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March 6, 2008

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Members of the Board of Education  
Baldwin UFSD  
District Office  
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Dr. Henry Kiernan, Superintendent  
Members of the Board of Education  
Bellmore-Merrick Central High School District  
1260 Meadowbrook Road  
N. Merrick, NY 11566

Dr. William R. Bolton, Superintendent  
Members of the Board of Education  
Copiague School District  
2650 Great Neck Road  
Copiague, NY 11726

Leon J. Campo, Superintendent  
Members of the Board of Education  
East Meadow UFSD  
Salisbury Center  
718 The Plain Road  
Westbury, NY 11590

Dr. Janet Ceparano Wilson, Superintendent  
Members of the Board of Education  
Harborfields Central School District  
2 Oldfield Road  
Greenlawn, NY 11740

Report Number: 2008M-47

Dear Superintendents and Members of the Boards of Education:

One of the Office of the State Comptroller's primary objectives is to identify areas where local governments and school districts can improve their operations and provide guidance and services that will assist local officials in making those improvements. Our goals are to develop and promote short-term and long-term strategies to enable and encourage local government and school district officials to reduce costs, improve service delivery and to account for and protect their entity's assets.

In accordance with these goals, we conducted an audit that addressed whether the Baldwin, Bellmore-Merrick, Copiague, East Meadow and Harborfields school districts have correctly classified their legal counsel, Mr. Lawrence Reich, as a district employee and properly enrolled him in the New York State and Local Employees Retirement System (ERS).

This report of examination letter contains our findings and recommendation. We discussed the findings and recommendation with appropriate officials and considered their comments in preparing this report. School district officials generally agreed with our findings and recommendation. Their responses are summarized in Appendix A of this report.

### **Summary of Findings**

The Baldwin, Bellmore-Merrick, Copiague, East Meadow and Harborfields school districts did not have formal procedures to distinguish between employees and independent contractors. As a result, the districts were incorrect in classifying Mr. Reich as an employee and should not have reported him as an employee to the ERS.

### **Background, Scope and Methodology**

School districts employ a wide variety of people to perform school district functions to deliver necessary services. While the majority of these individuals are public employees, other individuals are contractors and consultants. In general, the basic distinction between an employee and an independent contractor is that an employee undertakes work under the direction of the employer as to the manner in which the work is to be accomplished, while an independent contractor agrees to undertake work, but is not subject to orders of the employer as to the manner used to perform that work. Employees have their work hours and duties fixed by their employer, and they are compensated by salary or wages and other benefits (e.g., sick leave, vacation leave) based on collective bargaining agreements or other employment agreements. Independent contractors, on the other hand, are usually retained to do specialized or expert services, but are not supervised with respect to how those services are rendered. School districts do not spell out a contractor's work hours and duties in a job description, and generally they do not provide equipment or other resources to perform the agreed upon services. ERS provides guidelines that can help school districts make this determination correctly. The Office of the State

Comptroller's (OSC) Financial Management Guide for Local Governments<sup>1</sup> also provides information to help distinguish between independent contractors and employees.

It is important to be able to distinguish between "employees" and "contractors" because public employers put their employees on the payroll, which requires withholding and contributing toward employees' payroll taxes and benefits, including insurance and other benefits. Enrolled employees earn service credits during their period of public employment, which can entitle them to a pension from ERS. Contractors are not eligible to join ERS or to receive retirement system service credits.

In August 2006, OSC received an anonymous complaint concerning the Harborfields Central School District. Among other issues, the complaint alleged that the District had classified an attorney, Mr. Lawrence Reich, as an employee while at the same time, paying his law firm a retainer for legal services. In December 2006, we initiated an audit at the District and during the course of that audit, reviewed the circumstances of the District's classification of Mr. Reich as an employee. In addition, District officials also raised concerns to us about this issue and asked that we provide a determination as to whether this arrangement was appropriate. During our review of whether the District had appropriately classified Mr. Reich as an employee, we learned that other school districts had simultaneously employed Mr. Reich under similar circumstances. Since the issue then required an audit of multiple districts, we issued our audit report on the Harborfields Central School District (2007M-231) in December 2007, while we planned and initiated a separate audit of Mr. Reich's employment status.

As part of our audit, we interviewed key school district officials to determine if they had procedures for classifying individuals who perform professional services as employees or independent contractors and whether they performed an analysis to determine if Mr. Reich was an employee. We reviewed relevant documentation, such as contracts between the districts and Mr. Reich, payment histories for Mr. Reich and his firm, payroll records for fiscal years 2005-06 and 2006-07, retainer agreements and ERS records. In addition, we attempted to review any available documentation indicating the days worked by Mr. Reich. Our audit covered the period from July 1, 2006 through June 30, 2007. We extended our scope to prior time periods, where appropriate.

