



Campbell-Savona Central School District Financial Condition and Internal Controls Over Selected Financial Activities

Report of Examination

Period Covered:

July 1, 2004 — June 30, 2006

2007M-228



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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

May 2008

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, in part, through our audits, which identify opportunities for improving district operations and Board of Education governance. Audits also can identify strategies to reduce district costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Campbell-Savona Central School District, entitled *Financial Condition and Internal Controls Over Selected Financial Activities*. This audit was conducted pursuant to Article V, Section 1 of the State Constitution, and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for district officials to use 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 Campbell-Savona 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. On September 1, 2000, the Business Manager became the Superintendent, but continued to handle both duties until his resignation in February 2006.

Internal controls are the policies and procedures adopted by District management, which when properly designed and implemented, help ensure accurate and timely financial reporting, compliance with laws and regulations, and the efficient and effective operation of the District. District officials are responsible for maintaining accurate and complete accounting records and providing reports to the Board. The Board should use these reports to make sound and prudent decisions about the District's financial condition and operations. A good system of internal controls can help prevent or detect errors and/or irregularities in a timely manner.

Because of a general fund deficit, the New York State Legislature authorized¹ the District to issue indebtedness to liquidate the deficit. As a result of this legislation, the District issued \$3,250,000 in bonds dated June 1, 2007. Final maturity of the bonds is June 1, 2017. This legislation also requires the Comptroller's Office to examine the District's budget for the period the bonds are outstanding. Our report of the District's 2007-08 budget was issued on May 1, 2007.

Scope and Objectives

The objectives of our audit were to identify the factors that contributed to the District's financial decline during the period July 1, 1998 through June 30, 2006 and to examine internal controls over claims processing, fringe benefits, and computer operations for the period July 1, 2004 through June 30, 2006. On July 26, 2006, the State Legislature adopted Chapter 417 of the Laws of 2006, which authorized the District to issue debt to liquidate the projected accumulated deficit in the general fund as of June 30, 2006. Subsequent to the end of our fieldwork, but prior to the issuance of the report, we became aware of a reported improvement in the District's financial condition. We reviewed the IPA's report for the fiscal year ended June 30, 2007 and verified certain components of fund balance, such as inter-fund receivables. In addition, we reviewed the budgeted and actual revenues and expenditures to determine the reason for the improved financial condition. Our audit addressed the following related questions:

¹ Chapter 417 of the Laws of 2006

- Did the Board effectively monitor and control District finances?
- Has the Board adopted realistic budgets and utilized long-term planning to identify and manage future operating requirements?
- Has District management designed and implemented effective internal controls over claims processing, fringe benefits, and information technology?

Audit Results

The Board has not effectively monitored and controlled District finances or adopted realistic budgets, resulting in a general fund deficit of \$3.2 million as of June 30, 2006.² However, because the District was in a deficit position, District officials obtained approval from the State Legislature and issued \$3.25 million in deficit financing bonds. This deficit financing and certain operational changes have allowed the District to complete the 2006-07 fiscal year with a general fund unreserved fund balance of \$1.5 million. This is a positive development. We do note that revenues totaling \$410,000 that contributed to the operating surplus, such as interest earnings and tuition, are unlikely to reach the same levels in future years. We also found the Board did not have procedures to plan for long-term operational and capital needs, which may contribute to more financial problems in the future. It is therefore essential that the Board strictly monitor revenues and expenditures to ensure that sufficient resources are available to meet future obligations.

The Board has also failed to take or require corrective action based on audit findings and provide proper guidance to District officials to carry out their duties. These factors also contributed to the financial problems faced by the District and provided taxpayers with little assurance that financial operations will be properly controlled within financial and budgetary constraints.

Although Board members established written policies for the procurement of goods and services, they did not monitor for compliance. When working properly, a purchase order system can be effective in controlling expenditures. However, we found purchase orders were not properly reviewed, purchase orders were issued after purchases were made, and individuals continually overrode the purchase order system allowing purchase orders to be generated even though appropriations were insufficient. Of the 928 claims we reviewed totaling \$504,556, 13 purchases totaling \$9,491 exceeded the purchase order amounts, 43 purchase orders totaling \$17,103 were issued after the purchases were made, and 112 purchase orders, totaling \$356,141 exceeded available appropriations.

In addition, because the Board did not appoint a claims auditor, it retained the responsibility for auditing claims. However, because of the limited nature of the Board's examination, we found that the Board did not properly audit any of the claims we reviewed. Further, the District does not have a policy for credit cards. None of the credit card purchases had prior approval and over half of the credit card purchases lacked supporting documentation. We also reviewed all 27 gas card purchases totaling \$9,898 during the audit period. The charges lacked supporting documentation and a mileage log was not kept for District vehicles.

² 35 percent of the 2005-06 adopted budget appropriations

The Board approves new hires and establishes wages, salaries and fringe benefits for employees by resolutions, individual employee contracts and collective bargaining agreements. However, the Board did not establish written procedures or guidelines for the calculation and payment of fringe benefits for five administrators. As a result, the District made unauthorized payments totaling \$12,500 and provided benefits totaling \$19,562 to employees for which there was no specific Board authorization.

Finally, the Board has not effectively addressed the safeguarding of computer data by establishing appropriate policies and procedures. Adequate and deliberate protection of computer data is necessary for District operations to proceed efficiently. We determined all three server rooms were accessible by anyone with a key to the outside doors. Further, access rights were not restricted to ensure a proper segregation of duties or impede the ability to override budgetary controls. In addition, the District did not disable the former Superintendent's account until we brought it to the attention of District officials (three months after his departure). Furthermore, management's ability to detect and properly address unauthorized activities was limited because the computerized financial system could not produce audit logs for review. Finally, the Board did not establish formal policies or procedures to address potential disasters. In the event of a disaster, District personnel have no guidelines or plan to follow to prevent the loss of equipment and data or data recovery procedures.

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 they planned to initiate corrective action.

Introduction

Background

The Campbell-Savona Central School District (District) is located in Steuben County and lies within the Towns of Addison, Bath, Bradford, Cameron, Campbell, Erwin, Thurston and the Village of Savona. 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. 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. On September 1, 2000, the Business Manager became the Superintendent but also continued his duties as Business Manager until his resignation in February 2006.

There are two schools and a transportation facility in operation within the District, with approximately 1,100 students and 208 employees (127 instructional, 12 administrative and 69 support staff). The District's budgeted expenditures for the 2005-06 fiscal year were approximately \$16.6 million, funded primarily with State aid, real property taxes, inter-fund transfers and fund balance. However, the District had operating revenues of only \$15.9 million and \$18.3 million in expenditures.

The Board is responsible for establishing a system of internal controls to provide reasonable assurance that District assets are properly safeguarded, financial reporting is accurate, purchases are made in accordance with District policy, and payrolls are accurate. A good system of internal controls should also provide for the timely identification of errors and/or irregularities, which may have occurred so that management can take corrective action. Once established, the Board has the responsibility to monitor the controls periodically to ensure that they are operating properly.

Because of a general fund deficit, the New York State Legislature authorized³ the District to issue indebtedness to liquidate the deficit. As a result of this legislation, the District issued \$3,250,000 in bonds dated June 1, 2007. Final maturity of the bonds is June 1, 2017. This legislation also requires the Comptroller's Office to examine the District's budget for the period the bonds are outstanding. Our report of the District's 2007-08 budget was issued on May 1, 2007.

³ Chapter 417 of the Laws of 2006

Objectives

The objectives of our audit were to identify the factors that contributed to the District's financial decline and to examine internal controls over claims processing, fringe benefits, and computer operations. Our audit addressed the following related questions:

- Did the Board effectively monitor and control District finances?
- Has the Board adopted realistic budgets and utilized long-term planning to identify and manage future operating requirements?
- Has District management designed and implemented effective internal controls over the claims processing, fringe benefits, and information technology?

