



Mount Vernon City School District Internal Controls Over Purchasing and Assets

Report of Examination

Period Covered:

July 1, 2004 - June 30, 2005

2006M-29



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State of New York Office of the State Comptroller

Division of Local Government Services and Economic Development

November 2006

Dear School District Officials:

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

The reports issued by this Office are an important component in accomplishing these objectives. These reports are expected to be a resource and are designed to identify current and emerging fiscally related problems and provide recommendations for improvement. The following is our report on the Mount Vernon City School District – Internal Controls over Purchasing and Assets.

This audit was conducted pursuant to the State Comptroller's authority as set forth in Article V, section 1 of the State Constitution and Article 3 of the General Municipal Law. The report contains opportunities for improvement for consideration by the Board of Education.

If we can be of assistance to you, or if you have any questions concerning this report, please feel free to contact the local regional office for your county listed at the back of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government Services
and Economic Development*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

The Mount Vernon City School District (District) is governed by the Board of Education (Board) which comprises nine elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the chief executive officer of the District and is responsible, along with other administrative staff, for the day-to-day management of the District under the direction of the Board.

One of the Board's managerial responsibilities is the establishment of a system of internal controls designed to provide reasonable assurance that District assets are properly safeguarded and purchases are made in accordance with District policy. Furthermore, an effective system of internal controls provides for the segregation of duties so that no single individual controls all phases of a transaction. When it is not practical to segregate duties because of limited staff resources, the Board should establish compensating controls. A good system of internal controls should also provide for the timely identification of errors and/or irregularities which may have occurred so that corrective action can be taken. Once established, the Board has the responsibility to monitor them periodically to ensure that they are operating properly.

Scope and Objectives

The objective of our audit was to review the District's internal controls over purchasing and assets for the period July 1, 2004 through June 30, 2005. We extended the scope of the audit to review the bond resolution and purchases/expenditures for the Middle School capital project. Our audit addressed the following related questions:

- Did the Board implement suitable purchasing practices to ensure that goods and services are acquired in the best interest of the District and its constituents?
- Did the Board implement suitable internal controls to ensure that District assets are properly safeguarded?

Subsequent to our audit fieldwork, we became aware of additional problems associated with the District's purchasing practices. As a result of these problems, we plan to immediately engage in an in-depth audit focused on the areas of concern. Upon completion of that audit, we will issue a separate audit report.

Audit Results

On February 9, 2000, the Board adopted a bond resolution which authorized the issuance of serial bonds aggregating \$100 million to finance the construction and reconstruction of various school buildings throughout the District. The Board should have adopted and submitted for voter approval two separate bond resolutions – one bond resolution authorizing the issuance of bonds to finance the construction of the two new school buildings and a second bond resolution authorizing the issuance of bonds to finance the construction of additions to or the reconstruction of existing school buildings. Change orders for the construction projects, totaling \$827,817, could not be located by District staff. Subsequently, District officials provided us with documentation showing that \$185,372 of these change orders were proposed but never approved or paid.

We found significant weaknesses existed in the District’s internal controls over purchasing practices. Although the District had policies and procedures in place for the acquisition of goods and services, there were instances where departments circumvented these procedures. The District did not seek bids for \$378,522 of purchases and public works contracts that were subject to competitive bidding. Also, the District paid four professionals \$836,988 when their contracts did not contain a clear understanding of the amount of compensation they were entitled to.

Additionally, we found the internal controls over the District’s assets were weak. District management failed to implement proper policies and procedures for the supervision of wire transfers. In one instance, this resulted in a \$941,709 transfer made to the wrong account. In two other unrelated instances, it resulted in the overpayment and underpayment of withholding taxes. The Board also assigned conflicting duties to three key members of its management team, the District Treasurer, Internal Auditor and Purchasing Agent. We also found that bank reconciliations are not completed timely and there is a lack of oversight of the extra classroom accounts.

Comments of District Officials

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as indicated in Appendix A, District officials generally agreed with our recommendations. OSC comments to the District officials’ response are in Appendix B.

Introduction

Background

The Mount Vernon City School District (District) is located in the City of Mount Vernon, Westchester County. The District is governed by the Board of Education (Board) which comprises nine elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the chief executive officer of the District and is responsible, along with other administrative staff, for the day-to-day management of the District under the direction of the Board.

There are 16 schools in operation within the District, with approximately 10,000 students and 1,300 employees. The District's budgeted general fund expenditures for the 2004-05 fiscal year were \$138 million, funded primarily with Federal and State aid, real property taxes and grants. As of June 30, 2005, the District has issued serial bonds amounting to approximately \$83.1 million to finance renovations and reconstruction of several educational facilities, including the construction of the Longfellow Middle School, for which approximately \$24 million was allocated.

One of the Board's managerial responsibilities is the establishment of a system of internal controls designed to provide reasonable assurance that District assets are properly safeguarded and purchases are made in accordance with District policy. Furthermore, an effective system of internal controls provides for the segregation of duties so that no single individual controls all phases of a transaction. When it is not practical to segregate duties because of limited staff resources, the Board should establish compensating controls. A good system of internal controls should also provide for the timely identification of errors and/or irregularities which may have occurred so that corrective action can be taken. Once established, the Board has the responsibility to monitor them periodically to ensure that they are operating properly.

Objective

The objective of our audit was to review the District's internal controls over purchasing and assets. Our audit addressed the following related questions:

- Did the Board implement suitable purchasing practices to ensure that goods and services are acquired in the best interest of the District and its constituents?
- Did the Board implement suitable internal controls to ensure that District assets are properly safeguarded?

**Scope and
Methodology**

During this audit we examined financial records, asset listings and vendor payment transactions of the District for the period July 1, 2004 to June 30, 2005.¹

Subsequent to our audit fieldwork, we became aware of additional problems associated with the District's purchasing practices. As a result of these problems, we plan to immediately engage in an in-depth audit focused on the areas of concern. Upon completion of that audit, we will issue a separate audit report.

We conducted our audit in accordance with Generally Accepted Government Auditing Standards. More information on such standards and the methodology used in performing this audit are included in Appendix C of this report.

**Comments of District
Officials and Corrective
Action**

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as indicated in Appendix A, District officials generally agreed with our recommendations. OSC comments to the District officials' response are in Appendix B.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, the Board should prepare a plan of action that addresses the recommendations in this report and forward the plan to our office within 90 days. For guidance in preparing your plan of action, you may refer to applicable sections in the publication issued by the Office of the State Comptroller entitled *Local Government Management Guide*. We encourage the Board to make this plan available for public review in the District Clerk's office.

¹ We extended the scope of the audit to review the bond resolution and purchases/expenditures for the Middle School capital project.

Middle School Construction Project

From February 2000 through August 2005, the District issued serial bonds, totaling approximately \$83.1 million from a \$100 million authorization, to finance the construction, renovation and reconstruction of various school properties. The District's management hired a construction management firm to oversee the execution of the projects and an owner's representative to act as liaison between management and contractors and to approve construction documents, such as change orders, on behalf of the District.

District management did not properly oversee the construction of the Longfellow Middle School. As a result, bonds were not properly issued, bond proceeds were used inappropriately, change orders were not available or were not properly authorized and information was not submitted in a timely manner to receive State aid.

Adoption of Bond Resolution and Use of Bond Proceeds - On February 9, 2000, the Board adopted a bond resolution which authorized the issuance of serial bonds totaling \$100 million. The bonds were intended to finance the construction and reconstruction of various school buildings throughout the District, referred to collectively as the "Project," at a total estimated cost not to exceed \$100 million.

