that comprised the total disallowance. . . . OAG staff reached out to the audited providers and was fairly successful in obtaining additional records. The OAG submitted those records to the auditors. We are first learning that the records characterized in the work papers as missing . . . are deemed by them to be duplicates.

"We cannot accept the recoupment recommendation as written."

Auditor Comment: We are pleased that DOE officials have taken steps to investigate the inadequate supporting documentation for the nine schools that are cited in the report. Before and after we issued the preliminary draft report to DOE, we gave an OAG auditor complete access to our work papers for review and copying. The work papers included all documentation we obtained from the schools. In addition, we provided the auditor with our analyses that showed all of the inadequately supported expenditures for each school and included our detailed reasons for deeming them inadequate. As stated previously, the OAG auditor had contacted the schools we cited and provided us any documentation she obtained. However, after receiving and reviewing that documentation, we found that it was the same as that we had already obtained from the schools, which we had deemed inadequate. With access to our work papers and analyses, it should have been clear to DOE that the documents they had obtained from the non-public schools and provided to us were inadequate.

Regarding the three non-public schools for which DOE officials have stated that they are still pursuing further documentation, DOE should at this point recoup the funds. We made numerous attempts to no avail to obtain the missing supporting documentation for these three non-public schools as well as for others. Since the documents we lack are from Fiscal Year 2005, and it is now Fiscal Year 2007—two years later—it is highly unlikely that the schools have them.

9. Ensure that non-public schools maintain adequate supporting documentation for all expenditures.

DOE Response: "DOE already has a substantial program of controls, which we continually review and upgrade. . . . The audit firm that is working with the OAG this school year is performing UPK program audits and desk reviews in addition to training Regional managers and UPK program providers and assisting with Regional managers' mid- and end-year expenditure reports review."

10. Ensure that all consulting services are approved by the Region prior to their use by the non-public schools.

DOE Response: "If consulting services are identified in the budget, and that budget is approved, the approval satisfies the *Expenditure Guide*."

Auditor Comment: We do not believe that simply approving an expenditure noted as "consultants" on a budget constitutes adequate expenditure review and approval. The budgets that are approved by DOE do not list each consultant selected by the non-public schools and associated costs; the only information listed in the budgets is the total amount for the school year that is expected to be expended for the "consultants" expenditure.

We noted that on its budget for Fiscal Year 2005, the Staten Island YMCA did not record any amount for its "consultants" expenditure. However, when we reviewed the End-of-Year Expenditure Form for this school, we found that a total of $15,790 was actually spent during Fiscal Year 2005 for the expenditure "consultants." We question DOE approval of this expenditure since it was not listed in the budget. As a result, we believe that it is in DOE's best interest to require the Regions to approve each consultant on a case-by-case basis. Moreover, to ensure that the procurement process of consulting services is conducted in a fair and competitive manner, bidding should be required for all consulting services. DOE approval should then be requested after providing proof that bidding was conducted and that the decision to select a consultant was made fairly and competitively.

11. Institute procedures to require the review of supporting documentation by DOE staff.

DOE Response: "DOE already has a substantial program of controls, which we continually review and upgrade. . . . The audit firm that is working with the OAG this school year is performing UPK program audits and desk reviews in addition to training Regional managers and UPK program providers and assisting Regional managers' mid- and end-year expenditure reports review."

Questionable Expenditures

Of the $208,141 in OTPS expenditures that had supporting documentation, $56,659 (27 percent) was questionable since the expenditures were either not related to the UPK program or not reasonable. For example, the Staten Island YMCA Nursery School purchased karate uniforms totaling $3,578 for children in its UPK program from Honda Martial Arts Supply Company. According to DOE officials, formal karate instruction is not to be conducted during the two and one-half hours offered by the UPK program. Therefore, we question why karate uniforms were purchased with UPK funds since this activity is not related to the UPK program.

In another example, a receipt for Children's Playhouse from Factory Appliance Service Wholesale New Appliances indicated a purchase of an air conditioner totaling $580, to be delivered to 950 Rockland Avenue (one of two school sites occupied by Children's Playhouse). We question whether UPK funds should have been used for this expenditure since 85 Monahan Avenue—and not 950 Rockland Avenue—is occupied by the UPK program.

We question the reasonableness of an equipment expenditure totaling $34,321 incurred by the Staten Island YMCA Nursery School of the purchase and installation of playground tiles. According to the DOE *Expenditure Guide*, schools have a "continuing obligation . . . to establish a cost allocation methodology and to allocate costs across programs." The Staten Island YMCA Nursery School should not have paid for the purchase and installation of playground tiles entirely from UPK funds since the playground is used by all of the school's early childhood programs (including three-year-old and summer day camp children). Moreover, the *Expenditure Guide* states that the Region is to approve in advance any equipment expenditures that exceed $1,000, and only after reviewing the submission of three written bids by the schools. There was no evidence that three written bids were ever submitted or that the Region pre-approved the expenditure.

Recommendations

DOE officials should:

12. Recoup the $56,659 identified in the audit as expenditures that were either not related to the UPK program or were not reasonable for the non-public schools we cited.

DOE Response: *"The DOE cannot agree with the recommendation that we recoup the entire $56,659, but will recoup a total of $11,761 based on the portion of expenditures that we determine were not appropriately allocated (e.g., 33 percent of playground tiles totaling $11,326) or were clearly outside the allowable programmatic expenditures (e.g., $435 for purchases related to graduation.) In certain instances, we cannot now commit to recoupment, but are pursuing with the provider whether additional records can be produced in support of such purchases as an air conditioner ($580) and 'Roto Rooter' services ($147). We further intend to conduct follow-up with the provider and Region regarding the cited transaction involving karate uniforms ($3,578) to determine whether, if the uniforms were actually purchased for the UPK program, the expenditure was made as result of a good faith misunderstanding of programmatic directives. With respect to the balance of the transactions identified . . . we will not seek recoupment.* [Italics in original.]

Auditor Comment: Again, we are pleased that DOE is planning to recoup $11,761 for some of the questionable expenditures we identified in the report and is in the process of investigating the legitimacy of some of the other questionable expenditures cited. With regards to the balance of the questionable expenses, DOE officials have stated that they will not seek recoupment because either they disagree with the bases for the findings or they feel that the costs involved in seeking recoupment far outweigh the benefit to be derived. Since DOE still has UPK contracts with these non-public schools, we do not believe it would be costly to recoup these funds.

DOE should recoup the $3,578 spent on karate uniforms. We know for a fact that the uniforms were purchased for the UPK program. We were informed by the Director of the South Shore Staten Island YMCA that karate was offered during the two and one-half hours in which the UPK Program was conducted. Whether or not the expenditure was due to a misunderstanding is not the issue. According to DOE officials, formal karate instruction is not to be conducted during the two and one-half hours offered by the UPK program. Accordingly, DOE should not pay for costs associated with this instruction.

13. Ensure that all expenditures incurred by the non-public schools are related to the UPK program and reasonable.

DOE Response: "DOE is continuously reviewing and upgrading our oversight efforts in every regard."

14. Ensure that non-public schools submit three written bids for those expenditures outlined in the *Expenditure Guide* that exceed $1,000. After reviewing the bids, DOE should approve the expenditure in writing.

DOE Response: "Although we will review with the identified providers the guidelines relative to the purchases in question, we will not seek recoupment for transactions (computer and classroom furniture expenditures) which, but for not having three bids, were made on behalf of the UPK program."

Auditor Comment: We questioned these expenditures not only because the non-public schools failed to obtain bids, but as DOE notes in a footnote in its response, also because they failed to obtain approval from the Region in advance, as required. According to the *Expenditure Guide,* these and other controls are not instituted merely to indicate that a purchase took place, but to also ensure that a purchase is reasonable, necessary, and directly related to the UPK program. The solicitation of bids for purchases exceeding $1,000 is intended to ensure that a purchase is conducted in a fair manner and is priced competitively. Regional pre-approval is intended to ensure that a purchase is related to the UPK program and necessary. DOE appears to have approved the questioned expenditures subsequent to their payment. Nevertheless, we urge DOE to ensure that all of its non-public schools comply in the future with the bidding requirements set forth in the *Expenditure Guide* and that DOE review and approve the related expenditures in advance and in writing.

Incorrect Classification of Expenditures

Of the $208,141 in OTPS expenditures that had supporting documentation, $13,812 (7 percent) was incorrectly classified on the End-of-Year Expenditure Forms by eight schools in our sample. For example, Smart Start Early Childhood Center spent $862 on mini scooters, swing carts, and tricycles, and classified this expenditure as "office/janitorial supplies" rather than as "instructional equipment." The Staten Island YMCA Nursery School spent $555 on a Canon laser fax machine and classified this expenditure as "miscellaneous" rather than as "office equipment." By not properly classifying expenditures, certain expenditures will be overstated and others will be understated, and the ability to properly plan future budgets can be compromised.

When we interviewed officials at the non-public schools to inquire how they report expenditures to DOE on the End-of-Year Expenditure Forms, some said that they often have a difficult time categorizing expenses since the forms do not list every type of expense incurred as part of the operations of a UPK program, which may have caused misclassifications. For example, one of the schools purchased book display stands, chairs, tables, and a couch and classified these purchases as "instructional equipment." Neither the End-of-Year Expenditure Form nor the DOE *Expenditure Guide* has a category for furnishings, the appropriate classification for these purchases. Further, some officials at the schools stated that the DOE *Expenditure Guide* does not provide a detailed description for each of the expenditure codes, which may have also caused the misclassifications. For example, the End-of-Year Expenditure Form lists "miscellaneous" as an expenditure code; however, the DOE *Expenditure Guide* has no description for this expenditure code.

Recommendations

DOE officials should:

15. Ensure that non-public schools accurately classify their expenditures on the End-of-Year Expenditure Forms.

DOE Response: "Our program of audit and desk reviews continues to provide field support both to the UPK program providers and Regional staff. The main effort in facilitating correct cost categorization by providers and review by DOE managers was rolled out recently in a new budget form that refines the cost categories . . . and requires electronic submission. The creation of that form was the first component of a project that encompasses electronic submission of mid- and end-of-year UPK program expenditure forms, all of which will align to provide consistent and easily comparable information."

16. Revise both the End-of-Year Expenditure Forms and the DOE *Expenditure Guide* to reflect all expenditures incurred in the operation of a UPK program. The expenditure codes listed in the DOE *Expenditure Guide* should be more descriptive and include examples of what types of purchases can be categorized under each specific code.

DOE Response: "*The DOE has already begun enhancing its UPK program oversight tools and processes.* [Italics in original.] Based on certain issues raised in this Report and questions posed by UPK program providers during the past two years of direct provider training sessions, the OAG already has revised the *Expenditure Guide* and *Frequently Asked Questions* to clarify certain of the cost category explanations and will continue to work with central DOE offices to review and improve it."

Questionable Bank Statement Activities Totaling $407,322

Our review of the bank statements for the period September 2003 through August 2005 for the nine schools in our sample identified questionable activities, such as cash withdrawals, checks issued, and wire transfers, totaling $407,322 by five of the schools. We reviewed the bank statements and noted any activities with unusually high dollar amounts and requested justification and supporting documentation from the schools to indicate that the activities were legitimate, necessary, and related to the UPK program.

For example, a review of the bank statements for Smart Start Early Childhood Center indicated that a $20,000 cash withdrawal had been made on February 22, 2005. The Administrative Director of the school stated that the cash withdrawal had been made by the Educational Director. She added that part of the cash withdrawal was to repay the Educational Director for a loan of $10,000 that she had made to the school on October 3, 2003, more than a year earlier. The other part of the cash withdrawal was to pay the building's rent that was owed for two months, totaling $10,000. It should be noted that since the Educational Director is also the owner of the building, the money she withdrew for rent was paid to herself.

To show that the withdrawal was indeed made by the Educational Director and then deposited in her own personal bank accounts, the Administrative Director provided us with the bank statements for the personal bank accounts of the Educational Director that reflected that $20,000 was deposited. However, we were not provided any other documentation, such as a loan agreement for $10,000 between DOE and the Educational Director or DOE written approval for this activity. We were also unable to determine whether the original $10,000 was even used for UPK expenditures. Moreover, we question the payment of rent made by a cash withdrawal rather than by a check, since according to the DOE *Expenditure Guide*, expenditures must be supported with invoices as well as with canceled checks. We further question the use of UPK funds to pay the entire cost of the rent with the other $10,000 since the building accommodates the Smart Start Early Childhood Center's other programs in addition to its UPK program. Without adequate supporting documentation, we could not determine whether the $20,000 cash withdrawal was legitimate, necessary, and related to the UPK program.

