



New Suffolk Common School District Selected Financial Operations

Report of Examination

Period Covered:

July 1, 2011 — March 31, 2013

2013M-197



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

December 2013

Dear 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 the New Suffolk Common School District, entitled Selected 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 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*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

The New Suffolk Common School District (District) is located in the Town of Southold, Suffolk County. The District is governed by the Board of Trustees (Board) which comprises three 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 District's chief executive officer and is responsible, along with the appointed Treasurer, for the District's day-to-day management under the Board's direction. The Treasurer is the chief accounting officer and is responsible for the District's finances, including maintaining the accounting records and reports.

The District operated one school during the 2011-12 and 2012-13 fiscal years, with about 20 students attending kindergarten through grade six and seven employees. Students in grades 7-12 attend other school districts to which the District pays tuition. The District's actual expenditures for fiscal years 2011-12 and 2012-13 were \$942,704 and \$894,757, respectively, which were funded primarily with real property taxes. Budgeted expenditures for the 2013-14 fiscal year were \$946,175.

Scope and Objective

The objective of our audit was to evaluate selected District financial operations for the period July 1, 2011 through March 31, 2013. We extended our scope to the 2007-08 fiscal year to analyze budgeting practices, fund balance trends and reserve account balances and to the 2013-14 fiscal year to analyze budgeting practices. Our audit addressed the following related questions:

- Did the Board adopt balanced budgets and adequately monitor financial operations?
- Did the Board properly compensate the former Superintendent?
- Does the Board properly audit claims to ensure that District assets are safeguarded?

Audit Results

The District retained excessive fund balance, exceeding the permitted statutory limit, in each of the fiscal years 2007-08 through 2011-12 by as much as \$228,694. Although the Board President stated the unexpended surplus fund balance¹ was for cash flow purposes, none of the adopted budgets included a planned balance as is permitted by law.

¹ The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted and unrestricted (comprising committed, assigned and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term "unexpended surplus funds" to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54) and is now classified as unrestricted, less any amounts appropriated for the ensuing year's budget (after Statement 54).

District officials have not properly budgeted for tuition and teacher personnel salaries. Instead, they improperly included appropriations from unofficial reserves in their budgets. Even with the addition of the improper tuition reserve appropriations, District officials still under-budgeted tuition appropriations for fiscal years 2008-09 through 2011-12 by \$151,113. Conversely, with the inclusion of the improper teacher salaries reserve appropriation, teacher salaries were over-budgeted by \$88,554 in the 2011-12 fiscal year. Currently, there is no authority under General Municipal or Education Law allowing the creation of a reserve for tuition or teacher salaries.

District officials consistently levied more than was needed for budgeted appropriations between fiscal years 2007-08 through 2012-13 because they included an additional amount to the tax levy for “General Fund Balance” which was not needed to fund appropriations. This has resulted in a total increased tax levy amount of at least \$124,170 for the five-year period.

The Board did not provide guidance or a detailed written job description to guide the Treasurer in the proper performance of her job. We found numerous deficiencies with the District’s accounting records and with the performance of the Treasurer’s duties. As a result, the Board does not have complete and accurate financial information to make informed decisions about the District’s finances.

The Board compensated the former Superintendent \$28,687 in the 2011-12 fiscal year through vendor disbursements as if he were an independent contractor rather than through payroll. This included an extra \$2,167 which was not provided for in his contract. The failure to withhold taxes on these earnings could expose the District to liability from Federal and State tax authorities.

Finally, we found that the Board does not audit the claims nor do they receive an abstract of claims for approval. Our test of 50 claims totaling \$42,592 found that none were audited by the Board. We also found that 31 claims, totaling \$24,766, were not approved by the individuals who initiated the purchases or by any other District official, did not have sufficient support to enable a proper audit and/or did not appear to be for valid District purposes. Without properly auditing and approving all claims before payment, the Board does not have adequate assurance that the purchases were properly approved or that the goods and services were actually received. In addition, by routinely paying claims without the Board’s audit, there is an increased risk of the misuse or diversion of District funds.

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 plan to take corrective action. Appendix B includes our comments on issues raised in the District’s response letter.

Introduction

Background

The New Suffolk Common School District (District) is located in the Town of Southold, Suffolk County. The District is governed by the Board of Trustees (Board) which comprises three 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 District's chief executive officer and is responsible, along with the appointed Treasurer, for the District's day-to-day management under the Board's direction. The Treasurer is the chief accounting officer and is responsible for the District's finances, including maintaining the accounting records and reports.

