



COMMONWEALTH OF PENNSYLVANIA  
DEPARTMENT OF PUBLIC WELFARE  
**BUREAU OF FINANCIAL OPERATIONS**  
3<sup>rd</sup> Floor Bertolino Building  
Harrisburg, Pennsylvania 17105-2675

**MAR 15 2007**

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JOHN H. BUNGO, CGFM, CFS  
DIRECTOR

Ms. Dorothy Klein  
Director  
Delaware County Mental Health/  
Mental Retardation Program  
Delaware County Human Services  
20 South 69<sup>th</sup> Street  
Upper Darby, Pennsylvania 19082

Dear Ms.Klein:

I am enclosing the final audit report of Community Interactions, Inc. as prepared by the Division of Audit and Review. You are receiving this report because your county currently contracts with the agency. Please review this report and be aware of the findings and recommendations contained in it.

The Department's Office of Developmental Programs and Office of Mental Health and Substance Abuse Services are in the process of dealing with the report's findings and recommendations.

If you have any questions concerning this matter, please contact Stan Futrick of the Division of Audit and Review at (610) 927-3636.

Sincerely,

John H. Bungo, CGFM, CFS

Enclosure

cc: Ms. Robyn Zippilli  
Mr. Michael Stauffer  
Mr. Kevin Casey  
Ms. Joan Erney  
Ms. Vicki Stillman-Toomey  
Ms. Lynne Baumeister  
Mr. Joseph Church  
Ms. Elizabeth Zeisloft



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JOHN H. BUNGO, CGFM, CFS  
DIRECTOR

Ms. Robyn A. Zippilli  
Executive Director and CEO  
Community Interactions, Inc.  
321 West Woodland Avenue  
Springfield, Pennsylvania 19064

Dear Ms. Zippilli:

I am enclosing the final report of Community Interactions, Inc., recently completed by this office. Your response has been incorporated into the final report and labeled as an Appendix.

I would like to express my appreciation for the courtesy and cooperation extended to my staff during the course of the fieldwork. I understand that Gary Clift was especially helpful in expediting the audit process.

The final report will be forwarded to the Department's Office of Developmental Programs, formerly the Office of Mental Retardation, and the Office of Mental Health and Substance Abuse Services to begin the Department's resolution process concerning the report contents. The staff from these Offices may be in contact with you to follow-up on the action taken to comply with the report's recommendations.

If you have any questions concerning this matter, please contact Richard Polek of the Audit Resolution Section at (717) 787-8890.

Sincerely,

John H. Bungo, CGFM, CFS

Enclosure

cc: Ms. Dorothy Klein  
Mr. Michael Stauffer  
Mr. Kevin Casey  
Ms. Joan Erney  
Ms. Vicki Stillman-Toomey

Ms. Lynne Baumeister  
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JOHN H. BUNGO, CGFM, CFS  
DIRECTOR

Mr. Kevin T. Casey  
Deputy Secretary for  
Developmental Programs  
Room 512 Health & Welfare Building  
Harrisburg, Pennsylvania 17105

Ms. Joan L. Erney  
Deputy Secretary for Mental Health &  
Substance Abuse Services  
Room 502 Health & Welfare Building  
Harrisburg, Pennsylvania 17105

Dear Mr. Casey and Ms. Erney:

In response to a request from the Office of Mental Retardation (OMR), Southeast Regional office, the Bureau of Financial Operations (BFO) performed an audit of Community Interactions, Inc. (CI). The audit was requested to assist the Southeast Regional Office of OMR in determining the propriety of the occupancy costs charged by CI. The audit addresses the occupancy (rent) costs incurred by CI and charged to Delaware County through June 30, 2004.

The mission of the BFO, accomplished through audit and review activities, is to assist the Department of Public Welfare (DPW) management to administer human service programs of the highest quality, at the lowest cost, with integrity.

**Results In Brief**

- CI has charged Delaware County \$401,272 in excess of allowable costs for rent payments through February 28, 2001, made to Independent Support Systems (ISS), a related party.
- Since March 1, 2001, through June 30, 2004, CI has overcharged Delaware County \$316,466 for occupancy costs for properties it considered debt free.
- CI has inappropriately listed many of the repairs and maintenance projects performed on the properties leased from ISS as renovations and/or improvements. As a result the property values used by CI in determining Continuing Participation Allowances (CPA) have been inflated.
- CI overcharged Delaware County \$108,475 for its consumers' use of vacation properties leased from ISS.
- Documentation for renovation/improvement costs is inadequate or unavailable. In particular, CI has no documentation for any renovation/improvement costs before July 1, 1997.

## **Background**

CI is a 501 (c)(3) not-for-profit corporation headquartered in Springfield, Delaware County, Pennsylvania. CI provides support services to people with mental retardation and mental health issues. The services provided by CI include community residential services, assisted living, community recreation services, employment services, in-home supports and mental health services.

CI leases many of its program sites from ISS, a related party. ISS is a not-for-profit real estate holding company. Through the period under audit It shared common ownership and control with CI. Through June 30, 2004, CI had leased 20 residential program sites, two vacation properties and CI's administrative offices. Since the audit began, ISS has sold some of the residences leased to or utilized by CI.

Through June 30, 2004, CI and ISS were related parties based upon the definition of "common ownership" and "control" as described in the 4300 Regulations. One individual on both the CI and ISS boards owned 51% of the certificates of both corporations and had the ability to overrule any and all board members at any time. The relationship of the two corporations was further evidenced in the annual audited financial statements and in the corporations' tax returns. In accordance with the regulations, related parties should be treated as one for reimbursement purposes. As a result billings through June 30, 2004, from ISS to CI must be based on cost.<sup>1</sup>

In 2001, ISS entered into a \$2,135,000 bond agreement with the Montgomery County Industrial Development Authority (IDA). The existing mortgages on properties leased by CI were satisfied with the bond proceeds. ISS management used the mortgaged properties as collateral for the bonds. Values equaling the outstanding liabilities on each property were provided to the bank underwriting the bonds. Accordingly, before a property could be removed as collateral, the aforementioned value had to be satisfied.

CI's funding is primarily through Delaware County's Mental Health/Mental Retardation (MH/MR) Program. For the fiscal year ended June 30, 2004, CI received funding of \$7.6 M through Delaware County.

## **Objectives/Scope/Methodology**

The BFO's audit focused on identifying allowable occupancy costs related to the CI properties used in their residential treatment program. Accordingly, our specific audit objectives were:

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[<sup>1</sup>During fieldwork, the legal counsel for CI disputed that ISS was a related party.]

**Objectives/Scope/Methodology (Continued)**

- To determine the propriety of all related party transactions involving real estate.
- To determine if the resultant occupancy costs charged to Delaware County were reasonable and in accordance with the 4300 Regulations.

In pursuing the objectives, BFO staff performed an overview of CI's operations. Included in this overview were limited tests and analysis in areas such as staffing, administrative costs and Board of Directors services. However, the primary emphasis of the audit was on the occupancy costs CI incurred through leases with a related party.

In auditing the occupancy costs, BFO staff interviewed representatives from CI's executive staff. We also reviewed accounting records, financial documents, mortgage and lease documents, settlement sheets, board minutes, and other pertinent data to the extent necessary to complete our objectives. Not all requested information was provided.

Fieldwork began with an entrance conference on July 14, 2004. The initial scope for the audit was the three year period ending June 30, 2004. The scope was expanded when fieldwork, and the lack of cooperation from CI management, suggested that the overcharges in occupancy costs may have resulted from fraud and/or abuse. The amount of the overcharges and the fact that CI and/or ISS had considerable cash holdings prompted us to extend our audit to the beginning date of the 4300 Regulations.

During the early stages of our fieldwork, the scope of our audit was impaired as we were denied access to certain requested information, including the ledgers and accounts of ISS. During this time, legal counsel representing both CI and ISS maintained that ISS and CI were not related parties, as defined in the 4300 Regulations. As a result, access to the books and records of ISS was denied. In addition, certain restrictions were imposed upon our fieldwork. In particular, all requests for information and/or documentation had to be made in writing to the aforementioned legal counsel. It was the legal counsel's decision as to whether the requested information was to be provided. The restrictions resulted in significant delays in our fieldwork. It also limited the BFO's ability to identify the actual costs associated with transactions between CI and ISS.

After trying for an extended period of time, it became evident that we could not complete the audit as planned under the imposed restrictions. Therefore, in late March 2005, we met with you and some of your senior staff to discuss our problems in completing the audit. You agreed to meet with CI management to facilitate the completion of our audit.

