



# Chittenango Central School District Internal Controls Over Cash Disbursements

Report of Examination

Period Covered:

July 1, 2006 — November 30, 2007

2008M-187



Thomas P. DiNapoli

# Table of Contents

	<b>Page</b>
<b>AUTHORITY LETTER</b>	2
<b>EXECUTIVE SUMMARY</b>	3
<b>INTRODUCTION</b>	5
Background	5
Objectives	5
Scope and Methodology	5
Comments of District Officials and Corrective Action	6
<b>CASH DISBURSEMENTS</b>	7
Recommendations	9
<b>CLASSIFICATION OF EMPLOYEES</b>	10
Recommendation	10
<b>APPENDIX A</b> Response From District Officials	11
<b>APPENDIX B</b> Audit Methodology and Standards	13
<b>APPENDIX C</b> How to Obtain Additional Copies of the Report	15
<b>APPENDIX D</b> Local Regional Office Listing	16

# State of New York Office of the State Comptroller

---

---

## **Division of Local Government and School Accountability**

November 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 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 Chittenango Central School District, entitled Internal Controls Over Cash Disbursements. 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 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 Chittenango Central School District (District) is governed by the Board of Education (Board) which comprises nine elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the chief executive officer of the District and is responsible, along with other administrative staff, for the day-to-day management of the District under the direction of the Board.

Responsibilities relating to District finances, accounting records and reports are largely those of the Assistant Superintendent for Business and the Treasurer. The Board appointed a claims auditor to assume the Board's powers and duties in regard to approving or denying claims against the District. The Board also appointed the Assistant Superintendent to certify District payrolls. All financial transactions are processed on the District's financial accounting software located on a server at the Onondaga-Madison-Cortland BOCES's Central New York Regional Information Center (CNYRIC). The District, as a public employer, enrolls its eligible employees in the New York State and Local Employees' Retirement System (ERS).

### **Scope and Objectives**

The objectives of our audit were to determine if District officials were properly safeguarding the District's financial resources and properly classifying employees for the period of July 1, 2006 to November 30, 2007. Our audit addressed the following related questions:

- Have District officials established internal controls over cash disbursements that are appropriately designed and operating effectively?
- Did the District's process for classifying workers ensure that the persons the District enrolls in ERS are entitled to membership in ERS?

### **Audit Results**

The District's system of internal controls did not adequately segregate the duties of the Treasurer to provide for an effective system of checks and balances for safeguarding District assets. In addition, the Treasurer did not affix or directly supervise the application of his electronic signature to District checks. Although our audit of cash disbursements disclosed no significant errors or irregularities, these weaknesses in internal controls significantly increase the risk that errors and/or irregularities might occur and go undetected and uncorrected.

In addition, we noted weaknesses in internal controls over the District's process for classifying workers whom the District enrolls in ERS. Although we did not find any exceptions, these weaknesses increase the risk that the District could improperly enroll non-employees (independent contractors) in ERS.

**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 Chittenango Central School District is located in the Towns of Sullivan, Cazenovia, Lincoln, and Lenox in Madison County, and the Towns of Cicero and Manlius in Onondaga County. The District is governed by the Board of Education (Board) which comprises nine elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the chief executive officer of the District and is responsible, along with other administrative staff, for the day-to-day management of the District under the direction of the Board.

There are five schools in operation within the District, with approximately 2,350 students and 390 employees. The District's budgeted expenditures for the 2007-08 fiscal year are \$36.7 million, which are funded primarily with State aid, and real property taxes.

Responsibilities relating to District finances, accounting records and reports are largely those of the Assistant Superintendent for Business, the Treasurer, and the accounts payable and payroll clerks. The Board appointed a claims auditor to assume the Board's powers and duties in regard to approving or denying claims against the District. The Board also appointed the Assistant Superintendent to certify District payrolls. All financial transactions are processed on the District's financial accounting software located on a server at the Onondaga-Madison-Cortland BOCES's Central New York Regional Information Center (CNYRIC). The District, as a public employer, enrolls its eligible employees in the New York State and Local Employees' Retirement System (ERS).