Scope and Methodology

We examined the financial condition, financial monitoring and long-term financial planning for the District for the period June 1, 1998 through June 30, 2006. We also examined the District's internal controls over claims processing, fringe benefits, and computer operations for the period July 1, 2004 through June 30, 2006. On July 26, 2006, the State Legislature adopted Chapter 417 of the Laws of 2006, which authorized the District to issue debt to liquidate the projected accumulated deficit in the general fund as of June 30, 2006. We also reviewed the IPA's report for the fiscal year ended June 30, 2007 and verified certain components of fund balance, such as inter-fund receivables. In addition, we reviewed the budgeted and actual revenues and expenditures to determine the reason for the improved financial condition.

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 they planned to initiate 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*.

Financial Condition

A school district's financial condition has an impact on its ability to provide educational services to students within the district. Districts in good financial condition collect sufficient revenues to pay short-term bills and meet the current portion of long-term obligations. The responsibility for effective financial planning and management of the District rests with the Board, the Superintendent and the Business Manager. The Treasurer also plays a role in the financial management of the District by reporting financial information to the Board.

The Board is responsible for ensuring that District expenditures do not exceed the budget approved by the voters and allowed by law. The Board and District management must make sure that budgets are prepared, adopted and amended based upon reasonable and accurate assessments of resources to fund appropriations. They must also make sure that policies, procedures and competent personnel are in place to ensure financial information is correct and reported in a timely manner. The Board is responsible for employing competent personnel who possess sufficient accounting and financial expertise to prepare accurate and timely reports and budgets.

The financial condition and cash flow deficiencies of the District were the result of decisions made by the Board in developing and adopting the annual operating budgets. The Board has continually overestimated revenues, underestimated expenditures and appropriated non-existent fund balance during the past six years. Furthermore, the Board did not obtain the information necessary to effectively monitor District finances. The Board did not receive budget to actual reports and completely relied on the former Superintendent, who also acted as the Business Manager, to handle the District's finances. In addition, the Board had not developed a comprehensive, multi-year operational plan, nor did they have any other procedures in place to adequately address the District's long-term financial needs.

Operating Deficits and Fund Balance

An operating deficit occurs when expenditures exceed revenues. An operating deficit can be planned for and financed by appropriating fund balance or unplanned due to over-expending appropriations, not receiving budgeted revenues, or a combination of the two. Fund balance is the accumulated difference between revenues and expenditures. The unreserved and unappropriated portion of fund balance allows the District to manage unexpected occurrences such as emergency repairs, cost and demand fluctuations in essential commodities (e.g., utilities and gasoline) and shortfalls in estimated

revenues. An inadequate unreserved and unappropriated fund balance limits management's ability to manage emergencies and unanticipated occurrences.

The District incurred operating deficits, totaling over \$3.9 million in the general fund for the fiscal years 2000-01 through 2005-06. The unreserved fund balance deteriorated from a positive balance during 2003-04 to a deficit of \$3.2 million as of June 30, 2006. This deficit was 20 percent of the \$16.6 million budgeted for the 2005-06 fiscal year. The following table illustrates the deterioration of fund balance and subsequent improvement:

| General Fund Balance at June 30 | | | | | | | |
|--|-------------|-------------|-------------|-------------|---------------|---------------|-------------|
| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
| Reserved | \$221,710 | \$79,734 | \$367,279 | \$335,168 | \$336,603 | \$197,415 | \$730,511 |
| Unreserved Appropriated | \$130,000 | \$130,000 | \$130,000 | \$230,000 | \$230,000 | \$0 | \$0 |
| Unreserved Unappropriated | \$16,011 | (\$129,302) | \$315,825 | (\$374,325) | (\$1,190,209) | (\$3,203,794) | \$844,817 |
| Fund Balance | \$367,721 | \$80,432 | \$813,104 | \$190,843 | (\$623,603) | (\$3,006,379) | \$1,575,328 |

The District issued bonds totaling \$3.25 million to retire the accumulated deficit and the IPA's financial report for fiscal year 2006-07 indicates that the District has ended the year with a fund balance of \$1.5 million. This is a positive development. However, we noted that the surplus was contributed to by \$410,000 in revenues that are unlikely to reach the same levels in future years; specifically, revenues of \$250,000 for interest revenue from investing the proceeds of the deficit financing and \$160,000 for tuition for foster children.⁴

It is essential for the District to develop realistic budgets and Board members to be cognizant of the financial condition of the District to avoid a recurrence of the cash flow and deficit fund balance problems that have plagued the District in the past. Management must strive for structurally balanced budgets that enable operations to be financed without an over-reliance on fund balance or non-recurring revenues. The District continually appropriated unavailable fund balance, overestimated revenues and underestimated expenditures, all of which contributed to the deterioration of fund balance in the past.

Appropriation of Fund Balance – School districts are permitted to maintain an unreserved fund balance (not to exceed 2 percent

⁴ The reason this is a non-recurring revenue source is that it was an accrual estimate. The actual tuition was much lower as the number of foster children was much lower than estimated.

of the upcoming year's budget)⁵ as a cushion against unforeseen circumstances. Districts can appropriate a portion of unreserved fund balance in the upcoming year's budget to help finance operations and reduce the tax levy. Although the operating deficits for five of the past seven years were planned by appropriating fund balance of approximately \$980,000,⁶ the actual deficits exceeded the planned amounts, in part, because the Board erroneously appropriated fund balance when none was available.

Revenues – An annual budget must provide sufficient financing to fund all expenditures in the budget. Accurate estimates of revenue reduce the need to use unreserved fund balance at year-end to compensate for revenue shortfalls and ensure the property tax levy will be sufficient to meet operating expenses.

The District overestimated revenues by more than \$2.18 million in five of the last seven years.⁷ The State aid and inter-fund transfer revenue estimates did not reflect a reasonable response to a clear and obvious downward trend in these revenues. Basic general and excess State aids were consistently overestimated.

Inter-fund transfers from the debt service fund were budgeted to finance debt service payments. However, because the debt service fund's cash assets were previously loaned to the general fund, cash was not available to transfer.

We also note that each year from 2000-01 through 2003-04, the District budgeted \$110,600 for the use of money. However, the District only realized revenue between \$30,587 and \$66,956 during this period. Given the District's declining financial resources, which left less cash available for investment, and the history of actual results not meeting estimates, the need to reduce this revenue estimate should have been evident.

Expenditures – Education Law provides that no expenditure shall be made, nor shall any contract, which involves the expenditure of money be entered into, unless an amount has been appropriated for a particular purpose.

District officials did not design and implement a system of controls to ensure that expenditures were within adopted budgets. During fiscal

⁵ This percentage was increased to 3 percent for fiscal years after 2006-07.

⁶ \$130,000 for the four years 00-01 through 03-04 and \$230,000 for the two years 04-05 through 05-06

⁷ (\$29,255) in 2000-01, (\$37,577) in 2002-03, (\$530,083) in 2003-04, (\$737,074) in 2004-05, (\$854,092) in 2005-06

years-ended June 30, 2001 to June 30, 2006, expenditures exceeded budgeted amounts in four of the six years.

The over-expenditures occurred because District officials failed to maintain or receive necessary financial records to monitor financial condition. Therefore, the Board was unable to closely oversee and monitor expenditures. District officials also failed to prepare budgets that responded to clear and obvious trends. For example:

- Employee benefits in 2005-06 were estimated to be \$3.1 million. However, this was 1 percent less than the actual cost in 2004-05 (\$3.14 million), and 14 percent less than the actual cost for 2005-06 (\$3.6 million).
- Handicap services in 2005-06 were estimated to be \$1.48 million. However, this was 3 percent less than the actual cost in 2004-05 (\$1.53 million), and 21 percent less than the actual cost for 2005-06 (\$1.87 million).
- Interscholastic sports in 2005-06 were estimated to be \$116,406. However, the District had already experienced costs of nearly \$160,000 in 2004-05. The actual costs for 2005-06 were nearly \$180,000.

