



Mattituck-Cutchogue Union Free School District

Internal Controls Over Selected Financial Activities

Report of Examination

Period Covered:

July 1, 2006 — November 30, 2007

2008M-102



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

August 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 Mattituck-Cutchogue Union Free School District, entitled 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 Mattituck-Cutchogue Union Free 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.

The Treasurer and the Deputy Treasurer (in the Treasurer's absence) were appointed by the Board as authorized signatories on the District's checks. The accounts payable clerk receives cash and makes bank deposits. The Treasurer also serves as the Business Manager, purchasing agent, and administrator of the financial software that the District uses to store its data and process financial transactions. The District's payroll clerk also serves as the Deputy Treasurer.

Scope and Objective

The objective of our audit was to examine the District's internal controls over financial operations for the period July 1, 2006 through November 30, 2007. Our audit addressed the following related questions:

- Are internal controls over cash receipts and disbursements appropriately designed and operating effectively to adequately safeguard District assets?
- Did District officials provide proper segregation of the duties assigned in the Business Office?
- Did District officials implement policies and procedures over information technology to adequately protect electronic data?

Audit Results

The Board and District officials did not always ensure that proper internal controls were in place and operating as intended for some of the District's financial operations. At times the Board had not adopted the necessary policy guidance and at other times District officials had not properly implemented the Board's policies.

For example, although the District had appropriate policies in place, the Treasurer and Deputy Treasurer did not have separate signature disks, could place each other's signatures on District checks, and allowed staff to apply their signature to checks without sufficient oversight. The accounts payable clerk did not enter 14 cash receipts totaling approximately \$8.7 million into the daily cash receipt log, as required by policy, and did not compare the log to bank deposits. Finally, 16 wire transfers totaling \$6.1 million were initiated and executed without proper authorization or independent review. As a result, District assets are not adequately protected and there is an increased risk that errors and irregularities could occur and go undetected.

District officials did not develop policies and procedures to provide the proper segregation of duties in the Business Office, and there was no indication of compensating controls. The payroll clerk was responsible for human resource functions and was also the designated Deputy Treasurer, and therefore was able to change employee data, process the payroll, and print signed paychecks without independent review. The Business Manager was also the financial system administrator, Treasurer, and purchasing agent; this individual had unlimited access to the financial information, granted access rights to users (including his own), approved purchases, and signed checks with little or no oversight. As a result of the lack of controls over the segregation of key financial duties, the District is at an increased risk of its financial data and funds being lost or misused.

Finally, District officials did not adopt comprehensive IT policies and procedures to ensure the security of the District's financial system and data. There was no policy guidance for granting remote access to financial data or granting user permissions; as a result, individuals had remote network access and user rights to areas of the financial system not required for their jobs, and the financial system administrator's job was performed by an individual who was not independent of the District's financial operations. The District also did not require teachers and students to use passwords that were complex or routinely changed, the District did not store backup data off-site or test its validity through periodic restorations, and District officials did not develop a formal disaster recovery plan. Without adequate controls over information technology, the District's financial system and electronic data are subject to an increased risk of loss or misuse with the potential for costly disruption of business operations.

Comments of District Officials

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they have initiated corrective action. OSC comments on the District's response can be found in Appendix B.

Introduction

Background

The Mattituck-Cutchogue Union Free School District (District) is located in the Town of Southold, Suffolk County. The District is governed by the Board of Education (Board) which comprises seven elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. 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.

The Treasurer and the Deputy Treasurer (in the Treasurer's absence) were appointed by the Board as authorized signatories on the District's checks. The accounts payable clerk receives cash and makes bank deposits. The Treasurer also serves as the Business Manager, purchasing agent, and financial software administrator. The District uses a financial software system to store its data and process financial transactions.

There are two schools in operation within the District, with approximately 1,600 students and 250 employees. The District's budgeted expenditures for the 2006-07 fiscal year were \$29.5 million, which were funded primarily with State aid, real property taxes, and grants.

Objective

The objective of our audit was to examine the District's internal controls over financial operations. Our audit addressed the following related questions:

- Are internal controls over cash receipts and disbursements appropriately designed and operating effectively to adequately safeguard District assets?
- Did District officials provide proper segregation of the duties assigned in the Business Office?
- Did District officials implement policies and procedures over information technology to adequately protect electronic data?