### **Objectives/Scope/Methodology (Continued)**

Following our meeting, progress on the audit was further delayed by the departure of the BFO's auditor in charge. Lack of available staff delayed a resumption of fieldwork to late 2005. Upon resumption of fieldwork, however, relations with CI and ISS staff improved greatly. While total access to ISS books and records was not granted, sufficient information and documentation was made available to enable us to complete the audit. In addition, CI and ISS management became noticeably more involved in assisting BFO staff to complete the audit process.

A closing conference was finally held on March 4, 2006. At the closing conference, CI management staff requested additional time to review the BFO's numbers and to provide additional documentation. Accordingly, several more meetings were held between BFO audit staff and CI/ISS management to clarify unresolved areas and discuss the proposed BFO draft report. The last of these meetings was held on August 7, 2006.

Governmental auditing standards require that auditors obtain an understanding of management controls that are relevant to the audit objectives described above. The applicable controls were examined to the extent necessary to provide reasonable assurance of compliance with generally accepted accounting principles. Based on the BFO's understanding of the controls, no significant deficiencies came to our attention other than those described in the issues included in this report. All fieldwork was performed in accordance with generally accepted government auditing standards. This report, when presented in its final form, is available for public inspection.

### **Results Of Fieldwork**

#### **Issue No. 1 - The CI Has Overcharged Delaware County \$401,272 For Occupancy Costs Through June 30, 2001**

A review of occupancy costs has disclosed that CI has overcharged Delaware County \$401,272 for rent expense. The costs in question relate to the period from July 1, 1987, through February 28, 2001.

The \$401,272 (Exhibit A) represents occupancy expenses in excess of actual costs that were charged to CI by ISS, its related party real estate holding company. For the period under audit, the ISS leased 20 residential program sites to CI, along with two administrative offices. The occupancy expenses were then passed on to Delaware County as rent.

### **Results Of Fieldwork (Continued)**

The leases for these properties required that CI pay for all occupancy expenses including but not limited to: rent, utilities, maintenance, and, taxes. According to the 4300 Regulations reimbursable rental costs passed on from a related party are limited to actual costs. Therefore, CI's rent charges to Delaware County should have been limited to the principal and interest owed on its mortgaged properties. Additional charges of up to 8% of the down payment could be reimbursed if non-county funds were used to satisfy down payments.

Through February 2001, all but one of the aforementioned 22 properties had mortgages. <sup>2</sup> Most were 15/5 year mortgages also known as balloon mortgages. Properties with 15/5 balloon mortgages need to be either paid off or refinanced after five years. These mortgages calculate interest payments over 15 years but require payment of the remaining balance after only five years. As a result, the balloon mortgages for the properties in question were refinanced several times.

To verify that CI's charges to the County were limited to actual costs, the BFO requested all pertinent financing documents for the 22 properties in question. These documents included but were not limited to: sales agreements; settlement sheets; mortgage documents; and, refinance materials including correspondence from lending institutions. With this material, the BFO verified the principal, interest, and down payment amounts allowable for rent between related parties. The BFO then compared these amounts to the amounts charged by CI.

In most instances, the amounts charged by ISS and passed on to Delaware County exceeded the expenses allowable per the 4300 Regulations. In total, the BFO determined that CI overcharged Delaware County \$401,272 for rents through June 30, 2001.

Representatives of CI disagreed that charges should be limited to actual costs. In particular, they believe that properties leased before the implementation of the 4300 Regulations on July 1, 1987, should be allowed to charge fair market rent even if leased from a related party. This position is not supported by the regulations.

The 4300 Regulations are very clear and specific that a related party is to be treated as if it were part of the provider for the determination and the reimbursement of costs. In this case reimbursable rent is limited to actual cost. Also, according to 4300.13.(b), *Related parties* identifies "control" as the most significant factor in determining if two parties are related. The BFO's audit confirmed that for both CI and ISS one individual had the ability to significantly influence or direct the actions or policies of both companies.

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<sup>2</sup> [For debt free properties, providers are allowed to negotiate up to 8% CPA in lieu of rent.]

## **Results Of Fieldwork (Continued)**

### **Recommendations**

The BFO recommends that the Delaware County MH/MR Program recapture the \$401,272 in question from the CI.

The BFO also recommends that CI abide by the 4300 Regulations and limit charges to Delaware County to actual costs on all related party rentals.

Finally, the BFO recommends that CI's management timely notify Delaware County programs of all dealings with related parties.

### **Issue No. 2 - CI Has Overcharged Delaware County \$316,466 In Occupancy Costs For The Forty Month Period Ended June 30, 2004**

CI overcharged Delaware County \$316,466 (Exhibit B) in occupancy costs for the 40 month period beginning March 1, 2001, and ending June 30, 2004. The overcharges resulted from CI inappropriately charging CPA in lieu of rent for the period March 1, 2001, through June 30, 2002, and then charging either CPA or rents based on "effective interest rates" (EIR) for the remaining two years.

During February 2001, ISS management used \$2,135,000 in bond proceeds to satisfy the mortgages on 21 properties leased to CI. [The Burmont Road site was debt free by this time and Germantown Pike was debt free by June 2001.] By satisfying the mortgages, ISS management took the position that as of March 1, 2001, the properties in question had become debt free and eligible for CPA in lieu of rent. Accordingly, at this time CI began charging occupancy costs to Delaware County based upon the CPA calculated by ISS.

The CPA charged for each property was equal to 8% of the total of its purchase price, along with the renovations and improvements booked by ISS. As of July 1, 2001, CI had calculated annual rent based on CPA to be \$369,531 for the 22 properties (see Exhibit C).

Then, in July 2002, CI's management inexplicably changed from charging rent based on CPA for many of the properties and began charging rent based on what it had determined was an (EIR). The EIR's were calculated by taking weighted averages of all the various interest rates the properties had while under mortgage. In a number of cases the rents charged using the EIR were higher than those based on CPA. However, in some the rents were lower. Overall, the total rent charged using the EIR was very similar to the CPA. Combined with the CPA, the total occupancy costs charged by CI for the 40 months ended June 30, 2004, totaled \$1,233,722 (Exhibit B).

### **Results Of Fieldwork (Continued)**

However, the BFO completely disagrees with the position that the properties in question were debt free. In accordance with generally accepted accounting principles, an issuance of bonds is treated as long term debt. Therefore, CI's decision to use the proceeds from the bond issuance to satisfy existing mortgages merely resulted in an exchange of one debt instrument for another.

In addition, ISS management was required to put the respective properties up as collateral for the bonds. For the ISS to sell any of the properties or remove any of them as collateral, a payment(s) had to be made to the bank underwriting the bonds. The payment(s) would be calculated based on the proportionate share of the bonds used to pay off the respective mortgage debt. [A list of the properties and their respective shares of the bond debt is attached as Exhibit F].

Finally, while the ISS no longer had mortgage debt on the properties in question, it had bond debt totaling \$2,135,000.

Accordingly, it is the BFO's position that the exchange of mortgage debt for bond debt did not render the respective properties debt free. As such, CI's decision to charge CPA and/or rent based on an EIR is inappropriate and not in accordance with the 4300 Regulations. As ISS was a related party for the period under audit, CI was limited to charging only actual costs to Delaware County.

In this case, the occupancy (rent) costs for the period March 1, 2001, through June 30, 2004, must be limited to ISS's actual costs of financing the bond debt. In reviewing the ISS' bond costs for the period in question, the BFO has determined that CI had legitimate bond expenses totaling \$754,204 for period in question. This included bond principal and interest costs, origination fees, annual fees, and interest hedge fees. In addition, two properties, Burmont Road and Germantown Pike were debt free and eligible for CPA calculated by the BFO to be \$43,040. The BFO has also allowed an 8% allowance for down payments paid for with CI funds. For the period in question, the 8% for the down payments totaled \$120,012. Accordingly, total occupancy costs eligible for reimbursement for the 40 month period were \$917,256. When compared to the \$1,233,722 charged, the CI overcharged Delaware County \$316,466 for the 40 month period ended June 30, 2004.

### **Recommendations**

The BFO recommends that the Delaware County MH/MR Program recapture the \$316,466 overcharged as occupancy costs since July 2001.

The BFO also recommends that CI's management acknowledge that the bond issuance did not render the properties debt free. Mortgage debt was merely exchanged for bond debt.

### **Results Of Fieldwork (Continued)**

Finally, the BFO recommends that CI be limited to charging the total annual bond debt expenses as rent for the properties secured by the bonds. CI should maintain complete and accurate documentation of all expenses associated with the bond issuance.

