

Three Village Central School District

Financial Operations

DECEMBER 2021



OFFICE OF THE NEW YORK STATE COMPTROLLER
Thomas P. DiNapoli, State Comptroller

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Report Highlights

Three Village Central School District

Audit Objective

Determine whether Three Village Central School District (District) officials provided appropriate oversight over financial operations.

Key Findings

District officials did not provide appropriate oversight over financial operations. District officials did not:

- Properly assign administrative and user access rights to the financial software.
- Establish an electronic banking policy or adequate bank transfers or electronic payment procedures.
- Segregate the Treasurer’s duties or provide adequate oversight.
- Present all claims to the claims auditor for review and approval prior to payment. At least \$37.9 million in claims were not reviewed or approved, as required, prior to payment.
- Ensure \$43 million in claims are processed through the normal accounts payable process. The Treasurer controlled most aspects of these transactions rather than the accounts payable department. Therefore, there was no segregation of duties.

Key Recommendations

- Adhere to the financial software policy, ensure all claims are audited and approved prior to payment and segregate the Treasurer’s duties or provide greater oversight as a compensating control.

District officials agreed with our recommendations and have initiated or indicated they planned to initiate corrective action.

Background

The District is located in the Town of Brookhaven, Suffolk County.

An elected seven-member Board of Education (Board) is responsible for the general management and control of financial and educational affairs.

The Superintendent of Schools (Superintendent) is the chief executive officer responsible, along with other administrative staff, for the day-to-day management under the Board’s direction.

The Deputy Superintendent for Business Services (Deputy) along with the Director are responsible for the oversight of business office personnel.

The Treasurer is the custodian of District funds.

Quick Facts

2018-2019 Appropriations	\$211,136,121
Enrollment	5,878
Employees	2,003

Audit Period

July 1, 2018 - September 30, 2019

Financial Operations

How Should District Officials Oversee Financial Operations?

A board and district management are responsible for establishing policies and procedures to provide reasonable assurances that cash and other resources are properly safeguarded and to ensure financial transactions are supported, authorized and recorded accurately. District officials should segregate duties so that no one individual controls all phases of a transaction.

When a financial software application is used to process transactions and maintain financial records, effective controls over access rights should allow users to access only those functions that are consistent with their job responsibilities and should prevent users from being involved in multiple aspects of financial transactions.

The financial software administrator should not be involved in financial operations, because an individual who has administrative rights can generally add new users, configure certain system settings, override management controls, create and change user access rights and record and adjust entries. Additionally, the periodic review of audit trail reports and user activity reports is an important control for detecting possible manipulation of financial data or other sensitive information. The review of these reports should be assigned to individuals who are independent of financial transactions.

When it is not practical to segregate duties, district officials should institute compensating controls, such as establishing procedures for the periodic review of bank statements and reconciliations, as well as accounting records to ensure they are up-to-date, complete and accurate.

When a board appoints a claims auditor, the claims auditor is responsible for auditing and approving claims before they are presented to the treasurer for payment. The treasurer should ensure that disbursements are authorized and supported by certified warrants or individual claims are approved by the claims auditor.

To safeguard cash assets, a board should adopt policies and procedures to properly monitor and control online banking transactions. Such policies should clearly describe the online activities district officials may perform and establish a process to verify the accuracy and legitimacy of online transactions. Officials must properly segregate the duties of employees granted access to the online banking applications to ensure that employees are unable to perform all financial transactions on their own.

“...[E]ffective controls over access rights should allow users to access only those functions that are consistent with their job responsibilities and should prevent users from being involved in multiple aspects of financial transactions.”

District Officials Did Not Properly Segregate Duties When Assigning Administrative and User Access Rights to the Financial Software

The Board adopted a financial software policy that states a Systems Administrator and an alternate will be designated by the Superintendent. The systems administrator reports to the executive director of instructional technology and has the authority to change the permissions for software users. In addition, the systems administrator must not be a business office employee and must not have a District business function. The policy also states that employees' permissions should appropriately reflect their duties. The business administrator is responsible for keeping appropriate records of the permissions granted and generating audit trail reports and user activity reports quarterly. However, officials did not implement the controls in the financial software policy.