Scope and Methodology

We examined internal controls over financial operations of the Mattituck-Cutchogue Union Free School District 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 C of this report.

**Comments of District
Officials and Corrective
Action**

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they have initiated corrective action. OSC comments on the District's response can be found in Appendix B.

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*.

Cash Receipts and Disbursements

An effective system of internal controls over cash procedures includes the safeguarding of District assets, which include not only the cash received and used by the District, but also the disks that contain the signatures of the Treasurer and Deputy Treasurer and the paper stock used to print checks. Further, the entire process of preparing, signing, and issuing checks requires security precautions to prevent unauthorized access and protect against intentional or unintentional loss or manipulation. In addition, the Treasurer must ensure that his or her signature is not used to make payments that have not been approved.

We found that controls over cash receipts and disbursements were not operating effectively because District officials did not always follow Board-approved policies. The Treasurer and Deputy Treasurer did not have separate signature disks, as required by policy, and were therefore able to place each other's signatures on District checks. Additionally, even though District procedures required cash receipts to be logged daily, the accounts payable clerk did not enter 14 cash receipts totaling approximately \$8.7 million into the daily cash receipt log, and did not compare the log to bank deposits. Finally, 16 wire transfers totaling \$6.1 million were initiated and executed without proper authorization. As a result, District cash assets are not adequately protected and there is an increased risk that errors and irregularities could occur and go undetected.

Treasurer's Signature Disk

Education Law establishes the Treasurer as the custodian of all District moneys. As the District official responsible for signing the checks, the Treasurer plays a critical role in the cash disbursement process. It is essential that the Treasurer controls access to his or her signature disk and ensure that it is not used to make payments that have not been approved.

The Board-approved policy states that signature disks are required to be maintained and controlled by the individual whose signature is stored on the disk. The Board appointed a Treasurer (who is also the Business Manager) and Deputy Treasurer, in the Treasurer's absence, to be signatories on the District's checks.

We observed the District's cash disbursement operations and found that the two electronic signature disks each contained the signatures of both the Treasurer and the Deputy Treasurer. These disks were secured in a locked filing cabinet in the Purchasing Department. The

Treasurer and the Deputy Treasurer both had keys to the cabinet and unrestricted access to both disks.

To print checks, the Treasurer would insert his disk and could choose either his own or the Deputy Treasurer's signature. This was also the case with the Deputy Treasurer's disk. Due to this control weakness, we examined 10 claims totaling \$17,921 and tested them for inconsistencies in amounts or payees. We found no inconsistencies. However, when the signatures of the Treasurer and the Deputy Treasurer are interchangeable, District officials cannot be certain of which official issued the checks, and the District is at an increased risk of unauthorized disbursements.

When we brought this issue to the Treasurer's attention, District personnel created separate signature disks for the Treasurer and the Deputy Treasurer, who now retain custody of their own signature disk.

Cash Receipts

District officials are responsible for establishing internal controls over cash receipts and collections to ensure that all receipts are properly accounted for and deposited. Such controls include procedures requiring that all cash and checks be received at a central location and entered in a cash receipt log. After the deposits are made, a comparison of validated deposit tickets to the receipt log by someone independent of the cash processing function verifies that the deposits are accurate and complete. An independent comparison of the deposit slips prepared prior to deposit against the entries in the receipt log can serve as an additional control. We found that, although the District uses a cash receipt log, all cash receipts were not recorded in the log. Without comparing the deposits to the receipt log entries, District officials do not have assurance that all cash and checks are properly accounted for and deposited.

The District's procedure for cash receipts includes keeping a daily log of cash received, but does not require the reconciliation of deposit tickets to the receipt log. We compared 55 cash receipts transactions totaling \$14,532,447 in June 2007, as recorded on the bank statement, to the cash receipt log and found that 14 receipts totaling approximately \$8.7 million – comprising one check for \$8,581,820 from the Town Receiver of Taxes, and the balance from cafeteria cash receipts – were not entered into the log. The accounts payable clerk told us that she did not receive all checks for deposit and, therefore, did not enter all District receipts in the log; for example, the cafeteria cash was collected and deposited by a vendor who contracted with the District to operate the school lunch program. District officials told us that the accounts payable clerk did receive the check from the Town Receiver of Taxes, but they could not

provide the reason it was not entered in the receipt log. There was no indication that anyone compared the receipts entered in the log to the bank deposit tickets for accuracy before the deposits were made, or to the validated tickets after the deposits were made. Without effective controls over the District's cash, District officials do not have assurance that all cash receipts are accounted for, and the District is at an increased risk of its funds being lost or misappropriated.

