



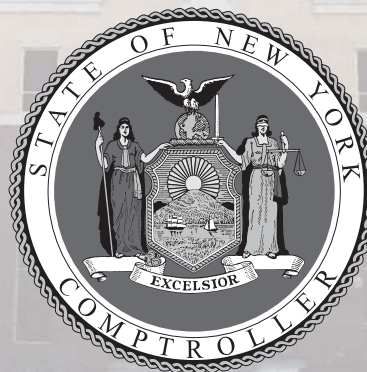
# North Warren Central School District Internal Controls Over Financial Operations

Report of Examination

Period Covered:

July 1, 2006 — August 10, 2007

2008M-82



Thomas P. DiNapoli

# Table of Contents

	<b>Page</b>
<b>AUTHORITY LETTER</b>	3
<b>EXECUTIVE SUMMARY</b>	5
<b>INTRODUCTION</b>	7
Background	7
Objective	7
Scope and Methodology	8
Comments of District Officials and Corrective Action	8
<b>CASH RECEIPTS AND DISBURSEMENTS</b>	9
Policies and Procedures	9
Segregation of Duties	10
Default Vendor Code	11
Recommendations	12
<b>EXTRA-CLASSROOM ACTIVITIES</b>	13
Recommendations	15
<b>CLAIMS AUDITING</b>	16
Recommendations	17
<b>INFORMATION TECHNOLOGY</b>	18
Policies and Procedures	19
Access Controls	19
Recommendations	21
<b>APPENDIX A</b> Response From District Officials	22
<b>APPENDIX B</b> OSC Comments on the District’s Response	27
<b>APPENDIX C</b> Audit Methodology and Standards	28
<b>APPENDIX D</b> How to Obtain Additional Copies of the Report	30
<b>APPENDIX E</b> Local Regional Office Listing	31

# State of New York Office of the State Comptroller

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

July 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 North Warren Central School District, entitled Internal Controls Over Financial Operations. 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

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# EXECUTIVE SUMMARY

The North Warren Central School District (District) is governed by the Board of Education (Board) which comprises seven elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the chief executive officer of the District and is responsible, along with other administrative staff, for the day-to-day management of the District under the direction of the Board.

### **Scope and Objective**

The objective of our audit was to assess internal controls over financial operations at the District for the period July 1, 2006 to August 10, 2007. Our audit addressed the following related questions:

- Are internal controls over cash receipts and disbursements appropriately designed and operating effectively to protect District assets?
- Are internal controls over extra-classroom activity funds adequate?
- Are internal controls over the claims auditing process appropriately designed and operating effectively?
- Are internal controls over the District's information technology appropriately designed to protect electronic data?

### **Audit Results**

We found weaknesses in several of the District's financial operations, generally caused by the Board's failure to adopt adequate policies and procedures, or, in the case of the extra-classroom activity fund, the failure to follow the adopted policy. For example, the District's policies and procedures for cash receipts and disbursements did not provide sufficient guidance to the employees involved in those processes and did not establish adequate segregation of duties. As a result, Business Office staff developed their own procedures making the District vulnerable to the possibility of errors and/or irregularities occurring and not being detected in a timely manner. We noted, for example, that certain manually processed checks were written in payment of claims that had not been audited and approved by the claims auditor and that the District did not use pre-numbered duplicate receipts and did not always deposit receipts in a timely manner.

The Board did not appoint a central treasurer to oversee the extra-classroom activity funds as required by the District's own policy. Extra-classroom deposits were not recorded in a timely manner and disbursements were not supported by adequate documentation. Additionally, the District was unable to provide all the club records we requested.

The policies and procedures guiding the claims auditing process were inadequate and, as a result, the District did not perform an effective audit of claims. The claims auditor was not properly instructed on the basic rules and requirements for performing an adequate audit and processing of claims for payment. An inadequate claims process also allowed the Treasurer to make payments on claims that were not submitted to the claims auditor for review and approval.

The District's information technology (IT) policies were outdated and inadequate. We found that the controls governing the District's computer system user rights had not been adequately established and certain network password controls were disabled. The Board had not established a formal disaster recovery plan, nor were there formal procedures for backing up and storing data. We identified other areas in need of improvement concerning certain IT controls. Due to the sensitivity of some of the information, specific vulnerabilities are not discussed in this report but have been communicated separately to District officials so they can take corrective action.

### **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 planned to initiate corrective action. Appendix B includes our comments on the issues raised in the District's response letter.

