



Alden Central School District Internal Controls Over Selected Financial Operations

Report of Examination

Period Covered:

July 1, 2005 — May 22, 2007

2007M-200



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

November 2007

Dear School District Officials:

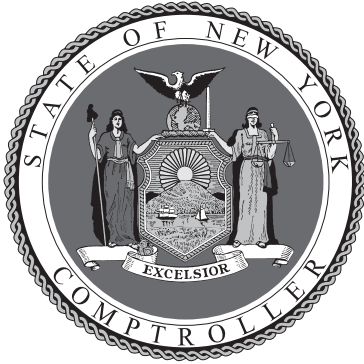
A top priority of the Office of the State Comptroller is to help school district officials manage their districts efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as districts' compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished through our audits, which identify opportunities for improving district operations and Board of Education governance. Audits can also identify strategies to reduce district costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Alden Central School District, entitled Internal Controls Over Selected Financial Operations. 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.

This audit's results and recommendations are resources for district officials in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

The Alden Central School District (District) is governed by the Board of Education (Board) which comprises 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.

Scope and Objective

The objective of our audit was to evaluate internal controls over selected financial operations for the period July 1, 2005 to May 22, 2007. Our audit addressed the following related questions:

- Did District officials establish procedures to help identify and prevent potential conflicts of interest?
- Has the Board exercised appropriate oversight and established controls to ensure that payroll and separation payments are accurate and supported?
- Are internal controls over claims processing appropriately designed and operating effectively?
- Are internal controls over contractual payments appropriately designed and operating effectively?

Audit Results

The Board has not established adequate procedures to help District officials identify and avoid conflicts of interest in violation of the General Municipal Law and the District's Code of Ethics. We also found deficiencies with respect to payroll, claims processing and contractual payments.

We found that one Board member has a prohibited conflict of interest. The Board member owns a daycare corporation, which operates year round on the District campus. The Board member represented to examiners that the program had gross receipts of approximately \$95,000 and \$106,000 for the 2005-06 and 2006-07 fiscal years. As owner of the corporation, the Board member is deemed to have an interest in the corporation's contracts. That interest is prohibited because this individual, as a member of the Board, had the power to approve the contract between the corporation and the District.

Further, certain provisions of the District's contract with the Board member's corporation are inconsistent with the terms under which another daycare provider uses District facilities. While the District does not charge the Board member's corporation for its use of District facilities, the District does charge another daycare provider a \$300 monthly rental fee for the use of District facilities.

Also, the Board did not consistently authorize salary, benefits and payments upon separation or enforce contract provisions, and continued to allow payments to be made prior to Board approval. Twenty employees were paid salaries totaling \$941,778, five employees were paid stipends of \$24,899 and four employees were paid health reimbursement arrangement (HRA) cash out payments of \$15,292, all without contractual authorization, and frequently without prior Board approval as required. Further, seven employees received merit payments totaling \$16,629 without documentation that they had met the terms and conditions of their contracts. We also found three employees that were paid \$34,153 for unused leave time and/or longevity without contractual authorization and a fourth employee that was paid \$7,426 pursuant to a settlement agreement that was not authorized by the Board. Finally, the gross wages on the former Superintendent's W-2 form were understated by \$9,649 due to a payment for unused HRA funds that was not included, as required.

We also found numerous deficiencies with the 54 claims totaling \$101,838 that we reviewed. There was a general lack of documented supervisory approval for purchases, a lack of itemized documentation to support claims, and debit card purchases totaling \$1,201 in the 2005-06 fiscal year were not reviewed by the claims auditor. Further, the claims auditor generally reviewed claims after the checks were already printed.

The District does not have Board-approved contracts on file for 16 vendors to stipulate services to be provided. These vendors received approximately \$2.1 million during the fiscal year. Eleven vendors have no contracts and the remaining five have contracts signed by a District employee but not approved by the Board.

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. District officials generally agreed with our recommendations and indicated that they are taking corrective action.

Introduction

Background

The Alden Central School District (District) is located in the Towns of Alden, Lancaster, Marilla and Newstead all in Erie County, as well as the Town of Darien in Genesee County and the Town of Bennington in Wyoming County. The District is governed by the Board of Education (Board) which comprises seven elected members. The Board is responsible for the general management and control of the District's financial and educational affairs, and ensuring that its policies are monitored for compliance, including the District's Code of Ethics. 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 1,900 students and 600 employees. General fund expenditures, net of interfund transfers and debt service, for the 2005-06 fiscal year were approximately \$23.6 million. Employee compensation and benefits represented \$18.1 million (77 percent) of total general fund expenditures. Expenditures were funded primarily with revenue from local taxes, State aid and grant monies.