> ***DOE Response***: "It appears that the auditors' true concern is not whether this is a legitimate loan from the owner to the school, but that there was no written loan agreement or approval by the DOE for that loan. It further appears that the auditors are suggesting that when an owner lends money to the UPK program to meet operating expenses, that the owner enter into an agreement with the DOE, a suggestion that we cannot accept as the loan is between the owner and the school, not the owner and the DOE."
>
> ***Auditor Comment*:** There is no evidence to indicate that the $10,000 reportedly loaned to the school, and which was reimbursed from UPK funds, was in fact used for the UPK program. We expected to find, but did not find, written DOE approval in the school's files for this loan. Furthermore, the Contract Administration Officer for Region 7 stated that he was not aware of the loan, did not have any documentation for this transaction,

and agreed that there should have been either a loan agreement between DOE and the Educational Director or written DOE approval.

Of further concern was that the Educational Director withdrew $10,000 to pay herself rent owed for two months. According to the DOE *Expenditure Guide,* rental costs based on rental agreements between related parties are reimbursable, but DOE approval is necessary. Again, there was no DOE approval for this transaction. In its response, DOE fails to address whether it investigated the payment of rent between related parties; thus we do not know whether DOE has determined whether this withdrawal was legitimate, necessary, and related to the UPK program. There must be adequate disclosure to DOE of transactions between related parties because these transactions can be construed as a conflict of interest.

Table IV, following, summarizes the questionable bank statement activities for each of the four schools cited and the justifications for these activities offered by school officials.

Table IV

Summary of the Questionable Bank Statement Activities for Each of the Five Schools Cited And the Justifications Offered by School Officials

School	Date of Bank Statement Activity	Bank Statement Activity	Amount of Bank Statement Activity	Justification of Activity Offered by School Official
Smart Start Early Childhood Center	February 22, 2005	Cash Withdrawal	$20,000	The Administrative Director stated that half of the withdrawal was to repay a loan made by the Educational Director; and the other half of the withdrawal was to pay rent owed for two months.
Bryan's Educational Center*	November 20, 2003	Transfer	$15,000	The Accountant stated that this transfer was made into the Executive Director-owner's personal bank account to pay rent.
Our Saviour's Lutheran Preschool	January 4, 2005	Check Payable to Baylist & Geist	$16,110	The Administrator stated that the check was issued from the UPK bank account to pay general liability insurance for not only the UPK program but for the entire school and the associated church. The Administrator stated that the UPK bank account was reimbursed by the church for the funds borrowed. She provided

School	Date of Bank Statement Activity	Bank Statement Activity	Amount of Bank Statement Activity	Justification of Activity Offered by School Official
				us with a bank statement (and canceled check) that showed that a deposit was made, totaling $16,076, on October 3, 2005, nine months later.
Children's Playhouse*	October 2004 through July 2005	19 Checks Payable to Cash and Endorsed by Executive Director-owner 2 Checks Payable to Executive Director-owner	$54,506 $10,000	Unexplained
CYCLE Day Care Center	September 2004 through June 2005 (Account where UPK funds are initially deposited) November 2004 through April 2005* (Account where UPK funds are transferred into)	3 Checks Payable to CYCLE Day Care Center 4 Checks Payable to 2412 Realty 3 Cash Withdrawals 2 Wire Transfers to 2412 Realty Wire Transfer to Cycle Day Care Center 1 Check Payable to Cycle Day Care Center 2 Checks Payable to 2412 Realty	$41,000 $25,000 $126,806 $36,500 $40,000 $8,000 $14,400	The Business Manager stated that checks and wire transfers were made to Cycle Day Care Center's general operating account to cover costs such as electric, gas, and the lease for the copy machine. He also stated that the wire transfers and checks payable to 2412 Realty were issued to pay rent. It should be noted that the Educational Director and owner of the building in which the UPK program operates is the same person. The Business Manager further stated that the cash withdrawals were made to pay Automated Data Processing (ADP) for payroll expenses.
Total			**$407,322**	

* The bank account in which UPK funds are deposited and disbursed also includes other than UPK funds.

DOE Response: "In the case of Bryan's Educational Center, the audit team reports a $15,000 bank transfer from the UPK program account to the Director-owner's personal bank account. From the Report, we glean that the audit team was advised by the provider's accountant that the funds were used to meet rent expenses. Rather than . . .

reconciling the provider's rental costs with the total supportable expenditures in that cost category, the auditors paint the transaction 'questionable.' "

Auditor Comment: During the audit, we made repeated attempts to find out about the wire transfer totaling $15,000 from the Executive Director-owner and to obtain supporting documentation. Neither the non-public school nor DOE provided us any evidence to support the contention that the $15,000 was in fact for rent expenses. Accordingly, our finding remains.

It appears from our analysis that some of the schools are freely able to manipulate UPK funds without any DOE oversight or authorization. There was no adequate supporting documentation to provide an audit trail. Therefore, we cannot be assured that the bank activities we cite were legitimate, necessary, and related to the UPK program. Moreover, when we brought these matters to the attention of DOE officials, they were not aware of them.

Recommendations

DOE officials should:

17. Investigate the questionable bank activities totaling $407,322 that we cited, and if warranted, recoup the moneys.

DOE Response: "It is the DOE's position . . . that although we cannot agree with the audit procedures used to arrive at the findings or certain of the conclusions drawn, OAG staff will review the propriety of the cited transactions to the extent that they have not done so already."

18. Ensure that they review bank statements as part of their monitoring of the UPK program at the non-public schools to ensure that UPK funds are properly deposited and that there are no unusual withdrawals, checks issued, or transfers.

DOE Response: "The review of bank statements will not be incorporated into the monitoring procedures. . . .

"We question whether following DOE-issued checks into providers' bank accounts and following disbursements from the bank accounts furthers the Comptroller's overall audit objective that is, at least nominally, concerned with the DOE's internal controls over monitoring UPK payments and is an appropriate procedure to determine the validity and completeness of UPK program expenditures."

Auditor Comment: To ensure that City funds received by the non-public schools for the UPK program are properly deposited and are appropriately spent, it is necessary to review not only Cash Receipts and Disbursements Journals, checks, and invoices, but also bank statements. Relying solely on the books and records (Cash Receipts and

Disbursements Journals) created by the non-public schools does not provide enough audit evidence—especially since we found that not all of the non-public schools, such as Children's Playhouse, maintain adequate books and records. Since our review of the bank statements found questionable transactions totaling $407,322 for five of the schools in our sample, DOE officials should reconsider their position and include the review of bank statements as part of their monitoring.

19. Require the non-public schools to seek DOE written approval before making loans or cash withdrawals involving UPK funds.

DOE Response: "We have revised the *Expenditure Guide* accordingly."

Other Issues

In this section, we discuss our concerns regarding some of the schools.

Children's Playhouse Concerns

There were numerous internal control concerns that increase the potential for fraud. During our unannounced visits to the Children's Playhouse, we observed:

- No segregation of duties for the ordering, authorizing, paying, and recording of goods and services—the Executive Director-owner herself performed all of these functions;
- Record-keeping practices that were inadequate;
- Of the $346,528 in UPK funds received during Fiscal Year 2005, $93,525 (27 percent) was used for administrative expenses; of the total administrative expenses, 69 percent was spent solely on the Executive Director-owner's salary—DOE requires that administrative expenses are not to exceed 10 percent of total UPK Program contract costs;
- Numerous checks, totaling $64,506, were either made payable to Cash and endorsed by the Executive Director-owner or made payable to the Executive Director-owner;
- The required number of teachers were not present in two of the classrooms;
- The number of children we counted did not match the number of children marked present on the attendance records —in some cases it was above while in other cases it was below; and
- In one of the UPK classrooms, the number of three-year-old children exceeded the number of four-year-old children, a practice not allowed by DOE since the UPK program is designed for four-year-old children.

No Segregation of Duties

There was no segregation of duties for the ordering, authorizing, paying, and recording of goods and services. The Executive Director-owner herself performed all of these functions. Comptroller's Directive #1, "Internal Controls," states that "key duties and responsibilities need to be divided or segregated among different staff members to reduce the risk of error or fraud."

Inadequate Record-keeping Practices

Supporting documentation for expenditures was not maintained in an organized manner. It took Children's Playhouse almost three months to provide us with supporting documentation for the OTPS expenditures chosen in our sample, which impeded the audit's progress. The delay was mainly a result of the Executive Director-owner's having to attend to personal business out of state and to her being the only person who had access to the supporting documentation, since it was maintained at her house rather than at the school.

Moreover, since the Executive Director-owner did not use a Cash Disbursements Journal—as is required by DOE—to record UPK expenditures, she had difficulty in figuring out how she arrived at the dollar amounts for the OTPS expenditures she reported to DOE on the End-of-Year Expenditure Form. As a result, the Executive Director-owner was unsure what supporting documentation should be given to us for the OTPS expenditures we selected in our sample. For example, the Executive Director-owner initially provided us with supporting documentation for the OTPS expenditure code "minor maintenance and repairs" that included an invoice for painting services totaling $4,000. However, later on during the audit, the Executive Director-owner informed us that this invoice should have been part of the supporting documentation for the OTPS expenditure code "miscellaneous purchases" rather than "minor maintenance and repairs." Furthermore, we were never provided with the canceled check for this expenditure totaling $4,000 to verify that the payment was indeed for painting services.

These poor record-keeping practices call into question the accuracy of the financial records of Children's Playhouse and raise the possibility that errors, and even fraud, could occur and go undetected.

Sixty-Nine Percent of Total UPK Administrative Expenses Spent on Executive Director-Owner's Salary

Of the $346,528 in UPK funds received during Fiscal Year 2005, $93,525 (27 percent) was used for administrative expenses; of the total administrative expenses, 69 percent was spent solely on the Executive Director-owner's salary. The Executive Director-owner justified her salary by stating that she spent 24 hours per week performing administrative work for the UPK program. We question the reasonableness of her UPK salary since there is an Office Manager who also takes care of administrative work for the UPK program, and administrative costs are required by DOE not to exceed 10 percent of total UPK contract costs. Moreover, we were unable to verify the hours the Executive Director-owner stated to have worked on the UPK program since she does not record her hours worked. According to the DOE *Expenditure Guide*, schools must maintain time records of both administrative and non-administrative employees' activity in all programs. All hours of the employees' workday must be accounted for.

DOE Response: "Even without backup documentation, it is reasonable and logical to credit the Executive Director's representation that in her official capacity, and as owner of the school, she spent at a substantial portion of her time dealing directly with issues related to the UPK program.

"OAG staff have considerable experience auditing UPK and preschool special education programs, both of which limit administrative costs. They have determined that, based on the nature and size of the combined UPK and private programs, 87 percent of the duties outlined by the Executive Director are consistent with the duties generally performed by educational or programmatic staff and should be allocated as such. . . . We arrived at an administrative expense total of $37,149, which is 0.7 percent above the ten percent cap."

Auditor Comment: Again, DOE officials appear to take lightly the DOE *Expenditure Guide* that they themselves prepared and intended for schools to follow. According to the DOE *Expenditure Guide*, schools must maintain time records of both administrative and non-administrative employees' activity in all programs. All hours of the employees' workday must be accounted for. Without having time records, we question how DOE could know for a certainty how much time the Executive Director-owner actually spent on administrative and non-administrative activities. During the audit, we brought this matter to the attention of the DOE Deputy Auditor General, who agreed that without time records it would be hard to determine the percentage of time spent on administrative duties and stated that not having time records available "is the bigger problem." We agree that it is important that the non-public schools maintain time records to account for all hours worked for the UPK program, especially in cases where employees may be dividing their time between administrative and non-administrative duties or between the UPK program and other private non-UPK programs offered at the non-public schools.

As pointed out in the audit, we noted that there was no segregation of duties at Children's Playhouse because the functions of ordering, authorizing, paying, and recording of goods and services—which are all administrative functions—were performed by the Executive Director-owner. Therefore, we stand by our position that the Executive Director-owner spent a substantial portion of her time dealing with administrative issues.