### **Issue No. 3 - A Majority Of The Renovation/Improvement Costs Reported By CI Should Be Classified As Repairs/Maintenance And Not Be Included In The Calculation Of CPA**

A review of the renovation/improvement expenses compiled by CI disclosed that up to 85% of these costs do not meet the criteria established in their definition in the 4300 Regulations. As such, those costs failing to meet the criteria should not be included in any calculation of CPA charged in lieu of rent for debt free properties.

As per the 4300 Regulations [Section 4300.87 (c)(2)(vii) ] : "The Department will reimburse a CPA for the use of space in debt free real estate. The CPA may not exceed an amount equal to 8% of return on the total of the property value plus the cost of renovations and improvements to the property."

Section 4300.87(2)(d) then defines renovations, improvements and repairs as: "Renovations are considered to be the adaptation of available space within a completed structure. Improvements extend the life or increase the productivity of the asset. Repairs and maintenance are considered to be those activities which either restore an asset to, or maintain it at, it's normal or expected service life."

The 4300 Regulations, as drafted, attempt to assure that both providers and county programs are treated fairly concerning property costs. In doing so, the regulations allow county programs to acknowledge adaptations made to properties that permanently alter their physical appearance and increase their value. This acknowledgement is made in part by including such renovation/improvement costs in the calculation of CPA.

According to CI's records, total renovation/improvement costs from the period 1984 through June 30, 2004, total \$1,117,943. This does not include \$305,361 in additional renovation/improvement costs reportedly incurred in CI's Woodland Avenue (Springfield) administrative offices. However, the BFO contends that this number is greatly exaggerated. A review of the descriptions of the reported renovations/improvements indicated that most did not meet the criteria established in the 4300 Regulations. Instead, most were for repair/maintenance costs one would expect to incur in the normal course of business. Among these costs were: blacktop sealer, paint, gardening supplies, door locks, and many other everyday repair/maintenance items. Many were for very small amounts. Accordingly, after carefully evaluating the reported renovations/improvements, the BFO identified only \$163,784 in expenses that we could classify as renovations/improvements.

### **Results Of Fieldwork (Continued)**

As discussed in Issue No. 2, ISS management considered the properties leased to CI as debt free with the issuance of the IDA bonds in February 2001. Based on this interpretation, management considered it appropriate to charge the 8% CPA allowed in the 4300 Regulations in lieu of rent. In doing so, CI charged Delaware County \$369,531 in CPA for the year ended June 30, 2002. As previously stated the BFO considered these charges to be inappropriate as the properties in question were not debt free. If, however, the properties were debt free, the CI's calculation of CPA would be significantly overstated because of the excessive renovations/improvements reported. The BFO estimates allowable CPA for this period to be \$280,835, (see Exhibit D) or \$88,696 less than the amount calculated by CI.

CI's management disagrees with the BFO's assessment. While they concede that some of the items in the ledgers should not have been listed as renovation/improvement costs, they disagree with our estimate of 85%.

### **Recommendations**

The BFO recommends that CI's and ISS management carefully review its procedures for identifying and reporting renovation/improvement costs. Only those costs incurred in permanent adaptations to properties should be considered renovation/improvement costs.

The BFO also recommends that CI review its current ledger of renovation/improvement costs and delete many of the costs which do not meet the DPW's definition of such costs.

The BFO further recommends that at the appropriate time, CI redo its CPA calculations including only those costs allowed by the 4300 Regulations.

Finally, the BFO also recommends that Delaware County's MH/MR Program carefully review any CPA requests made by CI when the properties used in Delaware County's programs become debt free. Any renovation/improvement costs included in the CPA calculation must meet the aforementioned definition.

### **Issue No. 4 - CI Has Not Properly Accounted For And/Or Documented The Costs Reported As Renovation/Improvements**

CI has not properly accounted for and/or documented its renovation/improvement costs. Our review disclosed that CI does not have supporting documentation (i.e. invoices, receipts) for all years up to June 30, 1997. In addition, many of the receipts/invoices maintained since then do not sufficiently document what particular renovations were made, or to which property they were made.

### **Results Of Fieldwork (Continued)**

Of the aforementioned \$1,117,943 in renovation/improvement costs [not including the \$305,361 charged to the Woodland Avenue office] \$567,576 or approximately 50%, were reportedly made before July 1, 1997. CI's management claims that they do not have any receipts/invoices associated with these costs. They stated that company policy was to retain records for only seven years.

In addition, some of the receipts and or invoices available for the costs incurred since July 1, 1997, do not adequately document that the costs were incurred. A review of the receipts/invoices on file at CI disclosed that some invoices/receipts were handwritten on blank pieces of paper. Others were price quotes obtained from vendors. Yet still others were receipts detailing long lists of supplies and materials purchased from building supply retailers. Although these lists indicated that provider funds were spent for building materials, they could not, in most cases, document that the materials were used for renovations and or improvements. Many were materials used in routine repair and maintenance work.

The 4300 Regulations are clear in requiring that costs included in the calculation of CPA be documented. The BFO contends that the documentation should be time and place specific and clearly identify the renovation/improvement completed. Furthermore, documentation for all renovation/improvement costs used in the calculation of CPA should be maintained regardless how long ago the costs were incurred. Section 4300.87(c)(2)(vii) specifically states that: "...The costs of renovations or improvements shall be the documented actual costs of the renovation or improvement at the time of its completion."

The management of CI contends that the ledgers they have maintained with renovation/improvement costs constitute documentation. Furthermore, they contend that retaining receipts and invoices from day one for all renovation/improvement costs is impractical. They contend that seven years is a reasonable limit for providers to be expected to retain receipts/invoices.

Section 4300.87 was developed to ensure that providers requesting CPA provide reasonable assurance that the renovations/improvements included in the CPA were incurred at the time and place reported. If county programs are going to pay CPA, they need to be reasonably assured that any renovation/improvement costs included in the CPA accurately reflect the work done to the properties. It is the BFO's position that CI's renovation/improvement ledgers, by themselves, do not adequately document these costs. The BFO contends that these ledgers merely provide brief descriptions of costs which may or may not have been incurred as reported in the ledger.

## **Results Of Fieldwork (Continued)**

### **Recommendations**

The BFO recommends that the management of CI maintain documentation for all renovation/improvement costs to be considered in the calculation of CPA. The documentation should specifically address the nature of the work performed, the people who performed the work, and the date and location of the work performed.

The BFO also recommends that the management of CI retain all such receipts/invoices for all costs to be included in CPA, regardless of the time period involved.

### **Issue No. 5 – The Purchase Price And Down Payment Amounts Claimed By CI For Its Springfield Administrative Offices Differ From The Amounts Obtained By The BFO**

The purchase price and the amount considered as down payment on the CI's Springfield (Woodland Road) administrative offices site differ significantly from the amounts obtained by the BFO when reviewing source documents. These differences need to be resolved as purchase price and down payment amounts directly affect the rent and CPA eligible for reimbursement.

In determining the amounts eligible for rent, the BFO examined source documents for all the properties CI leased from ISS. These documents included settlement sheets, mortgages, and title search documents. The amounts obtained from the source documents were then compared to the amounts maintained in CI's records.

For the Springfield site, CI's records listed the purchase price as \$495,361, with an additional \$47,547 in renovations. The Springfield settlement sheet, however, listed the sales price at \$190,000, while the mortgage taken by CI was for \$240,000.

Discussions with CI management disclosed that the purchase price was \$190,000 in 1997 when the building was first purchased. However, management claimed that the building purchased was empty for nearly five years and needed extensive renovations and reconfigurations to become a suitable office building. Accordingly, the additional \$50,000 in the mortgage was taken for the initial renovations. CI management further claimed that over the two year period ending June 30, 1998, CI and ISS put an additional \$300,000 in renovations into the building.

CI management then stated that the \$495,361 purchase price was actually the \$190,000 plus the additional \$305,361 in renovations. CI's management stated that they considered the \$303,361 in renovations to be down payment money, claiming that the renovations were necessary to get the building suitable for use. However, CI's interpretation raises several important questions.

### **Results Of Fieldwork (Continued)**

First, down payment money can be considered in determining allowable rent for buildings leased from related parties. Along with principal and interest expense, an 8% return on provider funded down payments is allowable for reimbursement. However, renovation expense, while included in CPA calculations, can not be included when determining rent from a related party. For CI, it was obviously in their interest to interpret the money claimed as "renovations" to be down payment money. By doing so, they were able to increase what would have been allowable principal and interest expense of approximately \$1,953 per month to the \$2,871 charged.

Second, while the CI's management claimed the "renovations" were necessary to get the building useful, records indicate that CI started charging rent [at \$2871 per month] for the site in July 1997. According to the renovation/improvements ledger maintained by CI, approximately half of the \$305,361 in "renovations" were not yet completed as of this date.

