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STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

June 2, 2015

James B. Milliken
Chancellor
City University of New York
205 East 42nd Street
New York, NY 10017

Re: CUNY SPS - Controls Over Bank
Accounts
Report 2014-S-78

Dear Chancellor Milliken:

Pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law, we examined controls over bank accounts at the City University of New York School of Professional Studies for the period January 1, 2008 through July 21, 2014. The objective of our audit was to determine whether there was fraud, waste, or abuse in the use of funds held in its bank accounts.

Background

The City University of New York School of Professional Studies (CUNY SPS) was founded in 2003 to meet the educational needs of working adults, organizations, and employers. In April 2014, CUNY SPS offered nine bachelor's degrees and six master's, as well as a number of certificate programs. The school's enrollment has grown to over 2,200 students in the credit-bearing programs and over 10,000 non-credit registrants each year. CUNY SPS's revenues increased from \$7.94 million in fiscal year 2009 to \$17.5 million in fiscal year 2013, and its expenditures increased from \$8.11 million to \$16.5 million for the same period. Over 70 percent of CUNY SPS's revenues come from tax levy allocations. As of December 1, 2013, CUNY SPS reported it had four bank accounts at two financial institutions. The four accounts were for Tuition and Fees, School Depository, Tax Levy funds, and the CUNY SPS Foundation.

Results of Audit

There was a lack of separation of duties in the handling of CUNY SPS finances, as well as poor internal controls over bank accounts held in the school's name. Consequently, a former Director of Business and Fiscal Operations (Business Director) at CUNY SPS had complete control over all aspects of the school's finances and bank accounts. Additionally, CUNY SPS lacked

adequate formal policies to open and close bank accounts. Consequently, the Business Director was able to obtain and sign checks for significant dollar amounts and use them to open two unauthorized bank accounts in the name of CUNY SPS. As of the end of our audit fieldwork, \$23,500 remained missing from a CUNY SPS account.

Unauthorized Bank Accounts

During our audit, officials informed us that the Business Director opened an unauthorized bank account in the college's name in December 2011. The Business Director was the sole signatory on the account that was opened with a \$50,000 check drawn on CUNY SPS's Tuition and Fees account. The unauthorized account was not discovered until 2013, after the Business Director was reassigned to a different position in CUNY.

We reviewed a copy of the cancelled check (for \$50,000) used to open the unauthorized account and determined that the check was requested and signed only by the Business Director, although CUNY policy requires dual signatures on checks for \$5,000 or more. During the four months after the account was opened, the Business Director withdrew amounts ranging from \$3,000 to \$6,000 at intervals of about two weeks. By April 2012, the balance of the unauthorized account was reduced to zero. We determined that the unauthorized transactions were not detected in a timely manner because there was no separation of duties in the fiscal operations of CUNY SPS.

Eventually, other senior SPS officials discovered the account and questioned the Business Director about the transactions. According to CUNY SPS officials, the Business Director claimed the cash was in his office to pay vendors at graduation. CUNY SPS officials indicated, however, that SPS does not pay any vendors in cash. The former employee eventually paid back the \$50,000, by making deposits into various CUNY SPS accounts, just before his employment was terminated.

In addition, we requested SPS officials to provide us with a list of all bank accounts held in the name of the college, and they provided us with a list of four accounts. However, when confirming these accounts with banks in the vicinity of CUNY SPS, we found five accounts (excluding the unauthorized account previously disclosed) in the school's name. CUNY SPS officials were unaware of the extra account. The Business Director opened this unauthorized account in July 2008 using \$5,000 (also taken from the Tuition and Fees account). The Business Director maintained this account for the next ten months, and deposited \$31,000 to it with funds from the Tuition and Fee account. However, the Business Director eventually withdrew the entire \$31,000 (mostly in increments of \$2,500). Although the Business Director subsequently returned \$12,500 of the total he withdrew, he did not pay back \$18,500 (\$31,000 - \$12,500) of the total taken.