## Objectives

The objectives of our audit were to determine if District officials were properly safeguarding the District's financial resources and properly classifying employees. Our audit addressed the following related questions:

- Have District officials established internal controls over cash disbursements that are appropriately designed and operating effectively?
- Did the District's process for classifying workers ensure that the persons the District enrolls in ERS are entitled to membership in ERS?

## Scope and Methodology

We examined the District's internal controls over cash disbursements and the classification of workers for the period July 1, 2006 to November 30, 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 they planned to initiate corrective action.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the GML, Section 2116-a (3)(c) of the Education Law and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and forwarded to our office within 90 days. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make the CAP available for public review in the District Clerk's office.

## Cash Disbursements

An effective system of internal controls over cash disbursements requires that key duties be segregated so that no one employee controls all the transaction steps related to expenditures. In general, transaction approval, accounting, and asset custody must be separated. For example, the same individual should not collect and record cash receipts, make bank deposits, prepare and post journal entries, sign checks, and perform or supervise the reconciliation of District bank accounts. The proper segregation of duties helps to prevent and detect errors, and reduces the potential opportunities for employees to initiate and conceal improper payments or make unauthorized changes to the accounting records. If it is not practical to adequately segregate duties, District officials must institute compensating controls such as an independent review of the accounting records by someone who is not involved in key transactions. Additionally, the periodic review of computer-generated reports, such as exception/change reports and audit logs, can help District officials monitor employees' work on the computerized accounting system. Once adequate internal controls are in place, the Board should monitor them periodically to ensure they are operating effectively.

District management has not established adequate internal controls over all cash disbursements. We found that the Treasurer's cash disbursement duties are not properly segregated and there is no oversight by other staff or management to compensate for the lack of segregation of duties. The Treasurer handles all cash accounting and disbursement functions for the trust and agency fund without review or oversight. During the 2006-07 fiscal year, \$29.8 million was disbursed from the trust and agency account using checks, external wire transfers, and inter-account bank transfers. In addition, the Treasurer is able to make wire transfers without confirming authorization from another employee and can prepare and sign manual disbursements checks without any review. He also has unrestricted access rights to the cash disbursement functions in the District's accounting system and can make journal entries without review that adjust cash balances. District officials do not review audit logs from the District's accounting system to monitor the Treasurer's accounting entries. The Treasurer also prepares the bank reconciliations for all bank accounts and receives the bank statements and cancelled checks directly. Cancelled checks, bank statements and reconciliations are not periodically reviewed by any other District official. Finally, the Treasurer does not exercise sufficient control over the use of his electronic signature on District checks.

The Superintendent told us the Treasurer's duties were not adequately segregated due to limited staff and Business Office staffing changes at the end of the 2006-07 fiscal year. A major weakness in internal control exists in an environment where the same individual maintains the accounting records, has cash custody, and performs cash reconciliations. Concentrating key duties with one individual increases the risk the Treasurer could misappropriate cash without detection or manipulate records to conceal the misappropriation from District officials. The lack of oversight and authorization over cash disbursements increases the risk for payment errors and/or improper disbursements to occur. The Assistant Superintendent for Business told us he began reviewing the detailed bank reconciliations prepared by the Treasurer after he was hired in November 2007.

Given the District's inadequate controls and lack of effective oversight procedures over the Treasurer and the Treasurer's lack of control over his electronic signature on checks, we tested samples of electronic bank transfers, journal entries, and payments by check totaling \$40.2 million. Our testing included all electronic transfers for a two-month period totaling \$30,148,356; 20 journal entries totaling \$2,845,607; withdrawals (checks and electronic transfers) from the trust and agency account totaling \$7,028,385; checks written from funds other than trust and agency totaling \$28,686; and transactions for one month relating to retirees health insurance premiums totaling \$135,988. We also reviewed bank reconciliations for all bank accounts for one month. We found no significant exceptions in our testing.