Third, as presented in Issues 3 and 4, CI had problems in maintaining adequate documentation for the renovation/improvements charged to its program sites. A detailed review of the \$305,361 charged as "renovations" for the Springfield site disclosed numerous questionable entries. Many were for small, ordinary items. Many other entries were identified as "miscellaneous maintenance supplies."

In addition, the BFO had problems with some of the individual receipts associated with the work performed on the Springfield site. Some of the receipts were inadequate and lacked proper headings and detail. Still others identified "renovation" work done on other program sites that was billed to the Springfield site. [Management claimed that these costs were charged to Springfield to facilitate billing for the materials.]

And fourth, the BFO had difficulty in determining whose money was actually used for the "renovations" in question. CI management agreed to provide documentation for the \$305,361. Management claimed that CI and ISS contributed \$196,000 in cash. \$80,000 was documented in a check from ISS to CI. However, the remaining \$116,000 was not adequately accounted for. A detail of the #575 account data submitted for the period in question appears to indicate that \$65,561 was charged to Delaware County. Other offsetting income totaling approximately \$41,000 appears to be income which should have been used as an offset to county funds. As 8% of the \$196,000 was submitted as allowable rent expense, the failure to document the \$116,000 is relevant.

Taking everything into consideration, the BFO finds it difficult to accept the \$305,361 as down payment funding eligible for an 8% return as rent. To be considered as down payment money we felt that CI had to prove both that its interpretation of using renovation costs as down payment was reasonable, and that the money for the renovations came from CI. We feel that CI's records fail to do this. In our opinion, the records do not adequately identify what work was actually performed. That the work

### **Results Of Fieldwork (Continued)**

met the criteria for renovations/improvements as compared to repairs/maintenance, and above all, that it was CI's money that was used for the work. We did accept the \$80,000 from ISS as down payment funds. We also included an additional \$79,942 in renovation costs that we felt met the criteria established in the 4300 Regulations for renovations/improvements.

Subsequent Event – During recently completed field work, which included meetings with CI staff, the BFO learned of several transactions involving properties initially financed with the IDA bond proceeds. Several of the properties, including the Springfield site in question, were apparently sold by ISS. A search of Delaware County courthouse records indicated that the Springfield site was sold by ISS to a family business operated by the founder of both CI and ISS. The records indicated that the property was sold for \$390,032 during 2004, but after the June 30, 2004, scope of our audit. The relatively low purchase price causes further concern over the legitimacy of the CI's claim that over \$500,000 was put into the purchase and renovation of the building.

In addition, since the release of the draft report, the BFO learned that variances between CI's listed purchase prices for the Burmont and Germantown Pike sites and official purchase documents resulted from CI's management claiming that early renovations on those sites should also be considered down payments. If treated as down payments the costs would be eligible for 8% allowances to be added to the rent calculations. In both cases CI's treatment of these renovations as down payments significantly increased the rents charged by to Delaware County. However, as both sites were obtained long before July 1, 1997, CI management has no documentation to verify that the costs, as reported, were actually incurred. They can also not verify that the costs were necessary to get the sites operational whereby they might be considered to be "down payments." Finally, CI has no records to verify that the "down payments" in question were CI funded. As such, the BFO does not accept them as down payment costs and did not consider them in the calculation of either rent or CPA.

### **Recommendations**

The BFO recommends that CI adjust the purchase price and down payment amounts it has recorded for its Springfield site. The \$495,361 listed the purchase price should be adjusted to reflect the \$190,000 listed on the settlement sheet.

The BFO also recommends that Delaware County, when applicable, recognize only the \$193,694 in purchase and settlement costs as the price of the Springfield site. In addition, only the \$80,000 supplied by ISS should be considered down payment funding eligible for 8% return on provider investment.

### **Results Of Fieldwork (Continued)**

Finally, the BFO recommends that Delaware County officials request that CI officials explain why the building with a book value of over \$500,000, which was used to charge the county CPA of \$2,871 per month, was sold to the founder of the company for \$390,032.

### **Issue No. 6 - CI Overcharged Delaware County \$108,475 For A Disproportionate Share Of Expenses For Two Vacation Homes Used By Consumers In Their Programs**

The review of occupancy expenses disclosed that for the seven year period ending June 30, 2004, CI overcharged Delaware County \$108,475 for the use of vacation homes by consumers in their programs (Exhibit E). The overcharge resulted from CI charging consumers rent for their use of the vacation homes while also charging Delaware County recreation expense for costs incurred in operating the homes. In addition, while CI failed to collect much of the rent due for the use of the homes, it appears that of the rent collected, a disproportionate share came from the consumers.

The properties in question are in the Pocono Mountains and Cape May, New Jersey.<sup>3</sup> During March of each year, consumers were given the opportunity to reserve up to seven days at either of the homes. Depending on the time of year, consumers were charged up to \$130 a night for use of the Cape May home and \$75 a night for the Pocono home. Although the consumers were given preference in using the homes, CI employees and board members also shared in their usage.

To determine if the amounts charged to the consumers were equitable, we reviewed the rents charged for the year ending June 30, 2003. In the review, we compared the number of days consumers used either home to the number of days used by staff and board members. Similarly, the review compared the amount of rent collected from consumers to that collected from staff and board members.

The records available disclosed that for the period in question, the consumers' use of the homes was disproportionately low. The review disclosed that the Cape May home was used for 182 days. Of these 182 days, the consumers used 37, or slightly over 20%. The Pocono home for the same period was used only 96 days with only 7, or less than 8%, being consumer days.

Furthermore, it appears that the consumers paid a disproportionate share of the rent. For the Cape May home for the period in question, a total of \$14,980 in rent was collected of which \$4,164 or slightly less than 28% came from consumers. For the Pocono home, only \$2,110 in rent was collected of which \$1,000, or about 47%, came from consumers.

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<sup>3</sup> [The Pocono home was sold during the BFO's fieldwork.]

### **Results of Fieldwork (Continued)**

In total, the records maintained by CI for these properties showed that \$27,185 in rent was due from both properties for the periods in question. Similarly, the records showed that only \$17,090, or 63%, was collected. But, of the amount due, only \$5,315 was due from consumers. Records indicate, however, that consumers contributed \$5,164 or 97% this amount. Therefore, a vast majority of the uncollected rent seems to be attributed to days used by non-consumers.

In addition, the CI reported that the homes incurred operating losses. To compensate for these losses, CI charged recreation expense to Delaware County in addition to the rents charged to the consumers. For the year ended June 30, 2003, CI's available records indicate that \$5,760 was charged for the Pocono home and \$9,452 for the Cape May home. When added to the rent (\$5,164), Delaware County was charged \$20,376 for the consumers' use of the two properties for the year in question. This averages out to \$463 per night.

For the year in question, the Pocono home was used only 96 days or 26% of the year. However, along with the low usage, CI collected only \$2,110 of the \$5,725 (37%) of the rent due. Furthermore, while the Cape May home was used a more reasonable 182 days, only \$14,980 of the \$21,460 (70%) rent due was collected. If CI increased the number of days the homes were used and did a better job in collecting rent, the homes could have operated without losses. Considering that the rents charged appear to be equitable to both parties, the BFO feels that it is not Delaware County's responsibility to make up for any losses that CI incurs in operating the homes.

Records indicate that for the seven years ended June 30, 2004, CI charged Delaware County \$108,475 in recreation expense. This is in addition to any rents collected from consumers.

We must note that the records maintained by CI for the year in question were less than adequate. The number of days that the homes were used was derived from a calendar. CI staff used the calendar to record when reservations were made by either consumers or others. CI management claims that the reservations were sometimes cancelled or changed without CI staff noting it on the calendar. CI management also claimed that staff often used the homes rent free in lieu of overtime pay for accompanying consumers.

The BFO agrees that the records provided may not reflect the actual usage of the homes in question. In particular, the BFO's inability to reconcile the rent collected to the dates of usage seems to indicate that variances exist in the CI's records. It is management's responsibility to maintain reliable and accurate records.

## **Results of Fieldwork (Continued)**

### **Recommendations**

The BFO recommends that Delaware County recapture the \$108,475 in question for the seven year period ending June 30, 2003. Accordingly, the BFO recommends that the OMR and the OMHSAS adjust the County's carryover accordingly.

The BFO also recommends that CI refrain from charging recreation expense to Delaware County when rent is being charged for the consumers' use of the vacation home still in use.

### **Observation - CI Is Registered As A Not-For-Profit Corporation But Still Has Shareholders In Control**

When CI was created in 1973, it was organized as a for-profit corporation on a stock basis. There were five shareholders. Two shareholders owned 47% and three others owned 2% respectively. All received one vote per share. Then in May 1975, the corporation was converted to a not-for-profit corporation. The shares were carried over to the not-for-profit with only two shareholders, one owning 51% and the other owning 49%.