Required Number of Teachers Not Present

The required number of teachers were not present in two of the classrooms. For example, in one of the classrooms (Class #303) the required number of teachers were not present. On two separate occasions, we observed only one person—an assistant teacher—heading this classroom that had eight children present during one of our visits and nine children present during a second visit. The Educational Director stated that the classroom had only one teacher due to its small size. Nevertheless, according to UPK rules, classes that have 18 or fewer children must have one certified head teacher in addition to one paraprofessional—either an assistant teacher or teacher's aide.

Discrepancy in Attendance Records

The number of children we counted during our visits did not match the number of children marked present on the attendance records for most of the classrooms—in some cases it was above while in other cases it was below. For example, during our visit to one of the classrooms (Class #302), 11 children were present. The head teacher for this classroom informed us that she normally teaches a classroom of 13 children, but said that two children were absent the day of our visit. As a result, we expected the attendance records to reflect 11 children present and 2 children absent. However, the attendance records reflected 15 children present and 3 children absent.

Three-year-old Children Improperly Included in One of the UPK Classrooms

Many three-year-old children were included in one of the UPK classrooms (Class #303), a practice not allowed by DOE since the UPK program is designed for four-year-old children. The Regional 7 Early Childhood Education Director stated that although not an encouraged practice, schools can combine the two age groups providing the number of three-year-olds in the classroom is at a minimum and does not exceed the number of four-year-olds. Our review of Class #303's attendance records for February and March 2006 (the months we conducted our unannounced visits to Children's Playhouse) revealed that for 32 out of 38 UPK instructional days during this period, the number of three-year-old children exceeded the number of four-year-old children, which should not have been allowed.

The above issues and irregularities indicate the possibility of fraud. At the exit conference, DOE officials stated that they are currently investigating the conditions cited at Children's Playhouse.

Recommendations

DOE officials should:

20. Investigate the conditions we cited at Children's Playhouse and, depending on the results of the investigation, consider terminating its UPK contract.

DOE Response: *"OAG and Regional program and operational staff have conducted site visits during which conditions outlined in the findings were addressed.* [Italics in original.]

"During the second week of the 2006/2007 school year, OAG, along with Regional operational and programmatic staff conducted an unannounced visit to Children's

Playhouse. Based on that visit and follow-up, we are satisfied that the conditions noted by the auditors have been remedied in that the student-to-teacher ratio is compliant; the attendance books were accurate; and the three and four year old students were in separate classrooms. OAG will include within its audit of Children's Playhouse a review of the staffing and attendance issues raised in the Report. A determination will be made whether disallowances should be taken."

21. Assist Children's Playhouse in developing a tighter internal control structure if DOE decides that the issues cited in our audit are a result of poor internal controls rather than intentional misappropriation of funds. DOE should ensure that all financial records are maintained accurately and in an organized manner, which should include ensuring that a Cash Disbursements Journal be maintained to record UPK expenditures.

DOE Response: "The OAG's audit of Children's Playhouse . . . is in progress. As of this date, however, the assigned OAG auditor has reviewed the Report's findings with the provider's accountant and has advised him of the resources available on the DOE website and the controls that must be in place to ensure compliance with UPK program fiscal requirements. Further, the accountant represents that he has undertaken responsibility for the Children's Playhouse bookkeeping functions that have been found wanting by the audit team. Recently, in response to the OAG's direction, the accountant prepared a revised general ledger, which we have received, that segregates expenditures related to the UPK program. The revised ledger is pending analysis by the OAG.

"After the OAG's site visit the Children's Playhouse Executive Director reported that she had opened a dual signatory checking account; and, by letter, we were advised that certain administrative duties, such as ordering and recording receipt of goods, had been delegated to the Educational Director and Office Manager."

Gan Day Care Center Incorrectly Used UPK Funds for Bonuses

Gan Day Care Center spent UPK funds incorrectly on bonuses, totaling $10,500, for six of its teachers. Documentation in the files showed that the Region 7 Contract Administration Officer questioned the bonuses and asked Gan Day Care Center officials to prepare a written justification for this expense. However, while DOE's files showed the justification from Gan Day Care Center, it did not show any evidence that DOE accepted the justification and therefore permitted the expense. We brought this matter to the attention of the Region 7 Contract Administration Officer who agreed that there was no written DOE approval permitting the bonus expense. According to the DOE *Expenditure Guide*, bonus compensation may be reimbursed only if budgeted and specifically approved in writing by the Region.

Recommendation

22. DOE should ensure that any bonuses budgeted by the non-public schools are approved in writing.

DOE Response: *"The DOE agrees that approvals for bonus payments from UPK funds must be in writing as stated in the Expenditure Guide."* (Italics in original.)

Lack of Written DOE Approval for Building Rental Agreements between Related Parties

There was lack of written DOE approval for building rental agreements between related parties. Specifically, the Directors for five (55 percent) of the nine schools in our sample were not only the Directors of the UPK programs but were also the owners of the buildings in which the UPK programs operated. Thus, the lessor and the lessee of the building rental agreements for these five schools were the same person. According to the DOE *Expenditure Guide*, rental costs based on a rental agreement between related parties are reimbursable. However, schools engaged in such transactions must request and receive approval in writing from the Region and provide appropriate documentation. DOE officials could not provide us any evidence of requests and written DOE approvals for the related-party rental agreements of the five schools. Related-party rental agreements could be construed as a conflict of interest, which is why they should be disclosed to and approved by DOE.

At the exit conference, DOE officials concurred with our findings regarding building rental agreements between related parties. As a result, the DOE *Expenditure Guide* was revised on October 13, 2006, to reflect the following, "Schools engaged in less-than-arms-length transactions must request and receive approval in writing from the Region, and provide appropriate documentation, which must include a lease agreement between the school and the property owner and a statement identifying to whom the rents will be paid. In no event will checks written to 'Cash' be acceptable as a record of rental payment."

Recommendation

23. DOE should ensure that non-public schools engaging in related-party rental agreements request and receive DOE approval in writing.

DOE Response: "*As recognized in the Report, the DOE agreed with the recommendation and revised the Expenditure Guide to provide clarification*. [Italics in original.] In addition, the OAG has circulated among providers for their response and has posted on its website a *UPK Provider Survey* that includes questions regarding this topic. The ROCs, working with the OAG and its audit partner, will follow-up with the UPK program providers to ensure compliance and select providers for audits and desk reviews to be performed by the OAG and audit firm."

Use of UPK Funds for Private Sanitation Services

Two of the nine schools in our sample used private sanitation services and paid the cost with UPK funds rather than having used the New York City Department of Sanitation (DOS) services free of charge. According to DOS procedures, if a non-profit organization or a private school is funded by a City agency, such as DOE, it is eligible for DOS services free of charge. To determine the prevalence of using UPK funds to pay for private sanitation services by schools, we interviewed officials of 40 randomly selected schools in Regions 6 and 7 that operated UPK programs as of April 2006. Three other schools, besides the two in our sample, also used UPK funds to pay for private sanitation services. Officials at some of these schools said they thought that they had to use private sanitation service because they were businesses and that they were not aware that they could use DOS services. DOE officials agreed that the schools should use UPK funds for children's services rather than for private sanitation services and stated that they would "share the auditors' information with the non-public schools."

At the exit conference, DOE officials concurred with our findings regarding private sanitation services. As a result, the DOE *Expenditure Guide* was revised on October 13, 2006, to state that "the costs associated with private carting cannot be charged to the UPK program inasmuch as the New York City Department of Sanitation offers it services free of charge to private schools that receive funding from the Department of Education."

Recommendation

24. DOE should investigate whether any non-public schools operating UPK programs have private sanitation services paid for by UPK funds, and if so, inform them that they are eligible for DOS service free of charge. Those non-public schools choosing to use private sanitation services should pay the cost from other than UPK funds.

DOE Response: *"As recognized in the Report, the DOE concurred with the finding and updated the Expenditure Guide accordingly.* [Italics in original.] Additionally, the DOE issued a written directive to UPK program providers notifying them of their eligibility to receive free services from the New York City Department of Sanitation and the procedures for obtaining these services."

THE NEW YORK CITY DEPARTMENT OF EDUCATION
JOEL I. KLEIN, *Chancellor*
Kathleen Grimm, Deputy Chancellor for Finance and Administration

January 29, 2007

Mr. John Graham
Deputy Comptroller
The City of New York
Office of the Comptroller
One Centre Street
New York, NY 10007-2341

Re: Draft Audit Report on Department of Education Controls over Universal Pre-Kindergarten Payments to Non-Public Schools in Regions 6 and 7 (MD05-072A)

Dear Mr. Graham:

This cover letter, with the attached detailed response of the New York City Department of Education ("DOE") to specific findings ("Response"), addresses the City of New York Office of the Comptroller's ("Comptroller") draft audit report dated December 8, 2006 and titled "Audit Report on Department of Education Controls over Universal Pre-Kindergarten Payments to Non-Public Schools in Regions 6 and 7." ("Report").

The audit was conducted over a period of two years and, in that period, covered a limited scope, to wit, only ten of more than 550 private agencies that were providing Universal Prekindergarten programs under contracts with the DOE during each of the audit years (Fiscal Years 2004 and 2005). It should be noted that the ten providers were selected from only two of the DOE's ten Regional Instructional Centers ("Regions"). And, those two Regional Instructional Centers are represented by a single Regional Operations Center ("ROC").

Managers representing the DOE's Regional and central offices met with the Comptroller's audit team at a formal exit conference on October 17, 2006 to discuss in detail preliminary audit findings that had been reported in draft. The audit work papers, which were made available to the DOE's Office of Auditor General ("OAG"), provided a basis for the OAG's further review of findings. Where disallowances based on missing or inadequate documentation were identified in the draft report, the OAG independently followed up with the cited UPK program providers. And, where that follow-up proved fruitful, OAG provided the audit team with additional records or explanations which, according to our analysis, should have significantly reduced the monetary findings. We are at a loss to explain why, despite our submission of relevant records in a timely fashion and cogent explanations of how educational programs such as UPK operate in the real world, the Report does not reflect a reduction of preliminary disallowances. Our calculations and comments regarding specific findings and recommendations are contained in the attached Response. We have reserved this writing for our more general observations.

Although the DOE has taken significant steps in the area of creating fiscal controls around its programmatic collaborations with private UPK program providers, we acknowledge that there is a place for constructive recommendations for improvement. Admittedly, as raised by the Report, changes in payment policy to providers to assist them with covering fixed expenses should have been in writing and applied consistently across Regions. We further thank the Comptroller for bringing to our attention opportunities, albeit limited, that had been overlooked for recoupment of funds paid to providers; certain ambiguities in the DOE's *Expenditure Guide for Programs Receiving UPK Funding* that the DOE has since clarified; and efficiencies that can be gained by offering providers the opportunity to use public sanitation services rather than private carting for trash removal. Nevertheless, as explained below and in greater detail in the attached Response, the relatively narrow scope of audit; disputable audit methodology; audit findings that invite the DOE to complete the audit tests started by the audit team; failure to consider the monitoring processes the DOE had in place during the audit period; and apparent zeal to attach dollars to relatively minor compliance findings, render many of the audit findings and the recommendations that flow from them only marginally relevant.

We make the following observations relative to the nature of the UPK program, the operational guidelines the DOE has promulgated for UPK program providers, and the tools developed by the DOE to measure compliance, to provide a context -- lacking in the Report - for understanding the DOE's relationships with UPK program providers.

Universal Prekindergarten, the product of legislation enacted in 1997 (New York State Education Law § 3602-e), is intended to provide curricula and activities appropriate to eligible four-year-olds and promote cognitive, linguistic, physical, cultural, emotional and social development through collaboration between the public school system and the child care community. As envisioned, the program was to fit within the pre-existing structure of providers of childcare and early childhood education, day care providers, early childhood programs, community based organizations, Head Start and nursery schools, family group day care and family day care that met the standards and requirements of the UPK program. As implemented by the DOE, powerful partnerships linking community-based organizations with the public schools have been created. Indeed, over the last eight years, the UPK program has increased the number of private UPK program partners from 125 in the start-up year to 556 and the number of children served from 5,336 to 31,369.

The financial support provided by New York State to operate UPK programs has remained fairly consistent over the last several years at an average of approximately $3,332 per student. Escalating facility and professional services costs throughout New York City have necessitated an additional tax levy contribution by the DOE averaging approximately $368 per student during the 2005-2006 school year to ensure availability of providers and program quality. In general, the State funds do not support administrative costs incurred by the DOE in overseeing the UPK program.