In addition, CUNY SPS officials found a check (for \$5,000) written from the Tuition and Fees account that was cashed, and the funds were not accounted for. There is no indication that the funds in question were returned to SPS. As a result, there was a total of \$23,500 (\$18,500 + \$5,000) missing from the CUNY SPS Tuition and Fees account.

Poor Internal Controls

CUNY SPS management is responsible for implementing proper internal controls to protect the school's assets from misuse. We determined that internal controls over CUNY SPS finances were poor. Specifically, there were insufficient controls in place to prevent the opening of unauthorized accounts or to detect the existence of such accounts. As a result, funds were withdrawn from one CUNY SPS account and used to open unauthorized bank accounts in the school's name, as detailed previously in this report.

We attributed the creation and use of the unauthorized accounts to limitations in management's monitoring of critical CUNY SPS revenue and deposit functions. Monitoring is the review of an organization's activities and transactions to assess the quality of performance and to determine whether internal controls are effective. According to a CUNY SPS official, staff performed monthly reviews of bank statements. However, this review did not include pertinent steps (including revenue and bank statement reconciliations) that could have helped CUNY SPS officials to timely detect the creation and use of unauthorized accounts and transactions detailed in this report.

Further, CUNY SPS did not follow CUNY policies and procedures to open bank accounts in the name of a college. These policies require that colleges notify the University Controller prior to establishing a new bank account by submitting a form explaining the reason for opening the new account. However, the required notifications of new bank accounts were not made. In addition, CUNY officials would have expected the Business Director to request other CUNY SPS officials to sign signature cards for the accounts. However, because the Business Director wanted to maintain the secrecy of the unauthorized accounts, he did not request or obtain the signatures of other CUNY SPS officials for those accounts. We discussed our audit results with CUNY SPS officials, and they agreed with our recommendations to strengthen controls and indicated they will take steps to implement them.

Recommendations

1. Effectively separate the duties for administering bank accounts and related financial activities functions so that no person has excessive control over the deposit and disbursement cycle. Where duties cannot be adequately separated, develop and implement appropriate compensating controls.
2. Fully comply with prescribed procedures for opening new bank accounts and the monitoring of existing accounts. Develop and implement additional policies and procedures to administer bank accounts, as warranted.
3. Periodically reconcile tuition and fee revenue collections and deposits with amounts transferred to the State Treasury.

Audit Scope, Objective, and Methodology

We audited CUNY SPS controls over bank accounts for the period January 1, 2008 through July 21, 2014 to determine whether there was fraud, waste, or abuse in the use of funds held in CUNY SPS's bank accounts.

To accomplish our objective, we reviewed pertinent information and records about bank accounts opened in the name of the college. This included examinations of account signature cards, bank statements, and copies of cancelled checks. We also interviewed CUNY SPS officials to obtain an understanding of internal controls relevant to their bank accounts. In addition, we performed an analysis of selected banking transactions.

We conducted our audit in accordance with generally accepted government auditing standards. 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.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions, and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.

Reporting Requirements

We provided a draft copy of this report to CUNY officials for their review and formal comment. We considered officials' comments in preparing this report and have included them in their entirety at the end of it. In their response, CUNY officials agreed with our recommendations and indicated certain actions they have taken and will take to address them. Also, our rejoinders to certain CUNY comments are included in the report's State Comptroller's Comments.

Within 90 days after final release of this report, as required by Section 170 of the Executive Law, the Chancellor of the City University of New York shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons why.

Major contributors to this report were Abe Fish, Diane Gustard, Robert Tabi, Jean-Renel Estime, and Brenda Maynard.

We wish to thank CUNY SPS management and staff for the courtesies and cooperation they extended to our auditors during this audit.