Certain administrators and office staff perform multiple tasks for the District. The Board appointed the Superintendent to certify payrolls and an employee outside of the Business Office to be the claims auditor. In addition, the Business Administrator is the purchasing agent and technology coordinator and two office staff have the roles of District Clerk and tax collector. The District uses a computerized accounting system to perform payroll and claims processing activities. The computerized accounting system was replaced during our audit period.

Objective

The objective of our audit was to evaluate internal controls over selected financial operations. Our audit addressed the following related questions:

- Did District officials establish procedures to help identify and prevent potential conflicts of interest?
- Has the Board exercised appropriate oversight and established controls to ensure that payroll and separation payments are accurate and supported?

- Are internal controls over claims processing appropriately designed and operating effectively?
- Are internal controls over contractual payments appropriately designed and operating effectively?

Scope and Methodology

We examined internal controls over potential conflicts of interest, payroll and separation payments, claims processing and contractual payments of the Alden Central School District for the period July 1, 2005 to May 22, 2007.

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 recommendations and indicated that they are taking corrective action.

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*.

Conflict of Interest

The General Municipal Law (GML) limits the ability of school district officers and employees to enter into contracts in which both their personal financial interests and their public powers and duties conflict. Unless a statutory exception applies, the GML prohibits district officials from having an “interest” in contracts with the school district that they serve when they also have the power or duty – either individually or as a Board member – to negotiate, prepare, authorize, or approve the contract; to authorize or approve payment under the contract; to audit bills or claims under the contract; or to appoint an officer or employee with any of those powers or duties. District officials are deemed to have an interest in the contracts of any corporation of which they are a stockholder. Contracts willfully entered into in violation of the GML are null, void, and wholly unenforceable. In 2000, the Board adopted a Code of Ethics for all District personnel, which prohibits conflicts of interest.

We found that a Board member has a prohibited interest in a contract with the District. This Board member owns a corporation which provides after-school and summer school care year-round on the District campus, for children age five through 12 that attend District schools. As appears to be permitted by the Education Law, the District does not charge the corporation for the use of District facilities. In addition, the District does not pay the corporation for running the programs. Instead, the corporation charges fees for its services to the parents of the children enrolled in the programs, and grossed approximately \$95,000 in 2005-2006 and \$106,000 in 2006-2007.¹

The Board member’s corporation operates on the District’s campus pursuant to at least an implied agreement and, hence, a “contract” between the corporation and the District. As owner of the corporation, the Board member is deemed to have an interest in the corporation’s contracts. Unless a statutory exception applies, that interest is prohibited because this individual, as a member of the Board, had the power to approve the contract between the corporation and the District. There do not appear to be any statutory exceptions applicable in this instance. Therefore, the Board member had an interest in a contract with the District that is prohibited by the GML.

Further, certain provisions of the District’s contract with the Board member’s corporation are inconsistent with the terms under which

¹ The Board member represented these were the approximate program revenues.

another daycare provider uses District facilities. As noted above, the District does not charge the Board member's corporation for its use of District facilities. The District, however, does charge another daycare provider, who facilitates the on-site Universal Pre-K program, a \$300 monthly rental fee for the use of District facilities. Therefore, it appears that the District does not have a consistent policy regarding charges for use of District buildings and space. It also appears that the Board member receives preferential treatment with respect to the use of District facilities.

When an official conducts business with the District in which he or she serves, taxpayers and the public at large may question the appropriateness of the transactions. Such transactions may create the perception of impropriety or improper enrichment at taxpayers' expense. Officials are accountable to the public at all times. It is therefore paramount that the Board institute procedures to help District officials identify and prevent future conflicts of interest.

Recommendations

1. District officials should take corrective action to eliminate the conflict of interest that exists.
2. The Board should review the conflicts of interest provisions of the GML and its Code of Ethics and establish procedures to help District officials identify and avoid potential conflicts of interest.
3. The Board should review the Education Law and develop a consistent policy regarding charges for the use of District facilities.

Board Oversight

The Board is responsible for ensuring that District officials make salary and payroll related payments only when required, and that such payments are accurate, supported and properly authorized. When the Board becomes aware that such payments are being made that they have not authorized, they need to take corrective action to ensure that District officials do not continue to violate proper procedures

We found that the Board routinely approved payments after the fact, and did not take appropriate action to prevent future payments from being made without their explicit approval when this practice came to their attention. We also identified two individuals who had administrator level access rights to the computerized financial application and incompatible duties within the District.