# Introduction

## Background

The North Warren Central School District (District) is located in the Town(s) of Chester, Hague, Horicon, Johnsburg, Thurman, and Warrensburg in Warren County; and Minerva and Schroon in Essex 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 Board appointed a Treasurer who also functions as Business Manager. A separate person was appointed as the claims auditor.

There is one school in operation within the District, with approximately 580 students and 140 employees. The District's budgeted expenditures for the 2006-07 fiscal year were \$11.6 million, which was funded primarily with State aid, sales tax, real property taxes, and grants. The District has a significant investment in its information technology resources, having expended about \$260,000 for technology products and services in 2006-07.

The District maintained an extra-classroom activity fund for 24 student clubs that had combined receipts of \$105,492 and combined disbursements of \$93,445 in 2006-07.

## Objective

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

- Are internal controls over cash receipts and disbursements appropriately designed and operating effectively to protect District assets?
- Are internal controls over the District's extra-classroom activity funds adequate?
- Are internal controls over the claims auditing process appropriately designed and operating effectively?
- Are internal controls over the District's information technology appropriately designed to protect electronic data?

**Scope and  
Methodology**

During this audit, we examined the District’s control environment and its internal controls over cash receipts and disbursements, extra-classroom activity funds, the claims audit process and information technology for the period July 1, 2006 to August 10, 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 planned to initiate corrective action. Appendix B includes our comments on the issues raised in the District’s response letter.

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

District officials are responsible for designing internal controls that help safeguard the District's resources and ensure these resources are used economically and efficiently. An adequate system of internal controls over cash receipts and disbursements includes clear policies and procedures that promote effective operations, the prudent use of resources and adherence to applicable laws and regulations. Control procedures should also provide for segregating critical duties, so that no one person controls all phases of a transaction. Written policies and procedures combined with job descriptions identifying responsibilities for specific activities help ensure that employees understand expectations and their personal role in the process. District managers must establish policies and distribute them to the appropriate employees.

The District did not establish policies and procedures over cash receipts and disbursements and did not establish a formal segregation of duties. The lack of specific guidance over the handling of cash increases the risk that key internal control activities may not be performed as expected. The absence of policies and procedures resulted in the cash receipts not being deposited and recorded in a timely manner and cash disbursements being made by the Treasurer prior to approval by the claims auditor. We also noted the lack of controls over the use of vendor accounts used to make payments.

### **Policies and Procedures**

Cash receipt and disbursement policies and procedures should contain specific guidance and information for District employees responsible for handling and accounting for cash. Effective policies should adequately address issues such as:

- The assignment of responsibility for collecting and recording cash payments made to the District in person or by mail;
- Ensuring that someone other than the person receiving and recording cash collections be responsible for reconciling bank accounts or preparing and making bank deposits;
- A provision for the timely deposit of District moneys; and
- Guidance as to the proper forms of disbursements for specific transactions, such as procedures for utilizing manual checks or electronic transfers.

The District had not established written policies governing cash receipts and disbursements or formal procedures to ensure the proper authorization and timeliness of transactions. The absence of such policies and procedures increases the likelihood that errors and irregularities could occur and go undetected and uncorrected.

## Segregation of Duties

An effective system of internal controls over cash receipts and disbursements requires the division of responsibilities such that no one individual performs incompatible duties and that the work of one employee is independently verified in the course of another employee's regular duties. While it may not always be possible to achieve an optimal segregation of duties, at a minimum, the duties of record keeping, bank reconciliation and cash disbursements should be separated.

Although the Board had established separate job descriptions for the Treasurer and Business Manager positions, one person performed the duties listed under both titles. The District employed an account clerk but did not have a written job description for that position. Because of the lack of any formal segregation of duties within the Business Office, Business Office staff developed their own informal procedures, which resulted in them performing certain incompatible duties. For example, the employee functioning as both the Treasurer and Business Manager often performed the same tasks as the account clerk including opening the mail, recording and depositing cash, and preparing journal entries. These duties are incompatible with the Treasurer's responsibility of reconciling bank statements. The lack of any significant segregation of duties related to the handling of cash receipts and disbursements significantly increases the risk that errors, irregularities, abuse, or even fraud could occur and not be detected in a timely manner. As a result of this weakness and the lack of policies and procedures, we examined both cash receipts and disbursement transactions.

Cash Receipts – A good system of internal controls over cash receipts provides for timely supervision of those charged with handling monies, as well as the issuance of duplicate press-numbered receipts in sequence for all cash collections. Additionally, good business practice requires cash and checks to be deposited daily or as quickly as possible to prevent the loss or misuse of cash.