The Board's failure to prepare realistic cost estimates significantly contributed to the deficits in the general fund.

School Lunch Fund – The fund has incurred operating deficits totaling over \$138,000 for the past five years and the unreserved fund balance has deteriorated from a positive balance during the 2003-04 fiscal year to a deficit of \$98,518 as of June 30, 2006.

This deterioration was caused by shortfalls in estimated revenues. We analyzed revenue trends for 2000-01 to 2005-06 and noted total revenues received were less than half (47 percent) of budgeted revenues, due to the use of the same budget estimates for more than one year. In particular, the revenue estimate for the sale of reimbursable meals in each budget was more than twice the amount actually received. Further, in the spring of 2003, the Treasurer stated she noted large discrepancies and notified the former Superintendent. However, the former Superintendent told her to use the same estimate as in the prior year. We did note the District contracted with GST BOCES to operate its cafeteria operations for the 2006-07 school year, which resulted in a reduction of its lunch fund deficit by \$55,637.

The cumulative effect of these poor budgetary practices was a decline in the combined general and lunch fund balance from a surplus of \$186,398

at June 30, 2001 to a deficit of \$3,302,312 at June 30, 2006. This decline of \$3,488,710 represents a significant weakening of the overall financial condition of the District.

The exhaustion of the District's positive fund balances resulted in insufficient cash flow to pay bills as they came due. We compared the general and school lunch funds' current assets (cash and other assets readily convertible to cash) to current liabilities (amounts due and payable within the fiscal year) and found the funds have not been cash solvent since the 2004-05 and 2002-03 fiscal years, respectively. As a result, the District used various methods to provide sufficient cash flow to finance District operations such as the issuance of revenue anticipation notes (RANs)⁸ each June since 2004 in the amounts of \$2.5 million, \$2.5 million, and \$5.78 million⁹, and the use of inter-fund advances¹⁰ since the 1997-98 school year. Because the District was in a deficit position, District officials obtained approval from the State Legislature to issue \$3.25 million in deficit financing bonds. According to the IPA's report for the 2006-07 fiscal year, the District ended 2006-07 with a general fund unreserved fund balance of \$1.5 million.

Long-Term Planning

Multi-year financial planning is a critical tool and is particularly important for districts that are financially stressed. Projecting operations several years into the future helps to identify structural imbalances between revenues and expenditures, allows officials to set long-term priorities and goals, provides a basis for assessing the impact and merits of alternative approaches to address financial problems, and helps to level the rate of tax increases and avoid sudden and severe cost-cutting measures. A long-term financial plan should be monitored and updated to ensure that decisions are guided by the most accurate information available.

The Board did not have procedures to plan for long-term operational and capital needs over the next three to five years. This lack of long-term planning limits the Board's ability to assess the effects of fixed or semi-fixed costs such as labor contracts or debt payments and inflationary costs such as health insurance and energy; and does not allow the Board to budget for the purchase or construction of capital

⁸ Represent a temporary source of cash borrowed on the pending collection of certain specific revenues estimated in the annual budget and must be issued within two weeks of the commencement of the fiscal year to which the estimates apply

⁹ 35 percent of the 2005-06 adopted budget appropriations

¹⁰ Not all District moneys are available to be advanced. For example, Local Finance Law (LFL) provides that proceeds of obligations may only be expended for the purpose for which the obligations were issued or, if they remain unspent at the completion of the project, must be set aside to redeem the debt. LFL specifically excludes loaning the proceeds of bonds and BANs to any other fund.

equipment and facilities in the most prudent and economical manner. This may contribute to more financial problems in the future and jeopardize the District's ability to maintain desired levels of service.

Recommendations

1. District officials should develop a plan to prevent the future recurrence of deficit fund balances and cash flow deficiencies. Included in this long-term operational plan should also be a long-term capital plan.
2. The Board should adopt budgets that accurately estimate revenues, expenditures and available fund balance and then monitor actual activity against the plan throughout the year.

Management Responsibilities

The Board is responsible for the overall financial management of the District, including establishing internal controls over financial operations and maintaining sound financial condition. The Superintendent and department heads share the responsibility for ensuring that internal controls are adequate and working properly to provide reasonable assurance that financial goals and fiduciary responsibilities are met.¹¹ A fundamental part of these controls is setting the tone at the top, which requires the Board to demonstrate a concern for good management and to follow appropriate procedures such as taking corrective action based on audit findings. Without adequate internal controls, taxpayers have little assurance that financial operations are properly controlled within financial and budgetary constraints.

The Board did not take or require corrective action based on audit findings, monitor financial operations or provide proper guidance to District officials to carry out their duties. The Board's inaction significantly contributed to the deteriorating financial condition of the District.

Board Response to Audits

The District's severe control weaknesses have limited the Board's ability to monitor and control financial operations, contributed to the District's financial stress, and could allow accounting errors and/or fraud to occur and remain undetected and uncorrected. Although the Board was aware of these weaknesses through annual audit reports and management letters prepared by the District's IPA, the Board and former Superintendent failed to take corrective action. The last four management letters cited the following deficiencies each year:

- Over-appropriations of fund balance
- Expenditures in excess of appropriations
- Overestimates of revenues
- Failure to monitor the general fund and lunch fund despite continuing operating losses
- Inter-fund advances contrary to Local Finance Law

¹¹ Control procedures include establishing authorization to execute transactions; properly designed records; security of assets and records; segregation of duties; periodic reconciliations and verifications; and the preparation of suitable financial reports.

- Inadequate computer controls/access rights
- Failure to maintain up-to-date fixed asset inventory lists.

These findings were red flags that the Board should have investigated. Following up on audit findings and instituting corrective action is an important part of the Board's oversight responsibility. In failing to fulfill its responsibility, the Board has set a bad example for District employees, established a poor tone at the top, and forgone the opportunity to correct budgetary and accounting deficiencies that were contributing to the District's deteriorating financial condition. Timely and decisive responses to the IPA's findings could have prevented or mitigated the financial stress that the District experienced.

The New York Legislature enacted the Laws of New York, 2005, Chapter 263 (Five Point Plan), which amended Education Law, in order to increase fiscal accountability within school districts. The Five Point Plan provides for the following: strengthening the internal claims audit function, requiring school board members to obtain financial oversight training, establishing more rigorous external audit standards, establishing new internal audit requirements, and establishing audit committees. Provisions of Education Law require the Board of most school districts to establish an audit committee to oversee and report to the Board on the annual independent audit of the District's records. According to the Five Point Plan, the audit committee was required to be established by January 1, 2006 by resolution of the Board. The Board appointed three of its members to the audit committee on February 27, 2006 and the committee held its first meeting on May 22, 2006, which was not in compliance with the Five Point Plan. An audit committee may have facilitated a more active response to the IPA's findings and thus improved the Board's oversight.

