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State Agencies Propose Regulations to Implement Governor Cuomo's Executive Order 38

On January 18, 2012, Governor Cuomo issued Executive Order 38 (EO 38), which requires certain state agencies to promulgate regulations applicable to both for-profit and not-for-profit entities that receive state financial assistance or state-authorized payments. Under EO 38, such regulations must limit the amount of state funding that such service providers can apply towards administrative expenses and executive compensation.

State agencies first published proposed regulations to implement EO 38 for public comment in May 2012 and again in October 2012 with an estimated effective date of January 1, 2013. State agencies published the latest round of proposed regulations this past March, which were open to public comment until April 12, 2013. As of the date of this News Alert, the proposed regulations that will implement EO 38 are scheduled to go into effect on July 1, 2013.

EO 38 stipulates two requirements that state agencies must implement through their specific regulations. The first requirement is that at least 75% of the state financial assistance or state-authorized payments must be directed to provide direct care or services, and not administrative costs. This minimum direct spending percentage will increase by at least 5% each year until it is capped at 85% in 2015.

The second requirement limits the amount of state financial assistance or state-authorized payments that service providers may apply toward executive compensation to a maximum of \$199,000 per annum. Though the commissioner of each agency has the discretion to adjust this figure annually based on undefined "appropriate factors," EO 38 sets a hard maximum at Level I of the federal government's Rates of Basic Pay for the Executive Schedule promulgated by the United State Office of Personnel Management.

EO 38 also requires implementation of a reporting obligation to facilitate state agencies' monitoring of their providers' compliance. Unless the provider is required to file an annual cost report with the state, the provider may choose either the calendar year or the fiscal year used for its financial reporting purposes as its reporting period for EO 38 compliance. If the provider is required to file an annual cost report with the state, then it must use the reporting period applicable to its

cost report. The "EO #38 Disclosure Form," which has not yet been released, must be filed with the state no later than 180 calendar days after the provider's covered reporting period.

The regulations proposed by the state agencies generally reiterate the requirements set forth in EO 38. However, the proposed regulations provide additional guidance regarding how the state agency will implement EO 38. For example, in its proposed regulations, the Department of Health (DOH) has clarified the definition of a "covered provider" by providing two thresholds. First, the provider must have received more than \$500,000 in state financial assistance or state-authorized payments during the covered reporting period, the year prior to the covered reporting period, and as an average annual amount during those two years. Second, state financial assistance or state-authorized payments must constitute at least 30% of the provider's annual in-state revenues for the prior year.

Under the DOH proposed regulations, if a covered provider receives state financial assistance or state-authorized payments from multiple sources, the provider's compliance with the restriction on allowable administrative expenses is determined by the total amount of program services expenses and administrative expenses paid for by funding received from all such sources. The DOH proposed regulations also clarify items that are not considered administrative expenses, such as capital expenses, property rental, mortgage or maintenance expenses, taxes, equipment rental, government assessments, equipment rental, and salaries and benefits attributable to policy development or research.

The DOH proposed regulations also define who is a "covered executive" for purposes of EO 38's executive compensation limits. A "covered executive" is a compensated director, trustee, managing partner, or officer whose salary and/or benefits, in whole or in part, are administrative expenses, and any key employee whose salary and/or benefits, in whole or in part, are administrative expenses and whose executive compensation during the reporting period exceeds \$199,000. The DOH Proposed Regulations look to the instructions to the Form 990 for definitions of the terms "director," "trustee," "officer," and "key employee."

The following thirteen state agencies have proposed regulations that would implement EO 38 for the direct-services programs that they fund or administer: (1) Department of Agriculture and Markets; (2) Department of Corrections and Community Supervision; (3) Department of Health; (4) Department of State; (5) Division of Criminal Justice Services; (6) Division of Housing and Community Renewal; (7) Office for the Aging; (8) Office of Alcoholism and Substance Abuse Services; (9) Office of Children and Family Services; (10) Office of Mental Health; (11) Office for People with Developmental Disabilities; (12) Office of Temporary and Disability Assistance; and (13) Office of Victim Services.