



West Canada Valley Central School District Internal Controls Over Selected Financial Activities

Report of Examination

Period Covered:

July 1, 2006 — December 31, 2007

2008M-168



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

October 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 West Canada Valley Central 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 West Canada Valley 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.

There is one school in operation within the District, with approximately 870 students and 185 full- and part-time employees. The District's budgeted expenditures for the 2006-07 fiscal year were \$13.1 million, funded primarily with State aid, real property taxes, and grants.

Scope and Objective

The objective of our audit was to examine the District's internal controls over selected financial activities for the period July 1, 2006, to December 31, 2007. Our audit addressed the following related questions:

- Are internal controls over cash disbursements appropriately designed and operating effectively to adequately safeguard District assets?
- Has the District established policies and procedures to ensure that goods and services are purchased in the most prudent and economical way?
- Are internal controls over the District's gasoline and diesel fuel inventories appropriately designed and operating effectively to adequately safeguard District assets?

Audit Results

We found that the Board and District officials need to take steps to improve the District's internal control environment. For example, internal controls over cash disbursements need to be strengthened. The financial duties of the Business Manager/Treasurer are not properly segregated and compensating controls are not in place. In addition, the Business Manager/Treasurer is not involved in the check-signing process and does not exercise control over the use of his facsimile signature to sign checks. Further, he does not compare checks to certified payroll registers, certified warrants, or individual claims approved by the claims auditor, or monitor the continuity of check number sequences between payroll and accounts payable periods. Although our testing did not disclose any evidence of improper

cash disbursements, there is an increased risk that inappropriate disbursements of District funds could occur and remain undetected.

Also, we found that policies and procedures do not ensure that purchases are made in the most prudent and economical way. We found that 15 out of 18 contracts we tested that were not subject to competitive bidding, totaling \$107,936, did not have documentation to show that competition was sought by obtaining written and/or verbal quotes, or requests for proposals. As a result, there is an increased risk that goods and services of maximum quality are not acquired at the lowest possible cost.

Finally, we also identified that internal controls over gasoline and diesel fuel need to be improved. We compared the maintenance department's records to the transportation department's records for November and December 2007 and found that the amount of fuel pumped per the transportation department's records exceeded the amount per the maintenance department's records by 270 and 34 gallons for diesel and gasoline, respectively. District officials were not aware of these variances because they had no process in place to compare usage records and investigate differences. As a result, there is an increased risk that fuel could be lost through leakage or stolen and not be detected.

Comments of District Officials

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. District officials generally agreed with our recommendations and indicated they planned to initiate corrective action.

Introduction

Background

The West Canada Valley Central School District (District) is located in the Towns of Fairfield, Herkimer, Manheim, Newport, Norway, and Schuyler in Herkimer County and the Town of Deerfield in Oneida 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 Superintendent is also responsible for certifying (approving) payrolls and serves as the District's purchasing agent.

There is one school in operation within the District, with approximately 870 students and 185 full- and part-time employees. The District's budgeted expenditures for the 2006-07 fiscal year were \$13.1 million, funded primarily with State aid, real property taxes, and grants.

The Business Office staff consists of a Business Manager/Treasurer who is primarily responsible for the District's finances, an accounts payable clerk who is responsible for processing claims, and a payroll clerk who is responsible for processing payrolls. On an annual basis, the Board appoints a claims auditor who assumes the Board's powers and duties for approving and denying claims against the District.

Objective

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

- Are internal controls over cash disbursements appropriately designed and operating effectively to adequately safeguard District assets?
- Has the District established policies and procedures to ensure that goods and services are purchased in the most prudent and economical way?
- Are internal controls over the District's gasoline and diesel fuel inventories appropriately designed and operating effectively to adequately safeguard District assets?

Scope and Methodology

We examined the District's internal controls over cash disbursements, purchasing and fuel inventory for the period July 1, 2006, to December 31, 2007.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix B of this report.

**Comments of District
Officials and Corrective
Action**

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. District officials generally agreed with our recommendations and indicated they planned to initiate corrective action.

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

Cash Disbursements

District officials are responsible for establishing internal controls over cash disbursements to safeguard District assets. The financial duties of the Business Manager/Treasurer must be properly segregated or compensating controls must be in place. In addition, the Business Manager/Treasurer must control the use of his facsimile signature to sign checks, and ensure that disbursements are authorized and supported by certified payrolls, certified warrants, or individual claims approved by the claims auditor. A good system of internal control can help to ensure that cash is disbursed only for valid business purposes and for the proper amounts.