The District did not use duplicate press-numbered receipts when collecting cash. The Business Office issued single press-numbered receipts to the payer and entered the receipt information manually into the cash receipts ledger. On a monthly basis the Treasurer posts the information to the computer accounting system. We traced 57 manually recorded cash receipts totaling \$576,672 to the computer

records and bank deposits to determine if they were deposited intact and on a timely basis and found that all were deposited intact although not always in a timely manner. We identified 26 receipts totaling \$29,782 that were held 7 or more days before being deposited. Nine of these receipts totaling over \$26,000 were not deposited for at least 12 days. Delay in depositing and recording cash receipts makes cash more susceptible to theft or loss.

Cash Disbursements – An effective control over cash disbursements provides that one person is unable to disburse or transfer cash without oversight from someone independent of the process. The District maintained two separate check stocks for the general, cafeteria, and trust and agency funds. One was pre-printed and was used for electronically processed and printed checks; the other was blank stock used for manually processed checks. The District manually processed 122 checks totaling \$31,841 out of the general and trust and agency funds during the 2006-07 fiscal year. We determined that none of these payments had been reviewed and approved by the claims auditor at any point in the process. None of the payments was of the type that could be paid prior to audit, such as freight charges, postage, debt service or utilities. We reviewed 16 manually processed checks totaling \$8,214 and determined that all the payments were for District-related purposes. However, when manual checks can be written without proper audit and approval it creates a potential for errors, abuse, professional misconduct, and even fraud occurring without being detected in a timely manner.

We also tested 55 cash transfers to determine if they were made to the proper District accounts in the proper amount and had adequate supporting documentation. They included transfers between bank accounts as well as wire transfers. The District did not have specific payroll documents for 10 of the 55 transfers we tested; however, we were able to trace them to other District accounts. According to the Treasurer, these 10 transfers were related to payroll transactions. However, she did not provide any documentation or further explanation supporting the purpose of the transactions, which ranged from \$450 to \$150,000. Although we did not identify any significant discrepancies while conducting our tests, the ability of the Treasurer to make bank transfers without adequate oversight and the failure to maintain documentation for all such transfers is a serious weakness. The lack of controls over both check writing and bank transfers increases the risk that cash can be disbursed for unauthorized purposes or amounts, or could occur without being recorded.

**Default Vendor Code**

Providing each vendor with an individual vendor number is an important part of an internal control system. Although Business Office staff assign a unique vendor number to the majority of

vendors doing regular business with the District, those that are classified as “one time” vendors are assigned the default vendor number of 9999.

This default code is normally expected to be used for inter-fund transfers and does not appear on the Vendor Master File. During our audit period, 146 checks totaling \$31,595 were written under the 9999 number. We tested 16 claims paid under the default vendor account and found all were for legitimate District purposes; however, we noted four claims that were paid to vendors who had previously been assigned their own unique vendor numbers and six claims were paid to vendors who were not one time vendors.

Paying vendors and employees using the default vendor code instead of using an individually assigned vendor number increases the risk that a fictitious vendor could be created, and that fraudulent activity could occur and go undetected.

The absence of adequate policies and procedures for cash receipts and disbursements increases the risk that key internal control activities may not be performed as expected and also increases the likelihood that errors and irregularities could occur and go undetected and uncorrected.

## **Recommendations**

1. District officials should establish cash receipt and disbursement policies that address the proper segregation of duties for each process.
2. Cash receipts should be deposited and recorded in a timely manner.
3. District officials should adopt procedures for the cash disbursement process including the use of check stock, the use of vendor accounts, the documentation of transactions, and the organization and retention of supporting documentation.

## Extra-Classroom Activities

Extra-classroom activity funds are raised through charges for, by, or in the name of organizations whose activities are conducted by students. Students raise and spend these funds to promote the general welfare, education, and morale of all students, and to finance the normal and appropriate extra-curricular activities of the student body. According to the District's records, the extra-classroom activity fund recorded \$105,492 in receipts and \$99,445 in disbursements and had a combined cash balance of approximately \$55,515 as of June 30, 2007.

The Regulations of the Commissioner of Education (Regulations) require each school district's Board of Education to make rules and regulations for the safeguarding, accounting, and auditing of all extra-classroom activities moneys received and disbursed. Boards also need to provide guidance for the conduct and operation of student activities, and outline the duties and responsibilities of the District employees who oversee the activities. The Regulations also require the Board to appoint a central treasurer to be responsible for the accounting of transactions for each individual student activity, depositing receipts, preparing checks for disbursements, and making regular financial reports to the Board on at least a quarterly basis. Having a good system of internal controls over these funds helps minimize the risk that errors or irregularities may occur and go undetected.