The District operated one school during the 2011-12 and 2012-13 fiscal years, with about 20 students attending kindergarten through grade six and seven employees. Students in grades 7-12 attend other school districts to which the District pays tuition. The District's actual expenditures for fiscal years 2011-12 and 2012-13 were \$942,704 and \$894,757, respectively, which were funded primarily with real property taxes. Budgeted expenditures for the 2013-14 fiscal year were \$946,175.

Objective

The objective of our audit was to evaluate selected District financial operations. Our audit addressed the following related questions:

- Did the Board adopt balanced budgets and adequately monitor financial operations?
- Did the Board properly compensate the former Superintendent?
- Does the Board properly audit claims to ensure that District assets are safeguarded?

Scope and Methodology

We examined the District's financial operations for the period July 1, 2011 to March 31, 2013. We extended our scope to the 2007-08 fiscal year to analyze budgeting practices, fund balance trends and reserve account balances and to the 2013-14 fiscal year to analyze budgeting practices.

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 is 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. District officials generally agreed with our recommendations and indicated they plan to take corrective action. Appendix B includes our comments on 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, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. 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 at the District.

Financial Condition

The Board is responsible for making sound financial decisions that are in the best interests of the District, the students it serves and the taxpayers who fund the District's programs and operations. Sound budgeting practices based on accurate estimates, coupled with prudent fund balance management, ensure that sufficient funding will be available to sustain operations, address unexpected occurrences and satisfy long-term obligations or future expenditures.

The general fund is the District's main operating fund in which financial transactions for its education programs and other operating activities are recorded. The general fund's financial condition depends on the Board's ability to develop realistic budgets and monitor the District's financial operations throughout the fiscal year. Further, the Board is required to obtain voter approval for its budgets. In preparing the general fund budget, the Board is responsible for estimating what the District will spend and what it will receive in general fund budget revenue (e.g., State aid), estimating how much fund balance will be available at fiscal year-end and, to balance the budget, determining what the expected tax levy will be. Accurate estimates help ensure that the real property tax levy is no greater than necessary.

Real Property Tax Law allows a district to retain a limited amount of fund balance (up to 4 percent of the ensuing year's budget) as unexpended surplus. Fund balance in excess of that amount must be used to fund a portion of the next year's appropriations, thereby reducing the tax levy, or to fund legally established reserves. There is no authority for a school board to budget for other than legally allowed reserves.

The District retained excessive fund balance, exceeding the permitted statutory limit, for fiscal years 2007-08 through 2011-12 by as much as \$228,694. District officials have improperly budgeted for tuition and teacher salaries by including unallowed reserve appropriations in their budgets. District officials also levied more property taxes than were needed for budgeted appropriations between the fiscal years of 2007-08 through 2012-13. Finally, we found numerous deficiencies with the District's accounting records and with the performance of the Treasurer's duties. The Treasurer did not provide the Board with accurate and complete financial reports which impeded the Board's ability to create accurate budgets and monitor those budgets.

Fund Balance

Fund balance is the difference between revenues and expenditures accumulated over a given period of time. It can provide a cushion against unforeseen events and economic fluctuations and provide cash flow during the year. Additional amounts can be restricted or reserved, for particular purposes, or appropriated to reduce taxes. Restricted fund balance represents moneys that the District has set aside and may use only for specific purposes. Unexpended surplus funds² represent uncommitted funds and may be used for cash flow purposes and unanticipated expenditures and/or revenue shortfalls. The estimation of fund balance is an integral part of the budget process. Fund balance can be assigned as a funding source in the budget or retained as unassigned. Any fund balance in excess of 4 percent of the ensuing year's budget must be used to lower property taxes or transferred to legally established reserve funds that are reasonable and in compliance with statutory directives. When fund balance is assigned as a funding source, District officials are essentially establishing a planned operating deficit for the ensuing fiscal year, financed by the amount of the assigned fund balance.

With voter approval, districts may raise an amount, in addition to the amount of the budget, in the tax levy in one fiscal year for cash flow purposes to pay for expenses of the succeeding fiscal year. Raising such an amount establishes a planned balance. The primary purpose of a planned balance is to avoid the cost of borrowing to meet expenses during the first part of the fiscal year before State aid and tax moneys are received. Education Law limits the planned balance of a district budget to the amount necessary to meet expenses during the first 120 days of the fiscal year following the fiscal year in which such tax is collected. The Suffolk County Tax Act further limits this amount to no more than 30 percent of the budget.