Internal controls over cash disbursements are not appropriately designed or operating effectively. The financial duties of the Business Manager/Treasurer are not properly segregated and compensating controls are not in place. In addition, the Business Manager/Treasurer is not involved in the check-signing process and does not exercise control over the use of his facsimile signature to sign checks. He also does not compare checks to certified payroll registers, certified warrants, or individual claims approved by the claims auditor, or monitor the continuity of check number sequences between payroll and accounts payable periods. Although our testing did not disclose any evidence of improper cash disbursements, there is an increased risk that improper disbursements or payment errors could occur.

Segregation of Duties

District officials are responsible for segregating financial duties so that no single individual controls all phases of a transaction and the work of one employee is routinely verified in the course of another employee's regular duties. When it is not practical to segregate duties because of limited staff resources, District officials should establish compensating controls, such as the managerial review of an employee's work.

District officials have not ensured that the financial duties of the Business Manager/Treasurer's are properly segregated, or that compensating controls are in place. The Business Manager/Treasurer is responsible for posting journal entries, making wire and inter-account bank transfers, and performing monthly bank reconciliations without the review or approval of another individual. The Business Manager/Treasurer also has the ability to process and print checks. These responsibilities would allow the Business Manager/Treasurer to initiate and conceal inappropriate transfers of District funds or inappropriate cash disbursements. Although the Board receives copies

of the bank reconciliations in the Business Manager/Treasurer's monthly reports, there is no indication that any District official verifies the completeness and accuracy of the reconciliations.

To address this risk, we reviewed journal entries for unusual transactions from July 2006 to June 2007, tested wire and inter-account bank transfers and bank reconciliations for one month, and tested a sample of cancelled checks as discussed in the next section of this report. Although our testing did not disclose any discrepancies, the failure to segregate duties without management oversight increases the risk that unauthorized transactions can be initiated and not be detected.

Check Signing

The Business Manager/Treasurer plays a critical role in the cash disbursement process as the District official responsible for signing checks. The Business Manager/Treasurer is responsible for ensuring that his actual or facsimile signature is affixed to District checks by him or by someone under his direct supervision. Except for a few statutory exceptions, the Business Manager/Treasurer should not sign checks until he receives certified payroll registers authorizing payment to employees, or certified warrants, or individual claims approved by the claims auditor authorizing payment to claimants. The Business Manager/Treasurer should not issue checks until he compares signed checks to certified payrolls and certified warrants to verify the accuracy of check amounts and payees, and that only those checks on the payrolls and warrants have been generated.

There are two signature disks that are used to affix the Business Manager/Treasurer's signature to District checks. One disk is at the Mohawk Regional Information Center (MORIC). MORIC employees use this disk to sign computer-generated payroll checks after the payroll clerk processes payroll runs and directs MORIC to print checks. Once signed, the payroll checks are delivered to the payroll clerk, who then mails or distributes them to the appropriate recipients. The second signature disk is in the Business Office. Both the payroll clerk and the accounts payable clerk have access to this disk. The payroll clerk uses the disk to sign payroll-related checks such as replacement checks, health insurance, and trust and agency checks. The accounts payable clerk processes vendor invoices and uses the disk to sign accounts payable checks, which she then mails to the vendors. We found that the Business Manager/Treasurer does not:

- Oversee the use of his signature disks by MORIC, the payroll clerk or the accounts payable clerk, or review the checks that are signed
- Compare payroll checks to certified payroll registers, or compare accounts payable checks to certified warrants or

individual claims approved by the claims auditor to verify they were authorized

- Monitor the continuity of check number sequences between payroll and warrant periods.

Checks containing the Business Manager/Treasurer's signature are produced without his oversight, the accounts payable clerk and payroll clerk have recordkeeping duties that are not compatible with their check-signing duties, and the Business Manager/Treasurer does not maintain accountability for all checks issued. Consequently, there is an increased risk that signed checks will not be produced for legitimate District purposes and in the correct amounts. To address this risk, we compared 50 payroll checks totaling \$41,063 and direct deposit reductions per bank statements for a two-month period to certified payroll transaction reports and direct deposit proof lists. We also tested 50 accounts payable checks totaling \$109,700 paid during 2006-07. Although we did not detect any improper payments, District officials should promptly correct the control weaknesses to reduce the risk that improper disbursements or payment errors could occur.