Wire Transfers

Wire transfers provide a means of direct access to the moneys held in the District's name. Appropriate controls over wire transfer activity include policies and procedures that require management authorization of a transaction before the transaction is initiated; itemized documentation to support the purpose, source, destination and amount of the transaction; and documentation to appropriately account for and record the transaction. District officials are responsible for ensuring the segregation of duties involved in wire transfer activity or providing compensating controls. For example, if the individual who executes wire transfers also records them in the accounting system, an independent review of the ledger entry by a District official can verify the accuracy of the transfers and help prevent errors or the improper use of funds.

The District did not have procedures requiring the Treasurer to authorize wire transfers, and District officials did not provide compensating controls. We examined 24 wire transfers totaling \$6,325,280 made in June 2007 and determined that 16 transfers totaling \$6,145,324, primarily for the District's payroll, were made without prior authorization. Most of the transfers were executed by the payroll clerk, who also recorded the journal entries in the accounting system after making the transfers. However, the Treasurer did not approve the wire transfers before the payroll clerk executed and recorded them. The failure of the Treasurer or other official to authorize and review wire transfers, particularly when one employee can both initiate and record the transaction, increases the risk that an employee could execute and conceal improper wire transfers.

Recommendations

1. District officials should periodically review controls over signature disks to ensure that the District's policy is being followed.
2. District officials should ensure that all cash receipts are recorded in a centralized location, and that personnel maintain a log of each cash item received. The validated deposit ticket should be compared to the log, and agreement between the deposit ticket and log noted, by someone other than the individual maintaining the log.

3. The Treasurer or other official should review and approve all wire transfers and corresponding journal entries before the transfers are executed and recorded in the accounting system.

Segregation of Duties in the Business Office

District officials are responsible for establishing internal controls to ensure that no one individual handles all or most aspects of a financial transaction. Such controls include policies and procedures that require, at minimum, the segregation of the key duties of transaction authorization, recordkeeping, cash custody, and disbursement. Effective controls provide for the work of one employee to be routinely verified in the course of another's regular duties. When segregation of duties is not feasible, compensating controls can minimize the risk that errors or irregularities might occur without being detected. For example, District officials can institute management reviews to ensure that the same individual does not perform conflicting duties without some form of oversight.

The duties involved in the District's human resources function include adding and deleting employee data, making changes to salary rates, and maintaining confidential employee records. The payroll function includes the calculation of payroll checks based on time records and employee information entered into the system, as well as the printing and distribution of payroll checks. All these functions were handled by the payroll clerk with no indication of management oversight. The Board also designated this individual as Deputy Treasurer, who can sign payroll checks in the Treasurer's absence. These diverse capabilities could conceivably allow the payroll clerk to perform unauthorized or improper activities – for example, adding new employees to the system and making payments to them – without detection. Although our testing of six cash disbursements totaling \$66,741 (for termination pay, medical insurance reimbursements, and compensatory time) did not identify any exceptions related to these overlapping duties, the lack of separation between key human resources and payroll processes places the District at an increased risk of errors or irregularities occurring without being detected by District officials.

Our audit also found that the Business Manager had multiple other responsibilities as the District's appointed Treasurer, purchasing agent, and financial systems administrator. Because these combined roles involve performing incompatible duties, this individual could conceivably initiate and conceal the improper use of District moneys. For example, the dual roles of Treasurer and purchasing agent would enable him to create a vendor in the system, approve a purchase order or contract, authorize payment, and disburse signed checks for goods or services that may not be appropriate or necessary for the District. Our audit found no indication of compensating controls. Additionally,

as financial system administrator, this individual could set user access rights to any modules of the financial system, and had the ability to override financial system controls. Our testing of 10 cash disbursements totaling \$17,921¹ did not identify any unauthorized transactions. However, the ability for the same individual to receive District moneys, initiate and approve purchases, make entries in the accounting system, and disburse payments leaves the District at risk of errors, irregularities, or fraud occurring and not being detected. Additionally, the failure to segregate the duties of financial system administration from the District's computerized financial activities places the District at an increased risk that its financial information could be inappropriately modified or misused.