Monitoring Financial Operations

Board members have a responsibility to serve the community and protect the public interest. They are responsible for the fiscal management of the District, have a fiduciary responsibility for District assets, finances and investments, and must exercise good faith, due diligence, care and caution. While we recognize the Board is not elected to run the day-to-day operations and must rely on professionals for this purpose, the Board needs to support District management, hold the Superintendent accountable for operations and proper service to the public, and ensure the District complies with applicable laws and does not engage in unauthorized activities. We found the Board did not exercise due diligence in their role as Board members, as:

- Board members are required to audit each claim against District funds before it is paid, or appoint an independent claims auditor to perform this essential control function. The Board has retained the responsibility to audit claims. However, the Board did not audit claims either before or after payment. Instead, the Board conducted a cursory review of paid claims by approving a monthly list of expenditures (warrant report) after the checks were disbursed. The report was provided to Board members without any supporting documentation.
- The New York State Education Department Commissioner's Regulations allow the Board to authorize the Superintendent to make budgetary transfers, but require the Board to set limits as to the amount that can be transferred without Board approval. Although the Board adopted a policy to authorize the Superintendent to approve budget transfers, no dollar limits were established, and the Board did not review or approve budget transfers made by the Superintendent from July 1, 2004 to June 30, 2006.
- The Board did not take action to ensure the Treasurer prepared and presented budget status reports as required. Had the Treasurer prepared and the Board reviewed budget status reports, they would have been alerted to the substantial over-expenditures and revenue shortfalls that were occurring. The new Business Manager is providing the Board with monthly revenue and expenditure status reports.
- The Board did not fulfill its responsibilities of stewardship, oversight and leadership by establishing policies and procedures required by law and sound business practices, such as the use of credit cards or use of the Internet, nor did the Board monitor the policies and procedures it did have in place, such as purchasing, claims processing and capital assets.

This lack of oversight resulted in a weak control environment and severe fiscal stress. The Board's failure to monitor financial operations and adopt policies and procedures to provide guidance to District officials significantly contributed to the District's pattern of deteriorating financial condition.

Recommendations

3. The Board should appoint a claims auditor or properly audit all claims prior to payment.

4. The Board should establish budget transfer limits and review budget transfers after they are made.
5. The Board should take action to address all findings and recommendations contained in management letters and reports issued by the Comptroller's office, the internal auditor or by their IPA.
6. The Board should require timely and complete financial and budgetary information throughout the year and use this information to monitor financial activity of the District.
7. The Board should review all financial operations by monitoring existing policies and procedures and, where appropriate, adopt policies and procedures to guide these operations.

Claims Processing

An effective claims processing system includes policies and procedures to ensure that every claim contains enough supporting documentation to determine whether it complies with statutory requirements and District policies, and that the amounts represent actual and necessary expenses. An effective procurement process helps the District obtain services, materials, supplies, and equipment of the right quality, in the right quantity, from the right source, at the right price, with sufficient appropriations available, and in compliance with applicable Board and legal requirements. This helps to ensure that taxpayer dollars are expended in the most efficient manner.

We noted the Board adopted policies and procedures for claims processing and procurement were not operating effectively, and could result in errors and irregularities occurring and not being detected. As a result, District personnel made unauthorized purchases from and payments to vendors, over-expended several appropriation accounts, did not appropriately audit claims, or account for credit card and gas purchases.

Purchase Orders

A purchase order system typically requires the purchasing agent to certify that funds are available before the goods can be ordered from the vendor and to document this certification by approving purchase orders that include detailed descriptions of the items to be purchased. When working properly, a purchase order system can be effective in controlling expenditures. The District's purchasing policy requires purchase orders be used where a budgetary appropriation has been made and the administrative manual requires the purchasing agent to review and approve purchase orders. In addition, the financial software has an important control feature that requires that sufficient appropriations be available before District personnel create purchase orders.

The purchase order system was ineffective because the previous purchasing agent¹² was not properly reviewing purchase orders, purchase orders were issued after purchases were made and employees were continually overriding the financial software to generate purchase orders when sufficient appropriations were not available. Further, management's ability to detect employee overrides was limited because the financial software could not produce audit logs for review. See related comment entitled

¹² The former Superintendent was also the purchasing agent for the period September 1, 2003 through February 2006.

“Information Technology – Audit Logs”. As a result, purchases were made in excess of authorized amounts and appropriations were over-expended.

Of the 928 claims we reviewed totaling \$504,556, 13 purchases totaling \$9,491 exceeded the purchase order amounts, 43 purchase orders totaling \$17,103 were issued after the purchases were made, and 112 purchase orders, totaling \$356,141 exceeded available appropriations.

Claims Auditing

Conducting a proper audit of claims before the District pays them is an integral part of any internal control system. Education Law requires the Board to audit each claim before authorizing payment or to appoint a claims auditor to perform this function. Each claim must be deliberately and thoroughly reviewed to determine whether it is for a valid, legal, and necessary obligation incurred by an authorized official; includes detailed receipts and written statements to indicate receipt of goods or services; and is in proper form, is mathematically correct, and does not include charges previously paid.

Because the Board did not appoint a claims auditor, it retained responsibility for auditing claims. However, Board members told us they scanned warrants for new or unusual vendors, or unusual payment amounts, but did not review individual claims or supporting documentation. Therefore, the Board did not properly audit any of the claims we reviewed. As a result of the Board’s failure to perform an appropriate audit of claims, Board members did not realize that the purchase order system was not being followed. Further, of the 928 claims we reviewed totaling \$504,556, 216 (23 percent) lacked sufficient detail and should not have been approved for payment until documentation was obtained.

The review of only summary warrant reports is a significant internal control weakness. The Board cannot determine from these documents whether the proposed payments represent actual, reasonable, and necessary obligations incurred by authorized District officials. Without a thorough audit of each claim, there is an increased risk that the District may pay for inappropriate expenses.

Credit Card Purchases

An effective system of internal controls requires the Board to adopt credit card policies and procedures to establish the parameters for use, procedures for monitoring use, promote accountability and responsibility and prevent improper use. Policies and procedures should specifically include:

- Authorized methods for obtaining credit cards

- Criteria for who will be issued credit cards
- Transaction limits
- Authorized use, including prior approval and business purpose justification
- Repercussions for improper use, including liability for damages and/or loss
- An acknowledgement form – stating that the employee understands and will comply with policies and procedures – for employees to sign
- Documentation and receipts to be submitted and a timetable for submission
- The separation of duties required between the purchasing, payment and reconciliation functions
- Records that must be maintained, such as a purchase and mileage logs
- Periodic reviews of use, including the need to assess the reasonableness of the nature and number of charges.

The District has one business credit card account and two gas credit card accounts. However, the Board has not adopted policies and procedures for their use. We reviewed all 23 business card purchases totaling \$2,215 during the audit period. We found:

- None of the charges had prior approvals
- Twelve (50 percent) of the charges totaling \$705 did not have detailed receipts
- Twenty-two (96 percent) of the charges included sales tax, which the District is exempt from paying
- Sixteen (70 percent) of the charges totaling \$1,686 were for food. The largest was a \$911 restaurant charge, in February 2005, to celebrate the boys' basketball sectional win, which included costs for faculty members and parents. Although the District was reimbursed for \$192 (21 percent) of the bill, there was no documentation to indicate this was adequate. Other credit card receipts did not include information showing the

business purpose, nor did they include explanations as to why meals and refreshments were required.

We also reviewed all 27 gas card statements totaling \$9,898 during the audit period. We found the charges lacked supporting documentation and a mileage log was not kept for District vehicles. Therefore, we could not determine if charges were reasonable, for District vehicles and for District business.

The lack of prior approval, detailed original receipts, documentation as to business necessity and mileage logs could result in excessive, unauthorized, or improper District expenses, and may result in officers or employees being held personally liable for undocumented charges.

Recommendations

8. The Board should ensure the purchasing agent verifies that sufficient appropriations are available before approving purchase orders, and that all purchase orders are approved before orders for goods and services are placed.
9. District officials should ensure employees do not override computer controls and review audit logs to monitor these controls.
10. The Board should ensure that District personnel provide sufficient detail for claims and the Board should properly audit claims prior to payment.
11. The Board should establish a credit card policy and procedures to adequately safeguard District assets.
12. The Board should ensure that every District credit card claim contains enough supporting documentation to determine whether it complies with District policies, and that the amounts represent actual and necessary expenses.
13. The Board should ensure mileage logs are kept and reviewed for all District vehicles to ensure gas purchases are reasonable, for District vehicles and for District business.