The bond resolution stipulated that bonds would be issued for two different purposes. One of these objects was the construction of two new school buildings, including a new middle school at the Longfellow Middle School for 500 students. The other purpose was the construction of additions to or reconstruction of a number of existing school buildings. The bond resolution determined that both of these objects had a maximum period of probable usefulness of more than five years and the bond resolution was subject to a mandatory referendum.²

Section 31.00(d) of the Local Finance Law provides that bonds for two or more purposes may be authorized by the same bond resolution if the maximum period of probable usefulness of the objects or purposes is five years or less or the bond resolution is not subject to either mandatory or permissive referendum. Here, the period of probable usefulness of the purposes for which the bonds were issued was in excess of five years and the bond resolution was subject to a mandatory referendum. Therefore, the Board should have adopted and submitted for voter approval two separate bond resolutions – one bond resolution authorizing the issuance of bonds to finance

² Local Finance Law section 37.00[b]

the construction of the two new school buildings and a second bond resolution authorizing the issuance of bonds to finance the construction of additions to or the reconstruction of existing school buildings.

The bond resolution also divided both purposes into two or more “phases,” and specified the estimated cost of each phase. The estimated cost of constructing the new Longfellow Middle School was specified in the bond resolution to be approximately \$24.2 million. On January 7, 2004, the Board authorized a transfer of \$1.1 million from the construction of the new Longfellow Middle School to increase the amounts available to construct additions to or reconstruct several existing school buildings.

Section 165.00(a) of the Local Finance Law requires the proceeds of bonds to be used only for the purpose for which the bonds were issued or to pay debt service on the bonds. In authorizing the transfer of the \$1.1 million from the construction of the new Longfellow Middle School to the other phases of the Project, the Board inappropriately permitted the proceeds of bonds issued for one purpose (the construction of new school buildings), to be used for a different purpose (the construction of additions to or reconstruction of existing school buildings).

Change Orders - All prospective bidders should have an equal opportunity to bid on a project the District intends to complete. Furthermore, where a contract is subject to the competitive bidding requirements, the award of a contract creates a binding contractual obligation in accordance with the terms of the bid specifications. Entering into a contract which materially varies from the bid specifications or materially amending an existing contract would constitute, in effect, a material alteration of the specifications after the bidding process and gives the successful bidder an unfair advantage over other potential bidders. Nonetheless, it is recognized that, as work goes forward, it is sometimes necessary to make changes to the initial plan. Where the change relates to details or relatively minor particulars and is merely incidental to the original contract, a change order may be issued without competitive bidding even if the increased cost exceeds the bidding limit. However, no important general change may be made which so varies from the original plan, of such importance or so alters the essential identity or main purpose of the contract as to constitute a new undertaking without seeking competitive bidding.

District records show change orders totaling \$946,868 were added to seven of the 10 construction contracts. Although we made several requests, change orders totaling \$827,817, could not be located by District staff. Therefore, we were unable to determine if the changes to the construction plans were legitimate changes that the Board

had approved. In addition, we were unable to evaluate these changes and determine whether or not the District should have requested bids for the additional work. Subsequently, District officials provided us with documentation showing that \$185,372 in change orders were proposed but never approved or paid. For the change orders that were available, \$12,543 was not properly authorized. Only the construction manager and the electrical contractor had signed the change orders. The change orders had not been signed by a District official and the architect. As a result, there is limited assurance that \$654,988 in expenditures were legitimate District costs.

State Aid - The total cost of a project determines the level of State aid that the District will receive. The timeliness in which change orders are submitted and final costs determined and submitted to the State Education Department (SED) affects the amount of aid that the District will get to finance the ensuing year's budget. SED requires that the District submit final cost reports by June 30 of the year within which the project is substantially completed. In addition, the District is automatically given a one year extension to submit these documents. Whenever the submissions of these costs are delayed the District is deprived of needed resources.

SED officials informed us that, as of August 8, 2006, the District had not submitted any change orders or final cost reports for this project. With the automatic extension the District will have until June 2007 to file the change orders and final cost reports. Although the District still has time to submit these change orders and final cost reports to SED, delayed submission can impact the final calculation of State aid available to the District. Failure to submit proper documentation to the SED in a timely manner could result in a reduction in State aid.

Recommendations

1. The Board should adopt amended bond resolutions to effect any changes to the purposes of original bond resolutions.
2. In the future, the Board should not adopt a bond resolution authorizing the issuance of bonds for more than one purpose unless the adoption of such a resolution is authorized by section 31.00(d) of the Local Finance Law. If the Board authorizes the issuance of bonds for more than one purpose, the Board should carefully estimate the maximum to be expended for each purpose.
3. The District should ensure that documentation is available to support the District's expenditures for all capital projects.
4. The District should ensure that all change orders and final costs reports are submitted to the SED in the most efficient manner to obtain timely State aid reimbursements.

Purchasing Practices

A good system of internal control over purchasing consists of policies, practices, and procedures that allow an organization to provide reasonable assurance that it is using its resources effectively (i.e., prudently and economically) and that it is complying with applicable laws and regulations. The Board is responsible for designing internal controls that ensure the prudent and economical use of its moneys when procuring goods and services and to protect against favoritism, extravagance, fraud and corruption.

District management did not have adequate internal controls over the process of soliciting bids for goods and services. The deficiencies resulted from inadequate procedures, lack of appropriate policies and lack of managerial oversight to ensure that employees do what is required. In addition, there were instances where District officials did not require necessary the legal documentation that was needed to provide adequate protection for the District's interest in contractual relationships.

Competitive Bidding

The District's procurement guidelines require that purchase contracts for materials, equipment and supplies involving an estimated annual expenditure exceeding \$10,000 and public work contracts involving an expenditure of more than \$20,000 will be awarded only after responsible bids have been received in response to a public advertisement. Purchases or public work contracts which are made from New York State contracts are exempt from bidding provisions.

Although the District has a procurement policy with relevant procedures in place for the acquisition of goods and services in accordance with the competitive bidding and procurement statutes, District officials did not always follow these procedures. Purchasing department personnel were not vigilant in ensuring that all goods and services were acquired in accordance with these policies. Furthermore, purchasing officials did not have a full understanding of the competitive bidding statute regarding the use of State contracts.

We reviewed purchasing transactions with five vendors totaling \$584,172 to determine if the District requested bids in accordance with its procurement policy. During the 2004-05 school year, the District paid three vendors \$378,522 for the following: surveillance equipment (\$173,892) and installation (\$128,440), vision testing and audiometer equipment (\$34,620) and cleaning supplies (\$41,570). These contracts were not awarded pursuant to the bidding requirements.

District officials claimed that they acquired and installed surveillance equipment through a vendor who had been awarded a New York State contract which exempted them from the bidding requirements. State contracts provide only for the specific items which are included in the particular contracts. The prices and descriptions of the items that the District purchased were not the same as those in the State contract. Therefore, we do not agree that the purchase and installation of this equipment was proper. Acquiring goods and services without bidding and not using a proper State contract, provides an unfair advantage to the vendors and provides no assurance that the District acquired these items at the best price.

Payments for Professional Services

Written agreements between the District and professionals provide both parties with a clear understanding of the services the professionals are expected to provide and the compensation for those services. A resolution of the Board is also a suitable method of authorization to pay professionals if the resolution clearly states the services to be provided and the basis for compensation. Amendments to agreements and resolutions need to be approved by the Board and provide a clear understanding of the intended changes.

For the period July 1, 2004 to June 30, 2005, the District paid six professionals \$924,804 to perform such services as construction management, accounting, counsel to the Board, owner's representative, communication consulting and bond counsel. Written agreements for the services of four of the six professionals totaling \$836,988 did not contain a clear description of the compensation these professionals were entitled to.

- For the period July 1, 2004 through June 30, 2005, the District paid a construction manager \$644,795, for service to commence through December 31, 2006. The original written agreement included handwritten changes including the starting date and terms, additional services and the effective period. Throughout sections of the agreement handwritten changes were made which only one party initialed. The starting date was initially September 1, 2000 but was changed initially to October and then to November of 2000. The effective period of the contract was changed from 53 to 60 months. Because of the uncertainty of the starting date and the effective period of the contract, it is not clear what the District intended to be the contractual requirements of the contract.
- The District paid its Board counsel \$128,385 for professional services and other expenses without a written contract. The

³ Owner's representative acts on the owner's behalf in approving construction documents, and is a liaison between contractors and the owner.