Although the Board had established a policy governing the operations of its extra-classroom activities, procedures to be followed in running the activity funds were not established or communicated to the faculty advisors and students. The Board had not appointed a central treasurer as required, resulting in an account clerk assuming those responsibilities without receiving adequate guidance. The lack of guidance resulted in transactions that were not documented and recorded in a timely manner and no reconciliation of the records maintained by the account clerk to the individual activity club records. The Board did not regularly receive extra-classroom activity fund reports, which are required to be submitted at least quarterly. District officials were unable to provide all the records we requested. As a result, the Board had no assurance that extra-classroom moneys were being properly accounted for in compliance with policy and good business practice.

Generally, activity club treasurers should turn over any moneys received to a central treasurer for deposit after recording the receipts

in the clubs' books. The central treasurers should issue receipts to the clubs, deposit the money in the bank, and maintain records of all receipts that should be periodically reconciled to the clubs' records. We found that students and faculty advisors deposited moneys received from their various activities directly into the District's extra-classroom activity fund bank account, later submitting the deposit receipts to the account clerk who functioned as the central treasurer. The account clerk was not always made aware of which clubs had made a deposit and at times was unable to properly record deposited moneys in a timely manner.

District officials could not provide all the supporting documentation we requested. One club, that reportedly received \$13,760 during the 2005-06 fiscal year, had no records at all. We reviewed 13 receipts totaling \$18,178 from four clubs and found that the records of receipts consisted of the bank deposit receipts given to the account clerk. The sources of cash received were not always adequately identified and accounted for in the clubs' records and due to a lack of adequate documentation, it was impossible to verify that all activity fund moneys received were deposited intact and in a timely manner.

To disburse moneys, student treasurers should first submit approved disbursement requests to the central treasurer. The requests should include an itemization of the planned expenditures, vendor documentation, and approval from an activity advisor. Upon review and approval of the disbursement requests, the central treasurer will subsequently prepare and sign checks made out to the appropriate vendors. The central treasurer should retain back-up documentation for each disbursement and the club treasurer should record all disbursements while also retaining copies of the supporting documentation.

We attempted to review a sample of disbursements to determine if they had proper supporting documentation and followed the proper approval process. District officials could not provide disbursement records for one club, which, according to the financial statements, disbursed about \$12,054 during the 2005-06 school year. We examined 17 disbursements of four other clubs totaling \$15,808 and found 10 of 17 disbursements totaling \$14,200 that were not supported by invoices, and one disbursement of \$119 that was supported only with some hand-written notes. The account clerk had not received guidance in the procedures to be followed for disbursing extra-classroom funds and processed checks for the noted transactions even though there was no supporting documentation. Due to the inadequacies of the documentation, it was impossible to determine if all disbursements were appropriate.

In practice, the account clerk issued monthly trial balances to the clubs and depended on the clubs to contact her in the event of discrepancies. The Board policy required the club treasurers to balance the clubs' books and reconcile them monthly; however, we found that this did not always occur. We tested the records by comparing the year-end cash balances of the account clerk's records with individual activity club records and found discrepancies in three of the four clubs examined.

The Board and appropriate District officials need to take steps to provide a better accounting for activity fund moneys and to comply with the Commissioner's Regulations. The failure to provide adequate oversight of activity fund operations and ensure that the activities are managed in accordance with the Commissioner's Regulations and good business practices increases the risk that fraud, abuse, errors and irregularities can occur and remain undetected.

### **Recommendations**

4. District officials should provide the oversight required to ensure that all extra-classroom activity moneys are properly documented and accounted for, safeguarded, and used as intended and that policies are followed.
5. The Board should appoint a central treasurer to be responsible for maintaining the extra-classroom activity fund checks, recording receipts, depositing money, and preparing monthly bank reconciliations, and reporting to the Board on at least a quarterly basis.

## Claims Auditing

The audit and approval of claims are critical elements of the District's internal control system over cash disbursements. Education Law requires school boards to audit claims against district funds before they are paid, or to appoint a claims auditor to assume the board's powers and duties to approve or disapprove claims. An independent claims audit can detect management abuses or improprieties, and ensures that funds are expended for authorized purposes and in accordance with board policies. This control is especially important when other internal control deficiencies exist, such as limited segregation in the Business Office related to the handling of cash disbursements. To maintain adequate independence, the claims auditor should report directly to the Board. Education Law prohibits district treasurers from paying claims without written authorization from either the clerk of the board or the claims auditor. This authorization is usually documented by a certified warrant attesting that the claims have been audited and approved for payment.