District officials granted the Director administrative rights to the financial software and access to every financial software module. As a result, the Director can perform most administrative functions in the financial software such as adding and modifying user access. In addition, the Director can perform entries in all of their financial system modules such as accounts payable, payroll, human resources and purchasing. While the Director stated she reviews various activity reports; this does not provide for adequate oversight and segregation of duties. In addition, there was no evidence the Deputy, as business administrator, generated and reviewed reports, in accordance with the financial software policy.

We reviewed user permission reports to determine whether employees' financial software access was granted based on job duties. We identified 11 employees, including the Director, with software permission access in excess of what was needed for their job duties.

We found:

- The Treasurer has full access to accounts receivable, accounts payable, budgeting and general ledger; and has limited access to employee data, payroll and purchasing.
 - With this access, the Treasurer's duties are not properly segregated, as discussed in more detail in the section below.
- Four payroll clerks have access to employee data and human resources.
 - This access allows them to change data such as employee pay rates, addresses and names. The Deputy stated they provided this access to payroll employees to make it easier to get payroll completed in a timely manner. However, this access does not provide adequate segregation of duties, because it could allow them to make changes to employee pay rates, addresses or names to make inappropriate payroll payments.

-
- A confidential secretary in the business office and the accounts receivable clerk have access to accounts payable.
 - While officials stated this access was granted so they could provide a back-up for an accounts payable clerk, this does not provide for adequate segregation of duties. Access should be granted if and when a backup is required. Otherwise, having full access could allow them to make inappropriate payments without detection.
 - A former human resources employee had access to human resources records and systems; an information technology employee had access to employee information; and a clerk typist had access to accounts receivable.
 - These employees did not need these access rights to perform their duties. Having access rights beyond what was required for their duties could allow them to perform inappropriate transactions. Officials acknowledged that all of these employees' access was not necessary and would be updated

We also reviewed user activity reports for seven employees in the business office to determine whether their activities were consistent with their job duties. We found the activities performed by five of the employees were consistent with their job duties. However, the Director and Treasurer performed functions that were not consistent with their typical job duties.

The Director had full access to the purchasing module and she adjusted, canceled and closed purchase orders – activities which should have been performed by the purchasing agent or the Deputy as the agent's backup. While the Director was granted purchasing module access and acted as a purchasing agent backup, she was not authorized to do so by the Board.

The Treasurer had full financial system access to accounts payable/cash disbursements and general ledger. The Treasurer was able to add and post invoices, assign check numbers and reconcile the payment through accounts payable/cash disbursements. We found the Treasurer added and posted invoices for electronic payments, then made the payment and reconciled the accounts, without adequate oversight. In addition, the Treasurer made vendor payments through journal entries. Payments posted through journal entries do not appear on the vendor history report.

For example, the purchasing agent issued a blanket purchase order for utilities on July 1, 2018 in the amount of \$1.7 million. On July 11, 2018, the Treasurer made a prior year utility payment for \$181,457 and posted the payment using a journal entry. The payment was not charged to a purchase order, bypassed the normal approval process in the software, and did not appear on the vendor history report. This increases the risk that a fraudulent transaction could occur without detection.

While the Director was granted purchasing module access and acted as a purchasing agent backup, she was not authorized to do so by the Board.

District officials did not:

- Adhere to their financial software policy and assigned administrator rights to the Director,
- Properly segregate duties within the software or
- Ensure user access rights were appropriate for employees' job description and that those rights were promptly adjusted or deactivated when employees' responsibilities changed.

As a result of not segregating duties for several staff, there is an increased risk unauthorized changes to the personnel and accounting records could occur and go undetected, which increases the risk that erroneous or fraudulent transactions could occur without detection.

District Officials Did Not Segregate the Treasurer's Duties

District officials did not properly segregate the Treasurer's duties or provide adequate oversight. The Treasurer, as the custodian of District funds, is responsible for signing District checks and making electronic fund transfers. In addition, she prepares and records journal entries, enters budget transfers and performs bank reconciliations. The District did not have an electronic banking policy, and there were no adequate procedures in place to authorize and approve bank transfers or electronic payments. In addition, the bank reconciliations were not reviewed.