Board had no documentation of its agreement other than its original resolution appointing the Counsel to the Board.

- The District paid its communication consultants \$39,911 in August 2004 for telephone bill verification services. This payment represented 50 percent of the \$79,823 refund which the District received from the service provider for over-billed services. The District had no written agreement which detailed the consultant's entitlement to this compensation.
- The District paid bond counsel \$23,895 for professional service. While District officials had a Board resolution which appointed bond counsel, they had no written agreement for this service.

The lack of written agreements with professionals deprives the District of protection in the event that these professionals default on their obligations. In addition, there is no clear understanding of what compensation these professionals are entitled to and the extent of service which is required for such compensation.

Recommendations

5. The District should ensure that all items which exceed the bidding thresholds are competitively bid.
6. The District should ensure that all purchasing officials and department heads are properly trained in all aspects of the bidding laws and the use of State contracts.
7. The District should ensure that written agreements with all professionals clearly define the amount of compensation and duration of the work to be performed. Any amendments to written agreements or Board resolutions should be clearly communicated and approved by the Board.

Controls Over Assets

One of the Board's managerial responsibilities is to establish and monitor a system of internal controls over District assets. A good system of internal controls should be designed to provide reasonable assurance that District assets are properly safeguarded; accounting transactions are authorized, recorded and reported properly; pertinent laws and regulations are complied with; work performed is monitored and reviewed routinely; and operations are efficient and effective. Furthermore, an effective system of internal controls provides for the segregation of duties so that no single individual controls all phases of a transaction. When it is not practical to segregate duties because of limited staff resources, the Board should establish compensating controls. Such compensating controls would include the Board or other administrative staff periodically reviewing the work in question, rotation of duties and mandatory vacations.

We found significant weaknesses in the internal controls over District assets. The Board did not ensure that policies and procedures that safeguard assets exist. The lack of segregation of duties and absence of management and supervisory review of wire transfers and the untimely preparation of reconciliations provide opportunities for significant errors and irregularities to occur without being detected and corrected.

Segregation of Duties

An effective system of internal controls requires the segregation of incompatible tasks and responsibilities (i.e., authorization, recordkeeping and custody) among various employees. Separating key tasks and responsibilities reduces the risk of error or irregularities. It provides for an independent review of an employee's work by someone else in the course of performing their normal duties. Management can mitigate many control weaknesses by performing reviews of employee work.

Wire Transfer Payments- One clerk is authorized to make payments by wire transfer to government agencies for statutory charges and payroll deductions. The Treasurer does not provide oversight over these payments. This clerk is also responsible for generating payroll records and calculating the taxes for the payrolls. No one reviews the clerk's work before she makes payments.

In June 2005, the Treasurer transferred \$941,709 to the gross payroll account instead of the main operating account, based on a transfer document which a clerk prepared. In the same month a clerk made two errors calculating payroll payments, overpaying the State \$15,973 and underpaying the Internal Revenue Service \$435. If the Treasurer

reviewed the wire transfer requests properly before they were made, the errors may have been prevented.

Management Positions - We found there was a lack of segregation of duties for three key members of its management team, the District Treasurer, Internal Auditor and Purchasing Agent. The conflicting nature of duties assigned to these three officers created areas of significant weakness in the internal control structure. Furthermore, in all three instances, there was no evidence that Board members fully exercised their oversight duty, which could have reduced the effect of such weaknesses.

The District Treasurer supervises the recording of cash disbursements, prepares the bank reconciliation and is a single signatory on the bank accounts. As a result, the Treasurer has the ability to execute and conceal irregular transactions. In addition, there is no independent review of the bank reconciliation for accuracy or to mitigate the effect of the incompatible functions.

The Internal Auditor is also the capital projects analyst. The job of the capital project analyst involves preparing documentation and submitting it to SED, interacting with the construction manager and supervising a clerk who records the disbursement of capital projects funds. The Internal Auditor is also required to audit and approve all claims against the District, including capital projects claims. As a result, the Internal Auditor audits her own work, as relates to capital project expenditures.

The Purchasing Agent approves the acquisition of assets and also maintains the inventory of capital assets. No physical inventory of capital assets is taken annually. Therefore, the Purchasing Agent records transactions which he approves without any objective review from an independent person. This could expose District assets to potential irregularities.

Bank Reconciliations

An effective internal control system over cash receipts and disbursements requires that bank accounts be reconciled to the accounting records monthly. Bank reconciliations are control activities designed to identify errors or irregularities and alert management to their occurrence. If bank accounts are not reconciled timely with adjustments posted from the reconciliations to the accounting records and differences investigated and corrected, errors and irregularities may worsen over time.

The District does not have specific procedures or policies in place to ensure that bank reconciliations are completed timely with differences corrected and adjustments made at month end before the next period

begins. As a result, the Treasurer does not complete reconciliations timely and does not research and correct adjusting items from the reconciliations to the accounting records timely.

As of November 15, 2005, the District's main operating account, which handles more than \$60 million in transactions annually, was not reconciled for the fiscal year ended June 30, 2005 and has not been reconciled for more than two years.

Both the gross payroll account, which handles payments to government agencies for payroll taxes, and the net payroll account, which handles paychecks to employees, had reconciliation differences each month for more than two years. As of November 15, 2005, these accounts had not been reconciled for the month ending July 31, 2005. The net payroll account and the gross payroll account also contained a journal entry for \$3,351.03 to void old outstanding checks. This entry was posted to the books in November 2004 and on their respective reconciliations as of June 30, 2005. Due to an error, this entry was not posted properly. However, this was not researched and corrected as of June 30, 2005.

Extra classroom accounts are maintained by each school for the purposes of supporting the respective school's student clubs and organizations. There is also a lack of Board and District management oversight of the extra classroom accounts and their respective bank reconciliations throughout the year, which allowed activities to go unrecorded, adjustments to be left out, and prevented bank accounts from being completely reconciled. The AB Davis School and Thornton School did not account for all of the activity that occurred in the extra classroom accounts during the fiscal year ended June 30, 2005.

- The AB Davis School had not recorded a check for \$362, drawn in June 2005, in the ledger as of June 30, 2005. Also, a deposit for \$2,430 made in August 2004 was not included in the ledger as of June 30, 2005. This account also had a reconciliation difference of \$931 as of June 30, 2005 that existed prior to April 2005. Deposits to this account range from about \$1,000 to \$9,000 every month.
- The Thornton School had also not recorded all activities in their extra classroom accounting ledgers for the fiscal year ended June 30, 2005. The bank reconciliation as of June 30, 2005 still contained a deposit of \$2,079.08 that occurred in March 2005 and a deposit of \$800 that occurred in February 2005. These deposits were not posted to the accounting records until July 2005. Deposits to this account range from about \$1,000 to \$5,000 every month.

Resolving reconciliation differences timely allows the District to detect errors or irregularities and correct them. Since District officials did not use reconciliations to correct errors, differences between bank and book balances fluctuated and compounded over time, making errors more difficult to detect and correct. The Board and District management's non-participation in the process weakened the benefit of bank reconciliations as a monitoring tool.

Recommendations

8. The Treasurer should review all payroll tax computations and wire transfer documentations before allowing clerks to execute wire transfers.
9. The Board should review the scope of duties of the District Treasurer, Internal Auditor and Purchasing Agent and separate the incompatible functions. If there are not enough qualified employees to effectively execute proper controls in the respective areas, compensating controls, such as an increase in management review, should be implemented to ensure that District assets are safeguarded.
10. The Assistant Superintendent of Business should ensure that all bank accounts are reconciled on a monthly basis. If differences exist between book and bank balances, these differences should be investigated and resolved promptly.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

The District officials' response to this audit can be found on the following pages.

The District's response letter also contained 21 additional exhibits that we did not include in our audit report. Since the District's response letter generally describes the exhibit's contents and their importance in sufficient detail, we did not include the exhibits in Appendix A. The 21 exhibits have been filed in our workpapers.