Although the Board appointed a claims auditor to examine and approve all claims, it did not provide guidance on its expectations for the claims auditor. District procedures called for the claims auditor to report to the Business Manager/Treasurer which negated the effectiveness of an independent audit of claims. The claims auditor informed us that she had not reported directly to the Board since her original appointment in August 2006. We found the District did not have an effective claims audit process in place, resulting in the approval of claims that lacked necessary documentation and instances where the Treasurer made payments that were not reviewed and approved by the claims auditor.

We reviewed 70 claims vouchers totaling \$145,569 that were approved by the claims auditor and determined that all were for District-related purposes. However, we noted two instances where invoices were paid twice, resulting in \$570 in overpayments. Nine out of 51 claim vouchers requiring a purchase requisition did not have one, and three claims lacked supporting invoices. We noted that purchase orders were signed by the Treasurer rather than the purchasing agent. As noted previously, we also found that the Treasurer made 122 payments during our audit period totaling \$31,841 without the knowledge and approval of the claims auditor. We attribute many of these deficiencies to the lack of direction given to the claims auditor about her specific audit responsibilities. The policy for the claims auditor position was inadequate and

the claims auditor did not receive a job description. The Business Manager indicated that manual disbursements were not provided to the claims auditor for review. Uncertainty and the lack of clear direction regarding the duties and responsibilities of those involved in the processing of claims for payment significantly increases the risk of improper payments being made and not detected in a timely manner.

## **Recommendations**

6. The Board should adopt a policy that clearly defines the duties of the claims auditor and requires that she prepare periodic reports and report directly to the Board.
7. The Board should develop and implement an adequate policy governing the claims audit process making sure that the claims auditor is fully aware of her responsibilities.

## Information Technology

The District uses information technology (IT) to initiate, process, record, and report transactions. It also relies on its IT system for computer education, Internet access, electronic mail (email), processing and storing student data, and maintaining financial records. The pervasive use and complexity of these computerized applications produces internal control risks such as unauthorized access to data, unauthorized changes to master files, and the potential loss of data.

The District can mitigate these risks through a combination of automated and manual controls including policies and procedures adopted by the Board, and limiting user access to protect data from loss by intentional or unintentional manipulation. The system of internal controls should include a disaster recovery plan and systematic backup procedures to restore lost or damaged data as quickly as possible. Disasters include sudden, unplanned catastrophic events (e.g., fires, computer viruses, or inadvertent employee actions) that compromise the integrity and data of the IT system.

During the audit period, the District had a technology network accessible to administrators, teachers, other staff members, and students. The network included firewall components, servers, switches, printers, wiring closets, wireless network access points, and various business and education software packages. The network was deployed throughout the school building in offices, classrooms, the library, and computer labs.

The District invested heavily in the human and technical resources of its IT system. For example, during the 2006-07 fiscal year the District expended more than \$260,000 for IT related products and services, including outside consulting. Additionally, the District employed a full-time Network and Technology Services Specialist and a part-time Technology Coordinator.

We found that District officials had not established adequate control policies and procedures to safeguard the District's IT system equipment and data. The IT system, including financial information and other sensitive data stored on it, is a critical resource that should be adequately protected from loss, damage, and destruction. Specific areas where internal controls need to be strengthened include policies and procedures, access controls, physical security, data backups, and disaster recovery.

## **Policies and Procedures**

District officials are responsible for establishing policies and procedures to provide guidance for District employees on all aspects of IT used at the District. Such policies should include, but not be limited to, acceptable-use standards for computers, the Internet and email, data safeguards, anti-virus protection, password security, remote access controls, physical access controls, data backup systems, and disaster recovery.

The Board's limited IT policies do not provide adequate overall controls over the District's technology systems. For example, the District's acceptable use policy for staff does not address use of web-based email, downloading and installing programs, and instant messaging. Further, the policy requires employees to report security problems to their supervisors without specific definitions of security problems. The acceptable use policy for staff had not been updated since 2001, while the acceptable use policy for students had not been updated since 2004. District officials agreed that the IT policies are outdated and are working to address them.