Very truly yours,

Carmen Maldonado
Audit Director

cc: G. Taylor, CUNY
NYS Division of the Budget

Agency Comments



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March 11, 2015

Ms. Carmen Maldonado
Audit Director
Office of the State Comptroller
Division of State Government Accountability
123 William Street - 21st Floor
New York, NY 10038

Re: CUNY SPS—Controls Over Bank Accounts
Draft Report# 2014-S-78

Dear Ms. Maldonado:

We have reviewed the draft report on OSC's audit of bank account controls at the CUNY School of Professional Studies. We appreciate the opportunity to comment on the findings and address the report's recommendations.

*
Comment
1

We disagree that a lack of separation of duties or poor internal controls enabled the former Business Director to open the two unauthorized accounts and embezzle SPS funds. We also disagree that the former Business Director had complete control over all aspects of the school's finances and bank accounts.

The SPS finance operation is administered by several individuals who respectively have responsibility for the school's budget, bursar, accounts payable, payroll, purchasing, and other financial functions. The system of internal controls in these areas was designed to provide that, among other safeguards, no one individual had the ability to both initiate and authorize the same transaction. The instances of fraud committed by the former Business Director owed more to management override of otherwise sound internal control system design than to poor internal controls. Management override of internal controls is considered an inherent limitation of any internal control system. In fact, the AICPA refers to management override as "the Achilles' Heel of Fraud Prevention." Because an entity's system of internal control is the responsibility of management and because management designs the controls that are integral to the system, an unscrupulous manager is in a unique position to thwart internal control processes.¹ With SPS, management override of controls was not only the catalyst that allowed the fraud to occur, but it was also the reason the fraud was not immediately discovered.

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Comment
2


¹ For example, the cash withdrawals the former Business Director made from the unauthorized accounts circumvented the no-cash policy he himself established for SPS.

*See State Comptroller's Comments, page 9.

Another contributing factor to the commission of the fraud and the amount of time it took to discover it was failure by the banking institutions in which SPS maintained its accounts to follow established instructions governing check processing for the school's accounts or to observe prudent business practices concerning the establishment of an institutional account and subsequent transactions attempted against the account.

*
Comment
3

The former Business Manager requested that the school's Bursar issue a \$50,000 check made payable to SPS under the pretext that the check was to fund another program of the school. That check was made against an account in a bank that had instructions that checks of that dollar amount required dual signatures. When the former Business Director deposited that check into the unauthorized account at the second bank, the check should have been dishonored by the originating bank. The bank's failure to do that constituted a breakdown of a critical control feature. Moreover, in permitting the former Business Director to open the unauthorized accounts in the second bank as the sole signatory when all other SPS accounts in the same bank had multiple signatories, and by allowing the former Business Director to make cash withdrawals against the unauthorized accounts in monthly increments just under the \$10,000 threshold (structured withdrawals), arguably to avoid the federal reporting requirements prescribed under the Bank Secrecy Act, the second bank facilitated the fraud and contravened the school's internal control safeguards.

*
Comment
3

A final point concerning the second bank, the one in which the unauthorized accounts were opened, is that when SPS made an initial request to the bank for a listing of all SPS-related bank accounts, neither of the unauthorized accounts was included in the original listing returned by the bank. It was only by dint of the work of the Associate Dean for Administration and his accounting manager who examined the accounts after the former Business Director's departure that bank eventually reported one of the unauthorized accounts. The second unauthorized account was appreciatively discovered by the OSC audit team and investigators, but OSC has subpoena power and other means for compelling the production of account information from banks that SPS does not have.

*
Comment
4

With respect to the adequacy of SPS's internal controls, the report cites the former Business Director's opening of the unauthorized accounts as evidence that SPS did not follow CUNY's policies and procedures for opening bank accounts. We believe that this finding mistakenly imputes the actions of a fraud perpetrator to the school as a whole, when in fact all of the valid accounts were opened in accordance with CUNY policy and procedures. Contrary to what the report indicates, the former Business Director did not request that SPS officials sign signature cards for the unauthorized accounts. He intended to keep those accounts secret so that he might enrich himself. In this regard, he acted in derogation of the CUNY policy and procedures that SPS demonstrably observed for its valid accounts. We do agree, however, that a more timely reconciliation of tuition and fee transfers might have enabled SPS to more readily discover the fraud.