Recommendations

4. District officials should realign the role of the payroll clerk to ensure that incompatible duties are not performed by the same individual. At a minimum, the same individual should not change employees' payroll data, calculate pay amounts, and disburse signed paychecks. If complete segregation of duties is not feasible, District officials should institute compensating controls such as periodic administrative oversight.
5. The responsibilities of the Business Manager should be realigned to ensure an adequate segregation of duties. The same individual should not initiate and approve purchases, update accounting records, disburse payments, and control access rights to the financial system.

¹ These were the same disbursements referenced in "Treasurer's Signature Disk" under Cash Receipts and Disbursements. These disbursements included \$4,911 for therapy services, \$2,734 for gasoline, and \$1,571 for office supplies.

Information Technology

Computer systems and data are a valuable resource that District officials rely on for initiating, processing, and recording the District's financial transactions, filing reports with State and Federal agencies, and making sound financial decisions in the best interests of the District. If the computers on which this data is stored fail, the problems that result could range from inconvenient to severe. Even small disruptions in electronic data systems can require extensive effort to evaluate and repair.

District officials are responsible for establishing and implementing internal controls, including policies and procedures, to provide reasonable assurance that assets and resources are adequately safeguarded against waste, loss, and misuse. Such procedures must require that access to computer data systems is controlled and monitored to reduce the risk of misuse or alteration of data which can cause financial loss to the District. Additionally, a formal disaster recovery plan is necessary to guide employees in preventing the loss of computer data, and in recovering the data and restoring computer operations in the event of a disaster.

District officials did not adopt comprehensive information technology (IT) policies and procedures. Specifically, there were no procedures for monitoring and controlling remote access to financial data, and employees had access to parts of the financial system not necessary for their jobs. Because the District did not require complex and frequently changed passwords, employees had not changed their network passwords in two years. The District did not store its backup data off-site or test its validity, and did not have a formal disaster recovery plan. Finally, the individual serving as financial system administrator also held key responsibilities for financial transactions. As a result of these control weaknesses, the District's IT system and electronic data are subject to an increased risk of unauthorized access that can cause its loss or misuse.

Remote Access

An important component of internal controls ensures that remote access (i.e., the ability to access the computer through the Internet or other external means) is controlled and monitored so that only authorized individuals may enter or retrieve data. Sound internal controls include policies and procedures addressing how and to whom remote access is granted, security issues, and monitoring and control.

District officials did not implement procedures to appropriately restrict, monitor, and control remote access. The District granted remote access to the Superintendent, the Business Manager (including access to financial data for his duties as Treasurer and purchasing agent), the Director of Special Education, the two school principals, the technical coordinator, and the technician. The remote access provided to these individuals enabled them to access only those system functions to which they already had on-site access rights; however, the ability to do so from a remote location increases the risk of unauthorized individuals gaining access to the financial system outside the District environment. Although we found no evidence of inappropriate access from a remote location, the failure to implement policies and procedures for remote access could result in financial data being manipulated, lost, or misused without timely detection.

User Access Rights

A key internal control over a district's computer system is the assignment of user access rights that preserve a segregation of duties within the computerized environment. Effective controls over user access rights restrict access to only those areas of the system necessary for employees to perform their jobs. An individual who has financial system administrative rights can add new users, create and change users' access rights, configure certain system settings, and override management controls. Accordingly, the financial system administrator should not be involved in the District's financial operations.

District officials did not develop policies and procedures to ensure that system access rights provide an adequate segregation of duties within the computerized environment. The District's two accounting clerks had access to areas of the system unrelated to their jobs, which District personnel explained was due to the small size of the administrative office staff and the need for the clerks to serve as backup for each other. However, there were no compensating controls such as periodic management oversight. Additionally (as noted under Segregation of Duties), the Business Manager – who held significant financial responsibility in the roles of Treasurer and purchasing agent – served as the District's financial system administrator, with unlimited access to the system. Having the ability to override system controls and set his own access rights to all modules of the financial system, this individual could conceivably circumvent required approvals and modify appropriated payments to vendors or employees. Although we found no evidence of impropriety, user rights that are not properly assigned and independently maintained increase the risk of unauthorized access to the District's IT system and improper use of its financial data.