## **Access Controls**

Access controls should provide reasonable assurance that computer resources are protected from unauthorized modifications. To control electronic access, a computer system or application needs a process in place to identify and differentiate among users. User accounts identify users and establish relationships between a user and a network, computer, or application. These accounts are created by the system administrator and contain information about the users, such as passwords and access rights to files, applications, directories and other computer resources. Access controls include establishing adequate passwords, limiting administrator accounts, and restricting users to only the applications that are necessary for their day-to-day operations.

Passwords – Passwords are one of the most basic controls that can be utilized to mitigate the risk of unauthorized users obtaining access to the District's computer systems. The more complex a password, the better the chances are that unauthorized users will be prevented from obtaining access to the system. Complexity includes, for example, requiring a combination of upper and lower case letters, numbers, and a significant number of characters. Passwords should not be simple words or names and it is also important to require that they be changed on a regular basis, usually every 30 to 90 days. Doing so significantly increases the District's protection in preventing unauthorized users from accessing sensitive information. Under no circumstances should passwords be written down and accessible to others as this would compromise all the other associated controls.

The District's password controls were inadequate. Passwords were required to be only four characters long and could be used up to 211 days. Network features that require password complexity and provide for storage of passwords in an encrypted format were disabled.

User Rights Controls – Administrative rights give users complete access to create, delete, and modify files, folders, or settings on a computer, in addition to installing or downloading software. A user with administrative rights could download or install software that may contain a virus or some other threat to the network, may not be compatible with the District's operating system, may take up too much space on the network, or may not even have a job related purpose. Furthermore, if users with administrative rights accessed a compromised website, malicious programs could be unknowingly introduced to the user's computer and the District's network. Therefore, it is important to ensure that general users are not given administrative rights and are only given the minimum access needed to complete their job duties in order to better protect the District.

We found that the controls governing the District's computer system user rights had not been adequately established. All employees with user rights at the District also had local administrative rights putting the District's network at an increased risk.

Physical Security – Maintaining adequate security over District IT systems helps to ensure that they are protected from loss and used effectively for their intended purpose. District officials can establish security over IT systems and equipment by controlling access to servers and by physically securing servers. However, the District did not establish policies and procedures for physically securing these important assets. We found the server room was not always physically secured. We viewed the server room on four occasions and found the doors were unlocked and the room unoccupied. District employees told us they have left the door unlocked when they were elsewhere in the school building but locked the door when they left the building. This increases the risk that unauthorized individuals could gain access to these systems during school hours when staff is absent from the server room. This could result in services being disrupted, costly equipment damaged, destroyed or stolen, and personal information being compromised.

Backups – Data should be backed up (i.e., copy made) on a routine basis and the backup copy stored at an environmentally and physically secure off-site location. We found the Board has not established policies or procedures for the backup of District information including its financial data. Currently, District financial data is backed up to a hard drive located within the server room and

is not taken off site. If the system were to become compromised and a backup was not available to restore it to normal operations, the District risks losing most, if not all, of its computer-processed data.

Disaster Recovery Plan – The District’s internal control system should include a formal disaster plan to address the possible loss of computer equipment and data and establish procedures for recovery in the event of such a loss. The plan should detail the precautions to be taken to minimize the effects of any disaster (e.g., fire, extended loss of power, inadvertent employee actions) and enable the District to either maintain or quickly resume its mission-critical functions. The plan should include a significant focus on disaster prevention. The Board had not established a formal disaster plan and consequently, in the event of a disaster, District personnel have no guidelines or plan to follow to help minimize or prevent the loss of equipment and data or guidance on how to implement data recovery procedures.

**Recommendations:**

8. The Board should adopt policies that communicate clear guidance for all aspects of the District’s information technology system.
9. District officials should implement procedures over the administration of user accounts including requiring strong passwords and training users in how to choose and secure passwords, requiring users to change their passwords on a regular basis and establishing restricted user accounts for all users.
10. The Board should strengthen controls over the physical access to the District’s server room to protect physical components of the IT system from unauthorized access.
11. District officials should store backups of District information at an environmentally and physically secure off-site location. In addition, this data should be periodically tested to verify it is capable of restoring the District’s system.
12. District officials should develop a disaster recovery plan.

## **APPENDIX A**

### **RESPONSE FROM DISTRICT OFFICIALS**

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

North Warren



Central School

June 26, 2008

State of New York  
Office of State Comptroller  
Glens Falls Regional Office  
One Broad Street Plaza  
Glens Falls, New York 12801

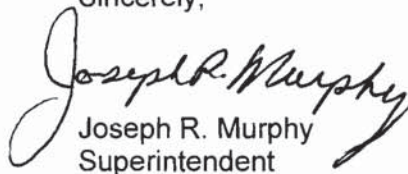
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This letter is in response to the audit of the North Warren Central School District conducted by the Office of the State Comptroller. We first want to thank the auditors for the professional and courteous manner in which they conducted the audit and exit interview. We also appreciate the recommendations and suggestions offered by the auditors.