Salary and Payroll-Related Payments

Although the Board generally recognized new and separating employees in the minutes, the Board did not consistently authorize salary, benefits and payments upon separation or enforce contract provisions, and continued to allow payments to be made prior to Board approval.

We tested payroll and separation payments for eight administrative and Business Office support employees who left the District's employ, and payroll payments to 22 additional employees in similar positions. Twenty-eight of the 30 employees we tested received unauthorized and/or inappropriate payroll payments totaling \$998,598:

- Salary payments to 20 employees totaling \$941,778 were not based upon Board-approved contracts or agreements. Fourteen employees were managerial confidential staff whose salaries were approved by the Board in the following fiscal year. Two administrative employees' salaries were also subsequently approved, but there was no evidence that the Board approved the salaries for the other four employees.
- Stipend payments to five employees totaling \$24,899 were made without proper Board authorization. Two stipends totaling \$6,100 were approved by the Board in the following fiscal year. Another stipend totaling \$12,000 was paid to an athletic director and recognized in the minutes, but by title only and with no indication of the amount. There also was no Board-approval for a \$2,000 payment to one employee as part of a pre-employment agreement. The only basis was a

memo from the former Superintendent to the former director of personnel.

- Inappropriate cash out payments to four employees totaling \$15,292 were made without contract authorization. Although these employees were allotted annual allowances towards their HRA² pursuant to Board approved contracts, these moneys were to be used only for eligible reimbursements, not as a means to increase salary payments.
- Merit payments to seven employees totaling \$16,629 were made without District officials properly documenting that the employees had met the conditions stipulated in their respective contracts. One of the employees was the former Superintendent who received a \$10,000 merit payment despite having no documented goals or criteria as required in his contract. The Board President indicated that the goals were discussed orally and those discussions were the basis for the payment.

Four of eight employees tested received unauthorized and/or inappropriate separation payments totaling \$41,579:

- Two employees were paid a total of \$28,986 for unused sick leave and \$1,000 each for longevity. These amounts were deposited into their HRA accounts. Neither employee was covered by a Board-approved contract or collective bargaining agreement that stipulated these payments upon separation. Apparently, the payments were based on correspondence prepared by the personnel director after consultation with the former Superintendent at the time the two employees were leaving service. There was no evidence that the Board had authorized these payments and therefore they were improper.

² A health reimbursement arrangement (HRA), commonly known as a 105(h) plan, is an employee benefit funded solely through employer contributions that are not considered taxable income for the employee, nor are the reimbursements to the employee to pay qualified medical expenses. In contrast to an employee funded flexible spending account (125 plan), which does not allow unused funds to be carried forward, a 105(h) plan has no limit on the amount the employer can contribute and remaining amounts at the end of the year can generally be carried forward to the next year. The employer is not permitted to refund any part of the balance to the employee or to a retirement plan, without including and reporting that amount in the employee's gross income. Moneys in these accounts should only be distributed pursuant to IRS regulations. Alden Central School District manages these accounts in-house, reimbursing its employees for eligible expenses. See IRS Publication 969.

- The former data resource coordinator was improperly paid \$3,167 for unused sick leave. There was no contract provision to pay for unused leave time upon separation.
- The former secretary to the Business Administrator was paid \$7,426 based on a settlement agreement. We viewed the settlement agreement and found it was only signed by the employee and the former Superintendent. This amount consisted primarily of payment for 51 days that she did not work. The former Superintendent facilitated the settlement with the District's legal counsel. We also viewed the Board minutes and found although the Board recognized the employee's resignation in the minutes, there was no indication that the Board had authorized the settlement. Further, the payments were made prior to the Board meeting when the Board accepted the employee's resignation.

Finally, the Board authorized a \$9,649 payment to the former Superintendent for unused HRA funds based on a Board approved employment agreement. However, this payment was not included in the former Superintendent's 2006 W-2 gross wages filed with the Internal Revenue Service (IRS), as required.³ As a result, applicable taxes were underreported to the IRS.

Access Rights

The Board should establish policies that provide that applicable duties are segregated, access to the computerized accounting system is limited to job responsibilities, and activity is monitored to mitigate the risk of improper payments and ensure that activity is proper and authorized. The ability to change user access should generally be reserved for employees that are independent of the Business Office, and such access should be limited.