Because of the lack of segregation of the Treasurer's duties, we re-performed bank reconciliations and traced electronic transfers for the District's 13 bank accounts for the period April 1, 2019 through June 30, 2019. Although we were able to reconcile each bank account, we found discrepancies between bank records and District records. Generally, when the Treasurer made a transfer between bank accounts, she prepared a journal entry form, which was approved by the Director and then entered in the financial system by the Treasurer. However, there was no authorization or approval for the bank transfer. We traced 65 bank transfers totaling \$148 million. Thirteen transfers totaling \$1.4 million, did not have an approved journal entry form. Eight of the transfers totaling \$1.4 million, from the general fund were for State aid received and transferred to the federal fund, cafeteria fund or the capital fund accounts. Four transfers totaling \$1,249 were to correct errors and one transfer for \$28 did not have an explanation.

In the three months of general fund bank reconciliations reviewed, we also found the Treasurer made 52 electronic payments totaling \$43 million for debt payments, utilities, health insurance, dental insurance, postage, workers' compensation claims and refunds to students. These payments did not go

The District did not have an electronic banking policy, and there were no adequate procedures in place to authorize and approve bank transfers or electronic payments.

through the typical accounts payable process. Instead, the Treasurer controlled most aspects of the transactions. The Treasurer stated that when she makes an electronic payment, she enters the claim into the system and generates a warrant, makes the payment and closes the warrant. In addition, 11 of these payments totaling \$7 million for health insurance, dental insurance, utilities and postage should have been audited and approved by the claims auditor, but were not.

Due to this finding, we reviewed claims auditor reports for the audit period and found 53 claims totaling \$37.9 million that should have been audited and approved by the claims auditor, but were not. In addition, eight of these claims totaling \$5.3 million (five utility claims totaling \$707,061 (the same utility claims discussed in the previous section), two health insurance claims totaling \$4.4 million and one dental insurance claim totaling \$137,068) were done through journal entries rather than on a warrant, because the purchase order that these claims should have been processed on was closed by the Director. The Director said this was done to expedite the payments.

Without adequate segregation of duties and proper oversight of the Treasurer's duties, there is an increased risk that erroneous or fraudulent disbursements could be made and remain undetected. In addition, claims were paid that were not reviewed and authorized by the claims auditor, resulting in a risk that erroneous, incorrect, or fraudulent payments could be made.

What Are the Requirements for Contracting for an Annual Audit?

Education Law requires school districts to use a competitive request for proposal (RFP) process when contracting for an annual audit of their records by an independent certified public accountant. After a district has contracted for this service, it may engage that provider annually for a maximum of five years, at which point the district must repeat the RFP process. Education Law does not forbid districts from hiring the same service provider for consecutive five-year engagements as long as they follow the RFP process.

An RFP Was Not Issued Every Five Years for Audit Services

District officials did not use a competitive RFP process every five years when contracting for their annual audit as required by Education Law. The last RFP for annual financial audit services was performed on March 31, 2011, more than eight years prior to the start of our audit. The Deputy told us he was not aware an RFP was required to be issued because the audit firm changed. However, the audit firm had not changed; the name had changed when it was acquired by another firm. During fieldwork on this audit, the District issued an RFP for auditing services in March 2020.

The failure to issue an RFP every five years leads to an increased chance the District may be paying more for its annual audit than had it utilized an RFP process as required.

What Do We Recommend?

The Board should:

1. Adopt an online banking policy that describes authorized online banking activities, specifies which employees are authorized to process transactions, and establishes a detailed approval process to verify the accuracy and legitimacy of online transactions.

District officials should:

2. Adhere to the financial software policy by assigning administrator rights to an employee outside the business office, and review user permissions.
3. Remove access rights from individuals that do not need the rights to perform their duties.
4. Segregate the Treasurer's duties or provide greater oversight by establishing mitigating controls to routinely monitor and review the Treasurer's work.
5. Ensure monthly bank reconciliations are reviewed for accuracy once the Treasurer prepares them.
6. Ensure all interbank wire transfers receive approval before being executed.
7. Ensure all claims are presented to the claims auditor for audit and approval prior to payment.
8. Comply with Education Law by issuing an RFP for external audit services every five years.