District officials have chosen to retain excess fund balance rather than return it to the taxpayers. As a result, the District exceeded the unexpended surplus fund limit in each of the fiscal years 2007-08 through 2011-12 by as much as \$228,694.

² The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted and unrestricted (comprising committed, assigned and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term "unexpended surplus funds" to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54) and is now classified as unrestricted, less any amounts appropriated for the ensuing year's budget (after Statement 54).

Table 1: Excess Unexpended Surplus Funds					
	2007-08	2008-09	2009-10	2010-11	2011-12
Unexpended Surplus Funds	\$240,756	\$210,253	\$225,621	\$218,442	\$255,820
Ensuing Year's Budgeted Appropriations	\$673,857	\$729,587	\$756,762	\$645,330	\$678,162
Limit for Unexpended Surplus Funds	\$20,216	\$29,183	\$30,270	\$25,813	\$27,126
Excess Surplus Funds	\$220,540	\$181,070	\$195,351	\$192,629	\$228,694
Actual Percentage Retained	35.73%	28.82%	29.81%	33.85%	37.72%

District officials assigned fund balance of at least \$11,085 during the 2007-08 through the 2010-11 fiscal years. However, even after assigning fund balance, the unexpended surplus funds still significantly exceeded the 4 percent statutory maximum. For the 2011-12 and the 2012-13 fiscal years, the District again exceeded the 4 percent statutory maximum because it did not assign any fund balance to the succeeding fiscal year but had a fund balance of \$228,694 and \$244,872, respectively, retaining about 38 and 26 percent of the following year's budget.

District officials did not attempt to reduce the fund balance to the 4 percent maximum. The Board President told us that he was unaware that the accumulation of surplus funds is included in the 4 percent calculation and that he believes the unexpended surplus funds are not fund balance, but rather an "operating balance," to be used to pay the District's first six months of bills so the District does not have to borrow money. Although the Board President stated the excess unassigned fund balance is for cash flow purposes, none of the adopted budgets included a planned balance as is permitted by Law.

Lastly, we found that taxpayers were not informed of these surplus funds. Budget mailings sent to taxpayers to inform them of the District's budget plans did not include fund balance amounts, as required, nor does the Board ever receive fund balance projections as part of the Treasurer's reports at Board meetings. This lack of transparency limits the ability of taxpayers and the Board to make informed budget decisions.

Unofficial Reserves

School districts may establish reserve funds to retain a portion of fund balance for specific purposes but must do so in compliance with statutory directives. While school districts are legally allowed to establish reserve funds, there is no authority under General Municipal or Education Law for a school board to include in its budget what

would amount to an unofficial reserve fund to pay for expenditures that were not included in the budget.

District officials have been improperly including unofficial reserve appropriations or contingency lines in their budgets. The District’s budgets for the 2007-08 through 2011-12 fiscal years have improperly included a “tuition reserve” appropriation which the Board President says is contingency moneys for additional, unexpected students who may move into the District after the budget adoption. However, even with the addition of the tuition reserve appropriation, the District has still under-budgeted tuition appropriations for fiscal years 2008-09 through 2011-12.

	2007-08	2008-09	2009-10	2010-11	2011-12
Budgeted Tuition	\$237,815	\$233,823	\$182,205	\$159,710	\$138,900
Actual Tuition	\$244,892	\$258,912	\$202,050	\$270,822	\$232,409
Difference	(\$7,077)	(\$25,089)	(\$19,845)	(\$111,112)	(\$93,509)
Unofficial Tuition Reserve Appropriations	\$28,500	\$15,000	\$16,500	\$31,942	\$35,000
Over/(Under) Budgeted Amount	\$21,423	(\$10,089)	(\$3,345)	(\$79,170)	(\$58,509)

Further, the 2012-13 budget includes budgeted tuition of \$175,760 plus a \$36,000 tuition reserve appropriation. Even with the addition of the unofficial reserve, the District has under-budgeted tuition by a total of \$25,118 based on the actual tuition expenditures of \$236,878.

In addition, District officials improperly included \$66,838 in the 2011-12 budget and \$55,075 in the 2012-13 budget in a second reserve appropriation, titled “teacher personnel reserve.” According to the Board President, this money would be used if the District does not ultimately receive full reimbursement from the State for the salary of a District teacher on special assignment. We analyzed the budgeted personnel costs and confirmed that the District did not use these additional appropriations for their intended purpose.