Mount Vernon City School District

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Brenda L. Smith
Superintendent of Schools

September 14, 2006

Office of the State Comptroller
Albany Regional Office
22 Computer Drive West
Albany, NY 12205-1695

Ladies and Gentlemen:

The members of the Mount Vernon City School District Board of Education, the Superintendent of Schools, and the administrative staff are appreciative of the work of the auditing team from the Office of the New York State Comptroller reflecting the period July 1, 2004 to June 30, 2005.

The School Board and administration have carefully reviewed and discussed each finding and recommendation. As noted in the exit conference held Thursday, August 24, 2006, we view this audit as an opportunity to strengthen our financial operations.

The District implemented changes before and during the Comptroller's audit that have strengthened our management controls. These changes include the following:

- The Board hired a claims auditor February 15, 2006, separating the claims auditor function from the internal auditor position.
- The responsibilities for bank reconciliations were reassigned from the Treasurer to another qualified employee May, 2006. Bank reconciliations will be reconciled on a monthly basis.
- The Board advertised for a Clerk of the Board in July, 2006, to separate the Clerk function from the Assistant superintendent for Business, which will allow the business administration more time for the oversight of business functions.

The Board is contracting with New York State Association of School Business Officials (NYASBO) for an evaluation of job responsibilities, staffing levels, use of technology and segregation of duties in order to maximize the efficiency and effectiveness of the business office. Specific emphasis will be placed on segregation of duty issues.

AWARD WINNING SCHOOL DISTRICT
SECONDARY SCHOOL RECOGNITION PROGRAM
UNITED STATES DEPARTMENT OF EDUCATION

The Board hired Fiscal Advisors & Marketing, Inc. from Syracuse, New York on January 4, 2006 and renewed the contract on September 6, 2006 to serve as an independent Building State Aid advisor to the School District. The fiscal advisors will assist with and/or review all forms relating to the Building Aid from the State Education Department. They will assist with the preparation and filing of Final Cost Reports on the District's capital program as required by the State Education Department.

- As required by recent legislation, the District has established its Audit Committee, which will provide additional oversight of financial operations and internal control.
- The Purchasing Agent attended the SAMPO Conference (State Association for Municipal Purchasing Officials), May 10-May 12, 2006, and received in-depth training on purchasing procedures, district procurement practices and the use of State contracts. The Assistant Superintendent for Business and the Purchasing Agent will attend the Fifth SAMPO Training Seminar in Long Island, New York, October 18-19, 2006. Classes will include Purchasing I and II; Detecting Criminal Antitrust Violations; School District Procurement Practices; Effective RFP's; OSC Audits; and Safe Cleaning Products (Green Products).
- The Board approved a written retainer agreement with its board counsel on November 2, 2005 and again on August 2, 2006.
- On September 18, 2006, the district will begin utilizing its financial management software's capabilities for electronic purchase orders. This will not only expedite the process of handling purchase orders it will free up time for the entire Purchasing Department to spend on adherence to purchase requirements.
- The District recognizes the need to ensure that the construction manager and owner's representative are more diligent in their review of proposed change orders and that the necessary AIA change order documents are properly executed. The District has implemented a new procedure for the review, approval and/or rejection of change order requests and will adopt the recommendations set forth in the Audit Report. In addition, the District will adopt amended bond resolutions to effect any changes to the purposes of the original bond resolution and in the future will not adopt a bond resolution authorizing the issuance of bonds for more than one purpose unless the adoption of such resolution is authorized by Section 31.00(d) of the local finance law.
- The District acknowledges that two change orders totaling \$67,582.28 were not approved by the owner's representative since he was no longer employed with the District at the time. However, the remaining change orders referenced in the audit report were reviewed, authorized and approved by the owner's representative even though some were not fully executed on an AIA change order document.

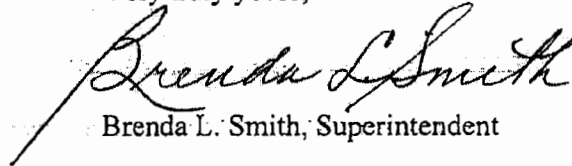
Mount Vernon City School District
Response to Audit Findings and Recommendations
September 14, 2006

In the next three sections, we present our responses to the specific audit findings and recommendations as they relate to the following:

- **The Middle School Construction Project**
- **Purchasing Practices**
- **Control Over Assets**

The Mount Vernon Board of Education and its school officials are committed to establishing and maintaining strong internal controls, and do not take lightly the public's trust in the financial operation of this district. As a matter of fact, we view it as critical as well as public's confidence in the members of the Board of Education and its employees.

Very truly yours,

A handwritten signature in cursive script that reads "Brenda L. Smith". The signature is written in black ink and is positioned above the printed name.

Brenda L. Smith, Superintendent

Enclosures

LONGFELLOW MIDDLE SCHOOL CONSTRUCTION PROJECT

I. CHANGE ORDERS

Audit Findings

District records show that change orders totaling \$946,868 were added to seven of the ten construction contracts at the Longfellow Middle School. Although several requests were made for these change orders, change orders totaling \$915,043 could not be located by District staff.

District Response

This letter and the accompanying documents are submitted on behalf of the Mount Vernon School District to address the audit findings above pertaining to change orders to seven of the ten construction contracts at the Longfellow Middle School.

Background

In 1999, the School District passed a bond referendum of 100 million dollars to finance the construction of two new schools and the renovation and reconstruction of various existing school buildings. The District hired Turner/Luster to act as construction managers for the Capital Projects Program and oversee the construction and renovation of the school buildings. The District also retained the services of three separate architectural firms to work on the various capital projects: EI Associates, Ted D'Amore Designs and Mount Vernon Joint Venture Architects Group led by Roberta Washington. Numerous construction management firms and architects were interviewed before the above selections were made.

At the time of the bond's passage, the District had in place a Superintendent of Buildings and Grounds who was responsible for overseeing the emergency repair projects which started in

1999. However, by the time the District began to proceed with the Capital Projects Program, the position of Superintendent of Buildings and Grounds had been abolished. In accordance with Civil Service Law Section 80 et seq., the District was unable to fill this position for a period of five (5) years.

With the absence of this position, the then Board of Trustees immediately recognized that it was imperative to hire an owner's representative to act on the Board's behalf as a liaison between Turner/Luster, architects and contractors and the Board Trustees, District Administration and staff. After a thorough search for an owner's representative, the District retained the services of Barry Jordan of Prism Strategic Services, to assist the Board in the numerous decisions which needed to be made on a daily basis to move the Capital Projects Program forward. The duties and responsibilities were set forth in a retainer agreement entered into between the District and the owner's representative. Among these duties and responsibilities was the handling of change orders which included review of any and all proposed change orders. The owner's representative was directly responsible for the review of change orders, deciding whether to accept and/or reject any change orders and reporting to the Board on a monthly basis the status of any proposed change orders for the entire Capital Projects Program.

The District's decision to hire an owner's representative was predicated in part on the need for an additional check and balance to ensure that Board members and the Mount Vernon School District were not taken advantage of by unscrupulous contractors. The Board was keenly aware and concerned that any change orders issued be necessary, reasonable and cost efficient. The system which was put in place required the owner's representative to review any and all proposed change orders and to accept such change orders only if they were necessary, cost

effective and in the District's best interests. The District was cognizant that in a project of this scale, there would inevitably be change orders.

The Board delegated the responsibility for reviewing, approving and/or rejecting change orders to the owner's representative because he was more experienced and better qualified to determine whether the proposed change orders were reasonable, necessary and cost effective. In addition, the owner's representative was in the best position to respond and review change order requests on a timely basis given the impracticability of convening a Board meeting each and every time there was a proposed change order which would require first going into the field to access whether the change order was necessary and, second, meeting with contractors to negotiate a fair price. Most Board members did not have the level of construction expertise required to handle such matters. Against this background, the Board hired an owner's representative to handle change order requests on their behalf and report to the Board on a monthly basis with respect to the status of any proposed change orders. The owner's representative's report would include a discussion and review of the proposed change orders, a cost estimate of the change order and any other options available. Every month the owner's representative presented a thorough report.