We are concerned that, despite its narrow focus on only ten UPK program providers in just two Regions, the Report invites conjecture about the DOE's controls over UPK programs overall. We also find troubling that the Report does not fairly represent the DOE's larger efforts to strike an appropriate balance between fostering workable partnerships within communities and fiscal and programmatic monitoring with available funds. The Report's failure to address the DOE's overall UPK program controls and monitoring efforts is an omission that is peculiar in light of the audit's stated objective "to determine whether DOE has adequate controls over UPK payments to non-public schools in Regions 6 & 7,"[1] but understandable in that the audit team conducted only the most superficial group interviews of managers of central offices that play key roles in providing guidance to and oversight for UPK program providers. And, while the managers brought to the auditors' attention during the exit conference and in conversations thereafter that the audit team had not obtained a complete picture of existing controls over UPK payments, the auditors did not seek to address this legitimate concern by conducting interviews before issuing the Report. Rather, they opted to change the word "interview" that had been used in the Preliminary report to describe the audit team's interaction with central DOE managers to the phrase "spoke to" in the instant Report -- hardly a substitute for actually doing what was necessary to offer the public a fair presentation of conditions.

Had appropriate inquiry been made, managers assigned to the DOE's Division of Contracts and Purchasing ("DCP"), OAG, and Office of Early Childhood Education would have had the opportunity to discuss with the audit team the robust program - outlined immediately below - that operates as a largely collaborative effort among the several responsible offices to provide support and oversight for UPK providers to *all* Regions[2] and extends to partnerships with other City and State agencies that are also responsible for general and special education preschool and early childhood programs.[3]

The DCP primarily is responsible for issuance of requests for proposals for UPK programs and development and approval of the resulting contracts between the Regions and private UPK program providers. DCP staff's availability to interpret contract language and assist with

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[1] By letter dated August 5, 2004, the Comptroller announced an audit the stated objective of which was to "determine whether the Department of Education has adequate internal controls over payments to non-public schools for the Universal Pre-Kindergarten Program." Thereafter, a survey that touched on all Regions was conducted. Post that review, the audit object was narrowed to focus only on controls relative to Regions 6 & 7.

[2] By way of example, recently, DCP and OAG managers' collaboration resulted in an upgraded budget form that enables UPK program providers to complete and submit their budgets electronically; the new budget forms will be tied to mid- and end-year financial disclosure reports to facilitate comparisons between budgeted and actual expenditures on behalf of the UPK programs.

[3] One example of an interagency project that we are proud to have joined is the task force that has been created between central DOE managers and the New York City Agency for Children's Services ("ACS") that primarily is concerned with creating processes and tools for fiscal oversight of private providers with multiple funding streams. Additionally, the DOE's Office of Auditor General, for many years now, has partnered with the New York State Education Department's Vocational and Educational Services for Individuals with Disabilities and ACS to conduct audits and real-time field reviews of private schools offering preschool special education, early intervention and other City sponsored programs in addition to UPK.

terminating contracts as appropriate supports the Regions' and ROCs' contract management responsibilities. With that close connection to the field and DOE-wide perspective, the DCP's assigned UPK subject-matter specialist, counsel and administrator are well positioned to effect timely changes to contract language and oversight processes as necessary to improve delivery of services to students. DCP's assistance to UPK Regional and central managers and other central offices further extends to the maintenance of a website that providers are directed to access for programmatic and operational guidance.

The UPK programmatic training and guidance provided by Office of Early Childhood Education supports the clear and direct connection between an instructionally rich UPK program and sound fiscal practices. While the cost per child in a private UPK program allows for the operation of an instructional program that meets the high standards set by the DOE, it does not leave room for diversion of funds. And so, when Regional early childhood specialists conduct private UPK program site visits, they bring with them the expertise gained through experience and training that allows them to take the measure of the program and report issues that may have at their root mismanagement of UPK funds.

Over the past several years the OAG's contribution to the DOE's centralized UPK monitoring structure has included UPK provider field reviews and audits conducted at the request of Regions and of its own initiative; assisting with UPK program provider training; and developing an on-line *Expenditure Guide for Programs Receiving UPK Funds*, *Frequently Asked Questions*, and UPK field work programs. OAG, additionally, has undertaken responsibility for administering contracts between the DOE and private audit firms engaged for the purpose of supporting the Regions' responsibility for monitoring the UPK program. In prior years, including those covered by the Report, the firms provided audit and provider training services directly to the Regions; for the past two years, the OAG has managed the entire engagement.

Between August 5, 2004, when the audit was announced, and December 8, 2006, the date of the Report, DOE managers were available, but were not asked to define their largely successful efforts to create an overarching structure of controls under which the Regions and their private partners implement collaborative UPK programs. We thus consider glib the auditors' global recommendation that we "develop and implement written fiscal review procedures for the ROCs to follow and monitor when assessing the UPK program." Our sustained efforts directed at programmatic and fiscal training for UPK program providers and Regional managers; updating published expenditure guidelines and responses to questions that derive from training and fieldwork; revising contracts; and enhancing financial reporting tools should more than meet the auditors' monitoring standards.

We suggest that had time been spent actually interviewing knowledgeable DOE managers, a more accurate picture of the DOE's internal controls would have emerged. Having recognized independently of the instant audit that improvements in the monitoring process can and should be made, DOE managers representing responsible central and Regional operations have been engaged in ongoing analysis of the process that has led to appropriate changes and enhancements, including an additional contract and fiscal compliance training program aimed at both Regional managers and providers.

We suggest, further, that inasmuch as the DOE welcomes the City Comptroller's Office as both a partner and as an outside, independent set of eyes and ears to identify weaknesses in internal controls and other conditions or deficiencies requiring correction, future audit endeavors involve a more collaborative approach between the Comptroller's audit mangers and DOE managers to ensure that audit findings are accurate and up-to-date and that recommendations are timely, sound and useful.

Sincerely,

Kathleen Grimm

Deputy Chancellor for Finance and Administration

KG:nf

Attachments

C: Joel I. Klein
Michael Best
Brian Fleischer
David Ross
Eleanor Greig-Ukoli
Sandy Brawer
Espi Semetis
Fred Mavaro
Maxine Needle
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Response to Draft Audit Report on Department of Education Controls over Universal Pre-Kindergarten Payments to Non-Public Schools in Regions 6 and 7 (MD05-072A)

This, with the attached cover letter, addresses the City of New York Office of the Comptroller's ("Comptroller") draft audit report titled "Audit Report on Department of Education ["DOE"] Controls over Universal Pre-Kindergarten ["UPK"] Payments to Non-Public Schools in Regions 6 and 7." ("Report").

As a preliminary observation, during the exit conference and now, in this response, we raise whether the testing methodology employed by the auditors furthers the stated audit objective, to wit, "to determine whether DOE has adequate controls over UPK payments to non-public schools in Regions 6 & 7." Specifically, we question whether following DOE-issued checks into providers' bank accounts and following disbursements from the bank accounts furthers the Comptroller's overall audit objective that is, at least nominally, concerned with the DOE's internal controls over monitoring UPK payments and is an appropriate procedure to determine the validity and completeness of UPK program expenditures. This is particularly a concern insofar as Central DOE managers responsible for guiding and overseeing the UPK program managers report that they were not interviewed by the audit team during the two and one-half years between the notice of audit and the issuance of the Report to determine the manner and extent to which the responsibility centers collaborate in the DOE's UPK program monitoring efforts.

Having been charged with responding to the audit as it was conducted, the DOE's Office of Auditor General ("OAG") staff, directed by an auditor with experience conducting UPK program provider audits, met with the Comptroller's audit team, reviewed the team's work papers and, as appropriate, sought – and received from providers and Central and Regional DOE managers - records and other explanatory documentation identified in the Preliminary Audit Findings as missing or deficient. The information thus gathered was turned over to the audit team with the understanding that OAG managers were available to clarify how the records impacted the findings. Clarification was not sought before the Report was issued.

The following addresses the Report's key findings with their accompanying recommendation(s).

Finding: *DOE has not developed formal fiscal review procedures for the ROCs to follow when monitoring UPK payments.* (Report, pp. 12-14). Based on the detail contained within the finding, two recommendations were made: 1) The "DOE should develop and implement written fiscal review procedures for the ROCs to follow when monitoring and assessing the UPK program. These procedures should include the steps that the ROCs will take to ensure that non-public schools comply with their contracts and the DOE *Expenditure Guide*. For example, DOE should ensure that the ROCs periodically visit the non-public schools and review the financial records." 2) "Develop and implement written procedures for the schools to follow and/or rewrite its contracts." (Report Recommendations 1 and 2, respectively).

Response: *The DOE has established a viable, adaptive program of oversight and monitoring.*

Notwithstanding that the auditors bypassed the opportunity to thoroughly interview central DOE managers about the UPK program, they apparently reviewed at least some of the UPK program guidance available on the website maintained by the DOE's Division of Contracts. However, that appropriate connections were not made between the documents on the website and their intended use is clear to us from the statement that "neither the contract, nor the outline of the key provisions of the contract, nor the DOE *Expenditure Guide* details the steps that the ROCs should follow in assessing whether the schools are in fact maintaining adequate books . . .." (Report, p. 13).

None of the documents cited was intended by the DOE to serve as a step-by-step guide to the *Regional Operations Centers ("ROC")* for monitoring the program. Instead, and more logically, the documents are intended to serve as a statement of the *providers'* obligations (contract) and as guidance in operating the UPK program (contract and *Expenditure Guide for Programs Receiving UPK Funding*, hereinafter referred to as "*Expenditure Guide*"). The *ROCs* are expected to be thoroughly familiar with the contracts and fiscal guidelines and to work with the OAG and the audit firms retained by the OAG to review providers' fiscal and key contract provision compliance.

As a further point, we offer the observation that UPK is not the only instructional program implemented by the DOE in collaboration with private providers. In fact, the DOE has a long history of serving preschool special education students in private schools, many of which now offer UPK. Relevant to our UPK discussion is that the special education programs function under the terms of contracts with the DOE that are similar in scope to the UPK contracts and that their fiscal activities are bound by guidelines contained in the New York State Education Department's *Reimbursable Cost Manual* - the prototype for the *Expenditure Guide*. There has never been a suggestion that either the special education contract or the *Reimbursable Cost Manual* was intended to serve as a "how to" guide for monitoring the program either by the State Education Department or the DOE.

As to the recommendation that the DOE develop and implement written review procedures for the ROCs, our response is that the DOE, through the OAG and private audit firms engaged specifically for this purpose, have trained Regional programmatic and operational staff and made available to them in hardcopy and on the website a work plan for auditing and conducting contract compliance reviews of UPK program providers. Further, the Regions have participated in training offered to providers in meeting fiscal responsibilities and have received auditors' assistance in analyzing expenditure reports submitted by providers. Further, during this current school year, the UPK monitoring program was expanded to include provider contract and fiscal compliance surveys and more drilled-down training opportunities for providers that required additional assistance.

The DOE considers "implemented" the recommendation that the DOE "develop and implement written procedures for the schools to follow." Providers already have been directed to comply with the *Expenditure Guide;* have been given further instructive guidance in the published *Frequently Asked Questions;* and have been provided with training materials and written self-assessments in the form of surveys.

The further recommendation that we consider rewriting our UPK contracts, presumably for the purpose of offering "written procedures for the schools to follow" is so vague as to thwart practical implementation. Our response is that the UPK contracts, which have been reviewed and approved by the New York City Law Department and registered by the Comptroller, provide a clear statement of obligations, among which are to expend UPK funds exclusively for the benefit of the program, maintain appropriate books and records, and make those records available for audit or other inspection.

Finding: *DOE Overpaid [Six] Schools $141,055 in UPK Funds.* (Report, pp. 14-18). The finding derives from a purely mathematical computation: the number of students enrolled in each of the ten UPK programs in the sample in Fiscal Year 2004/2005[1] multiplied by the contracted cost per student. The product of that operation was deducted from the actual payment made by the DOE to the provider. The finding is followed by three recommendations (pp. 17 & 18): DOE officials should 1) "Ensure that they adhere to the provisions of the UPK contracts with non-public schools when determining payments. If the method for determining payments changes, then the contracts need to be amended. In addition, there should be written guidelines governing the calculation of the payments. 2) Recoup the UPK overpayments made during Fiscal Year 2005 to the six schools in our sample. 3) Make adjustments for the incorrect payments made as of March 2006 to CYCLE Day Care Center and Smart Start Early Childhood Center based on the new contract payment term for the period July 1, 2005 through June 30, 2008." (Report Recommendations 3, 4 and 5, respectively).