Recommendations

1. District officials should assign financial duties so that the work of one individual independently verifies the work of another, in the course of their regular duties. Where incompatible duties cannot be segregated, District officials should establish supervisory review procedures to mitigate risk.
2. The Business Manager/Treasurer should control the use of his computerized signature at all times.
3. The Business Manager/Treasurer should review printed checks and compare them to certified payroll registers, certified warrants, or individual claims approved by the claims auditor prior to disbursement to verify that the checks are for legitimate purposes and for the proper amounts.
4. The Business Manager/Treasurer should track the sequence of all check numbers prior to disbursement to ensure that all checks are accounted for.

Purchasing

General Municipal Law (GML) requires the uses of competition in the procurement process to obtain services, supplies, and equipment of suitable quality and quantity, from the best-qualified and lowest-priced source, in compliance with Board and legal requirements. District officials are required to solicit competitive bids for purchases of more than \$10,000 and public works contracts of more than \$20,000. District officials may also participate in cooperative bidding with other governmental entities such as a Board of Cooperative Educational Services (BOCES), or make purchases using certain contracts awarded through the New York State Office of General Services (OGS) or a county. The Board is required to adopt written policies for the procurement of goods and services that are not subject to competitive bidding. It is important that these policies, or supplemental procedures or regulations developed by District officials, indicate when District personnel are required to solicit requests for proposals (RFPs), written quotes or verbal quotes, the number of each to be obtained, and the documentation that should be retained. These procedures allow the District to expend taxpayer dollars efficiently and guard against favoritism, extravagance and fraud.

While the Board has adopted a procurement policy, the policy does not indicate when District personnel should seek competition for procurements that are not subject to competitive bidding, and District officials have not developed procedures or regulations to supplement the Board's policy. Consequently, District personnel do not have guidance on when they are required to solicit RFPs, written or verbal quotes, the number of each to be obtained, and the documentation that should be retained to show compliance with the policy.

We examined claims relating to 25 contracts¹ totaling \$567,246 to determine if District officials complied with competitive bidding requirements and the extent to which District personnel sought competition for purchases that were not subject to competitive bidding. Seven of the contracts totaling \$436,810 were subject to competitive bidding. District officials appropriately solicited competitive bids or used State or BOCES contracts for these procurements. However, 15 out of 18 contracts totaling \$107,936, that were not subject to competitive bidding, did not have sufficient documentation to show that District personnel sought competition. Specifically, we found the following:

¹ Our testing included some public work contracts, individual purchases and aggregate purchases of commodities or like items.

- Seven contracts totaling \$28,315 had no documentation to indicate that any competition was solicited. These goods and services included maintenance of the football field (\$9,335), snow removal services (\$5,400), septic system pumping and dumping (\$5,100), and vacuums (\$3,160).
- Four contracts totaling \$35,185 had documentation to indicate that District personnel obtained estimates from the vendors from whom they purchased the goods and services. However, there was no documentation to show that written or verbal quotes were sought from any other vendors. These goods and services included the installation/relocation of fuel pumps (\$19,470), two purchases of curtains (\$12,175) and septic system repair and pumping (\$3,540).
- Four contracts for insurance and legal services totaling \$44,436 had no documentation to indicate that District officials used an RFP process or obtained any competition when they procured these professional services.

The Board has not provided clear guidance for the procurement of goods and services that are not subject to competitive bidding, and District officials have not developed supplemental procedures or regulations to do so. As a result, District officials and personnel do not generally seek competition in the procurement of goods and services that do not require competitive bidding, and there is an increased risk that goods and services of maximum quality will not be acquired at the lowest possible cost.

Recommendations

5. The Board should amend its procurement policy, or District officials should develop supplemental procedures or regulations, to provide detailed guidance for purchases that are not subject to competitive bidding. The policy, procedures, or regulations should indicate when District officers or personnel are required to solicit RFPs, written quotes or verbal quotes, the number of each that must be obtained, and the documentation that should be retained to show compliance with the policy.
6. District officials should ensure that all employees involved in the procurement process follow the District's procurement policies, procedures and regulations.