Treasurer's Signature — As the District official responsible for authorizing cash disbursements, the Treasurer plays a critical role in management's system of internal control. The Treasurer must ensure that his signature is not used for unapproved payments. The Treasurer must affix or directly supervise the use of his actual or facsimile signature. Unless a statutory exception applies, the Treasurer should sign checks only after receiving a warrant certified by the claims auditor directing the Treasurer to pay the related claims, or after receiving a payroll register certified by the Assistant Superintendent. The Treasurer should compare the signed checks with the certified warrant or certified payroll for accuracy and consistency before the checks are issued.

We identified deficiencies in the Treasurer's oversight of the check-signing function. District accounts payable checks and payroll checks are printed at the CNYRIC, and CNYRIC employees imprint the Treasurer's signature on the checks without any involvement by the Treasurer. The accounts payable and payroll clerks process their respective warrant or payroll run and direct CNYRIC personnel to print the related checks that contain the Treasurer's signature. CNYRIC

staff sends the checks directly to the accounts payable and payroll clerks who are responsible for processing the transactions, and they mail or distribute them. This process does not allow the Treasurer to directly supervise the check-signing function and does not give the Treasurer control over when his signature is applied to checks. Also, we found that the Treasurer does not compare checks to an approved warrant or certified payroll register before the District issues the checks to ensure that all check disbursements have been approved by the claims auditor (claims) or Assistant Superintendent for Business (payroll). Unless the Treasurer makes comparisons before the checks are issued, there is increased risk of unauthorized payments and District officials lack assurance checks are being produced for only legitimate District expenses.

## **Recommendations**

1. District officials should evaluate the Treasurer's duties and responsibilities, and where practicable, assign them to other Business Office staff to better segregate duties. Where it is not practicable to segregate some duties, District officials should establish sufficient compensating controls, including routine reviews.
2. A District official or employee who does not make entries on the computerized accounting system should review the system's audit logs on a regular basis to help ensure that no unauthorized disbursements have been made.
3. The Treasurer should control his electronic signature at all times. The Treasurer should review printed checks and compare them to the warrant for vendor checks or a payroll register for payroll checks prior to distributing them to verify that checks are only for legitimate District purposes.

## Classification of Employees

Local governments and school districts obtain services from both public employees and independent contractors and consultants. It is important that public employers enroll only public employees, elected officials and public officers in ERS to ensure that only persons entitled to ERS membership receive ERS service credit. The Office of the State Comptroller's *Financial Management Guide for Local Governments*<sup>1</sup> provides information to help distinguish between independent contractors and employees. The New York State and Local Employees' Retirement System (ERS) provides its own checklist of indicators<sup>2</sup> that can help localities and school districts make this determination correctly. In addition, as of April 3, 2008, the Office of the State Comptroller (OSC) made enhanced regulations available that more clearly define how local governments and school districts can determine whether providers of professional services are employees or independent contractors. These regulations are posted on the OSC website.<sup>3</sup>

For the period July 1, 2006 through November 30, 2007, we audited the status of persons the District enrolled in ERS to determine whether these individuals met the criteria for employee classification as established by the *Financial Management Guide for Local Governments* and ERS indicators. Although we did not find any material exceptions in the classification of employees, we identified weaknesses in the District's controls over the classification process. For example, District officials have not formally designated an individual or department who is responsible for making a determination of whether individual(s) providing professional services should be classified as an employee or independent contractor and they have not established any guidelines or procedures for determining employee/contractor classifications. Unless District officials correct these control weaknesses, they are at increased risk of improperly enrolling non-employees in ERS.

### Recommendation

4. District officials should strengthen controls over worker classification processes to help ensure that they correctly determine the status of individuals who work for the District in compliance with the *Financial Management Guide for Local Governments* and the regulations posted on the OSC website.

<sup>1</sup> *Financial Management Guide for Local Governments*, Subsection 8.4020, page 1, issued December 1992

<sup>2</sup> The ERS Checklist, entitled *Distinguishing Between an Employee and an Independent Contractor*, is available from ERS.