Response: *The DOE did not overpay UPK program providers $141,055. The DOE's payments to the audited UPK providers were consistent with a policy in effect at the time, but for one case of an overpayment of $17,250, which will be recouped by the close of School Year 2006/2007.*

Each provider's UPK contract has an associated total contract cost that is the product of the negotiated cost per student multiplied by the estimated maximum number of students that will be enrolled. Then, within that context, the DOE makes a payment in early September based on twenty percent of the estimated total contract cost, a process borne of the recognition that private schools, in much the same way as our public schools, must "gear-up" for the new school year by engaging staff, purchasing instructional supplies, materials and equipment and otherwise meeting administrative and facilities costs.

Similarly, we recognize that certain costs in operating the educational program are "fixed" even in cases where the provider does not meet the student enrollment estimate.

[1] Enrollment was determined by number of students on register on the last school day of the third week in November 2004 or the last day of October whichever was greater.

Thus, for example, the salary of a teacher who was hired to teach 18 students generally remains the same even if only 16 students enroll in the class.

An understanding of the policy that is the subject of the Report's finding rests on an appreciation of the role played by private UPK program providers and the consequences attendant upon the losing their services. Clearly, in enacting the UPK law, the State legislature recognized the importance of early education and the need to develop programs accessible to and operating within the community. In New York City, where many public schools are already operating in excess of their building capacity, there was no question that the DOE would enter into a significant number of partnerships with eligible private entities in order to meet the demand for seats. Today, still, in many of our communities, the demand for UPK seats exceeds the number of those available. The loss of UPK program providers therefore involves far more than a risk of having to return unspent UPK funds to the State. Clearly, and far more seriously, the loss impacts our ability to meet the significant educational needs of preschool-age students.[2]

In order to maintain availability of providers and the quality of the UPK program, the DOE determined in FY 2004/2005 that the best interests of the students were served by allowing a margin of ten percent above the number of students on register. Although managers explained the salutary purpose of the ten percent margin and the Division of Contracts and Purchasing ("DCP") provided a letter to the audit team supporting the policy, the response from the auditors was that absent a formal contemporaneous writing stating otherwise, they would hold the DOE to the strict terms of the contract in effect at the time, particularly since, as the Report notes, the policy was not applied consistently across the Regions or even within the Region under review.

If the question were whether it would have been better to formalize and consistently apply the margin policy at the time it was effected, the DOE would answer "yes." However, if the question posed, instead, were whether the DOE violated the law of contracts or its obligations to safeguard public funds, we stand on the action that was taken. Since the mandate from the State was to operate programs with our community partners to benefit four year olds and that partnership required taking cognizance of programmatic needs, which included the ability to meet fixed operating expenses, we believe that the ten percent margin policy, even as imperfectly applied, reflects a balance between those needs and our obligation to protect public funds.

Further, in response the auditors' contention that "if the DOE were to formally institute this [ten percent] allowance, it could have the unintended effect of discouraging schools

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[2] There is an additional educational aspect to the UPK program that is relevant to the discussion. Preschool-age children with disabilities, consistent with federal and State legal mandates, are often recommended for placement within private schools operating "integrated" classes, to wit, classes generally staffed with two teachers and at least one aide and comprised of students with Individualized Educational Plans (special education students) and typically developing students. The latter students may be those attending the class under the auspices of UPK. Inasmuch as it is well established that integrated classes benefit students in each educational component, we encourage providers that are already State approved special education providers to operate UPK programs as well. And, certainly, we wish to retain those that currently operate programs that support the educational needs of all preschool students for whose educational programs we are responsible.

from meeting the estimated target number, since they would be paid the same amount if they fell as much as 10 percent below the target." On this point, as well as on the Report's recommendation that we codify our margin policy, the audit team is aware that for providers operating under contracts that began in School Year 2004/2005 and later, provision had been made for assistance in meeting fixed UPK program costs. Specifically, the contracts allow for payments to be made on margins based on a schedule pegged to the percentage of under-enrollment. Under the terms of the contracts, the greater the percentage of variance between the estimated and actual enrollment, the greater the reduction in the percentage of margin. This provides an incentive for maintaining high enrollment numbers while allowing providers to maintain the quality of their UPK programs. To further reinforce the incentives for providers to meet their target enrollment numbers, the DOE will issue a written statement to the Regions clarifying a policy that where a provider does not meet its enrollment estimate, the next year the starting point for setting the estimated number of available UPK seats should be reduced to reflect the prior year's shortfall.[3]

With regard to the recommendation that we seek restitution of funds purportedly overpaid to six of the audited providers, we are steadfast in our position that the payment policy was appropriate as applied and have recomputed the auditors' numbers using the ten percent margin for each of the six schools. Based on our calculations, we reject the Report's recommendation for recoupment in large part. In five cases the number of students for whom payment was made fell within the ten percent range. However, we identified an overpayment in the case of CYCLE Day Care in the amount of $17,250. The overpayment will be recouped by the close of School Year 2006/2007. (*Attachment A*).

The final recommendation attached to the finding implicates the contractual schedule of payment adjustments for providers that did not meet estimated enrollment numbers and suggests that the DOE make adjustments for "incorrect payments" to two schools in School Year 2005/2006 as of March 2006. In the case of CYCLE Day Care, the auditors calculated an overpayment of $2,100; Smart Start Early Childhood Center, according to the auditors, was underpaid $593.

OAG performed its own calculations based on payments made by the end of the school year and official enrollment data[4] for each school. It was determined that CYCLE Day Care received payments for exactly the 81 students on register as of the official close of register date (November 18, 2005); no adjustments were required; and no overpayment

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[3] Of course, in accordance with the objective of serving children, if Regional managers are aware of circumstances that would provide a basis for increasing the enrollment estimate, Central DOE would have them exercise that good judgment. For example, Schools A and B each operate a UPK program in the same neighborhood and both fall short of enrollment estimates in the base year. If School B eliminates its UPK program, it would be beneficial to the community to allow School A to increase its available seats in the new year to accommodate students who might otherwise have attended School B.

[4] In School Year 2005/2006, enrollment was determined by number of students on register on November 18, 2005. The DOE's student attendance tracking system (ATS) was referenced to determine the number of students on the official register on that date.

was made by the DOE. OAG's calculations with respect to Smart Start Early Childhood Center identified an underpayment in the amount of $1,185.

Finding: *DOE Failed to Recoup $82,321 in Unspent UPK Funds.* (Report, pp. 18-19). The auditors base the finding on a comparison between information submitted by the audited schools on their Fiscal Year 2004/2005 End-of-Year Expenditure Forms and total payments made to them by the DOE in that fiscal year (Staten Island YMCA: $22,631; Smart Start Daycare Center: $11,661; Gan Day Care Center: $48,029). In the three instances, the auditors determined that payments exceeded expenditures and recommended that the DOE 1) "Examine the revised End-of-Year Expenditure Forms submitted by Smart Start Early Childhood Center and Gan Day Care Center and verify that the reported expenditures are proper and adequately supported." 2) "After examination, recoup any remaining unspent UPK funds for the schools cited." (Report Recommendations 6 and 7, respectively).

Response: *The DOE, for reasons stated below, disputes the finding in large part and calculates unspent UPK funds in the total sum of $22,706 (Staten Island YMCA: $22,631; Gan Day Care Center: $75).*

Preliminarily, the DOE acknowledges that the Staten Island YMCA in fact reported unexpended funds of $22,631. Those funds have been recouped in full as of this date. As explained below, but for that sum, and a $75 unexpended balance attributable to Gan Day Care Center, we dispute the finding. (*Attachment B*).

The Report reflects that after the exit conference the audit team received from the DOE revised End-of-Year Expenditure Reports for Smart Start Early Childhood Center and Gan Day Care Center. We infer from the Report that the quarrel with them is that the Smart Start Early Childhood Center revised report had not been turned over to the auditors during fieldwork, was not dated, and included "in-kind contributions" that had not been identified on the original report; and, that the Gan Day Care Center revised report was not accompanied with documentation demonstrating that the revised expenditures were valid.

During the audit exit conference the Region 7 representative advised the audit team that the Region was in possession of a "revised" End-of-Year Expenditure Report that had been submitted by Smart Start Early Childhood Center. Thereafter, a hardcopy of the revised End-of-Year Expenditure Report, signed by the school's Administrative Director, and dated August 20, 2005, was turned over to the OAG. (*Attachment C*). For reasons having to do with the difficulty of making a legible copy that could be faxed to the auditors, the OAG manager asked for and received from the Region a clean electronic version of the revised End-of-Year Expenditure Report that had also been submitted to the Region by the school in August 2005. Since that version of the expenditure report had been submitted electronically, it did not bear a dated signature. However, that was the version submitted electronically to the auditors by the OAG manager, and we apologize for any confusion that might have caused.

The matter of the purportedly undated Smart Start Early Childhood Center revised End-of-Year Expenditure Report having been resolved, we address an issue that surfaced from our comparison of two findings within the Report relative to Smart Start Early Childhood Center.

Specifically, within the finding that relied on a calculation of enrolled students *multiplied* by the contracted cost per student and a comparison of that product to the funds received by the provider, the auditors reported an "overpayment" to Smart Start Early Childhood Center of $27,328. In disputing the finding and the recommendation that we recoup the "overpaid" funds, we applied the margin policy in effect at the time and reiterate our position that the total payment of $316,224 to Smart Start Early Childhood Center was appropriate. (Pages 3 -5, above).

Based on our understanding of what the auditors are suggesting in the finding regarding "unspent UPK funds" we are again being asked to recoup funds that include those earmarked by the auditors elsewhere in their Report as an "overpayment." In addition to questioning the overlapping recoupment direction - which we suggest should have been reported more transparently - and for the reasons we have discussed already, we maintain that there is no basis for seeking recoupment from Smart Start Early Childhood Center. Our position rests on our having credited the expenditures disclosed in the revised End-of-Year Expenditure Report, a position that does not rely on the in-kind-contributions questioned by the auditors.

The Gan Day Care Center End-of-Year Expenditure Form, as originally submitted, reported expenditures on a cash, rather than an accrual basis as required by the DOE. That misunderstanding substantially impacted the amount of expenses reported in the staff salary cost category, since Gan Day Care Center was permitted to - and did - pay its staff over a twelve-month period despite that the UPK program operated over ten months.

Inasmuch as the original Gan Day Care Center End-of-Year Expenditure Form (*Attachment D*) bore a notation that the salary had been divided into twelve month payments and the auditors had been given that Form, we suggest that the audit team should have included within its fieldwork protocols a test of the salary cost category that would have facilitated an accurate assessment of expenditures. Moreover, the audit team simply could have compared the Gan Day Care Center's budget, which identified annualized salaries, and determined from those numbers and the twelve-month salary notation that the representations concerning salary expenditures were credible.

The OAG, using the accrual basis method, determined that the twelve-month payments correctly represented the amount that should have been reported as salary expense. These calculations however have identified an unexpended balance of $75, which we have recouped.

Finding: *<u>OTPS Expenditure Issues</u>. Expenditures Totaling $97,586 Lacked Adequate Supporting Documentation.* (Report, pp. 19-21). The Report recommends that the DOE 1) "Recoup the $97,586 identified in this audit as expenditures that are not supported by the records of the non-public schools we cited." 2) "Ensure that non-public schools maintain adequate supporting documentation for all expenditures." 3) "Ensure that all consulting services are approved by the Region prior to their use by the non-public schools." 4) "Institute procedures to require the review of supporting documentation by DOE staff." (Report Recommendations 8, 9, 10 and 11, respectively).

Response: *The DOE agrees that, to date, three providers have not submitted to the audit team or the OAG documentation adequately supporting total expenditures of $36,411; in those cases, the OAG will either pursue the documentation or seek recoupment, as appropriate.*[5] *However, it is the DOE's position that the paucity of information contained in the Report relative to the bases for the balance of the "disallowed" transactions renders a reasoned and directed response virtually impossible.*

We are particularly stymied in this regard insofar as the Report, providing little in the way of usable detail, dismisses documentation submitted to the audit team by the DOE, and offer as reasons that they already had the records and that the documentation generally failed to meet one or more of the criteria that appears in a bulleted list on page 21 of the Report.