Fringe Benefits

Districts generally establish the salaries and benefits for their employees in written labor agreements negotiated with collective bargaining units and individual employees. To ensure employees receive the compensation and benefits the District intends for them to receive, the Board must clearly define and authorize such payments. The documentation, proper implementation, and monitoring of a District's labor contracts are essential aspects of internal control. For those employees not covered by employment contracts or collective bargaining agreements, the Board may choose to establish District-wide policies or pass annual resolutions defining the compensation and benefits to be provided to these individuals.

The District did not follow these acceptable processes. As a result, the District made unauthorized payments totaling \$12,500 and provided benefits totaling \$19,562 to employees for which there was no specific Board authorization. Expenditures of this type should be fully supported by, and referenced to, applicable written agreements, formal policies and Board resolutions.

Administrative Employee Benefits

The Board authorizes and approves employee benefits for most District employees in individual employee contracts, collective bargaining agreements, or by Board resolution. However, we found no documentation to indicate the Board authorized or approved the benefit package prepared by the former Superintendent for five employees who were not covered by individual employee contracts or collective bargaining agreements.¹³ These administrators' benefits included leave time, salary, longevity payments, health and dental insurance, tuition reimbursement, flexible spending options and retirement benefits. The administrators also received stipends for contributions to 401K or 403(b) (TSA) accounts to cover premiums for life insurance, optical expenses/optical plan. Stipends of \$1,500 were paid twice a year¹⁴ until the former Superintendent increased the amounts to \$2,000 in 2005-06. From July 1, 2004 to June 30, 2006, they received stipends totaling \$12,500.

The payroll clerk stated she questioned the legitimacy of these payments, but was directed by the former Superintendent to pay them. The payroll clerk also brought her concerns to the attention of a Board member and the independent auditor. However, these payments continued to be paid. Prior to paying the June 30, 2006

¹³ High School Principal, Middle School Principal, Elementary Principal, Assistant Elementary Principal, and Director of Special Education

¹⁴ January and June

stipends, the payroll clerk brought her concerns to us. We met with a Board member and the interim Superintendent and determined that the Board had not authorized the stipends. Several other Board members also stated there was no approval for these benefits.

Health Insurance Benefits

The Campbell-Savona Teachers Association contract provides health insurance coverage to its members. The District pays 100 percent of the premium for individual coverage and ninety percent of the premium for the family plan. The payroll clerk maintains a list of eligible employees and deducts premiums from their paychecks.

We selected 17 of the 266 enrollees during the 2005-06 school year (both current and retired/former employees) to determine if they were eligible for health insurance and making proper contributions. All enrollees were making proper contributions. However, two individuals received health insurance that were not eligible for this benefit:

- The clerk of the works for a capital project – This individual was an independent contractor, and therefore not eligible for health insurance benefits. During our audit period, the District inappropriately paid \$18,522 for health insurance and \$220 for dental claims on behalf of this individual.
- A voluntarily terminated employee – Upon termination this individual’s health insurance was discontinued, as required, and she was therefore eligible to receive health insurance under COBRA.¹⁵ However, the current Superintendent instructed the payroll clerk to reinstate her health insurance for one month until her insurance coverage began at her new employer. This individual continued to pay 10 percent of the premium and the District paid the other 90 percent at a cost of \$820.

When the Board does not properly authorize and monitor benefits, it increases the likelihood that the District will incur unnecessary expenses and employees will receive benefits to which they are not entitled. Because the Board has not delegated its authority for benefit approval to the Superintendent, it is the Superintendent’s responsibility to ensure that only Board-authorized benefits are paid.

¹⁵ The Consolidated Omnibus Budget Reconciliation Act gives workers and their families who lose their health benefits the right to choose to continue group health benefits provided by their group health plan for limited periods under certain circumstances. Qualified individuals may be required to pay the entire premium for coverage up to 102 percent of the cost to the plan.

Recommendations

14. The Board should ensure all employees are covered by employment contracts or collective bargaining agreements, which clearly state all compensation and benefits.
15. The Board should formally approve all employee benefit arrangements.
16. District officials should monitor employee compensation and benefits to ensure they are consistent with Board approvals.
17. The Board should take the appropriate steps to recover the \$32,062 in unauthorized fringe benefit payments.

Information Technology

The use of information technology (IT) affects the fundamental manner in which the District initiates, processes, records and reports transactions. The extent to which computer processing is used in significant accounting applications, and the complexity of that processing, determines the specific risks that information technology poses to the District's internal control. The District's widespread use of information technology presents a number of internal control risks that must be addressed, including unauthorized access to data, unauthorized changes to data in master files and the potential loss of data. Controls to address these risks consist of a combination of automated controls and manual controls.

An effective system of internal controls to safeguard computerized data includes policies and procedures adopted by the Board to minimize the loss or corruption of essential data. Policies and procedures should limit user access to only authorized persons to protect data from loss by intentional or unintentional manipulation, and provide procedures to restore data if it is unavoidably lost or corrupted. The system of internal controls should also include a disaster recovery plan and a routine system of computer back up so that in the event of loss of computerized data, it can be restored with a minimal amount of inconvenience, as quickly as possible.¹⁶

District officials have not effectively addressed the safeguarding of computer data by establishing appropriate policies and procedures. Adequate and deliberate protection of computer data is necessary for District operations to proceed smoothly. District officials have not restricted physical access to IT assets, nor restricted employee access to only those modules of the computerized financial software that were required by their individual job description(s) and/or official duties. In addition, management's ability to detect and properly address unauthorized activities was limited because the computerized financial system could not produce audit logs for review. District personnel also have no guidelines or plan to follow to prevent the loss of equipment and data or data recovery procedures because the Board has not adopted a comprehensive disaster recovery plan. Finally, the backup tapes for each server are located in the same room as the server, which may render them useless in the event of a disaster. All of these may result in the potential loss of costly

¹⁶ A disaster includes any sudden, unplanned catastrophic event (e.g., fire, a computer virus or inadvertent employee action) that compromises the integrity and data of the information technology systems.

equipment, additional work for IT staff and a decrease in productivity for employees whose work is interrupted.

Physical Access Over IT Assets

An effective system of internal control restricts access to the components of the IT system, such as servers. Unrestricted access to the server room is dangerous to the security of the system. An individual could log into the network and applications, alter records or physically destroy the equipment so that no one could access the server. This could result in the District expending significant resources in both time and money to correct/repair data and equipment. Security is enhanced by keeping server room doors locked at all times, controlling the keys, documenting visitors' arrivals and departures, having only one entrance to each server room, and ensuring server rooms have adequate ventilation, ideally with their own HVAC system.

District officials have not established policies or procedures to ensure the system's equipment is in a secure location with adequate ventilation. The network servers and component parts are located in three server rooms. Although the main server is in the locked computer support technician's office (in the high school), several individuals have keys to the room. The other high school server is in a room attached to the library with two entrances. Although one entrance that leads to the hallway is always locked, the other is attached to the library. Anyone with a key to the outside doors of the school can access the server rooms. The elementary server room is attached to the library and has one entrance. However, during our tour of the facility, the door was open and District officials were unable to explain why this occurred. The main server room temperature is maintained with an air conditioner and the other two rooms are connected to the main HVAC system for the schools.

Security over IT assets helps ensure they are protected from loss, their value is maintained and they are used effectively. Network components must be physically secured in a locked room with adequate ventilation where access is controlled and tracked. Under the current conditions, it would be difficult to prevent unauthorized and/or malicious access to IT assets or to identify the party responsible if such access did occur. Server failures could result in the potential loss of costly equipment, additional work for IT staff and a decrease in productivity for employees whose work is interrupted.