Appendix A: Response From District Officials



**THREE VILLAGE
CENTRAL SCHOOL DISTRICT**

The mission of the Three Village Central School District, in concert with its families a community, is to provide an educational environment which will enable each student achieve a high level of academic proficiency and to become a well-rounded individual who is an involved, responsible citizen.

*Cheryl Pedisich
Superintendent of Schools*

November 23, 2021

Ira McCracken, Chief Examiner
NYS Office Building, Room 3A10
250 Veterans Memorial Highway
Hauppauge, NY 11788-5533

Dear Mr. McCracken,

The Three Village Schools would like to thank the Office of the State Comptroller for their time and effort in dedicating more than two years to perform a very detailed and thorough review of our financial operations. We are always looking for ways to improve our internal controls and your audit has identified an opportunity to address this issue. Most of the recommendations made in the report have already been implemented, and some have been in place for two years. We have also hired an experienced CPA to improve our internal controls and to further segregate duties among the business office staff.

We agree with the results of the audit and are pleased that all of the findings were related to procedures and there were no instances of improper or inaccurate payments. Our Corrective Action Plan will be developed with the Board of Education's Audit Committee, District Administration and our Internal Auditor, and filed with your office and the New York State Education Department.

We would like to thank you, once again, for the time and effort put into this audit.

Sincerely,

Cheryl Pedisich
Superintendent of Schools

Jeffrey Carlson
Deputy Superintendent

CP/me

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Appendix B: Audit Methodology and Standards

We conducted this audit 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. To achieve the audit objective and obtain valid audit evidence, our audit procedures included the following:

- We interviewed officials and employees, reviewed policies and procedures and Board minutes and reports to gain an understanding of financial operations and financial software.
- We reviewed all 13 bank account reconciliations prepared by the Treasurer during April 2019 through June 2019 for completeness and accuracy. We chose this three-month period, because we identified irregularities during our review of the District's April cash disbursement report. We also identified a payment made to utilities that did not appear on the report. As a result, we decided we would also include the following two consecutive months, which are the last two months of the District's fiscal year end.
- We reviewed the claims auditor reports to the Board to determine the warrant sequence. We reviewed the 49 missing warrants and the general ledger to identify claims not presented to the claims auditor.
- We reviewed all District bank wire transfers during April 2019 through June 2019 to determine whether the business office followed District procedures and all transfers were documented and approved.
- We reviewed the District's financial software user security profile report and user listing reports to determine whether user access was appropriate based on employee job duties and identify users that should not have access in the software.
- We reviewed the District's financial software user activity reports for seven employees that work in the business office to determine whether financial software entries coincide with their job duties.
- We reviewed the District's compliance with certain Education laws and regulations regarding claims auditing and a competitive process for retaining auditing services.

We conducted this performance audit in accordance with GAGAS (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.

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.

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, pursuant to Section 35 of General Municipal Law, Section 2116-1(3) (c) of New York State Education Law and Section 170.12 of the Regulations of the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the 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. We encourage the Board to make the CAP available for public review in the Clerk's office.

Appendix C: Resources and Services

Regional Office Directory

www.osc.state.ny.us/files/local-government/pdf/regional-directory.pdf

Cost-Saving Ideas – Resources, advice and assistance on cost-saving ideas

www.osc.state.ny.us/local-government/publications

Fiscal Stress Monitoring – Resources for local government officials experiencing fiscal problems

www.osc.state.ny.us/local-government/fiscal-monitoring

Local Government Management Guides – Series of publications that include technical information and suggested practices for local government management

www.osc.state.ny.us/local-government/publications

Planning and Budgeting Guides – Resources for developing multiyear financial, capital, strategic and other plans

www.osc.state.ny.us/local-government/resources/planning-resources

Protecting Sensitive Data and Other Local Government Assets – A non-technical cybersecurity guide for local government leaders

www.osc.state.ny.us/files/local-government/publications/pdf/cyber-security-guide.pdf

Required Reporting – Information and resources for reports and forms that are filed with the Office of the State Comptroller

www.osc.state.ny.us/local-government/required-reporting

Research Reports/Publications – Reports on major policy issues facing local governments and State policy-makers

www.osc.state.ny.us/local-government/publications

Training – Resources for local government officials on in-person and online training opportunities on a wide range of topics

www.osc.state.ny.us/local-government/academy

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