Audit Report

ARISE, Inc.

For the Period

October 1, 1999 through September 30, 2002

RF-0802-1

May 6, 2003

The University of the State of New York
THE STATE EDUCATION DEPARTMENT
Office of Audit Services
Albany, New York 12234

THE STATE EDUCATION DEPARTMENT / THE UNIVERSITY OF THE STATE OF NEW YORK / ALBANY, NY 12234

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May 6, 2003

Mr. Dale Fanning
Board President
ARISE, Inc.
1065 James Street
Syracuse, New York 13203

Dear Mr. Fanning:

The following is our final audit report (RF-0802-1) on ARISE, Inc. for the period October 1, 1999 through September 30, 2002. The audit was conducted pursuant to Sections 1120 and 1123 of the Education Law, and Section 248.2(f) of the Regulations of the Commissioner of Education. The audit was carried out in pursuit of Goal #5 of the Board of Regents/State Education Department Strategic Plan: “Resources under our care will be used or maintained in the public interest.”

A check for the total audit adjustments of $84,994 should be made payable to the Commissioner of Taxation and Finance and should reference this report number. Please send the check to:

State Education Department
Division of Fiscal Management
Attn: Donald Juron
Room 408 EB
89 Washington Ave
Albany, New York 12234

Ninety days from the issuance of this report, ARISE officials will be asked to submit a report on actions taken as a result of this audit. I appreciate the cooperation and courtesies extended to the staff during the audit.

Sincerely,

Daniel Tworek

Enclosure

cc: R. Cate, F. DeMay, W. Deschenes, M. DiVirgilio, L. Gloeckler, R. Gumson, R. Johnson, T. Sheldon, M. Tierney, C. Foster (DOB), B. Mason (OSC), T. McKeown, Executive Director

Executive Summary

Background and Scope of the Audit

ARISE, Inc. (ARISE) is an independent living center (ILC) that provides services to individuals with disabilities. ARISE spent about $4,492,559 during the 2001-02 fiscal year in carrying out its activities, which were funded in part by a $369,931 ILC contract and a $240,061 Supported Employment Program (SEP) contract administered by the Office of Vocational and Educational Services for Individuals with Disabilities (VESID). The ILC and SEP contracts are multi-year contracts. The audit reviewed the past three years. The ILC contracts were for the period October 1, 1999 through September 30, 2002 and paid ARISE $1,141,300 for the three-year period. The SEP contracts were for the period July 1, 1999 through June 30, 2002 and paid ARISE $617,734 for the three-year period. The disallowance for the ILC contract is shown on Schedule 1. VESID officials requested that the Office of Audit Services review certain aspects of ARISE’s fiscal practices.

This was a limited scope audit and the objectives were to assess ARISE's methods for allocating costs among different programs; control of equipment; purchasing practices; and the use of VESID funds for staff travel. To accomplish the objectives we reviewed applicable laws, regulations, and contract provisions, interviewed VESID and ARISE management and staff, examined records and supporting documentation, sampled transactions, and reviewed ARISE’s audited financial statements.

Audit Results

The audit found that improvement opportunities exist in the following areas:

1. ARISE needs to return $80,489 to the Department for non-related ILC contract expenditures, $502 for employee-related items, $1,111 for interest expense, and $2,892 for unreasonable allocations.
2. ARISE can improve compliance with the VESID contracts’ provisions by improving inventory procedures and entering into contracts for services with individuals and organizations.
3. ARISE has opportunities to improve management processes in the areas of policies for travel, allocation methodologies, and segregation of duties.

Table of Contents

INTRODUCTION **1**

NON GRANT RELATED EXPENDITURES **2**

RELATED ORGANIZATION 2
LOAN EXPENSE 3
EMPLOYEE-SUPPORTED DONATIONS 3
RECOMMENDATIONS 4

CONTRACT COMPLIANCE **5**

CONTRACTS FOR SERVICES 5
EQUIPMENT 5
RECOMMENDATIONS 6

OPPORTUNITIES TO IMPROVE MANAGEMENT PROCESSES **7**

TRAVEL 7
ALLOCATION METHODOLOGY 8
SEGREGATION OF DUTIES 9
RECOMMENDATIONS 9

Schedule 1 - Schedule of Revenues and Disallowances
Appendix A - Contributors to the Report
Appendix B – Comments of ARISE Officials
Appendix C – Apendix Ds of ILC Contract C005590 and SEP Contract C005409

Note: Appendix D of the ILC and SEP Contracts describe the activities authorized to be performed.