We feel that the results of the audit will make our district more effective, efficient and compliant in conducting school business. The Board of Education reviewed copies of audit findings and recommendations. The Board recognizes the need to update policies and procedures in order to remain accountable and committed to providing learning programs of excellence for all students.

Attached is our response to the Draft Report of Examination: Internal Controls Over Financial Operations for the period of July 1, 2006 – August 10, 2007. The recommendations provided in this report will be incorporated into our continuous improvement activities.

Sincerely,

  
Joseph R. Murphy  
Superintendent

North Warren Central School District  
Response to the Draft Report of Examination:  
Internal Controls Over Financial Operations  
July 1, 2006 – August 10, 2007

The following are our responses to recommendations:

Recommendation 1. District officials should establish cash receipt and disbursement policies that address the proper segregation of duties for each process.

We spoke with the auditor at length about the optimum way to divide the duties with the limited office staff we have. We are following her suggestions for segregation of duties for receipt of cash/checks, and deposit and reconciliation of same. The new procedures are currently in draft form, awaiting review by the board audit committee before incorporating them into the business office procedures manual. At the time of audit, we used single press-numbered carbon cash receipts onto an accounting ledger. The auditor recommends duplicate press-numbered receipts, which we have ordered and will begin using.

Recommendation 2. Cash receipts should be deposited and recorded in a timely manner.

Our procedure at the time of the audit was to make weekly bank deposits, with the exception of tax collection receipts that were deposited daily. In practice, we took any large cash deposit to the bank within 48 hours of receipt. We are now making deposits within 48 hours of receipts of all cash/checks. The auditor recommends that the board define "large deposit" amounts and set policy as to timeliness of deposits. The district is now preparing appropriate policy and procedure.

Recommendation 3. District officials should adopt procedures for the cash disbursement process including the use of check stock, the use of vendor accounts, the documentation of transactions and the organization and retention of supporting documents.

Since the OSC audit, we no longer use the manual check stock for any fund with the exception of student activity fund, and all checks go through the internal claims auditor before release. Student activity fund does not use computer check stock, so manual stock in this instance is acceptable to the OSC auditor. In any case, our changeover to new business office software in July will eliminate manual check stock entirely. However, we formally request that the comment stating that the internal claims auditor apparently was unaware of the existence of the additional manual check stock be removed from the report. This is inaccurate. The claims auditor was aware of the checks (drawn for conference registrations, postage, SED fingerprints, etc.) but did not audit them. We were present twice while the OSC auditor and the internal claims auditor discussed the manual checks and the need for her to audit them.

See  
Note 1  
Page 27

The audit report states that we did not provide any documentation or explanation for 10 bank transfers. We provided all bank transfer confirmations and supporting payroll documents as requested. Neither the account clerk nor the Business Manager has any recollection of not being

1

able to find documents or provide explanation. The OSC auditor further stated at the draft report meeting that she requested that we fax the documentation to her after she left. Again, we provided all supporting documentation that was requested. There were no missing records. We assume this is what the auditor refers to in her comment regarding organization and retention of supporting documentation. We believe this statement to be inaccurate.

We no longer use the default vendor account mentioned in this area of the report. We create a vendor number and include all information in the master vendor file.

Recommendation 4. District officials should provide the oversight required to ensure that all extra-classroom activity moneys are properly documented and accounted for, safeguarded, and used as intended and that policies are followed; and

Recommendation 5. The board should appoint a central treasure to be responsible for maintaining the extra-classroom activity fund checks, recording receipts, depositing money, and preparing monthly bank reconciliations, and reporting to the board on at least a quarterly basis.

The board appointed the account clerk as central district treasurer, and she has established a procedures manual for all extra-classroom accounts. All funds are now deposited at the bank by the central treasurer, and all deposits are turned in to her with an accounting as to source of funds. The central treasurer will continue to meet with advisors/treasurers periodically to confirm agreement in accounting records. All disbursing order back-up documentation to support the check request is now maintained in the business office instead of with the advisors. We provided all back up documentation to the OSC auditor as was provided to us by the club advisors. The central district treasurer is providing quarterly trial balances to the board for review.

Recommendation 6. The board should adopt a policy that clearly defines the duties of the claims auditor and requires that she prepare periodic reports and report directly to the board.