User Accounts and Passwords

Good internal controls include policies and procedures to limit access to computerized data. Access should be restricted to authorized users based upon the needs of their particular job functions. Access

controls provide reasonable assurance that computer resources are protected from unauthorized modification.

A system or application must be able to identify users to control access. A system administrator creates user accounts for this purpose, which contain information such as access rights to files, applications, directories and other computer resources, and to establish the relationships between users and a network, computer, or application. Users enter their user name and authentication to gain access. The computer compares this information with its database of user accounts. If a match is found, the computer gives access to the resources stipulated for the user account. Fingerprints or smartcards can be used to authenticate users, but the most common way is by using passwords.

Strong passwords should be used, which are at least eight characters long, and contain combinations of upper- and lower-case letters, numbers, and punctuation. Passwords should not contain words found in the dictionary; hardware or software names; repeated letters or numbers; addresses; phone numbers; or the users' names, family names, or pets' names. Most network and operating system software packages allow administrators to set a maximum age for passwords, after which they expire, and a maximum period of inactivity before the user is again required to be authenticated. Users should be required to change passwords every 30 to 90 days and computers should time-out after a reasonable period of inactivity.

Unauthorized users often commandeer legitimate user accounts to gain access. Once in a system, they may be able to manipulate a user account with administrator rights, which would allow access to install programs, download or destroy data, and the ability to change log files. An unauthorized user could feasibly cover his or her tracks. This unauthorized access can be detrimental to an organization's information technology capabilities.

The Board has not established policies and procedures for the creation and administration of network passwords. As a result, internal controls are not adequate. The technology coordinator provides employees with a user name and password when they are first granted access to the network. However, the assigned user names and passwords are basic and easily deciphered and users are not required to periodically change their passwords.

Access Rights

Access should be restricted to only those functions that are required by individual job description(s) and/or official duties and should be granted such that a proper segregation of duties is maintained,

including a segregation between the duties of administering access to the financial software and those of the Business Office.

Employee access was not properly restricted to only those modules that were required by their individual job description(s) and/or official duties. Three individuals had full access to all modules of the accounting software¹⁷ and 14 individuals had access to the purchasing module. In addition, the Treasurer and Business Manager had administrative access, enabling them to add/remove/update users and access rights, and perform other administrative functions including management overrides of system controls. Administrative access was incompatible with their daily Business Office activities, because, on a daily basis, they used the system to record journal entries, complete bank reconciliations, create purchase orders, and set up encumbrances. We also found the former Superintendent's user account was not disabled until approximately three months after he resigned, and then, only because we brought it to the District's attention. Due to the unrestricted access to the computerized financial system, there was increased financial risk to the District.

Audit Logs

A computerized financial system should provide a means of determining, on a constant basis, the identity of the individual accessing the system and what transactions were processed. Audit logs maintain a record of activity by system or application, and provide information such as the identity of each person who has accessed the system, the time and date of access, what activity occurred, and the time and date of logoff. Management, or management's designee, would review an audit log to monitor user activity to provide a mechanism for individual accountability, reconstructing events and problem monitoring. This tool provides a mechanism for individual accountability, reconstructing events and problem monitoring. However, we noted management's ability to detect and properly address unauthorized activities was limited because the computerized financial system could not produce audit logs for review.

Based on the weaknesses noted over the District's financial management software, we performed a variety of tests of payroll payments, maintenance of leave accruals, accounts payable payments and bank reconciliations to verify that transactions during the scope period were appropriate. Although our tests did not disclose any exceptions, the failure to properly monitor user activity could result in errors or irregularities occurring and not being detected and corrected in a timely manner.

¹⁷ Superintendent, District Treasurer, and payroll clerk

Backup/Disaster Recovery

An effective internal control system for information technology requires the adoption of a formal contingency plan. One of the cardinal rules for using computers is to protect data by backing up files regularly. Even the most reliable computer is apt to break down eventually. Data stored on servers should be backed up (a duplicate copy of information made) on a routine basis so it can be restored in the event of a loss. Many professionals recommend that you make two, or even three, backups of your files. Back-up copies of data should be stored in a secure offsite location.

The District performs nightly backups and the buildings where the computers are located are locked at night. However, the backup tapes for each server are located in the same room as the server. As a result, a fire or other disaster could not only destroy or damage the computers but also the backup tapes, resulting in a loss of essential data, which may not be recoverable.

A disaster recovery plan should be established to prevent loss of the computer equipment and data and provide procedures for recovery in the event of a loss. A disaster recovery plan describes how an organization is to deal with potential disasters and consists of the precautions taken to minimize the effects of a disaster and to enable the organization to either maintain or quickly resume mission-critical functions. Typically, disaster recovery planning involves an analysis of business processes and continuity needs and may include a significant focus on disaster prevention.

District officials had not established formal policies or procedures to address potential disasters. In the event of a disaster, District personnel have no guidelines or plan to follow to prevent the loss of equipment and data or data recovery procedures.

Recommendations

18. District officials should adopt policies and procedures to restrict physical access to IT assets. The policies should require servers to be located in areas that are protected from unauthorized access and have adequate ventilation, that accurate lists of computer locations be maintained, and that computers are physically secured when not in use.

19. District officials should establish and monitor policies and procedures for user accounts, including:

- Requiring strong passwords and training users on how to choose secure passwords.
- Requiring users to periodically change their passwords.

- Requiring sessions to automatically terminate after a period of inactivity.
 - Prompt removal/modification of access rights when individuals leave the employ of the District or have their duties modified.
20. District officials should establish a hierarchy of access controls based on job responsibilities, and monitor access levels to ensure critical duties are properly segregated. Someone independent of the business function, such as an IT staff member, should have administrative rights over the financial software system.
 21. District officials should work with the computerized financial software vendor to create audit logs.
 22. District officials should establish contingency plans including disaster recovery and computer data storage and back up.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



CAMPBELL-SAVONA CENTRAL SCHOOL

**LYNN LYNDES • SUPERINTENDENT OF SCHOOLS
8455 COUNTY RT. 125
CAMPBELL, NY 14821
PHONE • (607) 527-4550 EXT. 402
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May 8, 2008

[REDACTED]

Office of the State Comptroller
The Powers Building
16 West Main Street - Suite 522
Rochester, NY 14614

RE: Report of Examination - Response from District Officials

Dear [REDACTED]:

On April 8, 2007, representatives of your office met with the Board of Education and designated staff for the purpose of discussing the "Report of Examination" (hereinafter, "Report"). The meeting culminated a process which began in May 2006, when your examiners first met with the then serving Board of Education. At this "entrance meeting" the Board of Education was informed that the purpose of the audit would be to examine the "Financial Conditions and Internal Controls over Selected Financial Activities" for the period July 1, 2004 through June 30, 2006. The Board of Education asked that the scope of the proposed audit be expanded to include a complete examination of the district's finances to determine the causes of the district's deficit. As documented in this report, that request was honored, for which the Board is most appreciative and herein, expresses a grateful **thank you**. The current Board of Education is keenly aware of the resources, both time and money, expended in conducting the examination and getting to the "bottom of what happened." It appreciates the work ethic of the individual members of your staff who undertook the Report. In particular, the work of [REDACTED] must be commended.

In January 2006, the Board of Education, then serving, was shocked to learn that the District's financial position had declined to the point that the district was in a deficit position. The actions required to remedy the situation dramatically impacted our entire community. This examination independently reports on the roots of the problems that occurred and caused the District's General Fund deficit for the fiscal year ending June 30, 2006. The Board of Education believes that the publication of the Report is an important part of the process to ultimately restore our communities trust and confidence in its governance of the District.