- In the 2011-12 fiscal year, the District budgeted \$348,196 for personnel costs. With the addition of the unofficial teacher personnel reserve appropriation, a total of \$415,034 was available. Actual personnel costs for this fiscal year were only \$326,480, a difference of \$88,554. The unofficial teacher personnel reserve appropriation was not needed, which should have resulted in an operating surplus. However, the

District ended the 2011-12 fiscal year with an operating deficit of \$73,976, indicating that they used this unofficial reserve appropriation for a purpose other than intended.

- In the 2012-13 fiscal year, the District should have had an operating surplus of at least \$55,075, which is the amount of the unofficial teacher personnel reserve appropriation included in the budget. However, rather than an operating surplus, District officials ended the fiscal year with an operating deficit of \$12,393. Therefore, they have again used the unofficial reserve for other than its intended purpose.

By continually using unofficial reserve funds to offset the under- and over-budgeting for costs, instead of properly budgeting for tuition and personnel costs, District officials are not providing transparency to District residents who vote on and approve the District's budget.

Tax Levy

The Board is responsible for preparing and presenting the District budget for public vote. In preparing the budget, the Board must estimate District appropriations, what the District will receive in revenue (e.g., State aid), how much fund balance will be available at fiscal year-end (some or all of which may be used to fund the ensuing year's appropriations) and what the expected tax levy will be. Accurate estimates help ensure that the levy of real property taxes is not greater than necessary.

The District's tax levy has consistently been in excess of what was needed for budgeted appropriations. Generally, a district's tax levy is the difference between the total estimated appropriations and the total expected revenues. However, District officials calculate appropriations less revenues and then add an additional amount to the tax levy for "General Fund Balance" (or Operating Balance Reserve). The Board President told us that this amount is a planned contingency amount available for any other unexpected expenditures which may arise during the fiscal year. This "General Fund Balance" amount is not included as a projected appropriation or included in the total budget amount presented to taxpayers. Instead, it is simply an additional amount added directly to the amount to be raised by the property tax levy. Over the six budget years reviewed, the District levied a total of \$124,170 more than was needed for the budgeted appropriations because of this contingency amount that has consistently been added to the tax levy.

Table 3: Excessive Tax Levy						
	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
Budgeted Appropriations^a	\$629,025	\$622,432	\$746,087	\$899,704	\$747,168	\$769,237
Anticipated Non-Tax Revenues	\$73,494	\$55,621	\$172,465	\$121,124	\$129,526	\$46,142
Calculated Levy	\$555,531	\$566,811	\$573,622	\$778,580	\$617,642	\$723,095
Actual Levy	\$567,531	\$579,811	\$592,567	\$826,305	\$637,642	\$735,595
Excess Tax Levy	\$12,000	\$13,000	\$18,945	\$47,725	\$20,000	\$12,500

^a Includes unofficial reserve appropriations

For example, in the 2011-12 budget, the District included appropriations of \$747,168³ and estimated revenues of \$129,526, a difference of \$617,642 which should represent the necessary tax levy. However, the Board added an additional \$20,000 to this amount for a “General Fund Balance” contingency, levying taxes of \$637,642. The 2012-13 budget included appropriations of \$769,237⁴ and estimated revenues of \$46,142, for a difference of \$723,095, the amount of taxes that should have been levied. Instead, the Board added an additional \$12,500 to the tax levy for a “General Fund Balance” contingency, levying \$735,595 in taxes.

As a result, between the fiscal years of 2007-08 through 2012-13, the District has levied over \$124,000 more tax than was needed for budgeted appropriations.

Records and Reports

The Board is responsible for the District’s overall financial management, including monitoring and evaluating financial condition. To adequately evaluate financial condition, it is essential that complete, accurate and timely accounting records are maintained to properly account for and report the District’s financial condition and activities. The lack of adequate accounting records makes it difficult for the Superintendent and the Board to evaluate the District’s financial activities, and inaccurate records can obscure the District’s true financial condition.

The Board did not provide general guidance or a detailed written job description to guide the Treasurer in the proper performance of her job. In addition, there are no written procedures related to the Treasurer’s duties to guide her in the day-to-day financial operations required. The Treasurer told us that she does not know how to prepare and post journal entries, nor does she maintain a physical

³ Includes the \$35,000 unofficial tuition reserve appropriation and the \$66,838 unofficial teacher personnel reserve appropriation
⁴ Includes the \$36,000 unofficial tuition reserve appropriation and the \$55,075 unofficial teacher personnel reserve appropriation

record of journal entries made or evidence of approval or supporting documentation. Instead, she just does what the Board verbally directs her to do. In addition, the Treasurer does not provide the Board with adequate financial reports, such as fund balance projections and cash flow analysis.