The Business Administrator and the District Clerk/Secretary to the Superintendent had administrator level access rights to the computerized financial application, giving them the ability to change the access rights for all system users, access and make changes to accounting data and change security features within the application. This administrative access was incompatible with their daily activities of managing the District's financial operations. As a result, there is an increased risk of errors or irregularities occurring and not being detected and corrected.

³ HRA funds, when distributed for other than qualified medical reimbursement purposes, whether as cash or to a retirement plan, must be reported as gross wages for tax purposes.

Recommendations

4. District officials should ensure that payroll, separation and benefit related payments are based on properly authorized and clearly defined employee contracts or agreements.
5. The Board should formally approve employee settlement agreements prior to payment.
6. The Board or its designee, such as the internal auditor, should periodically monitor payments to ensure they are accurate, supported, and in accordance with applicable policies and contracts or agreements.
7. The Board should take appropriate steps to recover any improper payments made to former and current District employees.
8. The Board should consult with legal counsel and other appropriate advisors to determine what action needs to be taken to ensure the HRA is properly established and operating in accordance with Internal Revenue Service regulations.
9. The Board should contact the Internal Revenue Service and the New York State Department of Taxation and Finance to determine what amended reports and supplemental information should be submitted to address misreported payroll information.
10. The Board should ensure that District management establishes a hierarchy of access control to the computerized accounting system based on job responsibilities, and monitors access levels to ensure critical duties are properly segregated.
11. The Board or its designee, such as the internal auditor, should periodically monitor user access levels to ensure they are appropriate and adjusted in a timely manner.

Claims Processing

In general, the objectives of internal controls over claims processing are to ensure that every claim contains enough supporting documentation to determine that it complies with District policies, and that the amounts claimed represent actual and necessary District expenses. This helps to ensure that taxpayer dollars are used in the most efficient manner. The Board is responsible for auditing bills before they are paid, but may appoint a claims auditor for this purpose. The claims auditor is then responsible for ensuring that each claim is supported by proper original documentation, properly authorized, for a legal purpose and in conformance with District policies. The Board should provide a written job description to the claims auditor to ensure the claims auditor clearly understands how to perform his or her responsibilities to comply with statutory requirements and meet Board expectations.

The District's claims auditing process was not appropriately designed or operating effectively to properly safeguard District funds. There was a general lack of documented supervisory approval for purchases and a lack of itemized documentation to support claims. Further, the claims auditor generally reviewed the claims after the checks were already printed. The claims auditor indicated that she was not given any prescribed routines or procedures to follow and relied on the Business Administrator's signature on the claim as evidence that the claim was for an appropriate District expense.

We examined 54 claims totaling \$101,838, and interviewed the claims auditor and other District personnel to determine if claims were properly authorized, approved, documented, audited and paid in accordance with District policy. Several of the more significant exceptions and inconsistencies were as follows:

Lack of Authorization – Twenty claims lacked supervisory approval prior to purchase. For example, District policy indicates that Board members can be reimbursed for actual expenses incurred while representing the District. However, they must have prior Board authorization and submit an itemized bill. The supporting documentation for two of the three Board member reimbursement claims did not indicate the Board had approved the travel.

Similarly, the District policy for professional development opportunities allows personnel to attend conferences/seminars with pre-approval from the Superintendent, and the Superintendent's contract indicated he can travel with prior Board approval. We found

the professional development claims for six employees and five claims for the former Superintendent totaling \$4,383 did not indicate pre-approval by the Superintendent or the Board, as required.

Documentation – Three claims had no supporting documentation and an additional 27 claims lacked sufficient documentation. As a result, we could not determine whether these claims were for proper District expenses, approved by appropriate personnel or paid in accordance with District policies. For example, all eight reimbursement claims paid to the former Superintendent totaling \$6,144 were not sufficiently supported. There was no indication that he was on District business when he incurred meal expenses and the documentation for one meal was only the top portion of a receipt, with no evidence as to when, where or what was purchased.

Similarly, the former Superintendent’s claims for HRA medical reimbursement, totaling \$5,147, lacked original documentation, such as receipts, invoices and proof of payment, contrary to IRS regulations, which require evidence that such reimbursements are documented to prove that they are eligible and proper expenses.

Debit Card Purchases – We also found debit card purchases totaling \$1,201 in the 2005-06 fiscal year that were not reviewed by the claims auditor. For example, one debit card purchase of \$516 was for an order of holiday cards for District employees.

