



Odessa-Montour Central School District Treasury and Accounting Duties

Report of Examination

Period Covered:

April 1, 2005 - May 3, 2006

2006M-169



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State of New York Office of the State Comptroller

Division of Local Government Services and Economic Development

December 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 Odessa-Montour Central School District — Treasury and Accounting Duties.

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 school district officials.

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*

Introduction

Background

The Odessa-Montour Central School District (District) is located in the Towns of Odessa and Montour Falls, Schuyler County. The District is governed by the Board of Education (Board) which is comprised of seven 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 three schools in operation within the District, with approximately 858 students and 153 employees. The District's budgeted expenditures for the 2005-06 fiscal year were \$13.6 million, funded primarily with State aid, sales tax, real property taxes and grants.

The District is small with few administrative personnel to oversee the business operations. It is common practice within small school districts to assign nearly all business function duties to the Treasurer. The District had an occurrence of fraud involving the prior Treasurer back in 2001. The fraud was a result of the lack of segregation of duties without compensating controls, and it resulted in a loss to the District of approximately \$46,000, which was later recovered.

Objective

The objective of our audit was to examine the District's internal controls relating to treasury and accounting duties. Our audit addressed the following related question:

- Did the Board implement and monitor internal control improvements relating to the District's treasury and accounting duties?

Scope and Methodology

Our overall goal was to assess the adequacy of the internal controls put in place by officials to safeguard District assets. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: cash receipts and disbursements, purchasing, payroll and personal services, capital assets, and consumable inventories. Based on that evaluation, we determined that controls appeared to be adequate and limited risk existed in most of the financial areas we reviewed. We

did determine that risk existed in the area of treasury and accounting duties. Therefore, we examined internal controls over treasury and accounting duties for the period April 1, 2005 through May 3, 2006.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix B 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. District officials generally agreed with our findings and indicated they will submit a corrective action plan to address our recommendations.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a (3)(c) of the Education Law and Section 170.12 of the Regulations of the Commissioner of Education, the Board must approve a corrective action plan that addresses the findings in this report, forward the plan to our office within 90 days, forward a copy of the plan to the Commissioner of Education and make the plan available for public review in the District Clerk's office. For guidance in preparing the plan of action, the Board should refer to applicable sections in the publication issued by the Office of the State Comptroller entitled *Local Government Management Guide*.

Treasury and Accounting Duties

One of the Board's managerial responsibilities is the establishment of a system of internal controls. 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 as having the Board or other administrative staff periodically review the work in question, rotating duties, and making vacations mandatory. The Board could also require that monthly monitoring reports be produced by the District's financial software, and use the reports to monitor District financial activity.

Our audit tests did not disclose any instances of fraud or other exceptions. However, when a District has been the victim of fraud in the past that resulted from a lack of segregation of duties, it is the Board's responsibility to correct the weaknesses which allowed the fraud to take place. We found the Board had implemented some, but not all of the necessary corrective actions.

Control Environment — In 2001 the District experienced a fraud perpetrated by a former Treasurer. Our audit determined that some of the conditions that allowed this fraud to occur remained in place during our audit period. However, we also noted that in an October 6, 2006 management letter, the District's Independent Public Accountant (IPA) stated that the "risks associated with the lack of segregation of duties was significantly reduced during the 2005-2006 fiscal year, as a result of the District contract with the BOCES Central Business Office for accounting services." District officials have also indicated that subsequent to our audit period, they have taken certain corrective measures, such as providing for a review of the Treasurer's work for any discrepancies or irregularities.

The control environment sets the tone of an organization, influencing the control-consciousness of its people. Control environment comprises many factors, including the way management assigns authority and responsibility, and the attention and direction provided

by the Board. As noted above, during our audit period, the Board had not corrected some of the conditions that allowed the 2001 fraud to occur, and this may have reduced the effectiveness of controls in the management of financial operations. However, we also recognize that District officials have taken substantial corrective measures after our audit period, and we commend them for doing so.

Segregation of Duties — During our audit period, the District’s Treasurer was responsible for performing the District’s financial duties, including preparing and approving journal entries, signing all checks, recording all cash deposits, making all wire transfers, maintaining accounting records, and reconciling all bank accounts. When one person performs recordkeeping, check preparation and reconciliation duties, and there is no independent review of that person’s work, there is increased risk that District assets could be misused or stolen.

District officials have informed us that subsequent to our audit period, some of the duties previously performed by the Treasurer are now performed by other individuals. Examples include general journal entries (now being prepared by an accountant at the BOCES Central Business Office), and the preparation of monthly bank reconciliations (now being prepared by someone other than the Treasurer in the BOCES Accounting Department). Again, we commend District officials for taking at least some corrective action with respect to the segregation of duties. The only additional segregation of duties that remains to be implemented or otherwise compensated for is recordkeeping and check preparation.