The Report does not provide a means by which we can confirm whether the records we submitted to the audit team were, indeed, duplicates of records already in the auditors' possession. What we can say in that regard is that post-exit conference, OAG using the audit team's work papers and additional information provided during meetings with the auditors, performed an analysis of the items that comprised the total disallowance. But for cases where the dollar value of the finding suggested against devoting resources to recovering documents in the limited time available, OAG staff reached out to the audited providers and was fairly successful in obtaining additional records. The OAG submitted those records to the auditors. We are first learning that the records characterized in the work papers as missing, and that were subsequently submitted to the auditors, are deemed by them to be duplicates.

Further, although we are not in a position to address to specific transactions, we can offer general observations about the auditors' interpretation of the DOE's guidelines and approach to conditions that are not on all fours within the guidelines. We believe that within the finding's monetary "disallowance" are numerous situations involving consulting services where the providers presented to the audit team satisfactory documentation of service and expense, but were unable to produce written approvals by the Region and/or bids. The audit team deemed each "flaw" fatal to the transaction, referencing the section in the UPK *Expenditure Guide* that speaks to bids and the Region's pre-approval for consulting services, and refusing to accept the OAG and Region's position that if consulting services are identified in the budget, and that budget is approved, the approval satisfies the *Expenditure Guide.* This is offered as an example. Basically, what the DOE is having the greatest difficulty with is the auditors' lack of understanding of the UPK program overall and the application of a form over substance.

[5] The $36,411 is comprised of expenditures by CYCLE Day Care ($12,510), Our Savior's Lutheran Preschool ($6,710), and Staten Island YMCA ($17,191).

We posed the question internally whether, if a tested transaction meets the cost principle of "reasonable and necessary" and was supported, the DOE would be seeking recoupment from the providers simply because approval had not been apparent from a separate writing or bids were not sought. We have concluded that we would not. Despite the audit teams' apparent zeal to attach dollars to findings, our position is that some failures to adhere to *guidelines* requires written notice to the provider, training and an opportunity to conform; we attempt to exercise reasoned judgment before identifying a disallowance where the transaction is otherwise supported and would, but for a missing item, such as a pre-approval letter, be acceptable. It is unfortunate that the audit team did not take a similar approach.

Equity demands that a finding as serious as the one raised here be presented in a manner that informs the auditee and the public as to its underpinnings and that provides a framework for response. The DOE offers the following, not as a response to the finding - since we have no way to address that finding in full - but as a means by which a response may be facilitated. We propose that before issuing a final report the audit team meet with OAG staff to explain in detail the reasons for disallowing each of the items that comprise the finding.

With respect to the recommendations that derive from the finding, for the reasons stated, we cannot accept the recoupment recommendation as written. As to the remaining recommendations that are directed at controls, our response is that the DOE already has a substantial program of controls, which we continually review and upgrade. Although we have discussed oversight activities elsewhere in this response it is worth noting here that the audit firm that is working with the OAG this school year is performing UPK program audits and desk reviews in addition to training Regional managers and UPK program providers and assisting with Regional managers' mid- and end-year expenditure reports review.

Finding: *OTPS Expenditure Issues. Questionable Expenditures.* (Report, pp. 21-22). Citing three examples of "questionable expenditures" totaling $38,479, the Report recommends that the DOE 1) "Recoup the $56,659 identified in the audit as expenditures that were either not related to the UPK program or were not reasonable for the non-public schools we cited." 2) "Ensure that all expenditures incurred by the non-public schools are related to the UPK program and reasonable." 3) "Ensure that non-public schools submit three written bids for those expenditures outlined in the *Expenditure Guide* that exceed $1,000. After reviewing the bids, DOE should approve the expenditure in writing." (Report Recommendations 12, 13 and 14, respectively).

Response: *The DOE cannot agree with the recommendation that we recoup the entire $56,659, but will recoup a total of $11,761 based on the portion of expenditures that we determine were not appropriately allocated (e.g.,* 33 percent *of playground tiles totaling $11,326) or were clearly outside the allowable programmatic expenditures (e.g., $435 for purchases related to graduation). In certain instances, we cannot now commit to recoupment, but are pursuing with the provider whether additional records can be produced in support of such purchases as an air conditioner ($580) and "Roto Rooter" services ($147). We further intend to conduct follow-up with the provider and Region* *regarding the cited transaction involving karate uniforms ($3,578) to determine whether, if the uniforms were actually purchased for the UPK program, the expenditure was made as result of a good faith misunderstanding of programmatic directives. With respect to the balance of the transactions identified in the auditors' work papers, as we do not agree with the bases for the "disallowances," we will not seek recoupment.* The reasons follow.

This is not the first time between the Preliminary and Draft Report stages of the audit that DOE managers advised the auditors that certain items included within the total disallowance legitimately could be viewed as having been purchased for the benefit of the UPK program and that, in supplanting the judgment of programmatic experts, the auditors were demonstrating a lack of understanding of the program they had set out to audit.

Notwithstanding our efforts, no note appears to have been taken of our informed position. And so again, in this response, we state that we will not ask providers to return $300 for children's magazines purchased from Scholastic and Weekly Reader;[6] $30 for alphabet cookies; $21 for Thanksgiving food; $140 for a popcorn maker; or other such items – totaling $111 in our calculations – that we have determined fall within the category of instructional tools or security clearance costs properly charged to the UPK program ($50 for fingerprinting the secretary working at the UPK site) or are simply so immaterial in value ($42 for graduation items and $19 for fish food, for example[7]) that the administrative costs involved seeking recoupment far outweigh the benefit to be derived. Similarly, although we will review with the identified providers the guidelines relative to the purchases in question, we will not seek recoupment for transactions (computer and classroom furniture expenditures) which, but for not having three bids, were made on behalf of the UPK program.[8]

In summary, our response to the recommendations attached to the finding is that 1) We intend to recoup funds to the extent that we agree with the bases for the findings; 2) and

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[6] The auditors apparently opting for a hyper-technical interpretation, declined to accept DOE managers' explanation that the instruction in the *Expenditure Guide* that UPK funds not be spent on "periodicals" did not apply to instructional materials simply because they were delivered at fixed intervals, to wit, periodically. Consequently, in consultation with the programmatic office, the OAG clarified the instruction so that it now reads: "Costs of subscriptions to periodicals and membership in civic, business, technical, and professional organizations and coalitions (dues) are not reimbursable. However, since children's magazines add an additional literacy dimension to the program and especially to the parent involvement component, UPK funds can be used to subscribe to magazines that are written for children and magazines that are written for parents about children."

[7] The "questionable" $19 fish food transaction bubbled up when, according to the auditors, one of the audited UPK program provider's staff told the auditors that she did not recall seeing "pets" in the classroom. As a test of logic, we ask the question, which may very well be rhetorical: Is the public best served by directing a DOE Regional manager to pursue with the UPK program provider whether, within the last two and one-half years, a fish tank and their occupants were actually serving as pets in a UPK classroom and, thus, whether the food necessary to maintain the fish was purchased for the benefit of the UPK program?

[8] The disallowance in the cases identified by the auditors also involves the matter of "pre-approval" of the expenditure by the Region. In other sections of this response we took the position that the pre-approval could be intuited from the approval of a budget that identified the expenses in question.

3) As detailed elsewhere in this Response, the DOE is continuously reviewing and upgrading our oversight efforts in every regard.

Finding: *OTPS Expenditure Issues. Incorrect Classification of Expenditures.* (Report, pp. 22-23). With reference to the End-of-Year Expenditure Form, the auditors identified that seven percent ($13,812) of expenditures that had supporting documentation were misclassified.[9] The two examples cited are an $862 purchase of instructional equipment that had been entered as "office/janitorial supplies" and a $555 purchase of a fax machine entered as a "miscellaneous" expense. The Report recommends that the DOE 1) "Ensure that non-public schools accurately classify their expenditures on the End-of-Year Expenditure Forms." 2) "Revise both the End-of-Year Expenditure Forms and the DOE *Expenditure Guide* to reflect all expenditures incurred in the operation of a UPK program. The expenditure codes listed in the DOE *Expenditure Guide* should be more descriptive and include examples of what types of purchases can be categorized under each specific code." (Report Recommendations 15 and 16, respectively).

Response: *The DOE has already begun enhancing its UPK program oversight tools and processes.* Based on certain issues raised in this Report and questions posed by UPK program providers during the past two years of direct provider training sessions, the OAG already has revised the *Expenditure Guide* and *Frequently Asked Questions* to clarify certain of the cost category explanations and will continue to work with central DOE offices to review and improve it.

Further, our program of audit and desk reviews continues to provide field support both to the UPK program providers and Regional staff. The main effort in facilitating correct cost categorization by providers and review by DOE managers was rolled out recently in a new budget form that refines the cost categories, drives to allocated costs, and requires electronic submission. The creation of that form was the first component of a project that encompasses electronic submission of mid- and end-of-year UPK program expenditure forms, all of which will align to provide consistent and easily comparable information.

Finding: *Questionable Bank Statement Activities Totaling $407,322.* (Report, pp. 24-26). In addition to whatever other field work was conducted, the auditors analyzed the UPK program providers' bank statements. In so doing, they satisfied themselves generally that UPK funds paid by the DOE were deposited in the ordinary course. However, their further review of the account activities led them to make observations about withdrawals and report that a total of $407,322 in withdrawals were, on their face, questionable, insofar as they were in large dollar amounts, were made in "cash" and included wire transfers. Although, in some instances, providers offered explanations that could have been followed up during audit fieldwork, the Report invites the DOE to 1) "investigate the questionable bank activities totaling $407,322 . . . and if warranted, recoup the moneys." 2) "Ensure that they review bank statements as part of their monitoring of the UPK program at the non-public schools to ensure that UPK funds are properly deposited and that there are no unusual withdrawals, checks issued or transfers."

[9] Items included in the finding ranged in cost from $0.78 to $3,038.

3) "Require the non-public schools to seek written approval before making loans or cash withdrawals involving UPK funds." (Report Recommendations 17, 18 and 19, respectively).

Response: *For reasons we elucidate below, we cannot agree in whole with the recommendations that attach to the auditors' findings.*

Similar to the guidelines instituted by the New York State Education Department for private special education programs, the policies promulgated by the DOE do not require that UPK providers maintain a bank account for UPK transactions separate from other business funding sources, the thinking being that the providers should be able to maintain a cash flow that best serves the needs of the organization. Rather, the DOE requires that UPK programs maintain separate books identifying UPK program receipts and disbursements and report the expenditures made on behalf of the UPK program twice yearly. Further, our reference to books maintained by providers on an *accrual* basis (as required by the DOE) rather than bank statements that reflect transactions on a *cash* basis, facilitates the DOE's ability to oversee UPK program providers' fiscal activity as reported on the End-of-Year Expenditure Report.

When the OAG and private audit firms under contract to perform UPK audits conduct audits of the UPK program, the ledgers and End-of-Year Expenditure Report provide the basis for the audit. The providers' bank accounts may be reviewed to determine the completeness of the providers' books. To that extent, questionable transactions, that is, transactions that on their face do not support the corresponding expenditures, are followed up to the providers' books to determine the validity of the expenditures.

Under generally accepted auditing procedures, bank statement transactions are tested for the purpose of determining whether transactions reported on the bank statements are posted in the auditee's books. This type of testing does not address the *validity* of the transactions posted to the ledger which is the DOE's primary concern with respect to the UPK program expenditures. Validity of transactions is tested by analyzing the provider's books, comparing the transactions posted in the books to the expenditure report and corresponding supporting documentation, which includes invoices and proof of payment.

The Report implies that the observed bank activities represent inappropriate UPK expenditures. However, we posit that the audit team stopped short of completing the testing process to determine the validity of the expenditure on behalf of the UPK program. To exemplify our position, we point to the finding cited in the Report concerning Bryan's Educational Center and Smart Start Early Childhood Center (Report, p. 24, *Table IV*).

In the case of Bryan's Educational Center, the audit team reports a $15,000 bank transfer from the UPK program account to the Director-owner's personal bank account. From the Report, we glean that the audit team was advised by the provider's accountant that the funds were used to meet rent expenses. Rather than take the logical next step of reconciling the provider's rental costs with the total supportable expenditures in that cost category, the auditors paint the transaction "questionable."

