



## Governor Cuomo's Executive Order 38 and Regulations Affecting New York State-Funded Service Providers

*May 25, 2012*

On May 16, 2012, Governor Andrew M. Cuomo announced the release by thirteen New York State agencies of proposed regulations (the "Proposed Regulations") intended to implement Executive Order 38, which was issued by Governor Cuomo on January 18, 2012. Executive Order 38 directed the commissioner of each Executive State Agency that provides State financial assistance or State-authorized payments to providers of services to promulgate regulations within 90 days requiring that (i) at least 75% (with such percentage increasing annually by 5% to at least 85% in 2015) of State financial assistance or State-authorized payments be directed to provide direct care or services, rather than to administrative costs, and (ii) no State financial assistance or State-authorized payments be provided for executive compensation in excess of \$199,000 per year. In a press release, Governor Cuomo indicated that Executive Order 38 "will prevent public funds from being diverted to excessive compensation and unnecessary administrative costs, and will ensure that taxpayer dollars are being used to help New Yorkers in need."

If promulgated in current form, the Proposed Regulations would serve to limit the amount of State funds or State-authorized payments that may be spent for administrative costs and executive compensation, subject to the availability of certain waivers, and impose reporting obligations on certain State-funded nonprofit and for-profit service providers. The Proposed Regulations all follow the same template. The Proposed Regulations are currently available and are expected to be published formally by each agency on May 30, 2012. Following publication, the Proposed Regulations will be subject to a 45-day comment period and take effect on January 1, 2013.

- Applicability. If promulgated in current form, the Proposed Regulations would apply to any "covered provider," which would be defined as an entity or individual that: (i) has received more than an average annual amount of \$500,000 in State funds or State-authorized payments to render services for the benefit of members of the public ("program services") and (ii) derives a least 30% of its annual in-state revenues from State funds or State-authorized payments (measured on a consolidated basis with any parent or subsidiary organization). State, county, local, and tribal governmental units in New York State, certain individuals providing child care services, and individual professionals who provide program services individually, rather than as an employee of or officer of a corporation or other entity, would be excluded for purposes of the Proposed Regulations from the term "covered provider."

For purposes of the Proposed Regulations, “State funds” would be defined as funds appropriated by law in the annual State budget and “State-authorized payments” would be defined as payments of funds that are not State funds but are distributed or disbursed upon a State agency’s approval. The following would not be considered either State funds or State-authorized payments: (i) procurement contracts awarded on a “lowest price” basis, except for contracts for program services awarded on a “lowest price” basis; (ii) awards to State or local governmental units, except where used to pay covered providers through a contract or other agreement, (iii) capital expenses, including for the purchase, installation, and maintenance of real estate or other real property, or equipment; (iv) direct payments or the provision of vouchers used to secure specific services or health insurance premiums; (v) wage or salary subsidies paid to employers to support the hiring or retention of their employees; (vi) awards to entities engaged exclusively in commercial or manufacturing activities; or (vii) policy development or research.

- Limits on Executive Compensation. The Proposed Regulations would provide that, beginning on January 1, 2013, no more than \$199,000 per year of State funds or State-authorized payments may be used by a covered provider or its related entities for the payment of executive compensation to a covered executive. A “related entity” of a covered provider would be defined as an entity that that shares three or more officers, directors, trustees, or employees with the covered provider; that appoints 25% or more of the officers, directors, trustees, or employees of the covered provider, or vice versa; is controlled by a common parent entity as the covered provider; controls or is controlled by the covered provider; or substantially controls the executive compensation or financial affairs of the covered provider, or vice versa. “Executive compensation” would include all forms of cash and noncash payments, including, for example, salary, wages, bonuses, housing, and educational benefits, but does not include mandated payments such as Social Security, or health insurance premiums and pension contributions consistent with those provided to non-executive employees. A “covered executive” would be defined as a director, trustee, managing partner, or officer whose salary and benefits cannot be attributed to particular program services, such as the executive director or chief executive officer, controller or accounting personnel, and public relations personnel. If a covered provider contracts with a related entity for administrative or program services, the covered executives of the related entity would be considered “covered executives” of the covered provider. In addition, beginning on January 1, 2013, penalties would be imposed on any covered provider where the covered provider or its related entities: (i) provides executive compensation to a covered executive in excess of \$199,000 (including all sources of funding, not restricted to State funds and State-authorized payments) and (ii) (a) such compensation is greater than the 75th percentile of compensation provided to comparable executives of other providers of the same size and program service sector in the same or comparable geographic area as established by a compensation survey identified or recognized by the agency or the Director of the Division of Budget; or (b) such compensation was not reviewed and approved by the board, including at least two independent directors, upon consideration of comparability data; and (c) the covered provider or related entity does not have contemporaneous documentation to substantiate its compliance with the requirements in (a) and (b).

