



Hawthorne Cedar Knolls Union Free School District

Internal Controls Over Wire Transfers

Report of Examination

Period Covered:

July 1, 2014 – March 21, 2016

2016M-183



Thomas P. DiNapoli

Table of Contents

	Page
AUTHORITY LETTER	1
INTRODUCTION	2
Background	2
Objective	2
Scope and Methodology	3
Comments of District Officials and Corrective Action	3
WIRE TRANSFERS	4
Recommendations	6
APPENDIX A Response From District Officials	7
APPENDIX B Audit Methodology and Standards	10
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

July 2016

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 Hawthorne Cedar Knolls Union Free School District, entitled Internal Controls Over Wire Transfers. 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 New York State 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*

Introduction

Background

The Hawthorne Cedar Knolls Union Free School District (District) is located in Westchester County. The District was created in 1939 by a special act of the New York State Legislature to work in cooperation with a not-for-profit group, the Jewish Board of Family and Children Services (JBFCS), to provide services for emotionally handicapped children. The District works in collaboration with JBFCS to provide educational services to day students and students in JBFCS residential programs. The primary agencies that send students to the District are the New York City Administration for Children Services, New York State (NYS) Office of Mental Health, New York City Department of Education and social services departments from approximately six counties and approximately 15 school districts.

The District is governed by the Board of Education (Board) that is composed of seven members, two of whom are appointed by the NYS Education Department Commissioner (Commissioner). The other five Board members are selected by and serve at the pleasure of JBFCS. The Board is responsible for the general management and control of District finances and educational affairs. The Superintendent of Schools, who is the District's chief executive officer, and administrative staff are responsible for the District's day-to-day management under the Board's direction.

The District has, on average, approximately 390 students and 200 employees. There is a high turnover of the student population because students are discharged and admitted throughout the school year. The District's budgeted appropriations for the 2014-15 and 2015-16 fiscal years were \$21.6 million and \$22 million, respectively. Unlike other public school districts, the District's budget is not funded through a tax levy. Instead, the budget is funded through tuition revenue based on an approved tuition rate. The NYS Education Department establishes, and the NYS Division of Budget approves the rates that the District may bill to each agency or school district.

Objective

The objective of our audit was to review internal controls over the District's wire transfer process. Our audit addressed the following related question:

- Are internal controls over wire transfers appropriately designed and operating effectively to safeguard District funds?

**Scope and
Methodology**

We examined the District’s wire transfer process for the period July 1, 2014 through March 21, 2016.

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. Unless otherwise indicated in this report, samples for testing were selected based on professional judgment, as it was not the intent to project the results onto the entire population. Where applicable, information is presented concerning the value and/or size of the relevant population and the sample selected for examination.

**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 initiate corrective action.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of General Municipal Law, Section 2116-a (3)(c) of New York State 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 in the District Clerk’s office.

Wire Transfers

The Board and District officials are responsible for establishing an adequate system of internal controls to provide reasonable assurance that cash is safeguarded. When executing wire transfers, significant amounts of money can be disbursed, usually within minutes. Therefore, the Board must establish and approve a policy and District officials must develop procedures that provide a framework for comprehensive wire transfer controls. This would include policies and procedures intended to provide reasonable assurance that wire transfers of District funds are made only upon proper review and authorization and that protect against unauthorized and improper transfers. Another fundamental element of such controls is the adequate segregation of duties. District officials should require that at least two individuals be involved in each wire transaction, one for authorization and one for transmittal. It is also essential that wire transfer confirmations from the bank are not received by the same individual who initiates the transfers. The District initiated 452 wire transfers totaling \$36,082,610 during our audit period.

The District should have an agreement with each bank that specifically addresses wire transfers. The written agreement should have a provision that requires the bank to contact someone other than the person initiating the transaction to confirm the appropriateness of the transfer. Further, the financial institution should provide a written confirmation of the transaction no later than the business day following the day on which the funds were transmitted. When internal controls are not designed appropriately or operating effectively, there is a higher risk that errors and irregularities, such as unauthorized transfers, may occur and not be detected and corrected.

The Board has not adopted policies addressing electronic banking transactions and District officials have not developed written procedures for wire transfers. There is also a lack of segregation of duties in the wire transfer process. The Secretary for the Assistant Superintendent of Finance (Secretary) or District Treasurer initiates and authorizes wire transfers online and receives wire transfer confirmations without supervisory review. In addition, the District did not have comprehensive agreements with each bank that addressed electronic or wire transfers. These weaknesses increase the risk that inappropriate wire transfers could be initiated and not detected.