<sup>3</sup> [www.osc.state.ny.us](http://www.osc.state.ny.us)

## **APPENDIX A**

### **RESPONSE FROM DISTRICT OFFICIALS**

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

# CHITTENANGO CENTRAL SCHOOL

Thomas E. Marzeski, Superintendent

Chittenango Central Schools  
1732 Fyler Road  
Chittenango, New York 13037  
Telephone: (315) 687-2840  
Fax No.: (315) 687-2841

Office of the Superintendent of Schools

November 5, 2008

████████████████████  
Office of the State Comptroller  
Division of Local Government and School Accountability  
State Office Building, Room 409  
333 East Washington Street  
Syracuse, NY 13202

Dear ██████████:

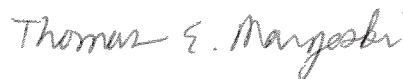
Please allow this letter to serve as our official acknowledgement of the receipt and review of the Draft Audit Report for the period covering July 1, 2006 – November 30, 2007 as prepared by your office. This will also confirm that an exit conference was held on October 30, 2008 at 8:00 a.m. in the District's Board room where the findings and recommendations were reviewed.

We would like to express our appreciation for the professionalism and thoroughness of the auditors in dealing with faculty and staff. We have found the audit process to be a valuable experience and welcomed the feedback. We are even more pleased that your sample testing of \$40.2 million in electronic transfers, checks and journal entries resulted in no significant exceptions. We are also pleased that the audit review of the classification of employees for Employee Retirement System (ERS) did not find any exceptions.

We will be submitting a proposed Corrective Action Plan (CAP) upon receipt of the Final Audit Plan in accordance to the 90 day requirement. Of the overall recommendations your office made relative to the strengthening of current policies and procedures, we have already begun the process of implementing changes.

On behalf of the Chittenango Central School District Board of Education and Administrative team, we thank you and your office for their due diligence and confirmation of our strong fiscal policies and procedures. We look forward to implementing your recommendations to further strengthen the organization.

Sincerely,



Thomas E. Marzeski  
Superintendent of Schools

TEM/kaq

## 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, and 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 objectives and scope by selecting for audit those areas most at risk. We selected controls related to cash disbursements and classification of employees for further audit testing.

For internal controls over cash disbursements, we focused our attention on the procedures for processing expenditures, maintaining accounting records, and reconciling bank accounts. To determine the effectiveness of internal controls and to evaluate the effect of deficiencies in those controls, we:

- Examined 20 manual cancelled checks to determine manual disbursements clearing the bank agreed with records and were supported by authorization for payment.
- Examined two months of bank transfers per bank statements to determine they were for District purposes.
- Examined 20 journal entries that decreased cash to related records to determine the legitimacy of entries posted.
- Examined one month of bank reconciliations for all bank accounts to determine the accuracy of balances reported.
- Examined 18 trust and agency fund disbursements and the related records to determine if the disbursements were proper and supported.
- Examined one month of retiree health insurance contributions transferred between bank accounts to the related voucher and cash disbursement to verify disbursement was for health insurance costs.

- Examined two months of trust and agency fund disbursements (i.e., cancelled checks and electronic transfers) to determine that the disbursements clearing the bank agreed with records and were supported by authorization for payment.

We also reviewed the District's process for classifying workers to ensure that the persons the District enrolls in ERS are valid public employees rather than independent contractors.

We conducted our 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

### HOW TO OBTAIN ADDITIONAL COPIES OF THE REPORT

To obtain copies of this report, write or visit our web page:

Office of the State Comptroller  
Public Information Office  
110 State Street, 15th Floor  
Albany, New York 12236  
(518) 474-4015  
<http://www.osc.state.ny.us/localgov/>

**APPENDIX D**  
**OFFICE OF THE STATE COMPTROLLER**  
**DIVISION OF LOCAL GOVERNMENT**  
**AND SCHOOL ACCOUNTABILITY**

Steven J. Hancox, Deputy Comptroller  
John C. Traylor, Assistant Comptroller

**LOCAL REGIONAL OFFICE LISTING**

---

**BUFFALO REGIONAL OFFICE**

Robert Meller, Chief Examiner  
Office of the State Comptroller  
295 Main Street, Suite 1032  
Buffalo, New York 14203-2510  
(716) 847-3647 Fax (716) 847-3643  
Email: [Muni-Buffalo@osc.state.ny.us](mailto:Muni-Buffalo@osc.state.ny.us)