Four of the current seven members of the Board of Education were members of the Board of Education responsible for the governance of the District for some or all the years leading up to fiscal 2006. The findings of the Report are clear. During the period 1998 through 2006, the Boards on which the four current members served did not fulfill their responsibilities and therefore those Boards are fundamentally accountable for failing to assure systems were in place which would have assured the fiscal integrity and efficient operation of the district. What this report does is identify what was not done or what should have been done. But, the Board knew on January 29th, 2006 when the district's independent auditor and Superintendent reported on the results of the audit for the year ending June 30, 2005 they had somehow failed. That Board took immediate action to address the matter which ultimately resulted in the finding made in this Report that, "[s]ubsequent, to the end of our field work we have become aware of reported improvements in the District's financial condition." and "...certain operational changes have allowed the District to complete the fiscal 2006-07 fiscal year with a general fund unreserved balance of \$1.5 million." The Board serving in 2006 acknowledged its failure to the Campbell-Savona community right from the "get go," but it and subsequent Boards have also fulfilled their promise to be diligent in their ongoing stewardship of the district.

The concern exists that the responsibility non-Board members had for what occurred is not represented adequately in the findings of the Report. It is appreciated that it may be impossible for an auditor to discern and therefore be able to report on what can't be found in writing during their work. However, during the course of the audit work, interviews and conversations took place which, it is believed, in some manner could have been reflected in the findings of the Report, with the result that the reader of the Report would have some understanding of the responsibility others had for what occurred. The "Five Point Plan" which was enacted by the State Legislature in 2005, now puts in place checks and balances which, if in place previously, would have made the Boards that governed the District from 1998 to 2006 more likely to have been able to take action that would have assured the fiscal health of the district instead of the fiscal failings that occurred because agents of those Boards didn't do what they should have.

As is noted in the Report, the poor financial condition of the District at the end of the 2005-06 school year was due to a combination of many issues that were occurring at the time and in the period leading up to that year. The members of the Board relied too heavily on the information they were receiving from the former superintendent/business manager and did not "dig deep" enough to realize that the figures they were supplied were not reasonable. Furthermore, although the District's Independent Auditor did what it "had to do", it did not do what it could have done to alert Boards of Education serving during this period. This lack of information, along with poor vigilance and skepticism from the Board allowed the fiscal situation to deteriorate. It is gratifying to find, however, that despite the weaknesses which have been documented in the Report, there is no evidence of fraud, embezzlement, or other illegalities by the parties involved in the finance of the District.

In the time since the Audit commenced, the Board and the Administration have painstakingly analyzed the factors leading up to the fiscal crisis and have taken deliberate action to minimize the risk of something similar happening in the future. Board members now receive training in school finance and are given monthly reports that allow them to

adequately analyze the fiscal standing of the District. An Audit Committee comprised of three Board members and two community members has been established and is very actively providing an additional resource upon which the Board can rely for oversight. The current Administration has been diligent in controlling spending and utilizing practices that limit the risk of fiscal mismanagement. The District has contracted with the Greater Southern Tier BOCES to provide additional business support and expertise in order to institute best practices.

The Report provides twenty-two recommendations which are addressed below. When implemented, these recommendations will improve the District's financial policies, procedures and accountability. Some of the recommendations were implemented during the period in which the audit was being conducted. Please be assured that an action plan will be immediately undertaken to determine how to implement the rest of the recommendations.

Sincerely,



Lynn Lyndes,
Superintendent of Schools



Darrell Cornett
President, Campbell-Savona Board of Education

RESPONSE TO RECOMMENDATIONS

Financial Condition

Recommendation 1: District officials should develop a plan to prevent the future recurrence of deficit fund balances and cash flow deficiencies. Included in this long-term operational plan should also be a long-term capital plan.

District response: The issues that contributed to the past deficit fund balances and cash flow deficiencies have been resolved through improved business practices and procedures that have been adopted and implemented by the district since the 2005-06 school year. However, the development of a long-term operational plan is necessary to ensure that the district has advance notice of potential issues which may require adjustments to the budget and can produce fiscal stress on the district. The district will begin to develop a truly comprehensive long-term plan during the 2008-09 school year. Before the comprehensive financial plan can be finalized, long-term educational and long-term capital plans need also be developed, and as such the involvement of many of the District's stakeholders is required.

Recommendation 2: The Board should adopt budgets that accurately estimate revenues, expenditures and available fund balance and then monitor actual activity against the plan throughout the year.

District response: The budget that the Board now adopts is crafted during a series of budget workshops. During these workshops, historical data from past years' expenditures and revenues are presented in order to assist the Board in determining if proposed budget figures are reasonable. Throughout the year, Board members are given monthly financial reports which show actual expenses and revenues as compared to budgeted amounts, so that they may monitor the status of the budget. Also included in the monthly financial reports are projected expenses and revenues that indicate the potential fund balance for the year.

Management Responsibilities

Recommendation 3: The Board should appoint a claims auditor or properly audit all claims prior to payment.

District response: The District has appointed an internal claims auditor. The individual is highly trained and is extremely diligent and assures that only appropriately authorized and documented claims are approved for payment.

Recommendation 4: The Board should establish budget transfer limits and review budget transfers after they are made.

District response: Board policy now states “Within legal limits as established by the Board, the Superintendent is authorized to transfer funds within the budget.” Although the limit has not been specified by dollar amount in the past, a limit will be discussed at the July 2008 reorganization meeting of the Board. However, a current safeguard now in place is that all budget transfers must be recommended by the District’s School Business Administrator prior to the Superintendent’s approval will be continued. Copies of approved budget transfers are provided to the Board on a monthly basis.

Recommendation 5: The Board should take action to address all findings and recommendations contained in management letters and reports issued by the Comptroller’s office, the internal auditor or by their IPA.

District response: Included in the duties and responsibilities of the Audit Committee of the Board, which was established in February 2006, is to “review every corrective action plan developed by the school district and assist the Board of Education in the implementation of such plans”. The Audit Committee has developed a plan of action to implement all of the recommendations and findings that have been received by the District. Included in the plan are details specifying timelines, responsible personnel, and criteria for success. This plan is reviewed and updated on a regular basis.

Recommendation 6: The Board should require timely and complete financial and budgetary information throughout the year and use this information to monitor financial activity of the District.

District response: Since April 2006, the Board has received a packet of monthly financial reports from the Business Administrator. Included in this packet are:

- An Expenditure Status Report which shows budgeted, actual to date, and projected expenditures for each budget area
- A Revenue Status Report which shows budgeted, actual to date, and projected revenues for each budget area
- An Internal Claims Auditor Report for each check run
- Copies of all approved Budget Transfer Request forms
- A Funds Summary which shows the balance in each of the District’s funds
- Any other reports that are requested by the Board

Recommendation 7: The Board should review all financial operations by monitoring existing policies and procedures and, where appropriate, adopt policies and procedures to guide these operations.

District response: The Board has begun the process of reviewing all of its required policies. In addition, the plan of action that was developed by the Audit Committee calls for the creation of a Business Office Procedures Manual in which the financial policies and procedures of the District will be established in writing. This manual will be developed over the next year and completed prior to June 30, 2009.

Claims Processing

Recommendation 8: The Board should ensure the purchasing agent verifies that sufficient appropriations are available before approving purchase orders, and that all purchase orders are approved before orders for goods and services are placed.

District response: Now, before a purchase order is approved, the Purchasing Agent determines if the expenditure is appropriate, if it is approved by the proper administrator, and if the funds are sufficient in the budget code from which the purchase will be paid. If the funds are not sufficient, a budget transfer is requested before the purchase order is issued. Orders for goods or services that are placed before a written purchase order can be issued must be verbally approved by the Purchasing Agent who assures that funds are available. The claims auditor notes this as an exception on the Internal Claims Auditor Report as a “confirming” purchase order. Confirming orders are only authorized in emergency situations. Employees of the District have been instructed not to make purchases without pre-approval of the Purchasing Agent. Employees who violate this directive are subject to disciplinary action.