The by-laws of the not-for-profit corporation required a board of directors with seven elected directors. These elected directors were given the power to manage, conduct, control, and direct CI in its mission. Each board member received one vote.

However, according to CI's by-laws, the two shareholders have a vote equal to any board member's when attending board meetings. More importantly, the shareholders have the ability to assign and remove board members. To remove a board member, all that is needed is a majority of the shareholder vote. With this ability, the shareholders actually have more influence and/or control than the board members. This is contrary to the way most not-for-profits are organized and operate.

It is the BFO's position that the shareholders ability to control the make-up of the board is counter-productive to CI's stated mission as a not-for-profit service provider. The shareholders possess undue influence. This can create problems for the organization as board members can be forced to execute in the interest of the shareholders, rather than in the interest of the organization and its consumers. It also promotes an unequal environment as the shareholders, who is not necessarily board members, are still allowed a vote if present at a board meeting.

It was noted in the minutes of a board meeting in the fall of 2005 that CI planned to change its organization. Shareholders would be replaced with the term certificate holders. Board members would also be certificate holders as well. However, the number of certificates held by each member was determined by the former

### **Results Of Fieldwork (Continued)**

shareholders. As such, as far as the BFO can determine, the same individuals still control the corporation. Although the language contained within the by-laws has been changed, the meaning behind the language is still the same and carries with it the same rights.

It is the BFO's position that the certificates and/or shares of a not-for-profit company should be retained by people independent of the company's operation. Control of most not-for-profits rests with the board of directors. By amending its corporation's by-laws and removing the aforementioned certificates from people involved in the company's day to day operations. CI can put the board of directors back in control of the company. CI needs a board of directors which can operate free of any undue influence. In doing so, CI will have a board of directors operating in the best interests of the company and the consumers it serves.

### **Exit Conference/Auditee's Response/Auditor's Commentary**

At the request of CI's management, an exit conference was held for this audit on January 31, 2007. In attendance, along with BFO and CI staff, were representatives of your Southeast Regional Office and Delaware County's MH/MR Program. Also in attendance were legal representation for both CI and ISS. During the conference, the auditee's written response, attached as an "Appendix" to this report, was discussed in detail.

Among other things, CI's response takes issue with the scope of our audit and the resultant overcharges presented in Exhibits A , B, and E. The response also questions our methodology for calculating CPA and our claim that CI management must be able to fully document all costs included in any CPA or rent calculations. To assure clarity, the BFO feels it is necessary to include the following comments concerning the auditee's response:

- As discussed in the Scope Section of this report, the BFO's scope for this audit was expanded due to concerns that fraud and/or abuse may have been involved in the charges ISS made to CI for occupancy costs.
- The large cash reserves held by ISS, along with the lack of evidence to suggest that management used the overcharges to benefit DPW consumers, prompted the BFO to review all occupancy charges back to the inception of the 4300 Regulations.
- The BFO does not take the position that all books and records must be kept beyond the county requirement of six years. The BFO is primarily concerned with the costs included in the calculation of CPA. As the participation in CPA is at the county's discretion, the BFO maintains that all pertinent documentation for renovation/improvement work, along with the respective costs, be maintained for

**Exit Conference/Auditee's Response/Auditor's Commentary (Continued)**

the periods being claimed for CPA. Without such documentation, the BFO maintains that it will be difficult for the county to determine if the renovations/improvements were in fact made and if the resultant costs were reasonable and appropriate.

- The BFO contends that the majority of renovation/improvement costs compiled by CI do not meet the criteria established in the 4300 Regulations and should not be included in the calculation of CPA. The BFO questions if, as presented in CI's response, it is reasonable to suggest that replacing a \$200 toilet is a renovation that qualifies for an 8% charge every year forward.
- Similarly, the BFO questions several instances [Burmont, Germantown Pike, and Springfield] were CI claims that reported renovation/improvement cost should be treated as down payments and be eligible for 8% allowances. For most of these costs insufficient documentation exists to support any of CI's claims.
- The major differences existing between the BFO and CI in the amount of the overcharges presented in Exhibits A and B are due primarily to two factors. The first concerns undocumented, early renovation/improvement costs listed for the Burmont and Germantown Pike (Lafayette Hill) sites. The costs, incurred before July 1, 1997, are undocumented and the source of the money used to fund these costs is unknown. CI management claims the costs were necessary to get the sites operational and should be considered down payments. The BFO claims it is unreasonable to expect a county to accept undocumented renovation costs as down payments and to pay 8% allowances annually on these costs. [The difference in the overcharge for the Springfield (Woodland Avenue) site was significantly reduced by the BFO accepting only \$80,000 (amount of non taxpayer dollars that could be verified) in renovation costs as down payment funding by CI.]
- The second major factor is the inclusion by CI of additional principal payments in their calculation of eligible bond costs for the period ending June 30, 2004 (Exhibit B). The BFO claims that ISS's decision to amend its original bond repayment schedule was made possible in part by the overcharges ISS made to CI. As county representatives were not aware of the overcharges and were not consulted as to ISS's use of these funds to amend their repayment schedule, the BFO maintains that they should not be accepted as eligible costs.
- Concerning the vacation properties, the BFO maintains that had all of the parties using the sites paid the rates charged by CI, little or no deficits would have occurred. The BFO does not feel the county should have to pay for costs which may have resulted from poor management and/or poor decisions.
- While CI's management now acknowledges that ISS is a related party, their position until the latter stages of fieldwork was different. Until then CI's legal representative maintained that according to his interpretation of the 4300 Regulations ISS was not related. The BFO has letters from CI's legal representative stating this claim.

Mr. Kevin T. Casey  
Ms. Joan L. Erney

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**Exit Conference/Auditee's Response/Auditor's Commentary (Continued)**

- Finally, the BFO maintains as valid its opinion that the stock certificate holders possess undue influence over the board of directors. CI's reported compliance with Not For Profit law does not change this opinion.

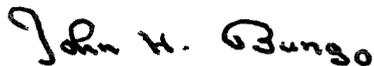
**Conclusion**

In conclusion, the BFO maintains that CI inappropriately overcharged Delaware County for occupancy costs since the program's inception. The overcharges resulted in significant cash reserves for ISS [over \$2,000,000 as of our audit]. Furthermore, the BFO claims that the overcharges were not used to benefit DPW consumers. Accordingly, the BFO maintains that Delaware County's MH/MR Program should recapture the \$826,213 in overcharges presented in the six issues in this report.

In accordance with our established procedures, please provide a response within 60 days to the Audit Resolution Section concerning actions to be taken to ensure that the report recommendations are implemented. In addition, the response should include the OMR and OMHSAS position on the issues and an observation included in the report. Any additional clarification or assistance can be provided by the BFO upon request.

Please contact Richard J. Polek, Audit Resolution Section, at (717) 787-8890 if you have any questions concerning this matter.

Sincerely,



John H. Bungo, CGFM, CFS

Attachments

cc: Ms. Robyn Zippilli  
Ms. Dorothy Klein  
Ms. Lynne Baumeister  
Ms. Michael Stauffer  
Ms. Vicki Stillman-Toomey  
Mr. Joseph Church  
Ms. Elizabeth Zeisloft

## EXHIBITS

**COMMUNITY INTERACTIONS, INC.  
SCHEDULE OF OCCUPANCY OVERPAYMENT  
FOR THE PERIOD JULY 1, 1987 THROUGH FEBRUARY 28, 2001**

<u>Property</u>	<u>Occupancy Allowable</u>	<u>Occupancy Charged</u>	<u>Net Overpayment</u>
Garrett	214,725	270,208	( 55,483)
Morton	145,615	191,862	( 46,247)
Whitney	159,596	184,470	( 24,874)
Ridley Park	167,751	187,288	( 19,537)
Cedar	246,854	284,000	( 37,146)
Bridge	159,334	182,532	( 23,198)
Burmont	147,050	262,400	(115,350)
War Trophy	124,640	138,000	( 13,360)
Orange	273,697	238,290	35,407
Olympic	121,850	122,310	( 460)
Bridgewater	98,516	100,056	( 1,540)
Brookthorpe	-	-	-
Crawford	78,952	85,100	( 6,148)
Dorchester	94,352	102,268	( 7,916)
Robbins	62,455	57,387	5,068
Gov. Markham	50,766	61,594	( 10,828)
*Verona	17,670	17,600	70
Locksley	-	-	-
*Bullens	18,003	13,914	4,089
*Brookside	15,781	16,700	( 919)
Springfield	125,864	134,937	( 9,073)
Germantown	<u>133,797</u>	<u>207,624</u>	<u>( 73,827)</u>
<b>Total</b>	<b><u>\$2,457,268</u></b>	<b><u>\$2,858,540</u></b>	<b><u>\$( 401,272)</u></b>

\* Mental Health Programs; all others: Mental Retardation Programs

**NOTE:** Of the \$401,272 overpayment, \$193,285 is for the period 7/01/1987 through 6/30/1997, and \$207,987 is for the period 7/01/1997 through 2/28/2001.