Passwords

Unique passwords serve to authenticate users' access to the District's computer system, and are a basic control for reducing the risk of unauthorized user access that can result in the loss or misuse of the District's data. Password complexity and the frequent changing of passwords are essential controls that help defeat attempts at unauthorized access. Complex passwords contain combinations of upper- and lowercase letters, numbers, and punctuation, are at least eight characters long, and are not commonly used or easily guessed. The frequent and regular changing of passwords reduces opportunities for unauthorized access.

The District's use of the computerized financial program was restricted to the administrative staff, whose passwords had to change every 30 days. However, there were no policies or procedures for password security; students and teachers were not required to change their network passwords and generally had not done so in two years. The District also did not specify complexity requirements for user passwords. Because of the inadequate controls over password security, the District's employee and student user accounts are vulnerable to unauthorized use that can result in the modification, loss, or improper disclosure of valuable data.

Storage and Testing of Backup Data

The District's ability to restore computer data relies on the integrity of its backup data. To help ensure its availability, the backup data must be stored at an off-site location and test-restored on a routine basis to verify that it can be used successfully to back up District systems should the need arise.

We found that the District's backup data was not stored at an off-site location geographically located outside the school district, but instead was stored in a different building within the district on campus each week. With no off-site storage, the backup data is vulnerable to the same disaster risks as its campus-based network, and the District could lose the backups if all District facilities were rendered inoperable. District officials also did not verify the validity of the backup data through periodic testing of the data restoration process. The failure to store backups off-campus and to periodically test-restore the backup data increases the risk that the District's backup data could be unavailable or unusable in the event that District systems or data were damaged.

Disaster Recovery Plan

A disaster recovery plan, sometimes called a business continuity plan, specifies how an organization should deal with a disaster such as a power outage, hardware failure, fire, flood, computer virus, or damage that could be caused by accidental or deliberate actions of users. Through contingency planning and appropriate precautions to protect its IT system and data, the District can avert or minimize

potential damage and maintain or quickly resume critical operations in the event of a disruption.

The District did not establish formal policies or procedures to address potential disasters. As a result, in the event of a computer failure, District personnel have no guidelines or plan to prevent the loss of equipment and data or to recover data that has been lost or damaged, and the District is at an increased risk of incurring costly disruption to its business operations.

Recommendations

6. District officials should implement procedures for granting remote access and user rights to the system based on an individual's position, level of responsibility, and other factors as appropriate. When it is not feasible to completely segregate an individual's duties on the computerized financial system, District officials should provide periodic oversight as a compensating control.
7. District officials should assign the duties of the financial system administrator to an individual who is not involved in the District's financial transactions.
8. District officials should require all District personnel who access the financial system to use passwords that are complex and periodically changed.
9. District officials should store the District's backup data in a location outside the geographic boundaries of the District's campus, and periodically test the validity of the backup data.
10. District officials should adopt a comprehensive disaster recovery plan.

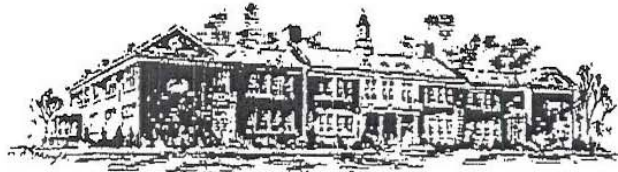
APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

JAMES F. McKENNA
Superintendent of Schools

TRICIA DESIDERIO
Director of Special Education



MICHAEL ENGELHARI
Business Manager

MATTITUCK-CUTCHOGUE U.F.S.D.
CENTRAL ADMINISTRATIVE OFFICES

July 28, 2008

[REDACTED]
Office of the State Comptroller
110 State Street
Albany NY 12236

RE: Written response to draft audit report
Mattituck-Cutchogue UFSD

Dear [REDACTED]:

I will comment on each section of the draft audit report in the order they appear.

EXECUTIVE SUMMARY

Scope and Objective

No Comments

Audit Results

The opening paragraph states that proper internal controls were not in place, policies were not adopted, and District officials were not implementing the policies that were in place. This paragraph is based on the fact that the Treasurer and Deputy Treasurer did not have separate signature disks and that 14 cash receipts were not recorded in a daily log notebook that one of the account clerks kept. The last item supporting this statement was that 16 wire transfers were done without proper authorization.