Introduction

ARISE, Inc. (ARISE) is an independent living center (ILC) that provides services to individuals with disabilities. ARISE's programs include advocacy, information and referral, transportation, family support services, peer counseling, equipment loan and repair, and recreation. ARISE spent approximately $10,583,025 during the 1999-2002 fiscal years in carrying out its activities. These activities were funded in part by $1,141,300 in ILC contract payments and $617,734 in SEP contract payments from the New York State Education Department's (Department) Office of Vocational and Educational Services for Individuals with Disabilities (VESID).

This was a limited scope audit and the objectives were to assess ARISE's methods for allocating costs among different programs, control of equipment, purchasing practices, and the use of VESID funds for staff travel. To accomplish the objectives, we reviewed applicable laws, regulations, and contract provisions, interviewed VESID and ARISE management and staff, examined records and supporting documentation, sampled transactions, and reviewed ARISE's audited financial statements.

ARISE officials agreed with the findings and recommendations of this report. Their comments on the matters contained in this report have been included where appropriate. Their final comments have been included in their entirety as Appendix B to this report.

Non Grant Related Expenditures

ARISE entered into an Independent Living Contract (C005590) and a Supported Employment Contract (C005409) with VESID. The ILC contract stipulates that expenses must meet the following general criteria to be considered allowable for reimbursement:

- Be necessary and reasonable for proper and efficient operation of the program.
- Be permissible under applicable State and/or federal laws and regulations.
- Conform to any limitations or exclusions set forth in laws, regulations, or other governing limitations as to type or amounts of items.
- Be the net amount after applying all applicable credits such as purchase discounts, project-generated income, and adjustments of overpayments.
- Must not be included as a cost in any other project or contract.

The audit found that certain expenditures included in the ILC Final Expenditure Report did not meet the provisions of the contract. The audit determined that expenses were used for an indoor riding arena, unapproved interest expense, and employee-supported expenses. These areas are discussed in the following sections.

Related Organization

ARISE at Marshall Farms, Inc. (Farm) is an 84-acre horse farm and recreational facility focusing on people with disabilities. It was incorporated separately from ARISE and is located in Chittenango, New York. ARISE has a controlling interest in the Farm.

ARISE included payments of $80,489 in its ILC contract expenditures that were for the Farm. These expenditures do not support the service requirements of Appendix D of the ILC contract. The payments were a contribution toward expenses for the construction of a riding academy building on the Farm's premises. The five payments were for $4,920, $211, $212, $73,521, and $1,625.

Management philosophy at the time of the decision favored using the ILC contract monies to sustain ARISE's operation, even when there was ambiguity as to whether the particular expense in question pertained to ILC objectives as stated in Appendix D of the contract.

ARISE officials agree that the money contributed to the building of the indoor arena is not an allowable ILC contract-related expenditure and that these monies should be returned to the Department. In order to prevent this from occurring, the general ledger and bank accounts for the Farm have been segregated from the ARISE general ledger/accounting system.

Loan Expense

The ILC Financial Procedures Handbook requires prior approval before an ILC commits to a business loan. This is one of several conditions that need to be present before the interest expense is reimbursable. Interest expense accumulated for ARISE's total operations should be allocated in a manner consistent with the revenue received from all of the funding sources.

The loan proceeds were used for all of ARISE's operations; however, the interest expense was charged entirely to the ILC contract. The expenses were $791 in April 2002 and $320 in September 2002.

ARISE officials agree the loan benefited the entire organization and, therefore, the $1,111 in interest expense should be allocated among all of the agency's operations. They will follow the recommended procedures for obtaining approval for loans in those instances when ARISE needs to borrow funds.

Employee-Supported Donations

Funds for fruit baskets and flowers for funerals, etc., are commonly employee-supported donations (known as sunshine funds) for the benefit of a fellow employee. The State does not routinely provide sunshine fund type benefits to its employees and, therefore, these types of expenditures are not considered appropriate by the audit.

The audit found sunshine fund type expenditures charged to the ILC contract totaling $502.