Fuel Inventory

District officials are responsible for designing and adopting internal controls over fuel inventories and monitoring adherence to those controls to ensure that fuel inventories are protected from loss or theft, and are used only for District purposes. District officials must provide clear guidance to staff members on how to safeguard fuel inventories including requiring that staff members maintain detailed inventory records, perform periodic physical inventories, reconcile fuel records to fuel deliveries, and maintain usage and leak test data. The New York State Department of Environmental Conservation (DEC) requires that the operator of any facility with a combined underground storage capacity of more than 1,100 gallons maintain daily inventory records for the purpose of detecting leaks. Records must be kept for each tank and must include measurements of deliveries, usage, inventory on hand, and losses or gains. Records must be kept current, account for all variables that could affect an apparent gain or loss, and must be in accordance with generally accepted practices. The DEC requires that records be maintained and available for inspection for a period of not less than five years. Failure to maintain and reconcile such records constitutes cause for DEC-ordered tests and inspections of the facility at the operator's expense.²

The District maintains a 500-gallon above-ground gasoline tank and a 4,000-gallon underground diesel tank. Purchases of gasoline and diesel fuel from July 1, 2006, to December 31, 2007, totaled \$118,932. The head of the maintenance department is responsible for maintaining fuel records. Each morning, maintenance department personnel measure the level of fuel in each tank³ and compare the inventory levels to perpetual inventory records that show beginning inventory, deliveries, gallons of fuel pumped (usage), and ending inventories. The total amount of fuel pumped each day is obtained from metered pump readings. In addition, the transportation supervisor keeps manual daily usage logs that show the amount of fuel pumped into different vehicles by bus drivers and other District personnel. However, District staff do not reconcile the fuel pumped per the perpetual inventory records in the maintenance department to the fuel pumped per the daily usage logs in the transportation department to verify that all fuel pumped has been accounted for.

² Title 6 of the New York Codes, Rules and Regulations, Part 613.4 [a]; [c]

³ Maintenance department personnel place a measuring stick into the fuel tanks to measure the amount of fuel in the tanks (in inches), and use a conversion chart to convert the stick reading (in inches) to gallons of inventory.

Due to this control weakness, we compared the fuel pumped records in the maintenance department to the fuel pumped per the usage logs in the transportation department for November and December 2007. We found that the amount of fuel pumped per the transportation department's records (usage logs) exceeded the amount of fuel pumped per the maintenance department's records (physical and perpetual inventories) by 270 and 34 gallons for diesel and gasoline, respectively. District officials were not aware of these variances because they had no process in place to compare the records of usage and investigate differences.

A number of factors may contribute to variances between the records including theft, the improper calibration of pump meters, and poor recordkeeping practices. District officials indicated that the discrepancies may have been caused by timing differences between when the tanks were stick measured (or physically inventoried) and when the drivers pumped fuel into vehicles. For example, drivers may have pumped fuel in the morning before the maintenance department stick measured the tanks. District officials also stated that they have obtained a proposal to upgrade the fuel system, using a key system for fuel pumps which will help strengthen controls.

The failure to reconcile the records of usage in the maintenance department to those in the transportation department results in a lack of accountability for fuel inventories and increases the risk that fuel could be lost through leakage or stolen and not be detected.

Recommendation

7. District officials should ensure that the amount of fuel pumped per the perpetual inventory records in the maintenance department is reconciled to the amount of fuel pumped per the daily usage logs in the transportation department and follow up on any material differences.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



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Superintendent of Schools

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Business Manager/Treasurer

B. ANN MAHER
Elementary Principal

FRANK SUTLIFF
Middle/High School Principal

MELISSA M. TUBIA
Guidance Coordinator

WILLIAM D. FRANK
Transportation Supervisor

October 15, 2008

[REDACTED]
Office of the State Comptroller
State Office Building Room 409
333 E. Washington Street
Syracuse, New York 13202-1428

SENT VIA FACSIMILE, EMAIL AND HARD COPY

Dear [REDACTED]:

In response to the ***Draft Findings on the Internal Controls over Selected Financial Activities***, we offer the following:

I. **Cash Disbursements-**

- a. Segregation of Duties: in line with the recommendations offered by the on-site auditors, we have altered a number of our practices as follows:
 - i. Payroll – instead of the payroll clerk entering new employees, a management confidential secretary in the superintendent’s office enters this data and the payroll clerk now has “view only” privileges on this.
 - ii. Accounts Payable – the clerk responsible for this will no longer be inputting vendor detail AND making payment to same; the payroll clerk will now enter this data and the accounts payable clerk will have “view only” privileges in this area.
 - iii. The District will be reviewing the components of a Central Business Office that is being established at the Herkimer BOCES in the 2009-2010 school year to see if

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our joining is feasible. This would alleviate many of the segregation issues noted in the report.