Recommendations

12. The Board should provide written guidance for the claims auditor and ensure that the claims audit function complies with Board policy, statutory requirements and general standards of good internal control.
13. The claims auditor should ensure that every claim contains adequate documentation, is properly itemized to demonstrate that it is a proper District expense, and complies with District policies.
14. The Board should ensure that travel is pre-approved in accordance with District policy.

Contractual Payments

Formal contracts and agreements are important elements of internal control to ensure the District's interests are protected. Payment for services should be based upon duly executed written contracts that clearly indicate the scope of services to be provided, a timeframe for delivery of services, the cost of services, and the timing and method of payment. Contracts should be reviewed by legal counsel, approved by the Board, and executed before services are provided. District officials should also routinely monitor progress during the contract term. For example, designated District officials should prepare status reports and distribute them to the Superintendent, other administrators and the Board. Claims for payment should fully itemize actual services to date, evidencing the terms and conditions of the contract are complied with, and should be reviewed by the claims auditor prior to payment.

We tested 22 claims for services provided to the District during the 2005-06 and 2006-07 fiscal years to determine if payments were properly audited and made in accordance with related contracts or agreements. We found that two were not itemized, two did not have an invoice attached, four lacked evidence that an appropriate official acknowledged receipt of services, and three lacked approval by the purchasing agent.

We also verified whether Board-authorized contracts or agreements were on file and periodically reviewed. Board-approved contracts or agreements were not on file to stipulate services to be provided by 16 of the 22 vendors. These vendors received approximately \$2.1 million during the year selected for audit.

- Eleven vendors had no Board approved contracts on file. One of the eleven is the third-party administrative service that manages the District's health and life insurance benefits. The District paid \$1.8 million to this vendor during the 2005-06 fiscal year.
- Five vendors had contracts that were signed by a District employee but not approved by the Board. The former Superintendent signed three of these, including a contract with an energy performance maintenance vendor, which he entered into in 1999. Payments to this vendor in the 2006-07 fiscal year totaled \$56,608. He also signed contracts with a local pre-school program provider and a weather monitoring service, for which payments in 2005-06 totaled \$65,000

and \$18,005, respectively. The remaining two contracts, for technical support and cafeteria services, were signed by department heads.

Without written agreements which stipulate scope of services and terms and conditions for payment, District officials are not in a position to effectively monitor vendor activity and ensure claims paid are accurate. District officials indicated that they are currently in the process of obtaining signed agreements for the many services provided to the District by vendors.

Recommendations

15. The Board should ensure that it authorizes all contracts for services to be provided to the District. All contracts should clearly define the services to be performed and the compensation to be paid.
16. District management should monitor contractual payments to verify they are made in accordance with contracts.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

2. *The Board should review the conflicts of interest provisions of the GML and its Code of Ethics and establish procedures to help District officials identify and avoid potential conflicts of interest.*
 - The Board and District officials will review the conflict of interest provisions of the General Municipal Law during a Board work session and Administrative Cabinet meeting.
 - The Board and District officials will review our policy on the Code of Ethics.
3. *The Board should review the Education Law and develop a consistent policy regarding charges for the use of District facilities.*
 - The Board, as a part of its routine and regular review of its policies, will address the issue of consistent charges for the use of District facilities.

Board Oversight

4. *District officials should ensure that payroll, separation and benefit related payments are based on properly authorized and clearly defined employee contracts or agreements.*
 - As a result of this audit, the Board and District will develop contracts for each employee that reflect the terms and conditions of employment as well as separation.
5. *The Board should formally approve employee settlement agreements prior to payment.*
 - All future settlement agreements will receive formal authorization prior to payment, with the board minutes attached as authorization for payment.
6. *The Board, or its designee, such as the internal auditor, should periodically monitor payments to ensure they are accurate, supported and in accordance with applicable policies and contracts or agreements.*
 - The internal auditor will be directed to review payments to insure they are accurate, supported and in accordance with applicable policies, contracts, or agreements. The internal auditor will report the findings to the District audit committee.

7. *The Board should take appropriate steps to recover any improper payments made to former and current District employees.*
 - The Board will review separation payments made to employees during the audit period. Those that the board determines to be improper will be reviewed with the Board's legal counsel for recovery.

8. *The Board should consult with legal counsel and other appropriate advisors to determine what action needs to be taken to ensure the HRA is properly established and operating in accordance with Internal Revenue Service regulations.*
 - The District has been investigating moving from a District monitored HRA to a 105h plan that will be monitored by a third party vendor. The District will be moving to a 105h plan solely with a third party vendor before the start of the next fiscal year for all employees currently under the District managed HRA.