The owner's representative oversight was put in place at the inception of the Capital Projects Program and before construction began at the Longfellow Middle School. The Board believed it was acting in a fiscally prudent manner by hiring an owner's representative to assist in the Capital Projects Program.

Audit Report

The audit report identified change orders totaling \$946,868 which were added to seven of the ten construction contracts. We have put together a spreadsheet to identify the seven contracts

and the proposed change orders for each contract at issue. Attached is a copy of the spreadsheet for your review. (See Exhibit A).

The seven contractors identified in connection with these change orders are as follows: ELQ, ROK-Built, Schenectady, ACS, Yonkers Electric, BRC Kitchen and Longo Associates.

On the attached spreadsheet, we have listed separately each proposed change order and the respective amount. The total amount of the change orders identified in the audit report is \$946,867.62 broken down by contract as follows:

<u>Contractor</u>	<u>Change Order(s) Amount</u>
ELQ	\$210,316.59
ROK-Built	\$626,692.45
Schenectady	\$ 36,761.00
ACS	\$ 19,280.78
Yonkers Electric	\$ 40,619.24
BRC Kitchen	\$ 4,700.00
Longo Associates	<u>\$ 8,497.56</u>
Total:	\$946,867.62

A response to each contractor/change order(s) is set forth below.

ELQ

There was a total of \$210,316.59 worth of change orders under this contract which represents thirteen separate change order requests as well as a \$38,000 allowance. On a prior occasion, the District provided the auditors with fully executed change orders totaling \$104,734.31 with supporting documentation. We attach again a copy of these documents for your review. (See Exhibit B). The individual amounts of these change orders are as follows:

See
Note 1
Page 47

Change Order Amount

\$ 17,971.28
\$ 37,733.85
\$ 5,843.75
\$ 4,974.11
\$ 4,362.90
\$ 1,760.00
\$ 2,158.16
\$ 16,011.14
\$ 2,469.25
\$ 6,275.56
\$ 5,174.31

Total: \$104,734.31

A review of the documentation previously provided regarding the above change orders totaling \$104,734.31 were reviewed, approved and accepted by the owner's representative and were fully executed change orders.

The District does acknowledge that the following proposed change orders in the amounts of \$4,729.73 and \$62,852.55 totaling \$67,582.28 occurred when the owner's representative was no longer working in the District and will be discussed separately herein.

The final item with respect to the ELQ contract involves the amount of \$38,000 which was not a change order, but rather an alternate bid which was part of an overall accepted bid approved by the Board in a separate resolution. An alternate bid was accepted so that in the event any monies became available as a result of cost savings, etc., the alternate project could be done. The Board was fully aware during construction of this alternate bid and voted to authorize this project if and when the necessary funds became available. (See Exhibit C).

See
Note 2
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ROK-Built

With respect to the ROK-Built contract, there were proposed change orders totaling \$626,692.45. (See Exhibit A). This amount is broken down as follows: 5 items totaling \$462,275.95 were listed as construction change directives and 17 items totaling \$164,416.50 represented 17 separate change orders.

On a prior occasion, the District provided the auditors with 17 fully executed change orders totaling \$164,416.50 with supporting documentation. We again attach a copy of these documents for your review. (See Exhibit D). The individual amounts of these change orders are as follows:

See
Note 1
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<u>Change Order #</u>	<u>Amount</u>
1	\$14,081.12
2	\$16,138.00
3	\$10,330.00
4	\$ 4,291.00
5	\$ 4,977.00
6	\$ 960.00
7	\$13,000.00
8	\$14,249.71
9	\$11,399.76
10	\$11,399.76
11	\$ 5,699.88
12	\$ 2,834.50
13	\$ 808.50
14	\$30,400.63
15	\$ 9,135.00
16	\$ 7,150.60
17	<u>\$ 7,561.04</u>
Totals:	\$164,416.50

The following items were listed as construction change directives totaling \$462,275.95.

These items are broken down as follows:

Proposals:

\$ 21,931.00
\$ 41,175.00
\$ 49,134.00
\$ 80,435.95
\$269,600.00

Totals: \$462,275.95

At the outset, it is important to understand that these five items (construction directives) were actually proposed change orders.

A close inspection of the documents will show that although the proposed change orders totaled \$462,275.95, the District accepted, authorized and agreed to only \$276,903.48 worth of these change orders and rejected \$185,372.47 worth of change orders. Therefore, the total amount at issue is \$276,903.45, not \$462,275.95 as reflected in the audit report.

See
Note 3
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<u>Proposed</u>	<u>Agreed Amount</u>
\$ 21,931.00	\$ 21,931.00
\$ 41,175.00	\$ 20,587.50
\$ 49,134.00	\$ 24,567.00
\$ 80,435.95	\$ 40,217.98
<u>\$269,600.00</u>	<u>\$169,600.00</u>
Subtotal: \$462,275.95	Subtotal: \$276,903.48
Difference: \$185,372.47	

Although the owner's representative reviewed, approved and authorized \$276,903.48 worth of change orders, these proposals were not fully executed on an A1A change order document. Enclosed please find backup documentation for the five change orders totaling \$276,903.48. (See Exhibit E).

See
Note 4
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Schenectady

With respect to the Schenectady contract, a review of the attached spreadsheet will show five separate proposed change orders in the amounts of \$1,869.00, \$25,912.00, \$3,109.00, \$2,826.00 and \$3,045.00 totaling \$36,761.00. On a prior occasion, the District provided the auditors with a fully executed change order totaling \$1,869.00 with supporting documents. We again attach a copy of these documents for your review. (See Exhibit F). The remaining four change orders in the individual amounts set forth above and totaling \$34,892.00 were reviewed, authorized and approved by the owner's representative but were not fully executed on an A1A change order document. Attached please find backup documentation pertaining to the above four change orders. (See Exhibit G).

See
Note 5
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See
Note 4
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ACS

With respect to the ACS contract, a review of the attached spreadsheet will show one change order totaling \$19,280.78. (See Exhibit A). Although paperwork for this change order was previously provided to the State Auditors, enclosed please find a fully executed change order with supporting documentation for this change order in the amount of \$19,280.78. (See Exhibit H).

See
Note 5
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Yonkers Electric

With respect to the Yonkers Electric contract, a review of the attached spreadsheet will show five change orders in the amounts of \$28,076.00, \$3,411.00, \$1,742.55, \$5,819.35 and \$1,570.34 totaling \$40,619.24. (See Exhibit A).

On a prior occasion, the District provided the auditors with a fully executed change order for the first change order listed above in the amount of \$28,076.00. We again attach a copy of these documents for your review. (See Exhibit I).

See
Note 5
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The remaining four proposed change orders totaling \$12,543.24 were reviewed, authorized and approved by the owner's representative, even though these proposed change orders were not fully executed on an A1A change order document. We have enclosed for your review backup documentation with respect to these four (4) proposed change orders. (See Exhibit J).

See
Note 4
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BRC Kitchen

With respect to the BRC contract, a review of the attached spreadsheet will show one change order totaling \$4,700. (See Exhibit A). This proposed change order was reviewed, authorized and approved by the owner's representative but was not fully executed on an A1A change order document. We have enclosed for your review the backup documentation with respect to this proposed change order. (See Exhibit K).

See
Note 4
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Longo Associates

With respect to the Longo Associates contract, a review of the attached spreadsheet will show three separate proposed change orders in the amounts of \$4,458.30, \$3,300.00 and \$739.26 totaling \$8,497.56. (See Exhibit A). These proposed change orders were reviewed, authorized and accepted by the owner's representative but were not fully executed on A1A change order documents. We have enclosed for your review the backup documentation with respect to these three (3) proposed change orders. (See Exhibit L).