We selected and reviewed 148 wire transfers for seven months,¹ totaling approximately \$11 million. We confirmed the wire transfer destination, the amount transferred, and the timing and receipt of the payment and receipt. All wire transfers tested were made to other District bank accounts, for routine payroll remittances to governmental tax authorities or to utility companies for monthly payments. However, all 148 transfers were initiated and authorized by either the Secretary or Treasurer without an independent review of the transfer's appropriateness. In addition, there was no evidence that the bank sent confirmations to the District for 118 of the 148 wire transfers totaling approximately \$9.5 million.

Although we found no improprieties in our review of wire transfers, the Board and District officials still need to improve controls over wire transfers to adequately safeguard District funds. Without proper segregation of duties, there is an increased risk that one person could initiate an inappropriate wire transfer and conceal it.

The District uses three different banks to make wire transfers among District bank accounts, as well as to make transfers to governmental tax authorities and to pay monthly utility payments. Although the District has an agreement with each bank and all three banks offer various security controls such as callback verification of transactions and email confirmation of those transactions, the District has not used those services.

We reviewed the three agreements the District has with the banks. One of the agreements offers the option, if requested by the District, to send email notices whenever the bank receives a debit for payment from an account. However, the District has not chosen this verification option. For another agreement, the District waived dual authorization security procedures and a callback verification with an authorized person for any outgoing wire transfers. The last bank offered security measures, such as dual control of wire transfer submission, whereby two authorized users are required in order to submit a wire transfer request, and further controls that require positive verification of wire transfer amounts by the second party prior to submission. However, District officials did not include those security controls in the agreement. As a result, District officials cannot be assured that funds are safeguarded because they do not have adequate wire transfer agreements with the financial institutions that have custody of District funds.

¹ We randomly selected the months of July and October 2014; January, April, August and November 2015; and February 2016.

Recommendations

The Board should:

1. Adopt electronic banking policies.
2. Include security controls in the written agreement with the banks in which District funds have been deposited.

District officials should:

3. Establish written procedures regarding wire transfers that ensure the duties of initiating, authorizing and recording wire transfer transactions are adequately segregated.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

HAWTHORNE CEDAR KNOLLS UNION FREE SCHOOL DISTRICT
226 Linda Avenue, Hawthorne, New York 10532-3795

BOARD OF EDUCATION

Daniel J. Leffell, President
James E. Miller, Vice President
Louis W. Bauman
David F. Everett
Miriam Fishman
Herbert J. Friedman
Joan Weber, Ed.D.

MARK K. SILVERSTEIN

Superintendent of Schools
914.749.2903/2905 Fax: 914.749.2904
E-mail: msilverstein@hks.org

July 7, 2016

Office of the State Comptroller
Newburgh Regional Office
33 Airport Center Drive, Suite 103
New Windsor, NY 12553

Attn: Ms. Tenneh Blamah, Chief Examiner

Dear Ms. Blamah:

We have reviewed your Report of Examination, #2016M-183, Internal Controls Over Wire Transfers, and, following our meeting on June 21, 2016, we would like to respond that we are in agreement with your findings and recommendations.

We recognize that the most recent revision to our District Policy# 5510 in December, 2012, does need to be updated and be more specific to Hawthorne Cedar Knolls Union Free School District. In addition, changes to the financial institutions we do business with, as a result of acquisitions and mergers with other financial institutions, has created the need for these procedures to be revised and changed. Although the audit revealed there was no misappropriation, misuse or fraud, we will revise our procedures and security controls to better conform to your recommendations.

I do want to commend our District Treasurer, Jane LaForge, for the financial accounting systems and controls that she has put in place during her time here, as well as those employees under her supervision that follow the procedures. Although, many areas of our business functions, systems, controls, policies and procedures were examined, we are extremely pleased that those systems met with your satisfaction.



Page 1 of 2

A Special Act Public School District Created by the New York State Legislature in 1939

We will submit a Corrective Action Plan detailing the steps taken to address these recommendations, including a revised policy and procedure within the 90 day time frame.

I would like to thank the examiner, [REDACTED], for his support, cooperation and professionalism during this review, and I would also like to thank you for your favorable comments regarding the organization of the records provided [REDACTED]. Your acknowledgement is greatly appreciated.

