



Lake George Central School District Internal Controls Over Payroll

Report of Examination

Period Covered:

July 1, 2011 — January 31, 2013

2013M-122



Thomas P. DiNapoli

Table of Contents

	Page
AUTHORITY LETTER	2
INTRODUCTION	3
Background	3
Objective	3
Scope and Methodology	3
Comments of District Officials	4
PAYROLL	5
APPENDIX A Response From District Officials	7
APPENDIX B Audit Methodology and Standards	9
APPENDIX C How to Obtain Additional Copies of the Report	11
APPENDIX D Local Regional Office Listing	12

State of New York Office of the State Comptroller

Division of Local Government and School Accountability

August 2013

Dear School District Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as 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 operations and Board of Education governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of Lake George Central School District, entitled Internal Controls Over Payroll. 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 are resources for local government 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*

Introduction

Background

The Lake George Central School District (District) is located in the Village of Lake George and the Towns of Lake George, Queensbury, Bolton, and Fort Ann in Warren and Washington Counties. 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 and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction.

There are two schools in operation within the District, with approximately 970 students and 255 employees. The District's budgeted appropriations for the 2012-13 fiscal year were approximately \$21 million, which were funded primarily with State aid and real property taxes. Payroll costs and associated employee benefit costs represent a significant portion of the District's annual expenditures. For the 2011-12 fiscal year these costs totaled approximately \$15.1 million¹ or 76 percent of the total general fund's \$20 million of expenditures.

Objective

The objective of our audit was to determine if the District established effective internal controls over payroll. More specifically, our audit addressed the following related question:

- Are internal controls over payroll appropriately designed and operating effectively to adequately safeguard District assets?

Scope and Methodology

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 condition, control environment, cash receipts and cash disbursements, purchasing, claims processing, payroll, information technology (IT) and application controls, and cash management. Based on that evaluation, we determined that controls appeared to be adequate and limited risk existed in most of the financial areas we reviewed. We did determine that risk existed in the payroll area and, therefore, we examined internal controls over payroll for the period July 1, 2011, through January 31, 2013. We expanded our scope through March 22, 2013, to review the appropriateness of approved payroll records.

¹ The total is a combination of \$9,487,025 in salaries and \$5,592,280 in employee benefits such as healthcare and pension costs.

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**

The results of our audit have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. District officials agreed with our findings.

Payroll

The Board is responsible for designing internal controls over payroll, which along with fringe benefits, represents the majority of a school district's annual budget. Effective internal controls can provide assurance that District employees are paid and provided benefits in accordance with contract provisions, and that transactions are appropriately recorded and authorized by management. Controls over payroll should consist of written Board authorization for salaries, hourly wages, and fringe benefits paid to District employees. Additionally, controls should include effective managerial oversight and adequate segregation of duties. In a small operation, where it is not possible to fully segregate duties, active supervision and oversight become even more important internal control components. Failure to establish and adhere to sound internal controls increases the risk that fraud, abuse or errors may occur and go undetected and remain uncorrected.

We commend District officials for establishing and implementing strong internal controls over payroll. Officials implemented specific procedures to ensure that the individuals reported and paid through the payroll process were bona fide District employees, were paid only approved salaries and wages, and received only the benefits to which they were entitled.

The Board and District officials established various control procedures over the payroll process that included providing adequate supervision and oversight. The Board approves the hiring of all new employees and accepts all resignations and retirements before any changes are made to payroll records. The District Clerk maintains all personnel files for new hires, and current and retired employees. The District Clerk also records all salaries and wages, and maintains a record of employee resignations and retirements, along with the effective dates in the Board minutes. The payroll clerk enters all new employee information into the payroll system, deactivates payments to employees who resign or retire, and processes the biweekly payroll. The District Treasurer (Treasurer) reviews and approves the accuracy of all payroll changes in the accounting system before payroll can be processed. The Treasurer also reviews and approves the check listing prior to the Business Manager's² review and the Superintendent's certification. Further, the Treasurer prepares the bank transfer for any payroll checks that are directly deposited into the various employee

² The Business Manager reviews the deductions report, payroll change reports, and compares the current payroll register to the prior payroll register to see if any changes were made from one payroll to the next.

bank accounts, which the Business Manager reviews and approves prior to the transfer's completion. Additionally, District officials perform an annual payroll payout in which all employees are required to sign for their paycheck and show proper identification to verify that only District employees are receiving pay checks.³

To assess these controls, we tested certain payroll-related records to ensure the legitimacy of employees and that employees received compensation according to the terms of their respective employment or collective bargaining agreements (agreements). We reviewed 13 payroll payments to ensure they were paid to legitimate District employees by verifying that signed agreements or approved time-tracking documents⁴ were on hand. We examined the payroll records of five key District employees⁵ and 10 randomly selected District employees⁶ to ensure that they were paid at the correct rates. We also reviewed payments to the five employees who received the highest one-time payments⁷ and 10 employees who received health insurance buy-out payments.⁸ We traced these payments to the Board-approved agreements to ensure the salaries and payments made were paid in accordance with agreement terms and that they were accurately calculated. Finally, we reviewed the records from four payroll periods⁹ to ensure that payrolls were properly documented, department heads approved them, and the Superintendent certified them. We found no exceptions with our testing. Establishing and adhering to strong internal controls decreases the risk that fraud, abuse, or errors may occur and go undetected and remain uncorrected.