See
Note 4
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Summary

In summary, the audit report identified change orders totaling \$946,868.62 with respect to seven construction contracts at the Longfellow Middle School. Of this amount, the District has provided to the State Auditors fully executed change orders with supporting documentation

for change orders totaling \$330,919.83. The remaining amount of \$615,947.79 has been

See
Note 6
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identified and accounted for as follows:

1. \$185,372.47 of change orders submitted by Rok-Built was rejected and not paid for.
2. \$38,000 was not a change order but rather an allowance which the Board authorized and approved.
3. Change orders in the total amount of \$324,993.04 were reviewed, authorized and approved by the owner's representative. The District has provided documentation related to these proposed change orders and has acknowledged that although approved by the owner's representative, these change orders were not fully executed on an AIA change order document.
4. With respect to the final two change orders pertaining to the ELQ contract in the amounts of \$4,729.73 and \$62,852.55 respectively, the District acknowledges that at the time of these two proposed change orders, the owner's representative was no longer employed with the School District and therefore the change orders were not reviewed, authorized or approved. During this period, the Board had assigned a District Administrator, Paul Berliner, to temporarily serve in the capacity of a quasi-owner's representative for the Capital Projects Program until such time as a new owner's representative was hired. Although Mr. Berliner interacted with the construction managers and reviewed change order requests, he was not authorized by the Board to approve or reject proposed change order requests. Therefore, those two change orders were reviewed, authorized and approved only by the construction manager and architect on the District's behalf.

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Note 3
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Note 2
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See
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As a result of this audit, the District recognizes the need to ensure that the construction manager and owner's representative are more diligent in their review of proposed change orders and that the necessary change order documents are properly executed. The District has since retained another owner's representative and effective immediately, the District has implemented a new change order procedure. The District has also discussed the audit report findings with the new owner's representative and has developed a plan moving forward to address concerns raised in the audit report with respect to the change orders. The new procedure will require the following steps be taken to ensure compliance with the recommendations and suggestions in the audit report:

- The contractor will prepare a change order request.
- The contractor will submit the change order request to the construction manager, architect and owner's representative for review.
- The construction manager, architect and owner's representative can reject the change order request.
- The construction manager, architect and owner's representative can approve the scope of the change order and negotiate the change order amount with contractor.
- The approved change order is then returned to the contractor for preparation of an A1A change order document.
- The contractor submits the A1A change order document to the District for execution.
- The owner's representative reviews and approves the A1A change order document.
- The District executes the A1A change order document.
- The original executed A1A change order document is to be maintained in the District files while copies of the executed A1A change order documents are distributed to the contractor and owner's representative.

While the Board acted in "good faith" to hire a qualified owner's representative at the start of the Capital Projects Program to safeguard District assets and oversee change order

requests, it appears the owner's representative was lax at times in making sure the proper change order paperwork was filled out. We remain confident that no District funds were misappropriated and that the District received fair value for money spent.

With respect to the Longfellow Middle School project, the total construction cost of the seven contracts listed in the State Audit was approximately 17 million dollars. The amount of actual and District paid change orders for these seven contracts totaled \$723,495.15 (\$946,867.62 less \$38,000 allowance and less \$185,372.47 of proposed Rok-Built change orders not accepted and paid for) which represents slightly less than 4.5% of the construction cost. On an industry-wide basis, this figure represents a relatively small amount of change order requests for a project of this scale and magnitude.

Nevertheless, the District recognizes the need to be vigilant in protecting District assets and adopting a process to make sure that any change order is necessary, reasonable, cost-effective and in the best interest of the District and the District will work diligently with the new owner's representative to make sure all required change order paperwork is properly filled out.

The District is grateful to the State auditors for making recommendations on how we can improve our oversight of the Capital Projects Program going forward and the District intends to implement the recommendations suggested with respect to the Capital Projects Program as follows: first, the Board will establish controls for the use of contingent allowances in construction contracts; second, the District will ensure that documentation is available to support the District's expenditures for all capital projects; and finally the District will ensure that all change orders and final cost reports are submitted to SED in the most efficient manner to obtain timely state aid reimbursements.

II. ADOPTION OF BOND RESOLUTION AND USE OF BOND PROCEEDS

Audit Findings

The Board adopted a Bond Resolution which authorized the issuing of several bonds totaling \$100 million dollars. The bonds were intended to finance the construction of various school buildings throughout the District. The bond resolution stipulated that the bonds would be used for two different purposes: first, the construction of two new school buildings including a new middle school at Longfellow Middle School for over 600 students; and second, renovation and reconstruction of existing school buildings.

According to the audit report, the Board should have adopted and submitted for voter approval two separate bond resolutions – one bond resolution authorizing the issuance of bonds to finance the construction of two new school buildings; and, a second bond resolution authorizing the issuance of bonds to finance the construction of additions to or the renovation of existing school buildings.

The second issue raised in the audit report with respect to the bond involves the Board authorizing the transfer of 1.1 million dollars from the construction of the new Longfellow Middle School to increase the amounts available to renovate several existing school buildings. In authorizing this transfer, the Board inappropriately permitted the proceeds of the bonds issued for one purpose (new schools) to be used for a different purpose (renovation of existing school buildings).

District Response

This letter and the accompanying documents are submitted on behalf of the Mount Vernon City School District to address the audit report findings above pertaining to the issuance

of one bond rather than two separate bonds and the transfer of 1.1 million dollars from one project (Longfellow Middle School) to another project (renovation of existing school buildings).

Background

Before embarking on the current Capital Projects Program, the Board did a district-wide feasibility study to examine the existing buildings and to develop a long term plan to renovate the existing schools and construct new schools where necessary. The budget was prepared based on estimates provided by the construction manager and architect. The needs that were assessed in the District exceeded \$260 million dollars; however, due to the debt limit and political considerations, the District agreed to borrow only \$100 million dollars.

During the planning stage of the Capital Projects Program, the District had on retainer as bond counsel, the law firm of Nixon Peabody, LLP which specializes in school construction bonds. The partner assigned to handle the District's bond work was Robert H. Carey. During this time, the District consulted regularly with Nixon Peabody regarding the issuance of bonds to finance the various capital projects. When it came time to prepare the language for the bond resolution to be voted upon by the public, the District again relied upon Nixon Peabody to advise them how to proceed. Counsel drafted the bond resolution and the District relied on counsel's representation that such issuance was valid, legal and proper.

As a result of the audit report, the District contacted Nixon Peabody. Mr. Carey assured the District once again that what the District did at the time was legal and valid. In addition, he forwarded to the District an opinion letter as well as an opinion letter from the Office of the Attorney General of the State of New York in support of his position. (See Exhibit A).

With respect to the second issue regarding the transfer of 1.1 million dollars from one project (Longfellow) to another (renovation of existing schools), the District relied on the advise

of its construction manager, Turner/Luster. The cost for Longfellow Middle School that was originally budgeted came in under the projected estimates. Since the bond authorization was done as a single authorization, it was the District's opinion based in part on the advice of its construction manager and prior bond counsel, that the District had the flexibility to transfer funds from one project to another.

As a result of this audit, the District has learned that two separate bonds should have been authorized at the inception of this Capital Projects Program. Therefore, it is the Board's intention to adopt the recommendations contained in the audit report; namely, to adopt amended bond resolutions to reflect any changes to the purposes of the original bond resolutions and second; in the future the Board will not adopt a bond resolution authorizing the issuance of bonds for more than one purpose unless the adoption of such resolution is authorized by Section 31:00 (d) of the local finance law.

III. STATE AID

Audit Findings

SED officials informed us that, as of August 8, 2006, the District had not submitted any change orders or final cost reports for this project. With the automatic extension the District could have until June 2007 to file the change orders and final cost reports. Although the District still has time to submit these change orders and final cost report to SED, delayed submission also delays the availability of State aid for the District. Failure to submit proper documentation to the SED in a timely manner could result in a reduction in State aid.

District Response

This response and the accompanying documents are submitted on behalf of the Mount Vernon School District to address the audit findings above pertaining to State Aid on the Longfellow Middle School.