ARISE officials agree that these expenses should be disallowed because of poor documentation and have implemented procedures to review expenses for proper documentation.

Recommendations

1. Return $80,489 to the Department for non-related ILC contract expenditures.

2. Establish procedures to prevent non-related contract expenditures from being charged to VESID contracts.

3. Ensure that approval is obtained from VESID before committing to a business loan and return $1,111 to the Department.

4. Establish procedures to prevent sunshine fund type expenses from being charged to the ILC contract and return $502 to the Department.

Comments of ARISE Officials

ARISE Officials concur with these recommendations.

Contract Compliance

ARISE needs to comply with the provisions of the ILC and SEP contracts it entered into with VESID. The audit found two areas where improvement opportunities exist for compliance with VESID contracts.

Contracts for Services

The VESID contracts require ARISE to enter into a separate contract for services with anyone who is not their employee prior to that person or organization performing services. These service contracts would be made available to VESID and contain the VESID copyright provisions of its ILC and SEP contracts.

The audit requested copies of seven contracts for services but ARISE could only provide a copy for one contract. As a result, ARISE is not in compliance with the provisions of the ILC and SEP contracts.

ARISE officials agree they were unable to provide the service contracts requested and have corrected this matter with the use of a standard contract.

Equipment

Appendix A1 of the VESID contracts specifies that the organization will maintain an inventory of all equipment and other non-expendable assets purchased, improved, or developed. The contracts define non-expendable assets, suggest the format of the inventory list, and require the submission of the list along with the Final Expenditure Report. The contracts also state the disposition of any items on the list requires prior approval from VESID. The revenues received from the disposal would be used to reduce the amount required for qualified expenditures.

The Office of the State Comptroller's Financial Management Guide (Guide), Volume 1, Subsection 3.2010, states that it is important to maintain adequate fixed asset records to meet the requirements of Generally Accepted Accounting Principles and as a tool for controlling fixed assets and planning replacements. The Guide, Volume 2, Subsection 2, 11.1010, also states that effective internal control systems are designed to ensure management that all resources entrusted to their care are used in accordance with all laws, policies, regulations, and sound business practices, where applicable. In addition, all resources should be safeguarded against waste, loss, and misuse.

Adequate internal controls include maintaining accurate accounting and inventory records, and performing periodic comprehensive inventories of assets. ARISE did not have their asset listing in the format required by the contracts. In addition, they did not submit their list of non-expendable assets with their final expenditure reports.

The audit found it difficult to account for the items purchased with contract monies; however, no exceptions were found in the sample.

Recommendations

5. Ensure that service contracts or agreements are in place before individuals or organizations provide services pursuant to the VESID contracts.

6. Establish procedures to ensure the equipment list is maintained in the format required and submitted along with the final expenditure reports.

Comments of ARISE Officials

ARISE Officials concur with these recommendations.

Opportunities to Improve Management Processes

Management is responsible for establishing effective management processes or controls. In its broadest context, management controls include the plan of the organization, methods, and procedures adopted by management to ensure that its goals are met. These processes include such areas as planning, organizing, directing, and controlling program operations. The audit reviewed several processes and found opportunities for improvement in the areas of travel policy, allocation methodologies, and segregation of duties.

VESID's ILC and SEP contracts require ARISE to maintain complete and accurate books, records, documents, accounts, and other evidence directly pertinent to performance of these contracts. They also require ARISE to submit budgets and a final expenditure report. The contracts include instructions on the budget, payment and reporting schedule, program work plan, and other considerations.

Travel

The ILC and SEP contracts specify reimbursement for travel, lodging, and subsistence at the per diem rate in effect at the time for New York State Management Confidential (M/C) employees. M/C employees are required to submit only actual, necessary, and reasonable expenses for reimbursement for official travel. A specific statement of the official business for which expenses were incurred is required under Section 109 of the State Finance Law for M/C employees. Each traveler requesting reimbursement for travel expenses must submit a detailed statement explaining the official business purpose for which expenses were incurred.

The audit sampled travel vouchers and found that many did not include a purpose for the travel. The detail supporting the expenditures was incomplete or, in some cases was not present. Many times, it was obvious that one person paid for the meal of another authorized fellow traveler; however, this was not supported by the documentation. Travel vouchers totaling $5,505 were charged to ILC #C05590, and $3,125 were charged to SEP #C005409. They require more complete documentation.