We also note that since July 1, 2005, when the District first entered into a written agreement with BOCES for Central Business Office services, several changes have been made to the services provided to the District. However, the District did not review and agree to the changes in writing prior to the time the changes were implemented. If the District does not review and approve changes in services provided before they are put in place, it may result in service changes that are not in the best interest of the District.

Computer-Generated Monitoring Reports — The Board receives certain documentation for review from the Treasurer, including the Treasurer’s monthly cash report, budget status reports and extra classroom activity fund reports. However, the Board does not require additional monitoring reports, such as audit logs and change reports, nor does the Board require an independent review of such reports, even though the District’s financial software is capable of producing them. Both these reports would help counter the risk inherent in

the Treasurer's performing recordkeeping and asset custody (check preparation) functions. An audit log shows when any user entered the system, what transactions the user performed, and what changes the user made to information in the system. A change report identifies changes made to the system, changes made to vendor or employee data, and changes made to accounts payable, payroll and general ledger data. If the Board required such reports and reviewed them, or caused them to be independently reviewed periodically, this monitoring activity would help compensate for the lack of segregation of financial duties.

Due to the internal control weaknesses noted above, we examined selected District financial transactions (e.g., bank reconciliations, warrants for unusual payments, bank charges, cash receipts, and bank deposits) for the period November 1, 2005 through January 31, 2006. Our tests did not disclose fraud or other exceptions. However, until the Board corrects the control weaknesses identified in this report, the District is subject to increased risk of errors, abuse or fraud occurring without detection and correction.

Recommendations

1. The Board should ensure that financial duties are assigned so that the work of one individual independently verifies another's in the course of their regular duties. The Board should segregate the duties of recordkeeping and check preparation, or provide for an adequate form of compensating control.
2. The Board should review and give prior written approval for any changes to the services provided by the BOCES Central Business Office to the District.
3. The Board or the recently formed Audit Committee should ensure that all bank reconciliations continue to be independently prepared or reviewed and compared to cash balances shown on the general ledgers. If discrepancies exist, the Board should request a detailed explanation and corrective action plan.
4. The Board should establish procedures requiring District officials to use monitoring reports generated by the financial software to help strengthen internal controls.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

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Superintendent of Schools

James R. Frame

December 11, 2006

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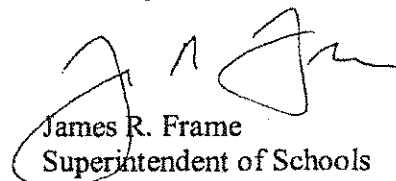
To Whom It May Concern:

On behalf of the Board of Education, I accept the findings of the New York State Office of the Comptroller's Audit Report dated December 1, 2006.

With the help of the Central Business Office service, as provided by the Greater Southern Tier BOCES, our business operations continue to improve as we build a stronger district financially. I note the recommendations and will submit a corrective action plan to address additional segregation of duties and improved financial procedures as outlined in the audit.

Odessa-Montour Central School District appreciates the opportunity for careful examination of our business function and welcomes future feedback from the Comptroller's Office. Thank you for your continued interest in district improvement.

Sincerely,



James R. Frame
Superintendent of Schools

JRF/kem

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by officials to safeguard District assets. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: cash receipts and disbursements, purchasing, payroll and personal services, and capital assets and consumable inventories.

During the initial assessment, we interviewed appropriate District officials, performed limited tests of transactions and reviewed pertinent documents such as District policies and procedures manuals, Board minutes and financial records and reports. In addition, we obtained information directly from the computerized financial databases and then analyzed it electronically using computer-assisted techniques. This approach provided us with additional information about the District's financial transactions as recorded in its databases. Further, we reviewed the District's internal controls and procedures over the computerized financial databases to help ensure that the information produced by such systems was reliable.

After reviewing the information gathered during our initial assessment, we determined where weaknesses existed, and evaluated those weaknesses for the risk of potential fraud, theft and/or professional misconduct. Based on that evaluation we then decided upon the reported objectives and scope by selecting for audit those areas most at risk. We then selected controls over the Treasury and accounting duties for further audit testing because of the lack of segregation of duties and related computer control weaknesses.

Our audit procedures included:

- Reviewing key control activities of the business office including the manner in which bank accounts are reconciled, duties are assigned and checks are signed.
- Reviewing District financial records, bank statements, and cancelled checks to verify that bank reconciliations were properly performed for checking and cash in time deposit accounts for the months of November 2005 through January 2006.
- Scanning warrants of all funds for unusual payments for the months of November 2005 through January 2006.
- Examining bank charges to determine if they were supported by cancelled checks, audited claims, payrolls, contracts or other appropriate documentation for all checking accounts for the months of November 2005 through January 2006.
- Examining bank wire transfers made from and to all bank accounts during November 2005 through January 2006 to determine if the transfers were proper.

- Comparing duplicate receipts with cash receipts journals of all funds, and comparing recorded receipts with bank deposits for the months of November 2005 through January 2006.
- Scanned payrolls and traced canceled check to a signed payroll report to verify accuracy of check number, payee name, payment amount, and payment date.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). 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.

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