Background

When a project has been approved by the State Education Department, specifications and plans are generated and mailed out for the upcoming bid. Once a bid is awarded, then bonds are issued to satisfy the upcoming expenditures. A State form SA139 is prepared and submitted to the State noting what the bid was awarded for. This form starts the time when aid would be awarded to the District. Once the project is completed and all the vendors are paid, a Final Building Cost Report is prepared and sent to the State. The State will then recalculate the aid that the District was receiving based on the submission of an SA139. The submission of the Final Building Cost Report will not be the report that will begin to generate aid to the District.

The Longfellow Middle school has been substantially completed and a Certificate of Occupancy has been obtained. However, a Final Building Cost Report cannot be prepared and submitted to the State until all vendors have been paid. In this case, there are several vendors who have still not been paid in full. Despite this, the District is not losing aid on this project since aid was granted when the SA139 form was submitted. The aid will be recalculated when the Final Building Project Report is submitted for final review. To say that the District "*could have*" until June 2007 is misleading, since the District ~~does have~~ until June 2007 to submit the Final Building Cost Reports.

See
Note 7
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Change Orders were submitted to the State Education Department for several projects including the Longfellow Middle School in 2004. Most of the Change Orders were returned to

the District to be certified and recorded on the State Education Change Order Certification form. On February 24, 2006, a memorandum was addressed to [REDACTED] of the State Education Department, along with numerous certified Change Orders that were returned to the District. The reason why these Change Orders are not reflected on the State's website is not a result of the District's inability to comply with the State Education Department requirements; but rather that the State has not yet entered the fully executed and documented Change Orders that have been submitted by the District since February 24, 2006.

The District intends to adopt the recommendations contained in the Audit Report to ensure that all change orders and final cost report are submitted to the SED in the most efficient manner to obtain timely State Aid reimbursements.

PURCHASING PRACTICES

Audit Findings

The audit found significant weaknesses in the District's internal controls over purchasing practices. Although the District had policies and procedures in place for the acquisition of goods and services, there were instances where departments circumvented these procedures. The District did not seek bids for \$378,522 of purchases and public works contracts that were subject to competitive bidding. Also, the District paid four professionals \$836,988 when their contracts did not contain a clear understanding of the amount of compensation they were entitled to.

District Response to Findings

Competitive Bidding

The Purchasing Agent attended the May 10-12, 2006 State Association for Municipal Officials in-depth training sessions on purchasing procedures and the use of State contracts. He will attend the October 18-19, 2006 training sessions on School District Procurement Practices, Effective RFP's, Purchasing 1 and 11; OSC Audits; and Safe Cleaning Products (Green Products). It is the District's resolve to scrupulously adhere to bidding requirements and requirements for use of State contracts. See Response to Recommendation 6.

Regarding the referenced \$378,522 of purchases:

- The District purchased metal detectors for \$ 38,079 utilizing State contract PC 58381. The successful vendor on the State contract was Integra Consulting and Computer Services, Inc.. The vendor on the District's purchase order was A+ Technical Solutions, Inc. Integra and A+ were owned by the same Board and operated as a joint venture. The District should have listed Integra as the vendor on the purchase order.
- The District purchased surveillance equipment and installation for \$ 190,128 utilizing State contract PC 58381. In the multiple cases where substitutions from the State contract were made, they were for equipment which met the District's needs at a lower cost and/or were of better quality. The District paid \$ 95,000 less for installation than the applicable State pricing.

See
Note 8
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See
Note 8
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The District purchased surveillance equipment installation for \$ 74,125 utilizing a State contract which was current during purchasing discussions, but which had expired two months prior to processing the actual purchase

See
Note 9
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order. The District paid \$ 18,000 less for installation than the applicable State pricing.

- The District purchased \$ 34,620 of vision testing and audiometer equipment based on the recommendation of the District's medical advisor. The District has used the same vendor for many years in order to maintain the level of service requested by the medical advisor.
- The District purchased \$41,570 of cleaning supplies based on a review by the Mount Vernon Health and Safety Committee of environmentally safe cleaning products.

There was no intent to circumvent bidding requirements or procedures. The additional training provided to the Purchasing Agent and the Purchasing Department combined with the review by the Assistant Superintendent for Business and the new Claims Auditor will ensure that bidding requirements and use of State contracts are thoroughly reviewed and followed at the time of purchase.

Regarding the Payments of \$836,988 for Professional Services:

- Construction Management payments of \$644,795:
The payments to the Board's Construction Manager were consistent with the Board's contract with the Construction Management Company. The District has enclosed a letter from the Board's attorney addressing audit concerns with respect to the Turner/Luster contract. (See Exhibit A).
- Board Counsel payments of \$ 128,385:
The District did not have a written contract with its attorney at the time of the audit. On November 2, 2005 the Board approved a written retainer agreement with its attorney and renewed that agreement on August 2, 2006.
- Communication Consultant payments of \$39,911:
In August 2004 the District paid a communications consultant \$39,911 for a telephone verification services audit conducted in 2002-2003. This represented 50 percent of a \$79,823 refund the District received as a result of the audit. Although a written document was never executed by the District, the document governing the terms and conditions of the audit, including payment terms, was the November 20, 2003 letter from Ms. Burwell of Communications Consulting Services, Inc. to Dr. Dawn Arno, then Assistant Superintendent for Business. The District has prepared a separate response which we have attached for your review. (See Exhibit B).

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Note 10
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Note 11
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- Bond Counsel payments of \$23,895:
The District has directed its attorney to finalize a retainer agreement with its bond counsel.

Recommendations

5. The District should ensure that all items which exceed the bidding thresholds are competitively bid.

Response

The additional training of the Purchasing Agent and Purchasing Department personnel, discussed in the next recommendation, as well as increased monitoring by the Assistant Superintendent for Business and the new Claims Auditor will ensure compliance with bidding requirements. .

6. The District should ensure that all purchasing officials and department heads are properly trained in all aspects of the bidding laws and the use of State contracts.

Response

The Purchasing Agent is a member of the NYS Association of Municipal Purchasing Officials. Over the last two years he has regularly attended their meetings.

From May 10 through May 12, 2006, the Purchasing Agent attended the SAMPO Conference which covered the following topics: Contract Administration, School District Procurement Practices, Introduction to Purchasing, Purchasing Audits by OSC, Ethics/Professionalism and, Model Procurement Code.

On October 18 and 19, 2006 the Purchasing Agent and the Assistant Superintendent for Business will both attend the SAMPO workshops on the following topics: Effective RFP's, Purchasing 1 and 11, OSC Audits and Safe Cleaning Products (Green Products).

The Assistant Superintendent for Business will randomly review and monitor purchases for compliance with bidding laws and use of State contracts.

On September 18, 2006, the district will begin utilizing its financial management software's capabilities for electronic purchase orders. This will not only expedite the process of handling purchase orders, it will free up time for the entire Purchasing Department to spend on adherence to purchasing requirements.

7. The District should ensure that written agreements with all professionals clearly define the amount of compensation and duration of the work to be performed. Any amendments to written agreements or Board resolutions should be clearly communicated and approved by the Board.

Response

The Purchasing Agent will ensure that all purchase orders for professional services contain the duration of the contract and compensation. The Board attorney will ensure that all contracts for professional services specify the duration of the work to be performed and the amount of compensation. Amendments to contracts will be sent to the Board for its prior approval..

CONTROLS OVER ASSETS

Audit Findings

The audit found the internal controls over the District's assets were weak. District management failed to implement proper policies and procedures for the supervision of wire transfers. In one instance, this resulted in a \$941,709 transfer made to the wrong account. In two other unrelated instances, it resulted in the overpayment of withholding taxes. The Board also assigned conflicting duties to three key members of its management team, the District Treasurer, Internal Auditor and, Purchasing Agent. The audit also found that bank reconciliations are not completed timely and there is a lack of oversight of the extra classroom accounts.

District Response to Findings

Segregation of Duties

Wire Transfer Payments

The Treasurer does provide oversight of transfer payments. The District followed its procedures for the supervision of wire transfers. The procedure was that all transfers required the prior approval of the Treasurer except those from a payroll tax withholding account to the Federal or State tax account. Payroll tax computations and transfers will now be reviewed prior to execution.