ARISE officials agree that they need to include the requirement to provide sufficient details of official business travel in their travel policy. They state that all travel-related expense reports must provide sufficient detail prior to reimbursement.

Allocation Methodology

General business practices suggest that an expense is allocable to a contract, project, service, or other activity, in accordance with the relative benefits received. An expense is allocable if it is treated consistently with other expenses incurred for the same purpose in like circumstances and if it:

1. is incurred specifically for the contract,
2. benefits both the contract and other work and can be distributed in reasonable proportion to the benefits received, or
3. is necessary to the overall operation of the organization, although a direct relationship to any particular cost objective cannot be shown.

In addition, any cost allocable to a particular cost objective under these principles should not be shifted to other contracts in order to overcome funding deficiencies, or to avoid restrictions imposed by law or the terms of the contract.

The audit found several exceptions noted in the sample of expenditures where the allocation to the ILC contract seemed disproportionate to the benefits received. These were costs whose reasonableness and allocability were difficult to determine. Vendor and amounts were:

Chase Manhattan	$ 52
American Express	$ 50
Gladd Security	$ 510
Source One System	$2,280
Total	$2,892

ARISE officials stated that previous management had used the ILC contract monies for expenses they felt necessary to the overall operation of ARISE and were generous in assigning percentages of costs to the contract. An example of this is 72 percent of the cost of carpet installation. The audit could not argue every allocation but did take exception to those cases where the ILC contract received 100 percent of the costs of expenses that the audit believed should be shared.

ARISE officials agree that charging 100 percent to the ILC contract for a purchase that benefits the entire agency should not be the agency's practice. ARISE agrees that the questioned charges of $2,892 should be returned to the Department.

Segregation of Duties

Internal controls or an internal control system is the integration of the activities, plans, attitudes, policies, and efforts of the management of an organization to provide reasonable assurance that the organization will achieve its objectives and mission.

Separation of duties is the division of key tasks and responsibilities among the various employees and sub-units of an organization. No one individual should control all of the key aspects of a transaction or event. By separating key tasks and responsibilities, such as receiving, recording, depositing, securing and reconciling assets, management can reduce the risks of error, waste, or wrongful acts occurring or going undetected. In cases where tasks cannot be effectively separated, management can substitute increased supervision as an alternative control activity that can help prevent or reduce these risks.

The audit found that the accountant opens the mail, lists the checks for deposit, makes the deposit, and reconciles the bank statements. There is potential for fraud to occur.

ARISE officials emphasized that there is adequate management overview of this operation to prevent error, waste, or wrongful acts. ARISE officials consider existing policies, procedures, and management review sufficient.

Recommendations

7. Establish a travel policy and procedures that require detailed documentation of expenditures for reimbursement.

8. Establish allocation methodologies for expenditures that benefit the entire organization and return $2,892 to the Department.

9. Ensure segregation of duties to reduce the chance of fraud, abuse, or waste of ARISE assets.

Comments of ARISE Officials

ARISE Officials concur with these recommendations.

Contributors to the Report
ARISE Independent Living Center, Inc.

- Calvin Spring, Audit Manager
- Ron Talarico, Associate Auditor (Auditor-in-Charge)
- Jean Stone, Senior Auditor

ARISE, Inc.
Schedule of Revenues and Disallowances
ILC and SEP Contracts

Period	Contract Name	Contract Number	Amount
October 1, 1999-September 30, 2000			$296,746
October 1, 2000-September 30, 2001	Independent Living Centers	C005590	$474,623
October 1, 2001-September 30, 2002			$369,931
			$1,141,300
Less: Non-related expenditures			$80,489
Employee-related items			$502
Unreasonable allocation			$2,892
Interest expense			$1,111
Total audit adjustments			$84,994
Net ILC contract			$1,056,306
July 1, 1999-June 30, 2000			$205,369
July 1, 2000-June 30, 2001	Supported Employment	C005409	$172,305
July 1, 2001-June 30, 2002			$240,061
			$617,735
	Supported Employment Contracts		$617,735
	Independent Living Contracts		$1,056,306
Total contract revenues			$1,674,041