



THE STATE EDUCATION DEPARTMENT / THE UNIVERSITY OF THE STATE OF NEW YORK /  
ALBANY, NY 12234

**TO:** The Honorable the Members of the Board of Regents  
Subcommittee on Audits/Budget and Finance

**FROM:** Valerie Grey

**SUBJECT:** Board of Regents Oversight – Financial Accountability

**DATE:** October 5, 2010

**STRATEGIC GOAL:** Goal 5

**AUTHORIZATION(S):**

### **SUMMARY**

#### **Issues for Discussion**

The following topics will be discussed with the Members of the Subcommittee on Audits/Budget and Finance:

1. Overview of the Office of Audit Services (Attachment I)
2. Discussion of the Subcommittee's Charge
3. Department's Annual Internal Control Certification
4. Completed Audits (Attachment II)
5. Final Report on the Results of School District Accountability Initiative (Attachment III)

#### **Reason(s) for Consideration**

Update on Activities

#### **Proposed Handling**

Discussion and Guidance

## Procedural History

The information is provided to assist the Subcommittee in carrying out its oversight responsibilities.

## Background Information

1. Overview of the Office of Audit Services  
Staff will brief the Subcommittee on the organization, structure, and activities of the Department's audit unit. (Attachment I)
2. Discussion of the Subcommittee Charge  
Staff will brief the Subcommittee on the role and responsibilities of the Regents Subcommittee on Audits, and discuss options for the charge of the newly formed Regents Subcommittee on Audits/Budget and Finance.
3. Department's Annual Internal Control Certification  
Staff will brief the Subcommittee members on the Department's process to help ensure key risks are identified and adequate internal controls are in place. Staff will also brief the Subcommittee on the requirement to annually certify to the Division of the Budget that the Department has complied with certain provisions related to internal controls.
4. Completed Audits  
The Subcommittee is being presented with 18 audits this month. A summary of key audits is attached. (Attachment II)

Audits are provided as follows:

### Office of Audit Services

Oneida-Herkimer-Madison BOCES Special Education Program Schedules –  
June 2000 - June 2005

Rome City School District Special Education Program Schedules – June 2000 -  
June 2003

United Cerebral Palsy and Handicapped Persons Association of the Utica Area,  
Special Education Program Schedules – June 2002 – June 2004

### Office of the State Comptroller

Eldred Central School District

Kinderhook Central School District

Mexico Academy and Central School District

New York City Department of Education Follow-up Report on School Nutrition

New York State Education Department and the Office of Children and Family  
Services Educators for Children, Youth and Families, Inc. Use of Contract  
Funds

5. Final Report on the Results of the School District Accountability Initiative  
Staff will brief the Subcommittee on the final results of the audits conducted as part of the school district accountability initiative.

Recommendation

For item two (Discussion of the Subcommittee Charge), guidance of the Subcommittee is sought and for items one (Overview of the Office of Audit Services), three (Department's Annual Internal Control Certification), four (Completed Audits), and five (Final Report on the Results of the School District Accountability Initiative), no further action is recommended.

Timetable for Implementation

N/A

The following materials are attached:

- Roadmap
- Overview of the Office of Audit Services (Attachment I)
- Summary of Audit Findings including Audit Report Abstracts (Attachment II)
- Final Report on the Results of the School District Accountability Initiative (Attachment III)

## **Overview of the Office of Audit Services**

### **Mission/Vision**

The mission of the Office of Audit Services (OAS) is to provide quality audit and related services for leadership and staff to enhance accountability with resources that assist the Department in raising the knowledge, skill and opportunity of the people in New York. Our vision is to be recognized as a leader by the education community in providing audit and related services.

The Regents Subcommittee on Audits provided oversight of (OAS). The role of the Subcommittee and its responsibilities is defined in a document entitled "Charge and Organizational Information." It was last reviewed and updated in January 2001. It will be updated based on discussion and guidance from the new Subcommittee on Audits/Budget and Finance.

### **Office of Audit Services (OAS)**

OAS administers the internal and external audit functions for the Department. It is also responsible for the receipt, review and analysis of the financial statements of school Districts, BOCES, private colleges and universities and certain non-degree granting institutions. It reports to the Chief Operating Officer and has a reporting relationship to the Board of Regents through a Subcommittee. The Director of Audit Services manages a staff of 18 professional auditors comprising one audit manager and six audit teams. Staff is deployed to meet the priorities defined in the Audit Plan.

OAS serves as liaison with the State Comptroller's staff and any other external audit organizations which audit Department-administered programs and activities.