Very truly yours,

Mark K. Silverstein
Superintendent of Schools

Cc: Daniel J. Leffell, President, Board of Education
[REDACTED]

MKS/amd



Page 2 of 2

A Special Act Public School District Created by the New York State Legislature in 1939

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To achieve our audit objective and obtain valid evidence, we performed the following procedures:

- We interviewed District officials and employees to gain an understanding of the wire transfer process.
- We obtained all District bank statements for the audit period and reviewed each month to document all wire transfers from District accounts. We then counted the number of transfers and the total amount transferred to determine our test population.
- We randomly selected seven of 21 months during our audit period using the data analysis sampling tool. Bank statements were obtained and reviewed for the seven months, from which we documented all 148 wire transfers totaling almost \$10.9 million. We verified the propriety of each transaction by reviewing the wire transfer destination and amount transferred as well as confirming the timing of the payment and receipt. We further reviewed documentation to determine if all wire transfers were initiated and authorized and if the confirmation was received by the same employee.
- We reviewed the bank agreements to determine if the agreements addressed electronic or wire transfers.

We conducted this performance audit in accordance with 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

HOW TO OBTAIN ADDITIONAL COPIES OF THE REPORT

To obtain copies of this report, write or visit our web page:

Office of the State Comptroller
Public Information Office
110 State Street, 15th Floor
Albany, New York 12236
(518) 474-4015
<http://www.osc.state.ny.us/localgov/>

APPENDIX D
OFFICE OF THE STATE COMPTROLLER
DIVISION OF LOCAL GOVERNMENT
AND SCHOOL ACCOUNTABILITY

Andrew A. SanFilippo, Executive Deputy Comptroller
Gabriel F. Deyo, Deputy Comptroller
Tracey Hitchen Boyd, Assistant Comptroller

LOCAL REGIONAL OFFICE LISTING

BINGHAMTON REGIONAL OFFICE

H. Todd Eames, Chief Examiner
Office of the State Comptroller
State Office Building, Suite 1702
44 Hawley Street
Binghamton, New York 13901-4417
(607) 721-8306 Fax (607) 721-8313
Email: Muni-Binghamton@osc.state.ny.us

Serving: Broome, Chenango, Cortland, Delaware,
Otsego, Schoharie, Sullivan, Tioga, Tompkins Counties

BUFFALO REGIONAL OFFICE

Jeffrey D. Mazula, Chief Examiner
Office of the State Comptroller
295 Main Street, Suite 1032
Buffalo, New York 14203-2510
(716) 847-3647 Fax (716) 847-3643
Email: Muni-Buffalo@osc.state.ny.us

Serving: Allegany, Cattaraugus, Chautauqua, Erie,
Genesee, Niagara, Orleans, Wyoming Counties

GLENS FALLS REGIONAL OFFICE

Jeffrey P. Leonard, Chief Examiner
Office of the State Comptroller
One Broad Street Plaza
Glens Falls, New York 12801-4396
(518) 793-0057 Fax (518) 793-5797
Email: Muni-GlensFalls@osc.state.ny.us

Serving: Albany, Clinton, Essex, Franklin,
Fulton, Hamilton, Montgomery, Rensselaer,
Saratoga, Schenectady, Warren, Washington Counties

HAUPPAUGE REGIONAL OFFICE

Ira McCracken, Chief Examiner
Office of the State Comptroller
NYS Office Building, Room 3A10
250 Veterans Memorial Highway
Hauppauge, New York 11788-5533
(631) 952-6534 Fax (631) 952-6530
Email: Muni-Hauppauge@osc.state.ny.us

Serving: Nassau and Suffolk Counties

NEWBURGH REGIONAL OFFICE

Tenneh Blamah, Chief Examiner
Office of the State Comptroller
33 Airport Center Drive, Suite 103
New Windsor, New York 12553-4725
(845) 567-0858 Fax (845) 567-0080
Email: Muni-Newburgh@osc.state.ny.us

Serving: Columbia, Dutchess, Greene, Orange,
Putnam, Rockland, Ulster, Westchester Counties

ROCHESTER REGIONAL OFFICE

Edward V. Grant, Jr., Chief Examiner
Office of the State Comptroller
The Powers Building
16 West Main Street, Suite 522
Rochester, New York 14614-1608
(585) 454-2460 Fax (585) 454-3545
Email: Muni-Rochester@osc.state.ny.us

Serving: Cayuga, Chemung, Livingston, Monroe,
Ontario, Schuyler, Seneca, Steuben, Wayne, Yates Counties

SYRACUSE REGIONAL OFFICE

Rebecca Wilcox, Chief Examiner
Office of the State Comptroller
State Office Building, Room 409
333 E. Washington Street
Syracuse, New York 13202-1428
(315) 428-4192 Fax (315) 426-2119
Email: Muni-Syracuse@osc.state.ny.us

Serving: Herkimer, Jefferson, Lewis, Madison,
Oneida, Onondaga, Oswego, St. Lawrence Counties

STATEWIDE AUDITS

Ann C. Singer, Chief Examiner
State Office Building, Suite 1702
44 Hawley Street
Binghamton, New York 13901-4417
(607) 721-8306 Fax (607) 721-8313