With respect to Smart Start Early Childhood Center, the auditors report a repayment of a $10,000 loan from the Educational Director/owner to the school as a "questionable transaction." However, it appears that the auditor's true concern is not whether this is a legitimate loan from the owner to the school, but that there was no written loan agreement or approval by the DOE for that loan.[10] It further appears that the auditors are suggesting that when an owner lends money to the UPK program to meet operating expenses, that the owner enter into an agreement with the DOE, a suggestion that we cannot accept as the loan is between the owner and the school, not the owner and the DOE.

It is the DOE's position with regard to the recommendations that although we cannot agree with the audit procedures used to arrive at the findings or certain of the conclusions drawn, OAG staff will review the propriety of the cited transactions to the extent that they have not done so already. Further, for reasons stated above, the review of bank statements will not be incorporated into the monitoring procedures. As for the recommendation that the DOE require approval of loans from a principal to the school, we have revised the *Expenditure Guide* accordingly.

Finding: *Other Issues. Children's Playhouse Concerns.* (Report, pp. 26-28). The Report raises issues with respect to the provider's internal controls (no segregation of duties; inadequate recordkeeping practices); purportedly questionable expenditures (Executive Director's salary exceeded administrative cost allowance; checks were drawn to "cash"); and contract compliance (teachers were not present in required numbers; attendance records did not accurately reflect actual attendance; and three and four year olds were in the same class). It is recommended that DOE officials should: 1) "Investigate the conditions we cited at Children's Playhouse and depending on the investigation, consider terminating its UPK contract." 2) "Assist Children's Playhouse in developing a tighter internal control structure if DOE decides that the issues cited in our audit are as a result of poor internal controls rather than misappropriation of funds. DOE should ensure that all financial records are maintained accurately and in an organized manner, which should include ensuring that a Cash Disbursement Journal be maintained to record UPK expenditures." (Report Recommendations 20 and 21, respectively).

Response: *The OAG has begun to address the recommendations. OAG and Regional program and operational staff have conducted site visits during which conditions outlined in the findings were addressed as follows.*

Internal Controls: The OAG's audit of Children's Playhouse (independent of the Comptroller's audit) is in progress. As of this date, however, the assigned OAG auditor has reviewed the Report's findings with the provider's accountant and has advised him of the resources available on the DOE website and the controls that must be in place to ensure compliance with UPK program fiscal requirements. Further, the accountant

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[10] The OAG has already reviewed documentation submitted by Smart Start Early Childhood Center showing the initial loan and the DOE's payment records showing that the first payment for the school year had been delayed. OAG, recognizing that the provider's operation required an influx of funds before DOE revenue was received, credited the legitimacy of the loan transaction.

represents that he has undertaken responsibility for the Children's Playhouse bookkeeping functions that had been found wanting by the audit team. Recently, in response to the OAG's direction, the accountant prepared a revised general ledger, which we have received, that segregates expenditures related to the UPK program. The revised ledger is pending analysis by the OAG.

After the OAG's site visit the Children's Playhouse Executive Director reported that she had opened a dual signatory checking account; and, by letter, we were advised that certain administrative duties, such as ordering and recording receipt of goods, had been delegated to the Educational Director and Office Manager. (*Attachment E*).

"Questionable" Expenditures: First, we address the conclusion drawn from the audit team's review of the Children's Playhouse Executive Director's salary. The Executive Director, who is also the owner of the school, was paid $64,800 by the UPK program, an expense that, according to the Report, represented 69 percent of the school's total administrative expenses of $93,525. The operating funds for the UPK program totaled $346,528.

In order to arrive at the conclusion that the administrative portion of the budget exceeded the ten percent DOE policy cap on administrative costs, the audit team applied the *entire* salary of the Executive Director as an administrative expense citing as their reason therefor that the school retained an "Office Manager" responsible for UPK administrative work. That there may be an individual serving in that title should not affect how the Executive Director's role should be viewed. Children's Playhouse is a neighborhood preschool that enrolled 144 students (104 UPK, 40 private students) during the audit period. By the DOE's standards the program is small. Even without backup documentation, it is reasonable and logical to credit the Executive Director's representation that in her official capacity, and as the owner of the school, she spent at a substantial portion of her time dealing directly with issues related to the UPK program.

OAG staff have considerable experience auditing UPK and preschool special education programs, both of which limit administrative costs. They have determined that, based on the nature and size of the combined UPK and private programs, 87 percent of the duties outlined by the Executive Director are consistent with the duties generally performed by educational or programmatic staff and should be allocated as such. Thus, in reallocating the Executive Director's salary into administrative and programmatic cost categories, the OAG applied $8,424 as administrative costs and the balance of $56,376 as programmatic. To arrive at the recomputed total administrative cost attributable to the UPK program we took out $64,800 from the $93,525 in administrative costs identified in the Report and added back $8,424 (the administrative expense portion of the salary). We arrived at an administrative expense total of $37,149, which is 0.7 percent above the ten percent cap.

The section in the Report to which this portion of the response is directed (Report, p. 26) again raises that "numerous checks" were drawn from the Children's Playhouse bank account to "cash" or the Executive Director. Since this issue appears elsewhere in the Report under a section outlining "Questionable Bank Statement Activities," and was addressed in that section, we will not revisit it here.

Contract Compliance: During audit field work conducted in Children's Playhouse in February and March 2006, the audit team identified issues related to contractually required student-to-teacher ratios and attendance procedures. In two instances, cited in the Report, the auditors observed only one adult – an assistant teacher - in the classroom with eight students on one occasion and nine on another. The Report further recalls a site visit during which the auditors noted discrepancies between the number of children actually in attendance and the number marked present in the teacher's attendance book. The auditors also found during site visits a classroom where three year olds were present in greater numbers than the four-year-old UPK students, a condition that is not encouraged by the DOE.

During the second week of the 2006/2007 school year, OAG, along with Regional operational and programmatic staff conducted an unannounced visit to Children's Playhouse. Based on that visit and follow-up, we are satisfied that the conditions noted by the auditors have been remedied in that the student-to-teacher ratio is compliant; the attendance books were accurate; and the three and four year old students were in separate classrooms.[11]

With respect to the recommendations, the DOE has been "investigating" the conditions cited in the Report and, as reported above, has already performed steps necessary to improving the school's performance. Additionally, the OAG will continue its audit, which tests compliance with fiscal and key programmatic contractual requirements, and, consistent with past practice will consult with the other central DOE responsibility centers upon completion of the audit to determine any action that may be warranted upon completion of the review.

Finding: *Other Issues. Gan Day Care Center Improperly Used UPK Funds for Bonuses*. (Report, p. 29). The Report raises that the school paid six teachers a total of $10,500 in UPK funds for what appeared to be "bonuses." When the Region questioned the expenditure in writing, the school provided an explanation – also in writing - that the payments were actually part of the teachers' salaries. Auditors found both written documents in the Region's files. The Report indicates that there was no written documentation that the Region accepted the explanation and that approval must be in writing. The recommendation is that the DOE "ensure that any bonuses budgeted by the non-public schools are approved in writing." (Report Recommendation 22).

Response: *The DOE agrees that approvals for bonus payments from UPK funds must be in writing as stated in the Expenditure Guide.*

Finding: *Other Issues. Lack of Written DOE Approval for Building Rental Agreements between Related Parties*. (Report, p. 29-30). The auditors, having found five instances among the nine schools tested where the UPK sites were operating in facilities owned by the schools' Directors, recommend that the "DOE should ensure that non-public schools

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[11] OAG will include within its audit of Children's Playhouse a review of the staffing and attendance issues raised in the Report. A determination will be made whether disallowances should be taken.

engaging in related-party rental agreements request and receive DOE approval in writing." (Report Recommendation 23).

Response: *As recognized in the Report, the DOE agreed with the recommendation and revised the Expenditure Guide to provide clarification.* In addition, the OAG has circulated among providers for their response and has posted on its website a *UPK Provider Survey* that includes questions regarding this topic. The ROCs, working with the OAG and its audit partner, will follow-up with the UPK program providers to ensure compliance and select providers for audits and desk reviews to be performed by the OAG and audit firm.

Finding: *Other Issues. Use of UPK Funds for Private Sanitation Services* (Report, p. 30). Certain of the schools within the audit sample paid for private sanitation services with UPK funds, believing, as noted in the Report, that businesses were not permitted to use City sanitation services. As the DOE was unaware that the private UPK programs could avail themselves of the City's services without cost to the program, the Report recommends that the DOE "investigate whether any non-public schools operating UPK programs have private sanitation services paid for by UPK funds, and if so, inform them that they are eligible for DOS service free of charge. Those non-public schools choosing to use private sanitation services should pay the cost from other than UPK funds." (Report Recommendation 24).

Response: *As recognized in the Report, the DOE concurred with the finding and updated the Expenditure Guide accordingly.* Additionally, the DOE issued a written directive to UPK program providers notifying them of their eligibility to receive free services from the New York City Department of Sanitation and the procedures for obtaining these services.

Attachment A

DOE's Analysis of Payments Using a 10% Margin

Response to Report Finding: "DOE Overpaid Schools $141,055 in UPK Funds"

	School	(A) Contract Cost/Child	(B) Contract Estimated # of Children	(C) # of Children Enrolled	(D) # of Children Within 10% Margin	(E) Cost Using 10% Margin (A x D)	(F) Total Payments Made by DOE	(G) Overpayments-Difference Between Total Payments Made by DOE and Cost Using 10% Margin	Comments
1	CYCLE Day Care Center	3,450	100	85	95	327,750	345,000	(17,250)	Difference will be recouped by the close of School Year 2006/2007
2	Children's Playhouse	3,332	108	93	104	346,528	346,528	-	
3	Smart Start Early Childhood Center	3,904	81	74	81	316,224	316,224	-	
4	Jewish Community Center of Staten Island	3,400	132	120	132	448,800	426,360	-	The School had been scheduled to receive $448,800. However, based on the End-of-Year Expenditure Report, payments would have exceeded expenditures by $40,459. Therefore, $22,440 was withheld from the School Year 2004/2005 final payment; the balance of $18,019 was recouped in School Year 2005/2006.
5	Gan Day Care Center	3,511	99	58	99	347,589	347,589	-	
6	Our Saviour's Lutheran Preschool	3,454	88	87	88	303,952	303,952	-	
	Total							(17,250)	

Attachment B

DOE's Analysis of "Unspent" Funds

Response to Report Finding: "DOE Failed to Recoup $82,321 in Unspent UPK Funds"

	School	(A) Payments Made by the DOE	(B) Expenditures per the End-of-Year Report	(C) "Unspent" Funds	Comments
1	*Gan Day Care Center	347,589	347,514	(75.00)	Withheld from School Year 2006/2007 payment
2	**Smart Start EEC	316,224	353,042	-	
3	Staten Island YMCA	612,000	589,369	(22,631.00)	Withheld from School Year 2006/2007 payment
	Total			(22,706.00)	

* The End-of-Year Expenditure Report originally submitted by the School reported salaries on a cash basis (September through June) and did not include payments made in July and August. The report was subsequently revised using the required accrual method to reflect the 12-month salary and submitted to the Region.

** The End-of-Year Expenditure Report the auditors received was incorrect. A revised report, (Attachment C) reflects the expenditures for the School.

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: 7 **District:** 20

CBO Name: Smart Start Early Childhood Center Inc.

VENDOR INFORMATION

CBO Address:	8411 Fort Hamilton Parkway; Brooklyn, NY 11209	**CBO Phone #:**	718.921.1968
Email Address:	smartstart@verizon.net	**CBO Fax #:**	
Tax ID #:	11-3324859	**Contract #:**	

CONTRACT INFORMATION

FY05 Contract Amount:	$316,224.00	**Actual Number of Children as of 11/19/04:**	
Cost per Child:	$ 3,904.00	**Revised Contract Amount (if applicable):**	
Contracted Number of Children:	81	**Year End Payments received against Original Fy 05 Contract Amount:**	$ 316,224.00

DUE DATE

Completed End of Year Expenditure Forms must be emailed to your Contract Administration Officer no later than July 14, 2005. A set of completed End of Year Expenditure Forms with original signatures must be maintained at each CBO site.