The signature disks did have both signatures on. This was corrected immediately with the auditors as witness. Thirteen of the fourteen cash receipts that were not recorded in the log were from school lunch deposits that the school lunch contractor deposits on a daily basis and turns in the deposit slips and associated reports on a weekly basis. The log is only for items that are mailed or delivered to the business office and deposited by the business office. The one deposit that was not logged in was an oversight, but was deposited in the bank timely and recorded in the financial software properly. The wire transfers were verbally approved in advance and followed up with written confirmation from the bank. The only thing missing was prior written authorization that is now being done on each wire transfer.

See
Note 1
Page 23

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The Board of Education does have a complete set of policies that were being approved as the audit was taking place. This policy project is now complete.

To say that proper internal controls were not in place, policies not adopted, and District officials were not implementing the policies that were in place based on the few minor exceptions noted above, seems overly harsh. A few exceptions noted would be more accurate.

See
Note 2
Page 23

The question on segregation of duties in a small District is not an easy one. Some of the employees in the business office wear many hats out of necessity. The payroll clerk is closely monitored by the Business Manager and each payroll is certified by the Superintendent. The Business Manager is closely monitored by the internal claims auditor on a weekly basis, the internal auditor several times per fiscal year, and the external auditors every couple of months. The Superintendent does work with and oversees the Business Manager on a regular basis. To say there is a total lack of controls on these two individuals seems overly critical:

See
Note 3
Page 23

Comprehensive IT controls and disaster recovery were not in place during the audit but are in the process of being put in place during this fiscal year.

Introduction

No comments on this section

Cash Receipts and Disbursements

Treasurer's Signature Disk

Treasurer's signature disk was discussed above and in this section it is noted it was corrected.

Cash Receipts

The process of cash receipts and the log was reviewed with the auditors while they were in the District and a new procedure was developed and has been used since. The handwritten log has been replaced by an electronic log that is compared to the deposit tickets from the bank.

Wire Transfers

The treasurer did verbally authorize wire transfers and received directly from the bank e-mail confirmation as soon as the transaction was complete. This went to the treasurer's e-mail account that could only be accessed by the treasurer and this is kept as a record by the treasurer before this wire transfer was entered in the financial system. A new form for prior written authorization has been in place since the audit and is always done before the wire transfer.

Segregation of duties in the Business Office

This was discussed above and while the size of the District creates this issue, there is oversight from claims auditors, internal auditors, and external auditors. The Business Manager does closely monitor the payroll clerk and the Superintendent does oversee the Business Manager.

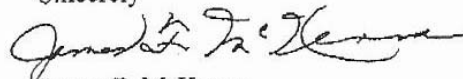
See Note 3 Page 23

Information Technology

No comments.

In closing, the Mattituck-Cutchogue UFSD intends to make all suggested corrections and appreciates the professional manner your auditors displayed during this audit. We appreciate any suggestions that help us maintain sound fiscal operations within the District. Please consider these comments during the process of writing the final report.

Sincerely



James F. McKenna
Superintendent

APPENDIX B

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

We commend the District for depositing the check in a timely manner and properly recording the information in the financial software. However, as mentioned in our report, this check was for a significant amount (\$8.6 million) and should have been recorded in the cash receipt log. Therefore, there was no indication that anyone compared the receipts entered in the log to the bank deposit tickets for accuracy before the deposits were made.

Note 2

The report has been revised.

Note 3

Our audit found no indication of compensating controls, such as management oversight, over the incompatible duties performed by the payroll clerk or by the Business Manager. We have modified the report for clarity.

APPENDIX C

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 cash receipts and disbursements and information technology for further audit testing. Additionally, based on our discussions with District officials during our planning process, we became aware of certain weaknesses in controls over the segregation of duties in the Business Office, which we also addressed in this report.

Our examination included the following:

- We observed operations and examined records to verify that receipts, disbursements, and cash transfers were made by authorized personnel.
- We traced receipts to the cash receipt log, deposit slips, and bank statements to verify that all cash was deposited.
- We reviewed wire transfers to determine that transactions were approved.
- We verified that signature plates, prepared checks, and blank checks were physically secured.
- We verified that proper segregation of duties existed for approving transactions, recording those transactions, and having custody of (access to) the resultant assets for each scope area audited.
- We reviewed timecards, payroll journals, leave time records, and collective bargaining agreements for selected employees.
- We examined internal controls over information technology.

- We interviewed District personnel and evaluated the internal controls and safeguards over computer-generated data.

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

APPENDIX D

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