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

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<sup>1</sup> Financial Management Guide for Local Governments, Volume Two, page 1, Subsection 8.4020, issued December 1992

## **Audit Results**

Mr. Reich was initially reported as an employee in 1978 at the Baldwin School District, in 1984 by Bellmore-Merrick, and in 1988 by Copiague and East Meadow. Harborfields first reported Mr. Reich as an employee in 1995. Mr. Reich ended his employment relationship with East Meadow in November 2001 and retired from the remaining four school districts in September 2006.<sup>2</sup>

Generally, the key in determining whether an individual is an employee or a contractor is information that provides evidence of both the entity's degree of control over the worker and the work, and the worker's degree of independence from the entity. These issues should be assessed by the employer when it makes a determination as to whether an individual should be considered an employee and whether service credit information should be reported to ERS. We found no evidence that any of the five districts had made a careful determination of their relationship with Mr. Reich when they started reporting him to ERS.

Behavioral control is demonstrated when the entity has a right to direct and control how the worker performs the tasks he or she was hired to do. Examples include work-related instructions (e.g., when and where to do the work; what resources are provided by the employer; which workers to hire to assist with the tasks; how to account for time worked; what sequence to use in doing the work), and other indications, such as a job description, that the entity has the right to control details of the worker's performance as an employee. In addition, training that an entity provides to employees, to ensure that work is performed in a particular way, is further evidence of behavioral control by an employer over an employee, as is a periodic evaluation of an individual's work performance. By contrast, contractors are generally hired to provide services without receiving explicit instructions from the entity regarding how to go about performing the services. Contractors also obtain their own training.

Financial control is demonstrated when the entity has the right to control the business-related aspects of the worker's job. Examples include how the worker is paid, the extent of the worker's investment in facilities used in performing the services, and the worker's ability to make his or her services available to others by advertising, maintaining a visible business location and seeking business opportunities. Whereas an employee is generally paid a guaranteed hourly/weekly rate, a contractor is usually (but not always) paid a flat fee or according to a schedule determined by a contract. Further, employees do not invest in their work facilities, nor do they generally maintain a business location to offer the services to others that they provide to the entity. Contractors also realize a profit or a loss in performing their services for the entity, but employees do not. Finally, multiple engagements to provide professional services are a possible indicator of a client/contractor relationship.

Our analysis of the facts relating to Mr. Reich's service at these five school districts leads us to conclude that Mr. Reich was an independent contractor and that the districts incorrectly

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<sup>2</sup> Service credit reported by multiple employers cannot result in more than one year of credit for a one year period. However, the final average salary that is used to calculate retirement benefits is based on the aggregated annual earnings from all employers.

classified him as an employee. Therefore, his time worked at the districts should not have been reported to ERS. We base our conclusion on the fact that school district officials did not exercise control over the Mr. Reich's daily activities:

- District officials at the five school districts neither supervised, controlled nor directed how Mr. Reich performed his work.
- The districts did not set Mr. Reich's hours and did not establish the number of hours that constituted a normal workday for Mr. Reich.
- None of the districts provided Mr. Reich with a place to work. Instead, Mr. Reich worked from his private law office.
- Mr. Reich did not work established and fixed hours at any of the districts. None of the districts had any time records documenting the days or hours he worked and did not maintain any record of work completed by Mr. Reich as an employee.
- At Harborfields, the District adjusted Mr. Reich's salary to recoup the employer's portion of FICA and Medicare taxes, and ERS contributions. Such an approach would be inappropriate for any individual who was truly an employee. There is no record that Mr. Reich objected to this arrangement.
- Mr. Reich used his own resources and supplies to complete his work. The districts did not provide Mr. Reich with any resources to carry out his day-to-day duties. For example, employers of attorneys normally would provide legal reference materials, but none of the school districts provided such materials to Mr. Reich.
- Mr. Reich could use other individuals who were paid by his firm to perform work for the districts.
- Mr. Reich provided services as an employee to several districts concurrently, and also offered his services to the public.

### **Recommendation**

District officials should submit corrected retirement reports to ERS related to Mr. Reich.

The Baldwin, Bellmore-Merrick, Copiague, East Meadow and Harborfields School Boards have the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a (3)(c) of the Education Law and Section 170.12 of the Regulations of the Commissioner of Education, the Board must approve a corrective action plan that addresses the findings in this report, forward the plan to our office within 90 days, forward a copy of the plan

to the Commissioner of Education, and make the plan available for public review in the District Clerk's office. For guidance in preparing the plan of action, the Board should refer to applicable sections in the publication issued by the Office of the State Comptroller entitled *Local Government Management Guide*.

Sincerely,

A handwritten signature in black ink, appearing to read "Ste J Hancox", written in a cursive style.

Steven J. Hancox  
Deputy Comptroller

## **Appendix A**

Officials at all five districts agreed that Mr. Reich was not an employee of the District and should not have been reported as such to ERS.

The Harborfields Superintendent informed us that when she started at the District in July 2005, the former Superintendent did not inform her of the arrangement between the District and Mr. Reich. However, when she became aware of the arrangement, she met with Mr. Reich and suggested that he submit documentation of his days and hours worked based on the sample reporting month provided by ERS. However, Mr. Reich never submitted any documentation to substantiate the days he worked. As a result, the District did not resolve this issue.