CERTIFICATION STATEMENT

I hereby certify that I have read and understand the above statement, that the information furnished in this report is true and accurate to the best of my knowledge. I further attest to the fact that there are records, documents, and allocation worksheets to support all the information contained herein. I acknowledged that the Region may reject this report if it has not been fully or accurately completed.

Administrative Name and Title: [redacted]

Financial Name and Title:

Signature:

Date:

Signature: [redacted]

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: ____________ **District:** ____________

CBO Name: Smart Start Early Childhood Center Inc.

DIRECTIONS: Answer this form carefully and completely

The End of Year Expenditure Form was designed to ascertain how much money has been spent on the UPK program.

Column A - *FY05 Registered Contract Budget*: The cost of each item should reflect the cost from your original approved budget form for FY05.

Column B - *Revised Budget as of 11/19/04 BEDS Date*: If the number of children registered as of 11/19/04 does not match your contracted amount, you should have revised your budget to account for the changed number of children. This column should reflect the revised cost of each category. If this column is not applicable, please LEAVE BLANK.

Column C - *CBO Actual FY 05 UPK Expenses*: The cost of each item should reflect the actual amounts that have been spent in FY 05. Please note documentation for all expenses is required to be maintained at your site.

Column D is automatically calculated. *This column does not need to be completed.*

Column E - *Explanation*: The purpose of this column is to explain the reason for the difference in Column D. Please select from the list below, and put the appropriate letter in this column. If Reason D is chosen, please elaborate in the Comment section at the bottom of the page.

Reason A- Full Balance will be expended for costs
Reason B- Category cost less than projected
Reason C- Category cost more than projected
Reason D- Other

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: ____________ **District:** ____________

CBO Name: Smart Start Early Childhood Center Inc.

OTPS FACILITY COSTS					
COST CATEGORIES	A	B	C	D	E
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
[illegible]	$48,000.00		$48,000.00	$0.00	
[illegible]	$2,834.62		$3,112.79	-$278.17	C
[illegible]	$2,887.95		$2,242.70	$645.25	B
[illegible]	$5,207.61		$5,117.13	$90.48	B
[illegible]	$200.00		$200.00	$0.00	
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	
COMMENTS					

OTPS ADMINISTRATIVE					
COST CATEGORIES	A	B	C	D	E
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Office Equipment Purchase	$500.00			$500.00	B
Office Equipment Rental				$0.00	
[illegible]	$4,715.54		$5,422.00	-$706.46	C
[illegible]	$5,168.81		$8,852.09	-$3,683.28	C
[illegible]	$950.00		$1,000.00	-$50.00	C
[illegible]	$4,028.00		$6,200.00	-$2,172.00	C
[illegible]	$77.26		$68.00	$9.26	B
[illegible]				$0.00	
[illegible]	$1,301.05		$1,988.00	-$686.95	C
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	
COMMENTS					

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: ____________ **District:** ____________

CBO Name: Smart Start Early Childhood Center Inc.

OTPS INSTRUCTIONAL					
COST CATEGORIES	A	B	C	D	E
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
[illegible]				$0.00	
Supplies	$4,073.31		$6,897.00	-$2,823.69	C
[illegible]				$0.00	
[illegible]	$4,989.60		$4,804.80	$184.80	B
Student Trips	$2,376.00		$2,340.00	$36.00	B
[illegible]	$5,087.40		$4,200.00	$887.40	B
Miscellaneous	$865.35		$739.00	$126.35	B
Subtotal OTPS INSTRUC	[illegible]	$0.00	[illegible]	[illegible]	
TOTAL OTPS	[illegible]	$0.00	[illegible]	[illegible]	
In Kind Contribution	$0.00		$36,818.30	-$36,818.30	
				$0.00	
				$0.00	
COMMENTS	In Kind Contribution of $ 36,818.30 [redacted]				

STAFF SALARIES AND WAGES					
COST CATEGORIES	A	B	C	D	E
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
[illegible]					
[redacted]				$0.00	
	$33,696.00		$29,484.00	$4,212.00	B
	$33,696.00		$54,756.00	-$21,060.00	C
				$0.00	
	$16,848.00		$12,636.00	$4,212.00	B
				$0.00	
	$14,883.75		$24,300.00	-$9,416.25	C
	$26,250.00		$31,218.03	-$4,968.03	C
	$26,250.00		$29,748.35	-$3,498.35	C
				$0.00	
	$13,230.00		$6,006.30	$7,223.70	B
	$13,230.00		$12,420.00	$810.00	B
	$7,717.50		$18,438.96	-$10,721.46	C

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: ______________ **District:** ______________

CBO Name: Smart Start Early Childhood Center Inc.

STAFF SALARIES AND WAGES (CONTINUED)					
COST CATEGORIES	A	B	C	D	E
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
[illegible]					
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	
[illegible]				$0.00	
				$0.00	
				$0.00	
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	
[illegible]	20.00%		15.00%	5.00%	
[illegible]	$37,160.25	$0.00	$32,851.15	$4,309.10	C
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	
GRAND TOTAL	[illegible]	[illegible]	[illegible]	[illegible]	
COMMENTS					

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: 7 **District:** 20

CBO Name: Gan Day Care Center

CBO Address:	4206-10 15th Avenue Brooklyn, N.Y. 11219	CBO Phone #:	718-435-2812
Email Address:	gandaycare@pngusa.net	CBO Fax #:	718-435-2503
Tax ID #:	11-2302049	Contract #:	9001119

FY05 Contract Amount:	$ 347,589.00	Actual Number of Children as of 11/19/04:	99
Cost per Child:	$ 3,511.00	Revised Contract Amount (If applicable):	
Contracted Number of Children:	99	Year End Payments received against Original Fy 05 Contract Amount:	330209.55

Completed End of Year Expenditure Forms must be emailed to your Contract Administration Officer no later than July 1, 2005. A set of completed End of Year Expenditure Forms with original signatures must be maintained at each CBO site.

I hereby certify that I have read and understand the above statement, that the information furnished in this report is true and accurate to the best of my knowledge. I further attest to the fact that there are records, documents, and allocation worksheets to support all the information contained herein. I acknowledged that the Region may reject this report if it has not been fully or accurately completed.

Administrative Name and Title: [redacted]

Financial Name and Title: [redacted]

Signature: ______________________ **Date:** __________

Signature: ______________________ **Date:** __________

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: 7 **District:** 20

CBO Name: Gan Day Care Center

[illegible]

The End of Year Expenditure Form was designed to ascertain how much money has been spent on the UPK program.

Column A - ***FY05 Registered Contract Budget*:** The cost of each item should reflect the cost from your original approved budget form for FY05.

Column B - ***Revised Budget as of 11/19/04 BEDS Date*:** If the number of children registered as of 11/19/04 does not match your contracted amount, you should have revised your budget to account for the changed number of children. This column should reflect the revised cost of each category.

Column C - ***CBO Actual FY 05 UPK Expenses*:** The cost of each item should reflect the actual amounts that have been spent in FY 05. Please note documentation for all expenses is required to be maintained at your site.

Column D is automatically calculated. ***This column does not need to be completed.***

Column E - ***Explanation*:** The purpose of this column is to explain the reason for the difference in Column D. Please select from the list below, and put the appropriate letter in this column. If Reason D is chosen, please elaborate in the Comment section at the bottom of the page.

Reason A- Full Balance will be expended for costs
Reason B- Category cost less than projected
Reason C- Category cost more than projected
Reason D- Other

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: 7 **District:** 20

CBO Name: Gan Day Care Center

COST CATEGORIES	A	B	C	D	E
[illegible]	$6,797.00		$6,797.00	$0.00	
[illegible]				$0.00	
[illegible]				$0.00	
[illegible]	$1,300.00		$1,094.00	$206.00	A
[illegible]				$0.00	
[illegible]					

COST CATEGORIES	A	B	C	D	E
[illegible]	$800.00		$624.00	$176.00	B,D
[illegible]	$1,200.00		$1,200.00	$0.00	
[illegible]	$1,300.00		$1,273.00	$27.00	B,D
[illegible]				$0.00	
[illegible]				$0.00	
[illegible]	$250.00		$0.00	$250.00	B,D
[illegible]	$200.00		$185.00	$15.00	B,D
[illegible]				$0.00	
[illegible]	$800.00		$235.00	$565.00	B,D
[illegible]	D:$1033.00 was used in OTPS Instructional categories.				

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: 7 **District:** 20

CBO Name: Gan Day Care Center

[redacted]

COST CATEGORIES	A	B	C	D	E
[redacted]					
	$8,272.00		$9,391.00	-$1,119.00	C,D
	$10,500.00		$12,467.00	-$1,967.00	C,D
				$0.00	
				$0.00	
	$2,971.00		$3,000.00	-$29.00	C,D
	$22,910.00		$22,410.00	$500.00	B,D
	$784.00		$800.00	-$16.00	C,D
[redacted]					
				$0.00	
				$0.00	
				$0.00	
	D:Excess monies from administrative expenses to be used for educational Instruction.				

[redacted]

COST CATEGORIES	A	B	C	D	E
[redacted]					
	$13,900.00		$11,583.00	$2,317.00	A,D
	$10,125.00		$8,438.00	$1,687.00	A,D
	$9,000.00		$7,500.00	$1,500.00	A,D
	$9,000.00		$6,300.00	$2,700.00	A,D
	$9,000.00		$7,500.00	$1,500.00	A,D
	$10,450.00		$10,450.00	$0.00	
	$3,300.00		$3,300.00	$0.00	
	$40,000.00		$33,333.00	$6,667.00	A,D
	$2,000.00		$2,000.00	$0.00	
	$2,000.00		$2,000.00	$0.00	
	$2,000.00		$2,000.00	$0.00	
	$14,500.00		$10,875.00	$3,625.00	A,D
	$1,500.00		$1,500.00	$0.00	

THE NEW YORK CITY DEPARTMENT OF EDUCATION
UPK Program End of Year Expenditure Form FY05

Region: 7 **District:** 20

CBO Name: Gan Day Care Center

COST CATEGORIES	A	B	C	D	E
[redacted]	$1,500.00		$1,500.00	$0.00	
	$1,500.00		$1,500.00	$0.00	
	$11,900.00		$8,925.00	$2,975.00	A,D
	$26,000.00		$21,667.00	$4,333.00	A,D
	$9,000.00		$7,500.00	$1,500.00	A,D
	$9,000.00		$7,500.00	$1,500.00	A,D
	$9,000.00		$7,500.00	$1,500.00	A,D
	$9,000.00		$7,500.00	$1,500.00	A,D
	$9,000.00		$7,500.00	$1,500.00	A,D
	$2,000.00		$2,000.00	$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
				$0.00	
	$3,000.00		$856.00	$2,144.00	C,D
				$0.00	
				$0.00	
	33.00%	0.00%	33.00%	-33.00%	
	$70,842.75	$0.00	$59,357.43	-$59,357.43	A,D

C.Excess substitute money is to be used for expenses in instructional category and for underestimating fringe costs.
D: Salary and fringe benefits were divided into 12 monthly payments.

THE CHILDREN'S PLAYHOUSE, PRE-SCHOOL & SUMMER DAY CAMP
DAY CARE • NITE CARE • WEE CARE
950 Rockland Avenue & 85 Monahan Avenue
Staten Island, New York 10314
718-761-0129

11-6-06

[redacted]
Office of Auditor General
Dept. Of Education
65 Court Street
B'Klyn, N.Y. 11201

[redacted]

Please be advised that my accounting firm of Michael, Adest & Company, has agreed to fulfill my accounting needs on a monthly basis in accordance with my contractual agreement with the Board of Education Universal Pre-K contract. According to my contract a letter of Engagement will be forth coming from my accounting firm for the current year. I will forward you a copy as soon as I receive it from Michael, Adest & Co. All tasks have been divided up between myself, the Educational Director and the Office Manager. (Ree: The ordering of supplies and materials)

As per the ABC Invoice: Please be advised that I do not own a school in Madison, N.J. A previous order was sent to Madison, N.J. as a gift. When the second order was placed for Universal Pre-K, there was a computer error, and the second order was sent to Madison, N.J. in error. The items were returned to the 85 Monahan Ave. address by the recipient. If need be I can have [redacted] sign an affidavit stating that we received the items back.

Thank you for your time and trouble in this matter.

Yours Truly,

[redacted]

Executive Director