Our review of the accounting records identified problems with account balances and postings resulting in an inaccurate depiction of the District's financial activity. For example, the fund balance in the accounting system was not accurate for the 2011-12 fiscal year. When asked the reason for the discrepancy between the accounting records and the amounts reported on the annual financial report⁵ submitted to the New York State Education Department, the Treasurer was unable to provide us with an explanation. The accountant informed us that discrepancies resulted from the Treasurer accidentally deleting year-end journal entries. The Treasurer told us that she was unable to make corrections because she does not know how to prepare or adjust journal entries, and the correction would be made when the accountant was available the following month.

In addition, the Treasurer did not document the journal entries made, did not maintain supporting documentation and there was no evidence of supervisory approval. For example, the Treasurer was unable to provide support for two entries totaling \$15,440. When asked what the entries were for, she provided a verbal explanation which seemed reasonable. However, the entries are not supported by invoices, bills or any other documentation to show the need for the adjustment.

The incomplete and inaccurate financial reports diminish the Board's ability to properly manage the District's financial resources. Without documented authorization of journal entries, there is an increased risk that errors or irregularities could occur without being detected and corrected.

Recommendations

1. The Board should maintain unexpended surplus funds within the allowed legal limits.
2. District officials should develop a plan to use the unexpended surplus fund balance identified in this report in a manner that benefits District taxpayers. Such uses could include, but are not limited to:
 - Establishing necessary reserves,
 - Financing one-time expenditures, and
 - Reducing property taxes.

⁵ Form ST-3

3. If the Board intends to retain moneys for cash flow purposes, it should do so as outlined in the law, by using a planned balance and returning such to taxpayers in the following year's budget.
4. The Board should disclose the total fund balance amounts on the property tax report card mailed to taxpayers during budget season.
5. District officials should develop a plan to budget for appropriations in a way that does not include unofficial reserves.
6. District officials should develop a plan to budget for moneys needed that does not increase the tax levy to a rate that is higher than necessary.
7. The Board should develop a written job description outlining specific duties required for the Treasurer.
8. The Board should provide the Treasurer with appropriate guidance and training to perform her duties.
9. The Board should ensure that the District's accounting records are accurate and contain sufficient detail to support general ledger balances.
10. The Treasurer should provide the Board with complete financial reports.
11. The Board should ensure that all journal entries are adequately supported prior to being recorded in the computer system.

Former Superintendent's Compensation

As a rule, officers and employees of a school district should be compensated through the payroll system. Therefore, as the District's chief executive officer, the Superintendent generally should be paid through the District's payroll system. Use of the payroll system facilitates proper Federal and State tax reporting and withholding, as well as proper reporting to the State retirement systems.

The District contracted with an individual to serve as its Superintendent each fiscal year from August 2005 through the 2011-12 fiscal year.⁶ According to the 2011-12 contract, the former Superintendent's compensation was \$26,520, comprised of the premium for an existing long-term health care policy and salary. The employment contract also provided for up to \$400 per year to be paid by the Board directly to a dental insurance company.

Since his employment in August 2005, the former Superintendent received his salary through vendor disbursements, rather than through the District's payroll system. The District issued a check to the former Superintendent each month although he did not submit payment vouchers to the District. The former Superintendent was also issued an Internal Revenue Service (IRS) Form MISC-1099 (which can be used to report payments to independent contractors). However, payments for the premium on the long-term health care policy and dental insurance were not included in the amount on the IRS Form MISC-1099. According to the Board President, the former Superintendent was not paid through payroll disbursements and the amounts of the premiums on the policy and dental insurance were not included on the IRS Form MISC-1099 because the former Superintendent receives Social Security benefits and a pension. The Board President also indicated that, had these amounts been reported to the IRS, they would have increased his compensation to a level which would have resulted in the former Superintendent's Social Security benefits and pension amounts being reduced.⁷

Although we are not aware of any statutory requirement that the former Superintendent be paid through the District's payroll system, by compensating him through vendor disbursements, the District did

⁶ For the 2010-11 and 2011-12 school year, the title of Principal was also included in the contract. Although outside our audit scope, we note that this raises the issue of whether an individual may simultaneously serve as both Superintendent and Principal.

⁷ We have been informed that the former Superintendent is not a member of the New York State and Local Retirement System. Whether this individual is properly receiving any other public retirement benefit is beyond the scope of this audit.

not withhold taxes from his earnings. The failure to withhold taxes on these earnings could expose the District to liability from Federal and State tax authorities.