Recommendation 9: District officials should ensure employees do not override computer controls and review audit logs to monitor these controls.

District response: The financial software that was in use by the District during the time of the Comptroller’s examination did not provide for audit logs. The software that is currently used does allow this feature. Also, the number of employees who have the authority to override computer controls has been limited to a very few individuals.

Recommendation 10: The Board should ensure that District personnel provide sufficient detail for claims and the Board should properly audit claims prior to payment.

District response: The Board gave the authority to audit claims to an Internal Claims Auditor. Before claims are submitted for payment, the School Business Administrator reviews the documentation and must approve the invoice for payment. If documentation is missing or insufficient, the claim is not submitted until satisfactory. After this approval, the Internal Claims Auditor must still give approval before payment is authorized.

Recommendation 11: The Board should establish a credit card policy and procedures to adequately safeguard District assets.

District response: The Board has begun the process of reviewing all of its required policies, including one that will deal with credit cards. The current practice is that the only employees with access to the business credit card are the Superintendent and the School Business Administrator. All purchases made with the credit card must be pre-approved with a signed requisition and purchase order and are audited the same as other claims. A written policy will be adopted prior to August 31, 2008.

Recommendation 12: The Board should ensure that every District credit card claim contains enough supporting documentation to determine whether it complies with District policies, and that the amounts represent actual and necessary expenses.

District response: When the credit card bill is now received, it is compared to purchase orders which have been issued for the credit card. The Business Administrator audits the documentation before sending it to the Internal Claims Auditor. If documentation is missing or insufficient, the claim is not submitted for payment.

Recommendation 13: The Board should ensure mileage logs are kept and reviewed for all District vehicles to ensure gas purchases are reasonable, for district vehicles and for District business.

District response: Mileage logs are already maintained for the vehicles that are under the control of the Transportation Department. Mileage logs have not been maintained for the vehicles used by the Maintenance Department. An appropriate form will be developed and put into use prior to July 1, 2008.

Fringe Benefits

Recommendation 14: The Board should ensure all employees are covered by employment contracts or collective bargaining agreements, which clearly state all compensation and benefits.

District response: All employees, with the exception of those represented by the Civil Service Employees Association, Inc. (CSEA), are now covered by written agreements. The District is currently in negotiations with the CSEA. It is the intention of the District to have written agreements with all employees as soon as this can be accomplished in accordance with the requirements of the Taylor Law and PERB.

Recommendation 15: The Board should formally approve all employee benefit arrangements.

District response: The payroll function of the District is now performed by the GST BOCES Central Business Office. All employee benefit arrangements are now approved by the Board of Education. Only upon written notification of Board action is the District's payroll clerk authorized to make benefit arrangement changes. A Board of Education policy will be formally adopted to make this current administrative practice policy by August 31, 2008.

Recommendation 16: District officials should monitor employee compensation and benefits to ensure they are consistent with Board approvals.

District response: The School Business Administrator now reviews payroll and benefit amounts when the preliminary budget is prepared each year and compares them to Board approvals and contractual obligations. Furthermore, necessary documentation now must be approved by the appropriate district administrator before the payroll is processed.

Recommendation 17: The Board should take the appropriate steps to recover the \$32,062 in unauthorized fringe benefit payments.

District response: Individual parties who received unauthorized payments will be contacted and asked to voluntarily reimburse the district. If repayment is not received, appropriate action will be taken as deemed prudent by the Board of Education.

Information Technology

Recommendation 18: District officials should adopt policies and procedures to restrict physical access to IT assets. The policies should require servers to be located in areas that are protected from unauthorized access and have adequate ventilation, that accurate lists of computer locations be maintained, and that computers are physically secured when not in use.

District response: The District has included many security enhancements in the capital project that was approved by the voters last summer. Included in this project are plans to improve the rooms in which the technology components are kept. These improvements include increased security features and upgraded climate control systems to ensure environmental integrity and consistency. The District has also recently completed an appraisal and inventory of its property. Technology equipment is listed individually on this inventory.

Recommendation 19: District officials should establish and monitor policies and procedures for user accounts, including:

- Requiring strong passwords and training users on how to choose secure passwords;
- Requiring users to periodically change their passwords;
- Requiring sessions to automatically terminate after a period of inactivity;
- Prompt removal/modification of access rights when individuals leave the employ of the District or have their duties modified.

District response: The Board recently began the process of reviewing all of its required policies. Information regarding proper password selection will be given to District computer users at the beginning of each school year. In addition, research has begun into the ability of the District's technology to require District computer users to change passwords on a periodic basis and to automatically terminate computer sessions after a period of inactivity. It will also become part of the District's dismissal procedures to include the elimination of technology rights.

Recommendation 20: District officials should establish a hierarchy of access controls based on job responsibilities, and monitor access levels to ensure critical duties are properly segregated. Someone independent of the business function, such as an IT staff member, should have administrative rights over the financial software system.

District response: With the new financial software system now in use, District employees are granted rights based on their need. As a result, the only person in the District with full access to the software is the Business Administrator, who currently has the sole authority to grant rights. Based on the recommendation, the administrative rights will be shifted to another person, yet to be determined.

Recommendation 21: District officials should work with the computerized financial software vendor to create audit logs.

District response: The financial software that was in use by the District during the time of the Comptroller's examination did not provide for audit logs. The software that is currently used does allow this feature and such logs now exist.

Recommendation 22: District officials should establish contingency plans including disaster recovery and computer data storage and back up.

District response: All administrative software is now hosted on offsite servers at GST BOCES and Erie 1 BOCES, which have disaster recovery plans in place. There are also selected District records which are backed up offsite through BOCES. In addition, District network servers are being backed up physically on a weekly basis onto temporary storage. Also, another server has been ordered which will be kept at the Savona Elementary School to serve as backup to the servers which are housed in the Jr.-Sr. High School.

Note: Regarding recommendations #18-22

The Superintendent of Schools will be forming a Technology Security Committee. The charge of the Committee shall be to review all District Information Technology policies and regulations and make recommendations to the Board of Education for future improvements to assure compliance with the recommendations provided in the Report.

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, and information technology.

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 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 objectives and scope by selecting for audit those areas most at risk. We selected financial condition and internal controls over the claims processing, fringe benefits, and information technology for further audit testing. Certain observations and lesser findings related to non-resident tuition and capital projects were discussed with District officials to help them strengthen internal control in those areas.

- We analyzed financial data from the ST-3 submitted to SED and the IPA financial statements for the last six fiscal years to determine operating surplus/deficits.
- We compared budget to actual financial data to determine the over-expenditure of budgeted amounts.
- We reviewed Board minutes to determine whether inter-fund advances and transfers were authorized.
- We analyzed transactions between funds to determine whether they were correctly recorded in the records and reported in the annual financial reports.
- We reviewed resolutions authorizing indebtedness and tested deposits of debt proceeds to determine conformity with State statutes.
- Within the procurement process, we interviewed the Board, Superintendent and Business Office staff about operating policies and procedures.
- Within fringe benefits, we interviewed District officials and employees to determine the fringe benefits received by employees. We also reviewed collective bargaining agreements,

individual employee contracts, Board minutes and resolutions, health insurance bills and emails.

- Within information technology, we interviewed employees in the IT department and Business Office concerning network passwords and administrative rights in the financial software. We reviewed user access rights, which detailed the administrative rights assigned and the last password change date. We also inquired about the existence of policies for contingency planning and/or disaster recovery.
- We visited each server room to determine the location of the servers and the condition of the rooms.
- We also reviewed the IPA's report for the fiscal year ended June 30, 2007 and verified certain components of fund balance, such as inter-fund receivables. In addition, we reviewed the budgeted and actual revenues and expenditures to determine the reason for the improved financial condition.

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.

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