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Comment
5

Recommendations

Recommendation 1

Effectively separate the duties for administering bank accounts and related financial activities functions so that no person has excessive control over the deposit and disbursement cycle. Where duties cannot be adequately separated, develop and implement appropriate compensating controls

Response

SPS agrees with this recommendation. The schools has hired a full-time accountant who, in accordance with accepted accounting practices, conducts monthly reconciliations of all institutional bank accounts.

Recommendation 2

Fully comply with prescribed procedures for opening new bank accounts and the monitoring of existing accounts. Develop and implement additional policies and procedures to administer bank accounts, as warranted.

Response

SPS agrees with this recommendation, but as described above, SPS followed prescribed procedures for all valid SPS bank accounts. To strengthen practices, SPS separated administrative duties for the administration of institutional bank accounts and related financial activities functions, thereby ensuring no one person has excessive control over the opening/closing of bank accounts, or over daily transactions such as deposits and disbursements.

Recommendation 3

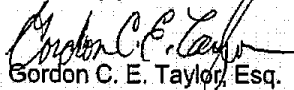
Periodically reconcile tuition fee revenue collections and deposits with amounts transferred to the State Treasury.

Response

SPS agrees with this recommendation. SPS will perform more timely reconciliations and will ensure that no one individual has exclusive oversight over the process.

Thank you again for the opportunity to respond to the draft report. If you have additional questions, please do not hesitate to contact me.

Very truly yours,



Gordon C. E. Taylor, Esq.
University Executive Director

cc: Chancellor James B. Milliken
Executive Vice Chancellor and COO Allan H. Dobrin
Vice Chancellor Matthew J. Sapienza
SPS Dean John Mogulescu

State Comptroller's Comments

1. We maintain that poor internal controls (including a lack of separation of duties) enabled the former SPS Business Director to open and use the two unauthorized bank accounts without timely detection. As detailed in our report, there were limitations in critical CUNY SPS revenue and deposit functions. Consequently, we recommended that CUNY SPS periodically reconcile tuition and fee collections and deposits with amounts transferred to the State Treasury. In addition, although CUNY SPS staff reviewed monthly bank statements, formal bank reconciliations were not performed. Ideally, the aforementioned reconciliations should be performed by someone other than the employee(s) who opened the accounts and/or make deposits to and payments from them. In their response, CUNY officials indicated that they hired an accountant to perform monthly bank reconciliations, and they agreed to separate pertinent financial administration duties. Also, officials did not annually survey nearby banks, as otherwise prescribed by SUNY policy, to identify potential unauthorized accounts (including, e.g., any accounts using CUNY SPS's federal ID number).
2. We acknowledge that management override of prescribed procedures can undermine an otherwise adequate system of internal controls. However, as detailed in our report and State Comptroller's Comment 1, there were significant weaknesses in certain CUNY SPS controls which enabled the former Business Director to open the two unauthorized accounts and divert CUNY SPS funds to them for his personal use without timely detection.
3. Regardless of the standard procedures used by the bank where the unauthorized accounts were opened, CUNY officials should have implemented sufficient controls to prevent and/or detect such accounts. For example, CUNY SPS officials should have required the bank to follow a prescribed protocol to open or close an account in the name of CUNY SPS. In addition, as previously detailed in the report and State Comptroller's Comment 1, there were significant weaknesses in other applicable CUNY SPS controls.
4. We acknowledge that valid CUNY SPS bank accounts were opened according to applicable CUNY policies and procedures. Nevertheless, we maintain that the two unauthorized accounts were not opened in compliance with established CUNY policies and procedures. For example, CUNY campuses are required to formally notify the University Controller prior to opening a new bank account and explain the need for the account. However, there were no such notifications for the two unauthorized accounts.
5. Based on CUNY's comments, we revised our report as appropriate to improve the technical accuracy of our presentation of the matter in question.