- Limits on Administrative Expenses. The Proposed Regulations would provide that, beginning on January 1, 2013, at least 75% of the covered operating expenses paid for with State funds or State-authorized payments must be used for program services, rather than for administrative expenses. The minimum percentage would increase by 5% each year until it reaches 85% on January 1, 2015. “Covered operating expenses” would be defined as program services expenses and administrative expenses authorized by agency regulations, contracts or other rules governing the disbursement of State funds or State-authorized payments. “Administrative expenses” would be defined as expenses that cannot be attributed directly to the provision of program services. Administrative expenses include salaries for staff performing administrative functions not attributable to program services, legal expenses not attributable to the provision of program services, and overhead expenses such as computer networks, audit services, and publicity expenses. Capital expenses, including expenditures related to real estate, property rental or maintenance expenses, and equipment rental would be excluded from both the definition of covered operating expenses and the definition of administrative expenses.
- Waivers. The Proposed Regulations would permit the relevant agency to grant waivers on the limits on executive compensation and administrative expenses on a showing of good cause.

In assessing whether a waiver on the limit on executive compensation should be granted, an agency would consider: (i) the extent to which the executive compensation is comparable to that given to comparable executives of other providers of the same size and sector and the same or similar geographic area; (ii) the extent to which the covered provider would be unable to provide the program services at the same levels of quality and availability without the waiver; (iii) the nature, size, and complexity of the covered provider’s operations and the program services provided; (iv) the covered provider’s review and approval process for the subject executive compensation, including whether the board, including at least two independent directors, approved the compensation, considered comparability data in its review of the compensation, and contemporaneously documented the review and approval process; and (v) the efforts of the covered provider to secure executives with the same levels of experience, expertise, and skills at lower levels of compensation. Waivers will be granted only to covered providers who have demonstrated compelling circumstances to support the granting of a waiver. A waiver with respect to executive compensation would remain in effect for the period of time specified by the relevant agency, but would be revoked if the executive compensation increases by more than 5% in any calendar year, or otherwise upon notice provided by the relevant agency.

In assessing whether a waiver on the limit on administrative expenses should be granted, an agency would consider: (i) the extent to which the administrative expenses are necessary or avoidable; (ii) whether a failure to reimburse specific administrative expenses would negatively affect the availability or quality of program services in the covered provider’s geographic area; (iii) the nature, size, and complexity of the covered provider’s operations and programs; (iv) the covered provider’s efforts to monitor and control administrative expenses and limit requests for reimbursement of such costs; and

(v) the nature and extent of the covered provider's efforts, if any, to find other sources of funding to support its administrative expenses. Waivers on the limit of administrative expenses would be granted only for a single year, but the relevant agency may extend the effective period of the waiver.

- Reporting. The Proposed Regulations would impose annual reporting obligations on all covered providers. Covered providers would be required to submit an annual disclosure form to the relevant agency. However, the Proposed Regulations do not indicate what information would be called for in the annual disclosure form. Failure to comply with the reporting obligations could result in the termination of the relevant agency contract or agreement.
- Non-Compliance and Enforcement. The Proposed Regulations would require that an agency provide notice to any covered provider that it determines may not be in compliance with the limitations on executive compensation or administrative expenses and which has not been granted a waiver. If the determination of non-compliance were to become final, the covered provider would have the opportunity to work together with the agency to develop a corrective action plan. The covered provider would have at least six months to implement the corrective action plan. Were a covered provider not to implement fully the corrective action plan within the time period allotted, the agency would be permitted, in its discretion, to: (i) modify the corrective action plan or extend the period for implementation, or (ii) issue a determination of non-compliance, together with a notice of sanctions, which may include: (a) redirection of State funds or State-authorized payments; (b) suspension, modification, limitation, or revocation of the covered provider's licenses or contracts or other agreements with the covered provider; and (c) any other lawful actions or penalties deemed appropriate by the relevant agency. Sanctions will be subject to administrative appeal by the covered provider.

Executive Order 38 can be found at  
<http://www.governor.ny.gov/executiveorder/38>.

Governor Cuomo's Press Release regarding Executive Order 38 can be found at  
<http://www.governor.ny.gov/press/1182011EO>.

Governor Cuomo's Press Release regarding the Proposed Regulations can be found at  
<http://www.governor.ny.gov/press/05162012State-Funded-Providers>.

An example of the Proposed Regulations can be found at  
<http://w3.health.state.ny.us/dbspace/propregs.nsf/4ac9558781006774852569bd00512fda/fe1abd5a1b78ad8585257a00005afe2e?OpenDocument>.

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