The claims auditor is now preparing periodic reports to the board. Policies and procedures will be updated and implemented.

Recommendation 7. The board should develop and implement an adequate policy governing the claims audit process making sure that the claims auditor is fully aware of her responsibilities.

The claims auditor stated she provided the OSC auditor with her checklist for auditing district claims. She also maintains a procedures manual received from training for claims auditors. The Board Committee will update the claims auditor job description. As stated previously, the OSC auditor states that the claims auditor was not even aware the district disbursed manual check payments. This is inaccurate, and we request this language be removed from the report.

Recommendation 8. The board should adopt policies that communicate clear guidance for all aspects of the District's information technology system.

Current district policy is in the process of being reviewed and updated with the special intent of informing all users of procedures and processes for using district information technology. Procedures will be communicated through direct staff involvement, written in handbooks for both staff and students. The board is preparing policy and procedures governing E-mail, acceptable use, and security.

Recommendation 9. District officials should implement procedures over the administration of user accounts including requiring strong passwords and training users in how to choose and secure passwords, requiring users to change their passwords on a regular basis and establishing restricted user accounts for all users.

District procedures describing receiving, using and losing accounts will be communicated to all staff, students and parents. In addition each user will be trained in how to use and change passwords according to district policy and district administrators along with IT personnel will monitor the process.

Recommendation 10. The Board should strengthen controls over the physical access to the District's server room to protect physical components of the IT system from unauthorized access.

New procedures are being developed to secure the IT room. At this time all doors are locked when the room is unoccupied. Keys to the IT room are limited. Security cameras are now in place in the IT room and in the hall way outside the room.

Recommendation 11. District officials should store backups of District information at environmentally and physically secure off-site location. In addition, this data should be periodically tested to verify it is capable of restoring the District's system.

The district is installing a new system for processing and maintaining personnel and financial records. District data will be stored off site with retrieval of information to reconstruct records in the case of a disaster. The district will develop oversight procedures for testing its capability to retrieve and restore data. In addition the district regularly updates our Firewall (██████████), the web filter (██████████) and our E-Mail filter (██████████).

Recommendation 12. District officials should develop a disaster recovery plan.

The district is working with the Eastern Suffolk BOCES as an offsite service to store and provide retrieval of ██████████ student and other district information. Also, the district is installing ██████████ as an offsite storage and retrieval of financial data. Storage and retrieval systems will be monitored and checked to ensure that the district may reconstruct data systems.

## APPENDIX B

### OSC COMMENTS ON THE DISTRICT'S RESPONSE

#### Note 1

During our exit discussion District officials indicated the claims auditor was aware of additional check stock used to disburse manually processed checks, so we removed wording from the draft report that indicated she was not aware of these checks. However, officials agreed that none of these manually processed payments were reviewed and approved by the claims auditor.

#### Note 2

The Treasurer indicated during our audit that the ten transfers in question were related to payroll transactions. However, she did not provide back-up documentation to support these transactions. We requested this documentation on several occasions during and after our audit field work and the information was never provided to us.

## 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, 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 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, extra-classroom activity, claims processing and information technology for further audit testing.

During this audit, we examined the records and reports of the North Warren Central School District for the period July 1, 2006 through August 10, 2007. However, in order for us to complete audit steps for our review of extra-classroom activities it was necessary to trace certain transactions that occurred in the prior fiscal year. To accomplish the objectives of the audit and obtain valid audit evidence, our procedures included the following steps:

- We reviewed Board minutes for our audit period, the District's policy manual, job description manual and the staff handbook for all applicable policies and procedures.
- We interviewed Board Members, District officials, and employees to learn about cash receipts and disbursements at the District. We reviewed all pertinent policies and procedures governing cash receipts and disbursements. We reviewed bank statements, bank reconciliations, trial balances, deposit slips, cash receipt records, cash disbursement records, and other corresponding records.
- We interviewed Board Members, District officials, and employees to learn about the extra-classroom activities at the District. We reviewed all pertinent policies and procedures governing extra-classroom activities. We reviewed activity club records including receipts and disbursements, and District records including receipts, disbursements, trial balances, and monthly newsletters.

- We interviewed Board Members, District officials, and employees to learn about claims processing at the District. We reviewed all pertinent policies and procedures governing claims processing. We tested claims packages and supporting documentation.
- We interviewed District officials and employees to learn about the District’s information technology process. We reviewed all pertinent policies and procedures governing information technology. We reviewed and/or observed password requirements, staff user rights on the District’s network, and physical security over the server room and backups.

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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