Serving: Allegany, Cattaraugus, Chautauqua, Erie,  
Genesee, Niagara, Orleans, Wyoming counties

**ROCHESTER REGIONAL OFFICE**

Edward V. Grant, Jr., Chief Examiner  
Office of the State Comptroller  
The Powers Building  
16 West Main Street – Suite 522  
Rochester, New York 14614-1608  
(585) 454-2460 Fax (585) 454-3545  
Email: [Muni-Rochester@osc.state.ny.us](mailto:Muni-Rochester@osc.state.ny.us)

Serving: Cayuga, Chemung, Livingston, Monroe,  
Ontario, Schuyler, Seneca, Steuben, Wayne, Yates  
counties

**SYRACUSE REGIONAL OFFICE**

Eugene A. Camp, Chief Examiner  
Office of the State Comptroller  
State Office Building, Room 409  
333 E. Washington Street  
Syracuse, New York 13202-1428  
(315) 428-4192 Fax (315) 426-2119  
Email: [Muni-Syracuse@osc.state.ny.us](mailto:Muni-Syracuse@osc.state.ny.us)

Serving: Herkimer, Jefferson, Lewis, Madison,  
Oneida, Onondaga, Oswego, St. Lawrence counties

**BINGHAMTON REGIONAL OFFICE**

Patrick Carbone, Chief Examiner  
Office of the State Comptroller  
State Office Building, Room 1702  
44 Hawley Street  
Binghamton, New York 13901-4417  
(607) 721-8306 Fax (607) 721-8313  
Email: [Muni-Binghamton@osc.state.ny.us](mailto:Muni-Binghamton@osc.state.ny.us)

Serving: Broome, Chenango, Cortland, Delaware,  
Otsego, Schoharie, Sullivan, Tioga, Tompkins  
counties

**GLENS FALLS REGIONAL OFFICE**

Karl Smoczynski, Chief Examiner  
Office of the State Comptroller  
One Broad Street Plaza  
Glens Falls, New York 12801-4396  
(518) 793-0057 Fax (518) 793-5797  
Email: [Muni-GlensFalls@osc.state.ny.us](mailto:Muni-GlensFalls@osc.state.ny.us)

Serving: Clinton, Essex, Franklin, Fulton, Hamilton,  
Montgomery, Rensselaer, Saratoga, Warren, Washington  
counties

**ALBANY REGIONAL OFFICE**

Kenneth Madej, Chief Examiner  
Office of the State Comptroller  
22 Computer Drive West  
Albany, New York 12205-1695  
(518) 438-0093 Fax (518) 438-0367  
Email: [Muni-Albany@osc.state.ny.us](mailto:Muni-Albany@osc.state.ny.us)

Serving: Albany, Columbia, Dutchess, Greene,  
Schenectady, Ulster counties

**HAUPPAUGE REGIONAL OFFICE**

Jeffrey P. Leonard, Chief Examiner  
Office of the State Comptroller  
NYS Office Building, Room 3A10  
Veterans Memorial Highway  
Hauppauge, New York 11788-5533  
(631) 952-6534 Fax (631) 952-6530  
Email: [Muni-Hauppauge@osc.state.ny.us](mailto:Muni-Hauppauge@osc.state.ny.us)

Serving: Nassau, Suffolk counties

**NEWBURGH REGIONAL OFFICE**

Christopher Ellis, Chief Examiner  
Office of the State Comptroller  
33 Airport Center Drive, Suite 103  
New Windsor, New York 12553-4725  
(845) 567-0858 Fax (845) 567-0080  
Email: [Muni-Newburgh@osc.state.ny.us](mailto:Muni-Newburgh@osc.state.ny.us)

Serving: Orange, Putnam, Rockland, Westchester  
counties