In addition, we found nothing in the Board minutes indicating that the Board approved the former Superintendent's 2011-12 contract or salary. Instead, the contract was signed by the Board President. The Board President informed us that the Board did not vote on the Superintendent's contract but simply approved his salary by adopting the annual budget, which includes the Superintendent's salary. The amount shown in the budget agrees with the amount stated in the contract.

Furthermore, although the former Superintendent's employment agreement indicates that for the performance of his services he was to receive a total amount of \$26,520, he was actually paid \$28,687 in salary for the 2011-12 school year. The extra \$2,167 in compensation is not provided for in the employment agreement. Instead, the additional compensation was supported by a handwritten note from the Treasurer stating "final check for June 2012 at 2010/11 rate as negotiated." The Board President explained that the additional compensation was for a month in a previous year that the District had not paid the former Superintendent. District officials were unable to provide any additional support for this explanation and our review of a vendor history report from September 2005 through June 2011 provided by the Treasurer did not identify an unpaid month.

Recommendations

12. The Board should ensure that individuals who serve as officers or employees of the District be compensated through the payroll system.
13. The Treasurer should maintain relevant documentation to help ensure that compensation is paid in accordance with applicable contracts.
14. The Board should formally authorize, by resolution, all employment contracts, compensation and fringe benefits afforded all officers and employees, including the Superintendent.
15. The Board should review the circumstances surrounding the extra \$2,167 in compensation to the former Superintendent and attempt to recover it, if appropriate.

Audit of Claims

The audit and approval of claims is one of the most critical elements of the District's internal control system. Education Law requires the Board to audit and approve all claims against the District prior to directing the Treasurer to pay them. One exception is that the Board may, by resolution, authorize payment in advance of audit for claims related to public utility services (electric, gas, water, sewer and telephone), postage, freight and express charges. However, claims for such prepayments must be presented at the next regular Board meeting for audit.

It is essential for the Board to conduct a thorough review of each claim to determine whether it is a proper and valid charge, to verify that each purchase was properly authorized, and to ensure that each claim is itemized, including a receipt for the goods or services purchased, and confirmation of receipt. It is important that the Board's authorization to pay claims is documented. Board approval should be documented by the signatures or initials of individual Trustees on the claims and by entries in the Board minutes.

Further, documentation is provided generally through the preparation of an abstract of audited claims. An abstract is a listing of all claims audited and approved for payment.⁸ Once prepared and executed, the abstract of audited claims should be forwarded to the Treasurer, authorizing the Treasurer to pay the claims. Prior to disbursement, the Treasurer should verify that all claims listed have been audited and approved for the amounts listed. The Treasurer, as the chief fiscal officer, must ensure that disbursements are made only after proper Board audit, that disbursements are supported by appropriate documentation and that District resources are only used for valid District purposes.

The District paid 611 claims, totaling \$931,162, during the audit period July 1, 2011 through March 31, 2013. District officials told us that the Board does not audit claims and the Treasurer does not prepare an abstract of claims. Furthermore, the Board has not authorized, by resolution, claims which may be paid in advance of audit.

⁸ Minimum requirements for an abstract generally include the claim number, name of claimant, amount approved, fund and appropriation account chargeable. Abstracts can be prepared weekly, biweekly, bimonthly or monthly, depending on when claims are audited.

Because the Board does not audit the claims, we selected 50 claims,⁹ totaling \$42,592, paid during the audit period. We reviewed supporting documentation to determine if the claims appeared to be for legitimate District purposes and if they were audited prior to payment. We verified that none of them were audited by the Board. Further review of the claims revealed that:¹⁰

- Thirty-one claims, totaling \$24,766, were not approved by the individual who initiated the purchase or by any other District official. For example, an invoice for \$384 for diesel fuel purchases had no signature or initials on the invoice to confirm its accuracy or approval, nor did it include the individual receipts printed from the service station from which the fuel was purchased.
- Twelve claims, totaling \$7,865, did not have sufficient support to enable a proper audit. For example, a \$917 disbursement to a local restaurant included only a typed sheet of paper identifying that dinner for 21 people, plus a 20 percent service charge, was purchased for a total of \$809. There was a handwritten addition to the total of \$108 but no explanation as to why the total bill had increased. The sheet of paper was not on any letterhead and an itemized receipt was not attached. Further, there was no signature or initials of a District official approving the purchase.
- Five claims, totaling \$2,712, did not appear to be for a valid District purpose. For example, a \$1,152 disbursement to a local restaurant was a handwritten check which simply stated “staff dinner.” The support attached to the check stub was a handwritten receipt which stated 24 people multiplied by \$40 per person with an added tip. A detailed receipt was not available. There was no signature or initials of a District official approving the purchase and the business reason for the dinner was not identified. The other payments were made to two restaurants, a florist and an individual for a cake.