EXHIBIT A

**COMMUNITY INTERACTIONS, INC.  
SCHEDULE OF OCCUPANCY OVERPAYMENT  
FOR THE PERIOD MARCH 1, 2001 THROUGH JUNE 30, 2004**

<u>Property</u>	<u>Rent Charged By CI</u>		
Garrett	72,546		
Morton	45,372		
Whitney	32,120		
Ridley Park	39,920		
Cedar	51,480		
Bridge	42,620		
War Trophy	56,098		
Orange	78,404		
Olympic	50,748		
Bridgewater	42,372		
Brookthorpe	62,240		
Crawford	41,268		
Dorchester	49,364		
Robbins	46,524		
Gov. Markham	52,240		
*Verona	52,364		
Locksley	65,312		
*Bullens	44,328		
*Brookside	48,544		
Springfield	148,648		
		1,122,512	
Add: Burmont	54,988		
Germantown Pike	56,222	<u>111,210</u>	
			1,233,722
Less: Bond Costs:			
Principal & Interest	(548,210)		
Origination Fees	(146,251)		
Annual Fees	( 59,743)	( 754,204)	
Less: CPA Allowances:			
Burmont	( 23,800)		
Germantown	( 19,240)	( 43,040)	
Less: 8% Down Payments		<u>( 120,012)</u>	
			<u>( 917,256)</u>
Excess Rent Charged			<u>316,466</u>

\* Mental Health Programs, all other Mental Retardation Programs

**EXHIBIT B**

**COMMUNITY INTERACTIONS, INC.  
SCHEDULE OF CONTINUING PARTICIPATION ALLOWANCE (CPA), AS  
CALCULATED BY COMMUNITY INTERACTIONS, AS OF JULY 1, 2001**

<u>Property</u>	<u>Acquisition (Selling Price Settlement Costs)</u>	<u>Renovations</u>	<u>** Total</u>	<u>** Annual CPA</u>
Garrett	\$141,006	\$133,506	\$274,512	\$21,961
Morton	135,798	32,437	168,235	13,459
Whitney	92,338	28,123	120,461	9,637
Ridley Park	112,500	37,188	149,688	11,975
Cedar	161,377	31,633	193,010	15,441
Bridge	105,677	56,634	162,311	12,985
Burmout	110,250	97,269	207,519	16,602
War Trophy	167,850	34,242	202,092	16,167
Orange	218,141	35,372	253,513	20,281
Olympic	153,925	29,787	183,712	14,697
Bridgewater	128,799	17,704	146,503	11,720
Brookthorpe	233,500	15,286	248,786	19,903
Crawford	117,365	9,434	126,799	10,144
Dorchester	141,849	32,085	173,934	13,915
Robbins	158,746	27,998	186,744	14,940
Gov. Markham	179,850	60,286	240,136	19,211
*Verona	141,782	15,015	156,797	12,544
Locksley	244,608	14,144	258,752	20,700
*Bullens	173,199	23,883	197,082	15,767
*Brookside	183,364	31,333	214,697	17,176
Springfield	193,694	346,004	539,698	43,176
Germantown	<u>135,915</u>	<u>78,214</u>	<u>214,129</u>	<u>17,130</u>
<b>Totals</b>	<u>\$3,431,533</u>	<u>\$1,187,577</u>	<u>\$4,619,110</u>	<u>\$369,531</u>

\* Mental Health Programs, all other Mental Retardation Programs

\*\* CPA derived by multiplying the amount in Total column by 8%

**COMMUNITY INTERACTIONS, INC.**  
**SCHEDULE OF CONTINUING PARTICIPATION ALLOWANCE (CPA), AS**  
**CALCULATED BY THE BFO, AS OF JUNE 30, 2003**

<u>Property</u>	<u>Acquisition (Selling Price Settlement Costs)</u>	<u>Renovations</u>	<u>** Total</u>	<u>** Annual CPA</u>
Garrett	\$141,006	13,705	\$154,711	\$12,377
Morton	135,798	4,830	140,628	11,250
Whitney	92,338	-	92,338	7,387
Ridley Park	112,500	8,925	121,425	9,714
Cedar	161,377	2,300	163,677	13,094
Bridge	105,677	3,960	109,637	8,771
Burmont	89,195	-	89,195	7,136
War Trophy	167,850	-	167,850	13,428
Orange	218,141	-	218,141	17,451
Olympic	153,925	4,665	158,590	12,687
Bridgewater	128,799	-	128,799	10,304
Brookthorpe	233,500	12,000	245,500	19,640
Crawford	117,365	-	117,365	9,389
Dorchester	141,849	-	141,849	11,348
Robbins	158,746	3,600	162,346	12,988
Gov. Markham	179,850	5,667	185,517	14,841
*Verona	141,782	-	141,782	11,343
Locksley	244,608	5,650	250,258	20,021
*Bullens	173,199	6,800	179,999	14,400
*Brookside	183,364	11,740	195,104	15,608
Springfield	193,694	79,942	273,636	21,891
Germantown	<u>72,090</u>	<u>-</u>	<u>72,090</u>	<u>5,767</u>
<b>Total</b>	<b><u>\$3,346,653</u></b>	<b><u>\$163,784</u></b>	<b><u>\$3,510,437</u></b>	<b><u>\$280,835</u></b>

\* Mental Health Programs, all other Mental Retardation Programs

\*\* CPA derived by multiplying the amount in Total column by 8%

EXHIBIT D

**COMMUNITY INTERACTIONS, INC.  
SUMMARY OF VACATION PROPERTY EXPENSES  
CHARGED TO THE DPW**

<u>Fiscal Year</u>	<u>Pocono</u>	<u>Cape May</u>	<u>Total</u>
07/1997-06/1998	\$ 8,160	\$ -	\$ 8,160
07/1998-06/1999	14,052	-	14,052
07/1999-06/2000	11,483	-	11,483
07/2000 -06/2001	8,912	10,997	19,909
07/2001-06/2002	7,435	12,060	19,495
07/2002-06/2003	5,760	9,452	15,212
07/2003-06/2004	<u>6,373</u>	<u>13,791</u>	<u>20,164</u>
<b>Total</b>	<b><u>\$62,175</u></b>	<b><u>\$46,300</u></b>	<b><u>\$108,475</u></b>

EXHIBIT E

**COMMUNITY INTERACTIONS, INC.  
SCHEDULE OF PROPERTIES PLACED AS COLLATERAL  
FOR THE IDA BONDS AS OF FEBRUARY, 2001**

<u>Property</u>	<u>% Of Bonds</u>
Garrett	1.38%
Morton	1.88%
Whitney	1.30%
Ridley Park	1.39%
Cedar	2.18%
Bridge	1.37%
War Trophy	4.64%
Orange	3.32%
Olympic	4.25%
Bridgewater	3.64%
Brookthorpe	8.59%
Crawford	4.10%
Dorchester	3.38%
Robbins	4.86%
Gov. Markham	6.05%
*Verona	6.25%
Locksley	9.65%
*Bullens	5.90%
*Brookside	6.32%
Springfield	10.82%
Tennyson	2.91%
Future Purchases	<u>5.82%</u>
<b>Total</b>	<u><u>100%</u></u>

\* Mental Health Programs, all other Mental Retardation Programs

**AUDITEE'S RESPONSE  
APPENDIX**



## COMMUNITY INTERACTIONS, INC.

March 2, 2007

John H. Bungo, CGFM, CFS  
Director, Bureau of Financial Operations  
Third Floor, Bertolino Building  
Harrisburg, PA 17105-2675

**Re: Response By Community Interactions, Inc. To The Bureau of Financial  
Operations Draft Audit Report**

Dear Mr. Bungo:

I enclose the response by Community Interactions, Inc. to the draft audit report by the Bureau of Financial Operations which addresses occupancy costs incurred by Community Interactions, Inc. through June 30, 2004.

I thank you for providing this opportunity to comment.