The referenced \$941,709 transfer from the Operating account was reviewed and approved by the Treasurer prior to execution. The Treasurer subsequently identified the mistake and corrected it.

The District agrees that a clerk made two separate errors calculating tax withholding payments. Payroll tax computations and transfers will now be reviewed prior to execution. Please see the response to recommendation 8 and 9.

Management Positions

The District agrees that there is a lack of segregation of duties for the Treasurer, Internal Auditor, and Purchasing Agent. The responsibility for maintaining the Fixed Asset Inventory will be reassigned from the Purchasing Agent; the functions of Internal Auditor and Capital Projects Accountant will be separated and the entire process of disbursement of funds is being reviewed in conjunction with the New York Association of School Business Officials. Please see the response to recommendation 9.

See Note 12 Page 48

Bank Reconciliations

Operating Account

The District agrees that all accounts should be reconciled on a monthly basis. The audit finding refers to the District's main account. The District has a total of 23 accounts, 21 of them were reconciled at the time of the audit. The responsibilities for bank reconciliations have been reassigned from the Treasurer to another qualified employee. Please see the response to recommendation 10.

Extra Classroom Accounts

The District agrees that all extra classroom accounts should be reconciled on a monthly basis and will require all Principals to submit monthly reconciliations to the Internal Auditor.

Presentations have been made at two Principals Meetings. A workshop for classroom account bookkeepers was conducted and this will become annual retraining.

Recommendations

- 8 The Treasurer should review all payroll tax computations and wire transfer documentations before allowing clerks to execute wire transfers.

Response

At the time of the audit, the procedure was that all transfers required the prior approval of the Treasurer except those from a payroll tax account to the Federal or State tax account. The payroll tax transfers were reviewed after the fact. We will now have the payroll tax computations and transfers reviewed prior to execution.

- 9 The Board should review the scope of duties of the District Treasurer, Internal Auditor and Purchasing Agent and separate the incompatible functions. If there are not enough qualified employees to effectively execute proper controls in the respective areas, compensating controls, such as an increase in management review, should be implemented to ensure that District assets are safeguarded.

Response

The Board has hired a Claims Auditor, separating that function from the Internal Auditor position.

The responsibilities for bank reconciliations have been reassigned from the Treasurer to another qualified employee.

On-line banking has been set up and the procedure where transactions are initiated by the Treasurer and completed by the Assistant Superintendent for Business is being implemented.

The Board has advertised for a Clerk of the Board. Given the size of the District, it is the Board's intent to separate the Clerk function from the Assistant Superintendent for Business function.

The Board has contracted with NYASBO for an evaluation of job responsibilities, staffing levels, use of technology and, segregation of duties in order to maximize the efficiency and effectiveness of the Business Office. Particular emphasis will be placed on segregation of duty issues.

- 10 The Assistant Superintendent for Business should ensure that all bank accounts are reconciled on a monthly basis. If differences exist between book and bank balances, these differences should be investigated and resolved promptly.

Response

The responsibilities for bank reconciliations have been reassigned from the Treasurer to another qualified employee. The Assistant Superintendent for Business will now ensure that all bank accounts will be reconciled on a monthly basis.

APPENDIX B

OSC COMMENTS TO THE DISTRICT'S RESPONSE

Note 1

We do not agree that the referenced change orders were fully executed. These change orders were signed by the owner's representative on October 29, 2004. However, the owner's representative lacked the authority to sign those change orders because his contract expired on October 8, 2004. District officials have not presented us with any documentation to indicate that the Board extended the representative's contract.

Note 2

District officials provided documentation supporting that the amount of \$38,000 was an alternate bid and not a change order. The District payment document which we originally relied on was incorrect. The amount of the alternate bid was incorrectly included in the total change orders to date and omitted from the contract sum. We have adjusted the report accordingly.

Note 3

We have amended our report to show that these change orders were not paid.

Note 4

Change orders often involve a significant amount of money. Obtaining verbal approval for change orders is not sufficient. Change orders require the authorization of the construction manager, contractor, architect and the owner. In order to ensure that each party has reviewed and approved the change order, change orders should be in writing and signed by each party.

Note 5

After our exit conference, District officials presented us with three change orders, \$1,869, \$19,280 and \$28,076 that were fully executed. We have reduced the amount in the finding to reflect the receipt of these three change orders.

Note 6

We disagree. District officials presented us with \$330,920 in change orders. Of this amount, \$269,151 was executed after the owner's representative's contract had expired and \$12,543 was not signed by the District or its representative. We found that \$49,226 of change orders were fully executed. We adjusted our report to reflect the receipt of these change orders.

Note 7

We have amended our report to clarify this issue.

Note 8

We examined the State contract referenced in the District's response. The vendor which was referenced on the payment record was the successful vendor on the State contract. However, the District purchased items that were not included in the State contract. Therefore, the exception to the competitive bidding laws does not apply.

Note 9

While the District asserts that it paid less for installation than the State contract price, it did not provide any documentation relating to the actual cost of the equipment.

Note 10

District officials claim that the payments to the construction manager were consistent with the contract and the District submitted a letter from its attorney. The attorney's letter stated that although the changes were not initialed by all parties, the contract was a binding agreement between the District and the construction manager and that the president of the Board was aware of the changes when he signed the contract.

We were unable to determine conclusively from the contract that we reviewed that the Board President was aware of the changes and signed the document after the changes were executed. In the future, all parties should initial changes to a contract during the signing process.

Note 11

According to the District's exhibits, the District's former Director of Technology authorized a consulting firm to audit telephone bills from providers in return for 50 percent of the refunds. The Board did not authorize the action and attempted to withdraw from the agreement. The District's attorney wrote a letter to the consulting firm to that effect and the communication consulting firm threatened to sue the District. District officials agree that no written contract was in place and emphasize that they acted in the best interest of the District. This sequence of events supports the need to have written contracts with vendors for professional services.

Note 12

We amended the report to state that the \$941,709 transfer was not properly reviewed by the Treasurer.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

During this audit, we reviewed internal controls over assets and purchasing for the District for the period July 1, 2004 to June 30, 2005. To accomplish our audit objective our procedures included the following to obtain valid audit evidence:

- We interviewed the Superintendent, Internal Auditor/Capital Project Analyst, Purchasing Agent, Treasurer, Assistant Superintendent for Business and other relevant officials and employees of the District and SED to obtain an understanding of the internal controls procedures that were in place at the District with regard to the purchasing practices, financial operations and capital assets.
- We reviewed the duties of the Treasurer, Internal Auditor/Capital Projects Analyst and Purchasing Agent and conducted various tests of transactions relating to these areas. These tests included: reviews of bank reconciliations, wire transfers, inspection of assets and capital assets inventory records.
- We reviewed contracts which the Board awarded for the construction of a new Middle School to determine if proper procedures were used in awarding such contracts and whether or not District officials had submitted relevant documentation to SED, including change orders that would have increased the total construction costs of the project. We examined the following records: vendor payment histories, contractors' payments applications, resolutions awarding contracts, bond issuance resolutions, contracts for ten vendors, change orders, as available, and newspaper advertisements.
- We reviewed payments to six professionals to determine whether the payments were made in accordance with service agreements. We examined the following documents: resolutions of the Board, vendor payment histories, claim voucher packages, including professionals' invoices and written contracts, when available.

For the Middle School capital project, we only documented the amount which the District had recorded as expenditure from its inception to January 3, 2006 and we obtained all information that we deemed necessary between June 30, 2005 and January 3, 2006. However, we did not audit any transactions which might have occurred during this period.

We conducted our audit in accordance with Generally Accepted Government Auditing Standards. Such standards require that we plan and conduct our audit to adequately assess those district operations within our audit scope. Further, those standards require that we understand the district's management controls and those laws, rules and regulations that are relevant to the district's operations included in our scope. An audit includes examining, on a test basis, evidence supporting transactions recorded in accounting and operating records and applying such other auditing procedures, as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for the findings, conclusions and recommendations contained in this report.

APPENDIX D

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APPENDIX E

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