Without properly auditing and approving all claims before payment, the Board does not have adequate assurance that the purchases were properly approved or that the goods and services were actually received. In addition, by routinely paying claims without the Board’s audit, there is an increased risk of the misuse or diversion of District funds.

⁹ Twenty-three judgmentally selected based on vendor name and 27 randomly selected using a random number generator

¹⁰ Some claims have multiple deficiencies

Recommendations

16. The Treasurer should prepare an abstract of claims which includes, at a minimum, the claim number, name of claimant, dollar amount, fund and appropriation account chargeable. This abstract should be signed by the Board members auditing the claims and should direct the Treasurer to disburse funds accordingly.
17. The Board should ensure that all claims are audited and approved before the Treasurer pays the claims. Any claims allowed by law and authorized by Board resolution for the Treasurer to pay prior to audit should subsequently be presented to the Board for audit and approval.
18. The Board should ensure that each claim is sufficiently itemized and contains the necessary supporting documentation to ensure that it is a proper District charge.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

The District officials' response to this audit can be found on the following pages. As part of their response, District officials refer to exhibits that are not included with the final report. We did not include these exhibits because the information contained in the District officials' response was sufficient to address the findings in the report.

In addition, the District's response letter refers to page numbers that appeared in the draft report. The page numbers have changed during the formatting of this final report.

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BOARD OF TRUSTEES

TONY DILL, PRESIDENT

JOSEPH POLASHOCK, VICE PRESIDENT

BROOKE DAILEY, MEMBER

MICHAEL COMANDA, SUPERINTENDENT

As per your letter dated November 8, 2013 (attached) and the guidance document entitled "Responding to an OSC Audit Report" (attached), please consider the following to be the New Suffolk Common School District's audit response.

From this document and our conversations with the auditors assigned to this project, it is my understanding an audit response should express the district's position regarding the draft findings and recommendations. In brief, herein is our position.

1. We do not dispute the technical findings included in the report.
2. Prior to receiving your report, multiple steps had already been taken to correct issues discussed during and at the conclusion of the audit. Specifically these steps include:
 - a. Adoption of Payroll Policy #6800
 - b. Adoption of Sick Bank Policy #5119
 - c. Adoption of Investment Policy #4300
 - d. Adoption of Staff Internet Usage Policy #7534
 - e. Adoption of Breach Notification Policy #5221
 - f. Adoption of Capital Asset Management [Policy] # 4112
 - g. Significant work [toward] realignment of current financial statements and budget procedures.
3. Following authorization by the Board of Trustees of the additional expense involved, we are currently in the process of interviewing properly credentialed candidates for the new position of School Business Administrator. We expect this individual will provide the Board with a more comprehensive overview of district finances and guide the restructuring of our budget format so as to bring it into alignment with the audit findings (greater detail will be given in the corrective action plan).

Although we accept the technical findings and recommendations in the draft report, we are upset and disappointed by the manner in which the report characterizes several of the errors identified. None of these characterizations are necessary to explain the nature of the error being cited and, although technically correct and understandable to an accounting professional, all are misleading and potentially inflammatory to the lay public. Specifically I refer to the description of our budgeting process and format as "lacking transparency" (pages 10, 11 and 12) and the implication that the district has levied excessive and unnecessary taxes (page 13).

See
Note 1
Page 24

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The budgeting format we have used for the past ten years was developed by a group of district residents as a direct response to their extreme displeasure with the prior use of a format more in line with accepted standards. Because the earlier format only reported past budget appropriations and not actual expenses, it was perceived by our voters as lacking transparency. The public felt that going to an expense based format would, in fact, greatly improve transparency and afford district voters a clear view of how their money was actually being spent.

Although we understand this format incorrectly labels some expense lines and fails to include the General Fund Balance, it is nevertheless viewed by our residents as something transparent and understandable. From discussions with the auditors, we believe that, if afforded the chance by the public, modifications can quietly be made to the expense based format they understand that will bring it into compliance with the necessary laws and accounting standards. However that can only be accomplished with their support and acquiescence. That support will be very difficult to muster if the final audit report describes as “lacking transparency” the very approach they developed and believe affords greater transparency.