Sincerely,

Robyn A. Zippilli  
Executive Director/CEO  
Community Interactions, Inc.

cc:	Dorothy Klein	Thomas Crofcheck
	Michael Stauffer	Stan Futrick
	Kevin Casey	William Lenahan
	Joan Erney	Stephen Durham
	Vicki Stillman-Toomey	Charles Barto
	Lynne Baumeister	Betty MacLeod
	Joseph Church	Gary Clift
	Elizabeth Zeisloft	

321 West Woodland Avenue Springfield, PA 19064 610-328-9008 Fax: 610-328-4597

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"Your Life... Your Choice... Our Mission"

Appendix  
Page 1 of 13

## **Introduction**

Community Interactions (“CI”) has received the draft audit report as prepared by the Division of Audit and Review of the Bureau of Financial Operations (“BFO”) and provides this response to the findings of the draft audit. Our response and concerns are limited to the crucial points of the draft audit that we believe should be addressed at the exit conference.

### **Scope of the Draft Audit**

First, the work statement of the scope of the draft audit needs to be clarified. The draft audit requested by the Southeast Regional Office of the Office of Mental Retardation (“OMR”), was not conducted to review only the occupancy costs charged by CI to the Delaware County Office of Mental Retardation (“Delaware County”) for services provided through June 30, 2004. The BFO auditors reviewed all aspects of CI’s operations, including program, staffing, Board service, and vehicle expenses. The statement regarding the scope of the audit should be revised to indicate all of the areas that were reviewed.

Second, the timeframe of the audit should be plainly stated. No beginning date for the scope of the audit is noted until Issue No. 1 under Results of Fieldwork on page 4. At that point the audit references the occupancy costs in question related to the period from July 1, 1987 through February 28, 2001. Issue No. 2 on page 6 references the occupancy costs for the period of March 1, 2001 through June 30, 2004. The timeframe covered by the audit is 17 years.

As CI has stated at several of the meetings with BFO auditors, there is no requirement that CI maintain occupancy records for the 17 years covered by the draft audit. The record keeping regulation at Chapter 4300.132 (b) requires county programs and providers to maintain records for reimbursed claims for at least 4 years after the close of the fiscal year. CI has complied with the regulation.

The record keeping provision of each contract with Delaware County for the past several years has stated the provider is to keep records for a minimum of 6 years following the expiration or termination of the contract, or for such other period as the County prescribed. (No other period was prescribed.) CI has complied with the terms of the contracts. CI did not maintain records for the 17 year period because neither the provisions of the regulation nor the require maintaining documents for a timeframe that approaches 17 years.

CI knows of no basis for BFO to begin an audit in July, 2004 and extend its findings back 17 years. CI does not believe this represents an appropriate practice. Fiscal Years ended June 30, 1987 through June 30, 1997 have been closed and made final long ago. However, if those years are still open, are other fiscal years also still open? What fiscal years are closed? Could BFO extend the timeframe of the draft audit beyond the Chapter 4300 regulations and go back 25 years under the Chapter 6100 regulations? The scope of the draft audit extends back many years beyond any reasonable period. The scope of the audit must be limited to the timeframes in the regulations or the contract to ensure any audited entity can still produce documentation and also can expect that at some reasonable time its fiscal reporting periods can be closed. Seventeen years later is not a reasonable time.

#### **Occupancy Cost Calculations**

For the period of time beginning July 1, 1997 and ending June 30, 2004, CI agrees that it and its landlord, Independent Support Systems, Inc. ("ISS") were appropriately determined to be related parties. The relationship between the parties was not hidden. The relationship was fully disclosed in the CI Financial Statements and Independent Auditor's Report submitted to Delaware County each year. A copy of the relevant page for the year ended June 30, 2004 is attached as Exhibit 1. No allegation has been made that the lease costs exceeded fair rental

value. In a number of instances, such as Bridge Street, North Orange Street, Olympic Avenue and Robbins Road, the lease costs remained static for periods of several years rather than increasing annually because the goal was not to maximize rental charges and revenue, but to make secure and suitable housing available to the program over the long term. The CI and ISS related party relationship no longer exists. As a result, new leases were negotiated and became effective as of July 1, 2006; however, CI recognizes that from July 1, 1997 through June 30, 2004, rental costs charged by CI to Delaware county should not have exceeded costs ISS incurred as the owner of the leased properties as follows:

July 1, 1997 - February 27, 2001

CI believes the appropriately calculated difference in the rental amounts and related party costs for the period of July 1, 1997 - February 27, 2001, are shown on Exhibit 2.

February 28, 2001 - June 30, 2004

The properties listed on Exhibit 2 referenced above, with the exception of Burmont Road and Lafayette Hill which already were debt free, were refinanced with Industrial Development Authority Bond Funds (“IDA”) effective February 28, 2001. A listing of the properties pledged as collateral for the IDA funding is attached as Exhibit 3. Each of the properties, as shown on Exhibit 3, also were allocated a portion of the IDA funding based upon the portion of the IDA required to satisfy the amount of indebtedness remaining for that property. Utilizing the costs to ISS for IDA funding and including an appropriate continuing participation allowance (“CPA”) for down payments, CI believes appropriately calculated rental amounts for the period of February 28, 2001 through June 30, 2004 are shown on Exhibit 3. Rental amounts for the properties that were debt free are shown on Exhibit 4.

The differences in amounts CI and BFO have calculated occur largely due to differences in what each believes either constitutes renovations or improvements or documents the renovations or improvements made many years earlier.

### **Renovations/Improvements and Constructions Costs**

As noted on page 9 of the draft audit, CI disagrees with the interpretation BFO has applied to renovations and improvements. CI utilized the capital expenditure rules used by the Internal Revenue Service. CI maintained logs of capital expenditures for real estate renovations/improvements from purchase date of the property. CI recognizes that some items could be regarded as repairs, but the vast majority of the expenses are for renovations or improvements, such as replacement of floors or windows to extend the life of those assets. The documents CI provided demonstrated the expenditures were for those purposes. For example, a repair to an existing toilet was classified as a repair, but replacement of the toilet was classified as an improvement because it extends the life of the asset.

As another example, CI submitted showed the expenditures that were incurred for the major construction of the administrative office building on Woodland Avenue. When purchased, the Woodland Avenue building was a hulk or a shell that had been vacant for five years. Windows were broken out or missing. There were holes in the roof. It had no functioning mechanicals. There was no heat or air conditioning. The electricity, water and sewer had been disconnected; however, the building was centrally located in the county and could be rebuilt to meet CI's needs more cheaply than it would have cost to purchase comparable existing space. The building was gutted and essentially had to be reconstructed, including roof and window replacement, as well as the addition of 2,000 square feet of office space, a sprinkler system and a parking lot in order to serve as the CI administrative office. CI received an occupancy permit

and began to move into the building in January, 1998. CI believes BFO has erroneously determined most of the costs of the Woodland Avenue costs were repairs or maintenance when those costs were incurred for the overall reconstruction of that property to serve as the administrative office.

CI made as many documents available to BFO as it could regarding the Woodland Avenue construction and for other locations. However, for the period before July 1, 1997, many of the documents simply were no longer available. The governing regulation at Section 4300.132(b), and before it, the governing regulation at Section 6161.1, require records be maintained for 4 years and 5 years, respectively. CI complied with those reasonable standards. The regulations regarding record keeping recognize it is reasonable that records will not be maintained forever. BFO does not. BFO recommends receipts or invoices be maintained regardless of the time period involved. Applying BFO's recommendation, source documents must be maintained for thirty, forty, fifty years or longer. No provider can assure compliance with the records retention requirement BFO has recommended. Accordingly, no provider should be subject to the records retention standard BFO has recommended or audit for a time frame that exceeds the regulatory record keeping requirement by so many years.

### **The Two Vacation Homes**

The vacation homes project was an experiment that looked good on paper, but in the end did not work as planned. The concept of providing a mountain or shore location to consumers or staff for vacations seemed sound. Both locations provided a place where consumers could go and not face problems with hotels or private owners who were concerned about damage or breakage and liability. That was very important. And both locations were always available and accessible. Since owners of vacation rentals often had such reservations about renting to people

with disabilities for these expressed reasons, CI thought offering a shore property and a mountain property as vacation locations would provide a great benefit to the consumers it serves.

Consumers always had first choice in reserving and using either location and were charged an amount that was less than would have been charged for comparable accommodations. Although staff were allowed to use both locations thereby making the vacation property available to staff who otherwise could not afford a comparable vacation, the real purpose in allowing staff use was to help cover the costs of maintaining vacation properties over 12 months. Consumers and staff used both properties, but after awhile, consumers preferred the shore property and stopped using the Pocono property. CI stopped using and charging for the Pocono property by April 30, 2004. All vacation property charges to Delaware County for the shore property ended June 30, 2004. CI tried to continue to offer the Cape May property use to consumers and staff for another full vacation season, trying a number of ways to increase the off-season use to break even. Ultimately the costs and headaches of offering a vacation property grew to the point that CI terminated its shore property lease by November 30, 2005.