- b. Check signing: while we take confidence in the fact that 50 checks spanning two months time were tested and no findings were made, we will nonetheless consider all recommendations from the OSC as we seek to rectify this situation.

II. **Purchasing** –

- a. Procurements regulations in consonance with District Policy 5410 have been developed and we anticipate that they will be approved by the Board of Education on 15 October, 2008. These regulations dictate the course of action to be taken under §104b of General Municipal Law that are not otherwise addressed in §103. Specifically, we have categorized procurements in dollar amounts and spelled out actions required at each level. These regulations have been reviewed with supervisory staff at a meeting held on 26 September, 2008.

III. **Fuel Inventory** –

- a. Discrepancies in records were discovered in the course of the audit that could not be reconciled. The District was aware that this would be an issue and addressed it as such in the pre-audit meeting with OSC on-site staff. We also noted that we were in the process of installing an electronic fuel monitoring system that required a vehicle-specific magnetic key, a personal identification number, and the mileage/hours of the vehicle being fueled. This information can be viewed and audited by District administration.

Thank you for the opportunity to respond to the findings of your office and we will submit the Board approved Corrective Action Plan in due course.

Lastly, we enjoyed the professional relationship and learning opportunities presented to us during [REDACTED] and [REDACTED] time on our campus. They are fine folks that serve your office well.

Sincerely,

A handwritten signature in black ink, appearing to be 'KGS', written over a large, loopy circular flourish.

Kenneth G. Slentz
Superintendent of Schools

KGS/jg

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by officials to safeguard District assets. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: financial oversight, cash receipts and disbursements, purchasing, and payroll and personal services.

During the initial assessment, we interviewed appropriate District officials, performed limited tests of transactions and reviewed pertinent documents, such as District policies and procedures manuals, Board minutes, and financial records and reports. In addition, we obtained information directly from the computerized financial databases and then analyzed it electronically using computer-assisted techniques. This approach provided us with additional information about the District's financial transactions as recorded in its databases. Further, we reviewed the District's internal controls and procedures over the computerized financial databases to help ensure that the information produced by such systems was reliable.

After reviewing the information gathered during our initial assessment, we determined where weaknesses existed, and evaluated those weaknesses for the risk of potential fraud, theft and/or professional misconduct. We then decided upon the reported objective and scope by selecting for audit those areas most at risk. We selected cash disbursements, purchasing and fuel inventory for further audit testing. To accomplish the objectives of our audit, our procedures included the following:

- We interviewed District officials and employees and reviewed Board policies, procedures, and meeting minutes to obtain an understanding of the District's internal controls related to our audit objectives.
- We reviewed journal entries for unusual entries from July 2006 to June 2007.
- We examined all wire and inter-account and transfers on the October 2007 bank statements and verified that the transfers were appropriate.
- We tested bank reconciliations for December 2006.
- We verified the 2006-07 annual salaries of the payroll clerk, tax collector (the mother of the payroll clerk), Superintendent, and the Business Manager/Treasurer.
- We tested the reliability of electronic disbursement data from the District's computerized accounting system by comparing total check disbursements made during 2006-07 to bank statements and comparing a sample of 500-recorded disbursements to cancelled checks.
- We traced 50 payroll checks totaling \$41,063 from bank statements to electronic disbursement data and certified payroll transaction reports to ensure that the payments were approved. We also traced direct deposit reductions on the District's bank statements to the amounts listed on

certified payroll transaction reports and then to the total of the direct deposit proof lists for July and September 2007.

- We examined supporting documentation for a risk-based sample of 50 accounts payable disbursements totaling \$109,700 to determine if the payments were audited and approved by the claims auditor, and were for proper District purposes.
- We reviewed the District's procurement policy, and judgmentally selected and tested claims relating to 25 contracts totaling \$567,246 for evidence of bids, State contracts, cooperative bidding arrangements, requests for proposal, written quotes or verbal quotes.
- We reviewed gasoline and diesel fuel records maintained by the maintenance and transportation departments and compared manual fuel usage logs to records showing changes in pump readings and stick readings for the months of November and December 2007.

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

APPENDIX C

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