Similarly we believe the implication that our public has been overtaxed can be very misleading to a lay person. We understand that several reserve accounts were established and a lump sum general contingency included in the budget all of which were not in accordance with either the law or accepted regulations and principles. Consequently it was technically incorrect to include them in the amount to be raised from taxes and, on that basis, the resulting tax rate was too high.

Our discussions with the auditors, however, revealed that, had we chosen the correct line item titles or concealed contingency amounts in inflated expense projections, all these appropriations would have been considered proper. Thus the amount to be raised from taxes and the tax rate would have remained unchanged. So while from an accounting view, the rate may have been incorrectly calculated, from an actual expense view, the rate was necessary to fund that year’s operations. On an expense basis, the district has operated at a loss two of the past three years. During that time, our year end fund balance has declined by 28%. It would be extremely helpful to all of us if we could move forward expeditiously and not have to spend considerable time explaining to our lay public that, with respect to the cost of operating our school, they have not actually been over taxed.

See
Note 2
Page 25

See
Note 3
Page 25

At our exit conference we thanked the auditors for educating us to some of the intricacies of school accounting and even suggesting possible ways in which we could rectify the problems with our budgeting format. We were very appreciative of their efforts since the previous audit by

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your office reviewed budgets in the same format but made no mention of any problems. We did ask the auditors to rework some of the language in the report, not to alter in any way their findings or recommendations but to remove or soften some of the characterizations of those findings in the interests of not causing our reform efforts to be stymied by an inflamed public opinion.

We believe such wording modifications would be consistent with your stated intent that these results are resources “for local government officials to use ... in meeting the expectations of their constituents”. Our constituents expect to see their school budgets presented in the expense based format they developed. We are seeking a way to do so consistent with your recommendations. Toward that end, we simply ask that you revisit the tone and tenor of parts of the draft report with these factors in mind.

Respectfully submitted,

Michael Comanda

Superintendent, New Suffolk Common School District

See
Note 4
Page 25

APPENDIX B

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

We have revised our report to address District officials' concerns.

Note 2

We did not recommend that District officials conceal contingency amounts in inflated expense projections. If actually needed, these amounts should be included in the budget in the proper appropriation. If not needed, as is identified in the report for the unofficial teacher personnel reserve, it should not be included in the budget.

Note 3

As shown in Table 3 in the report, the District has levied taxes in excess of what was needed for budgeted appropriations in each of the last six fiscal years.

Note 4

The scope of our prior audit, issued in January 2008, did not include a review of the District's budget practices.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to determine if the Board provided adequate oversight of fiscal operations. To accomplish this, we performed an initial assessment of the internal operations 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 management, cash receipts, cash disbursements, claims processing, purchasing, payroll and personnel services, asset management and information technology.

During the initial assessment, we interviewed appropriate District officials to obtain an understanding of the organization and the accounting system, performed limited tests of transactions and reviewed pertinent documents, such as District policy and procedure manuals, Board minutes and financial records and reports. In addition, 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 financial condition, payroll-related transactions for the former Superintendent and audit of claims for further audit testing. To accomplish the objective of this audit and obtain valid audit evidence, our procedures included the following:

- We performed an initial assessment of internal controls in place for the financial records and the claims processing to determine the overall effectiveness. This included interviewing appropriate District officials to gain an understanding of the procedures used to account for the District's financial operations.
- We examined the District's financial condition for the period July 1, 2007 to March 31, 2013.
- We reviewed Board minutes, District policies, adopted budgets, balance sheets, tax levy warrants and ST-3 data for the 2007-08 through 2012-13 fiscal years.
- We compared budgeted amounts to actual results of operation and the amount of fund balance appropriated for fiscal years ending in 2008 through 2012. We also interviewed District officials about the excessive unexpended surplus fund balance.
- We reviewed the adopted budget along with year-to-date budget status report and the projected year end results for the 2012-13 fiscal year.
- We reviewed the adopted budget for the 2013-14 fiscal year. We also analyzed the District's tax cap calculation.
- We requested and reviewed the 2010-11 and 2011-12 contracts for the former Superintendent along with all payments made to him and any available supporting documentation for the audit

period. We also requested and reviewed the former Superintendent's IRS Form MISC-1099 for the years ended 2011 and 2012.

- We interviewed the District Treasurer and the Board President to determine if abstract reports are distributed to and/or reviewed by the Board and whether or not the Board audits the claims.
- We selected 50 District claims, 23 selected judgmentally based on vendor name and 27 selected randomly using a random-number generator, to determine if the claims appeared to be for legitimate District purposes and if they were audited prior to payment.

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.

APPENDIX D

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