The vacation project was not administered as well as it should have been. No deposits or advance payments were required. Consumers and staff canceled their reserved times without any penalty or consequence. The records that were maintained frequently did not reflect these last minute changes so collection of rent appears to show consumers were charged and staff were not. This was not the case. CI also disagrees that staff were allowed to use the vacation homes in lieu of paying overtime for accompanying consumers. While, in the end, CI agrees the vacation project should have been better administered, CI believes BFO's recommendation to deny any support for that project. It should be noted that the charges listed for the seven year period on Exhibit E of the BFO report only represent 60% of the project's deficit. CI charged the other

40% to its fund balance each year to represent the portion of use by staff and to account for the prime and off season aspects that were difficult to quantify. A fair resolution of this issue would reflect that self-disallowance and permit CI to retain the remaining funds it expended in trying to provide available vacation homes for consumers who wished to use them.

### **Certificate Holders of The Corporation**

BFO has made the observation that the bylaws of CI should be amended because BFO believes certificate holders of CI stock possess undue influence over CI and removal of the stock from those certificate holders will work in the best interest of CI and the consumers it serves. While BFO is entitled to its opinion, in conducting an audit BFO must base its findings and recommendations on some authority other than its opinion. BFO has neither shown where the corporate structure of CI fails to comply with the Non-Profit Corporation law or the Chapter 4300 regulations nor has BFO stated a legal basis for its position in the draft audit or at the exit conference on January 31, 2007.

CI's corporate structure is in compliance with both the Non-Profit Corporation Law and the Chapter 4300 regulations. In addition, the Board of Directors has been given the authority to operate CI. As noted below, CI's Bylaws place its Board of Directors in control of all business affairs of the organization.

#### Article V - Board of Directors

##### 5.1 General Powers

*All the business and affairs and all the property of the Corporation shall be managed, conducted, controlled and directed by the Board of Directors. All powers of the Corporation are hereby granted to the Board of Directors, which shall have and is hereby vested with the power and authority to do or cause to be*

*done any and all lawful things for and on behalf of the Corporation, except as otherwise expressly provided by law, the Articles of Incorporation or these Bylaws.*

Bylaws of Community Interactions, Inc.

**COMMUNITY INTERACTIONS, INC.****Community Living Arrangement Programs and Adult Day Programs****Notes to Financial Statements****(3) Debt Service**

Capital expenditures and debt service payments are charged directly to expense. Notes payable in the amount of \$96,531 as of June 30, 2004 are not reflected in the statement of financial position.

**(4) Note Payable Bank**

At June 30, 2004, the Organization had a \$1,000,000 line of credit secured by all of the Organization's assets with a bank to be drawn down as needed with an annual interest rate of 4.25%. As of June 30, 2004, the Organization had drawn down \$77,668 against this line of credit, which is not reflected in these financial statements.

**(5) Related Party Transactions**

Rent was paid by the Organization to a related entity, Independent Supports Systems, Inc. (ISS, Inc.) in the amount of \$375,246 for the year ended June 30, 2004.

ISS, Inc. charged an administrative expense to the Organization in the amount of \$36,275 for the year ended June 30, 2004.

**(6) Overhead Allocations**

Overhead allocations are charged to the various cost centers substantially based on total direct costs of each cost center to total direct costs.

**(7) Pension Plan**

The Organization has established a noncontributory defined contribution pension plan covering all employees accumulating more than 500 hours of service during the plan year. Contributions are based on a percentage of the eligible compensation of plan participants and are funded as accrued.

Pension expense for the year ended June 30, 2004 was \$155,922.

**COMMUNITY INTERACTIONS, INC**  
**SCHEDULE OF OCCUPANCY EXPENSES**  
**FOR THE PERIOD JULY 1, 1997 THROUGH FEBRUARY 27, 2001**

<u>Property</u>	<u>Allowable</u>	<u>Charged</u>	<u>Net</u>
Garrett	51,255	75,724	(24,469)
Morton	50,033	74,052	(24,019)
Whitney	36,796	49,192	(12,396)
Ridley Park	37,348	50,248	(12,900)
Cedar	56,802	78,100	(21,298)
Bridge (Boothwyn)	35,347	48,972	(13,625)
Burmont	54,648	70,400	(15,752)
War Trophy	58,880	66,000	(7,120)
Orange	73,978	74,360	(382)
Olympic	59,106	59,796	(690)
Bridgewater	48,180	50,028	(1,848)
Brookthorpe	-	-	-
Crawford	45,232	50,600	(5,368)
Dorchester	54,032	60,808	(6,776)
Robbins	57,752	53,724	4,028
Gov. Markham	48,760	58,916	(10,156)
Verona *	17,670	17,600	70
Locksley	-	-	-
Bullens *	18,000	13,914	4,086
Brookside *	15,781	16,700	(919)
Springfield	152,415	126,324	26,091
Germantown	<u>51,788</u>	<u>55,704</u>	<u>(3,916)</u>
Total	1,023,803	1,151,162	(127,359)

\* OBH Program sites, all others are MR Group Homes.

EXHIBIT 3

COMMUNITY INTERACTIONS, INC  
SCHEDULE OF OCCUPANCY EXPENSES

FOR THE PERIOD FEBRUARY 28, 2001 THROUGH JUNE 30, 2004

PGMH#	LOAN AMOUNT	ALLOCATION OF IDA LOAN	ANNUAL 8% OF ORIGINAL DOWNPMT	RENT CHARGED		RENT CHARGED		RENT CHARGED		TOTAL FOR IDA BOND PERIOD
				2/27/2001 to 2/27/02	2/27/2002	2/27/2003 to 2/27/04	2/28/2004 to 6/30/04			
320	34,456	1.78	2,016	21,306	21,960	21,960	7,320	72,546		
326	43,778	1.88	2,112	13,464	13,832	13,832	4,611	45,371		
331	30,174	1.3	912	9,636	9,636	9,636	3,212	32,120		
332	32,292	1.39	1,524	11,976	11,976	11,976	3,992	39,920		
333	50,776	2.18	2,112	15,444	15,444	15,444	5,148	51,480		
334	31,820	1.37	1,260	12,894	12,894	12,894	4,328	42,620		
337	97,976	4.64	3,516	16,776	16,732	16,942	5,647	56,097		
338	76,666	3.32	1,452	20,280	23,928	25,648	8,549	78,405		
340	89,880	4.25	3,420	15,244	15,604	15,604	5,201	50,749		
341	183,397	8.59	19,220	18,972	18,036	18,036	6,012	62,240		
346	87,833	4.1	2,028	13,800	10,140	12,996	4,332	41,268		
348	72,765	3.38	2,580	14,808	14,488	15,052	5,017	49,365		
352	104,019	4.86	14,844	13,780	13,424	13,424	4,475	46,523		
353	111,497	6.05	-68	18,164	15,628	13,836	4,612	52,240		
361	206,026	9.65	20,700	19,800	18,608	18,608	6,203	65,311		
365	76,874	3.64	2,784	12,364	12,572	13,076	4,359	42,371		
366	125,409	5.81	-	-	-	-	-	-		
585	222,083	10.82	9,280	40,268	45,504	47,156	15,719	148,647		
991	61,451	2.91	-	-	-	-	-	-		
1200	126,578	5.9	-	13,356	13,356	13,212	4,404	44,328		
1201	134,250	6.32	-	13,756	17,172	13,212	4,404	48,544		
1202	135,000	6.25	540	21,120	12,540	14,028	4,676	52,364		
	2,135,000	100	36,004	338,876	334,750	336,662	112,221	1,122,509		
				319,294	161,837	321,869	107,290	910,290		
				36,004	36,004	36,004	14,135	122,147		
				355,298	197,841	357,873	121,425	1,032,437		
				16,422	(136,909)	21,211	9,204	(90,072)		

ACTUAL PAYMENTS ON IDA LOAN  
DOWNPAYMENT ALLOWANCE  
TOTAL ALLOWABLE AMOUNTS

DIFFERENCE

**COMMUNITY INTERACTIONS, INC**  
**SCHEDULE OF OCCUPANCY EXPENSES**  
**FOR THE PERIOD MARCH 1, 2001 THROUGH JUNE 30, 2004**  
**FOR DEBT FREE PROPERTIES**

<u>Property</u>	<u>Allowable</u>	<u>Charged</u>	<u>Net</u>
Burmont	49,680	54,988	(5,308)
Germantown	<u>47,080</u>	<u>56,222</u>	<u>(9,142)</u>
Total	96,760	111,210	(14,450)