9. *The Board should contact the Internal Revenue Service and the New York State Department of Taxation and Finance to determine what amended reports and supplemental information should be submitted to address misreported payroll information.*
 - The District will contact the Internal Revenue Service and the New York State Department of Taxation and Finance. The District will then file the appropriate amended reports to address any payroll information that may have been misreported.

10. *The Board should ensure that District management establishes a hierarchy of access control to the computerized accounting system based on job responsibilities, and monitors access levels to ensure critical duties are properly segregated.*
 - The Board has recently hired a Director of Instructional and Information Technology/CIO whose responsibilities will include maintaining and granting access rights to District employees who use the District accounting software. Rights will be granted, based upon job responsibilities, to ensure that critical duties are properly segregated.

11. *The Board, or its designee, such as the internal auditor, should periodically monitor user access levels to ensure they are appropriate and adjusted in a timely manner.*

- The Director of Instructional and Information Technology/CIO will be responsible for periodically monitoring and adjusting user access levels including eliminating accounts as employees exit the employ of the District. The internal auditor will periodically monitor access levels.

Claims Processing

12. *The Board should provide written guidance for the claims auditor and ensure that the claims audit function complies with Board policy, statutory requirements and general standards of good internal control.*

- District officials are currently reviewing the Administrative Regulations Manual that will provide guidance as to the implementation of the District Policies. Close attention will be paid to the area of claims processing to address the issues identified in this audit.

13. *The claims auditor should ensure that every claim contains adequate documentation, is properly itemized to demonstrate that it is a proper District expense and complies with District policies.*

- The claims auditor will receive training on the administrative regulations that apply to claims processing so as to ensure adherence to the policies and processes.

14. *The Board should ensure that travel is pre-approved in accordance with District policy.*

- Approved conference forms will be required of all board members and staff prior to the payment of claims for travel.

Contractual Payments

15. *The Board should ensure that it authorizes all contracts for services to be provided to the District. All contracts should clearly define the services to be performed and the compensation to be paid.*

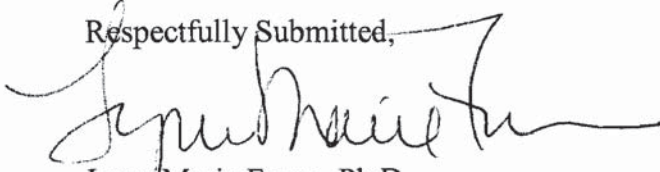
- The Board will authorize all contracts for services to be provided to the District. This requirement will be communicated to all administrators and staff members to ensure that contracts are properly forwarded to the Board for authorization.

16. District management should monitor contractual payments to verify they are made in accordance with contracts.

- Contractual payments require the approval of the purchasing agent and will be monitored to ensure they are within contract specifications.

We would like to reiterate that we have viewed the audit process as a learning experience to improve the processes within our District. The District accepts the recommendations of the audit and will move swiftly and deliberately to improve not only those areas addressed in the audit, but in all areas.

Respectfully Submitted,



Lynn Marie Fusco, Ph.D.
Superintendent of Schools



J. Daniel Oles
President of the Board

LMF/caw
Certified/Return Receipt
(audit response)

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: financial oversight, cash receipts and disbursements, purchasing, payroll and personal services.

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. We then decided upon the reported objective and scope by selecting for audit those areas most at risk.

We selected internal controls and procedures in place to identify and prevent potential conflicts of interest, separation payments, regular payroll payments, claims processing and contractual payments for services for further audit testing.

For conflicts of interest, we requested and obtained representations from the Superintendent, Board members, and other selected District officials as to their outside employment and business interests and those of their spouses. We reviewed vendor reports, claim vouchers and other records to determine if the District had financial transactions with any business that could constitute a prohibited conflict of interest.

For Board oversight of payroll and separation payments, we reviewed policies and procedures, interviewed District officials, observed transactions and examined employee earnings records, contracts, payroll registers, Board of Education minutes, employee attendance records, personnel files, W-2 forms, and worksheets prepared by the payroll clerk and Business Administrator.

Within claims processing and contractual payments, we focused our attention on the authority and approval of purchases and payment for various types of goods and services acquired. We interviewed officials, observed transactions and examined financial records such as vendor history reports, contracts, agreements, warrants, claims, District policies and regulations, and Board of Education minutes to determine the effectiveness of internal controls and any effects of deficiencies in those controls.

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

APPENDIX C

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APPENDIX D
OFFICE OF THE STATE COMPTROLLER
DIVISION OF LOCAL GOVERNMENT
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