³ This occurred in the second pay period in January and we observed this process while onsite for the audit.

⁴ We randomly selected 10 District employees. Then, to ensure that we included substitute employees in our sample, we judgmentally selected three additional individuals employed by the District who were substitutes. All these payroll payments were made during the 2011-12 fiscal year. Time-tracking documentation was reviewed for these three employees because they were not subject to any of the District agreements.

⁵ Key employees included the Superintendent, Business Manager, District Treasurer, payroll clerk, and account clerk who were paid gross salaries and wages totaling \$12,876 on the December 28, 2012, payroll.

⁶ We reviewed payroll payments totaling \$18,097 for these 10 employees.

⁷ We judgmentally selected the five payments that were the largest one-time payments totaling \$55,446 made to District employees during the 2011-12 fiscal year. Two were payments for accumulated leave upon retirement and three were annual stipends to coaches.

⁸ We randomly selected these 10 payments totaling \$20,000 that were paid during the 2012-13 fiscal year.

⁹ We judgmentally selected two payrolls for each of the fiscal years 2011-12 and 2012-13.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

Patrick M. Dee
Superintendent of Schools
Email: deep@lkgeorge.org

July 25, 2013

Jeffrey P. Leonard, Chief Examiner
Office of the State Comptroller
Glens Falls Regional Office
One Broad Street Plaza
Glens Falls, NY 12801-4396

Mr. Leonard,

This letter is in response to the NYS Comptroller's report, "*Internal Controls Over Payroll Report of Examination*". The examination took place at the Lake George Central School District Office, from January 2013 through March 2013.

We would like to commend your department for the professionalism and courtesy displayed by your staff. We extend our thanks to [REDACTED] and [REDACTED]. They represent your office exceptionally well, and their thoroughness and professionalism should be commended. Through this process, we have enhanced a relationship with your office that will be beneficial to the district for many years to come. The expertise and assistance provided by your office is appreciated, and will continue to be utilized.

We are very pleased with the results of the audit, which contained no findings in any areas tested and reviewed. The District is proud of the staff in the Business Office for their hard work and high standards that made this possible.

We would like to extend our thanks to the staff of the Glens Falls Office, and express our appreciation for their professionalism and assistance.

Sincerely,

Patrick Dee
Superintendent of Schools
Lake George Central School District

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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 condition, control environment, cash receipts and disbursements, purchasing, claims processing, payroll, IT and application controls, and cash management.

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. Based on that evaluation we determined that controls appeared to be adequate and limited risk existed in most of the financial areas we reviewed. We then decided on the reported objective and scope by selecting for audit those areas most at risk. We selected payroll processing for further audit testing.

During the audit, we examined the payroll records and reports for the period July 1, 2011, to January 31, 2013. To accomplish our audit the objective and obtain valid audit evidence, our procedures included the following steps:

- We reviewed Board minutes and the Board-approved policy handbook to determine if the District had policies for payroll processing.
- We interviewed and observed appropriate District officials and employees to learn about the procedures and timekeeping documentation used to process payrolls.
- We reviewed the Board-approved collective bargaining and employment agreements to gain an understanding of employee compensation and incentive payments for different classes of employees.
- We interviewed and observed appropriate District officials and employees to identify if the payroll processing duties are adequately segregated and reviewed all pertinent payroll records.

- We randomly selected 10 full-time employees and judgmentally selected three substitute employees¹⁰ for fiscal year 2011-12. We reviewed their signed employment agreements and/or time-tracking documentation to ensure that they were bona fide District employees.
- We judgmentally selected three substitute employees based on our computer-assisted analysis of the District's financial data for fiscal year 2011-12 to verify the legitimacy of their employment with the District.
- We judgmentally selected five key District employees, the Superintendent, Business Manager, District Treasurer, payroll clerk, and account clerk, and verified the accuracy of their gross pay by comparing the amounts they were paid on the December 28, 2012, payroll with their individual contracts and time-tracking documentation.
- We compared the gross pay for 10 employees¹¹ with their individual contracts and time-tracking documentation to verify the accuracy of the amounts paid.
- We judgmentally selected the employees paid the five highest one-time payments (separation and stipend payments) for the fiscal year 2011-12 and reviewed the payments to determine if they were calculated correctly.
- We reviewed the health insurance buy-out payments for 10 employees¹² for the fiscal year 2011-12 to determine if they were made to the appropriate employees and for the correct amount based on employment agreements.
- We reviewed payroll documentation for two pay periods from 2011-12 fiscal year and two pay periods from 2012-13 fiscal year to verify that proper payroll documentation was approved by District officials and department heads based on District policies and procedures.

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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

¹⁰ We used a random number generator to get our starting point and then chose every 16th employee to select 10 District employees. However, because the first 10 employees we selected did not include any substitute teachers, teacher aides, bus drivers or food service workers employed by the District, we expanded our sample by judgmentally selecting three of these type of District employees.

¹¹ We used a random number generator to get our starting point and then selected every 12th employee. We traced two employees to the October 21, 2011, and February 24, 2012 payrolls and eight employees to the December 28, 2012, payroll.

¹² We used a random number generator to get our starting point and then selected 10 consecutive employees.

APPENDIX C

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