Audits of the Department's internal programs, activities and functions are conducted in accordance with the International Standards for the Professional Practice of Internal Auditing. Internal audits can examine compliance with laws, rules and regulations, reliability and integrity of data, economy and efficiency of operations, safeguarding assets, and accomplishment of goals and objectives.

External audits of school districts, BOCES and other entities receiving funding through the Department are conducted in accordance with Generally Accepted Government Auditing Standards. These audits can be financial audits or performance audits. Performance audits can include a wide variety of objectives including compliance, accomplishment of goals, and the reliability of data.

Auditing is standards driven, with specific requirements for the qualifications and competence of staff. It is a formal systematic and disciplined approach. Audit staff are educated as accountants and are required every two years, to receive 80 hours of continuing education related to auditing or related topics. An audit also requires adequate planning and supervision and sufficient evidence to draw conclusions. Unlike

monitoring, audits normally examine historical information and are independent from the process.

## **Current Audit Plan**

OAS has traditionally operated under a two-year plan. The Department's Audit Plan was developed by OAS, with input from Department executive staff and the Subcommittee on Audits, and specifies where the Department will focus audit activities. The Plan was based on input from each Deputy Commissioner as well as an assessment of risk. Once the Plan is approved, OAS begins to select candidates for audit and develops the audit schedule. In some instances, audit candidates are proposed by a program office or senior leadership.

The current Plan is designed to guide the work of the unit through June 30, 2011. It calls for audits of:

### Audits of School Districts

- State Foundation Aid – audits of the accuracy and reliability of key district data used to generate formula aid
- Key School District Data – audits of the accuracy and reliability of other data including student assessment, graduation, dropout, and cohort data
- New York City use of IDEA funds

### Internal Audits of Department Operations

- Procurement – will include an audit of some aspect of procurement including State operated schools
- Internal Control Assessment Process – will involve an audit of the Department's process to identify risk, controls, and corrective actions
- Grants Administration – will audit the Department's system for sub recipient monitoring
- The 211 waiver process – will audit the Department's compliance with enhanced requirements for Section 211 waivers
- Information Technology Cost Allocations – will audit the Department's process for allocating Information Technology costs to other offices

### American Recovery and Reinvestment Act (ARRA) Activities

- ARRA Payment Requests and Data on Results – Audits of the validity of ARRA payment requests submitted to the Department as well as the reliability of key ARRA reporting data
- Reviews of Department processes for approving applications, monitoring the use of funds, and ensuring the accuracy of ARRA information received from sub recipients

## Audits of Other Institutions

- Local Governments that Receive Funding from the State Archives and Records Management Improvement Fund – will audit compliance with grant guidelines and fiscal requirements

The Plan also devotes resources to the review of financial statements and administering the Fraud, Waste and Abuse hotline. During the course of the Plan's implementation, situations will arise which sometimes require departure from the Plan.

The determination of the number of audits that can be conducted is based on an allocation of staff time. The Plan estimates each auditor has 200 direct work days available each year. With 16 non managers, that would provide 3,200 audit days during a two-year plan period. The Plan then estimates resources needed to complete audits from the prior plan and adjusts accordingly.

An annual report on the performance of OAS as compared to the Plan is submitted to the Subcommittee in June of each year.

## **Future Audit Plan**

As mentioned above, the current Audit Plan expires June 30, 2011. A significant portion of OAS audit resources need to be focused on areas with the least audit coverage and on areas that provide significant information to Department management and the Board of Regents. In order to provide management with information to make decisions regarding audit priorities, OAS has begun to conduct a risk assessment of all Department major control systems as well as all organization units. This assessment measures nine factors and tabulates risk based on those factors.

When completed, this will provide a method to allocate resources so that mandated audit activity continues and other areas selected represent the highest risk.

## **Reporting on Audits Conducted by Outside Entities**

OAS serves as a liaison with other entities that conduct audits of the Department. The results of those audits are brought to the Subcommittee. These include the United States Department of Education, Government Accountability Office and the Office of the State Comptroller (OSC).

The OSC conducts a significant number of audits of the Department as well as of school districts and BOCES. The Comptroller is the Chief Fiscal Officer of New York State by virtue of the State Constitution. An essential characteristic of the Comptroller's office is its independence. This independence pertains especially to the Comptroller's role as state auditor. The Comptroller audits the operations of state government and its agencies and has devoted proportionate audit coverage to Department-administered programs and activities.

There are two groups devoted to the conduct of such audits. The State Government Accountability Group focuses on state government agency audits. This group focuses on audits of operations, programs and activities administered by the Department. The Local Government and School District Accountability Group conducts audits of counties, cities, towns, villages, and special-purpose governments such as school districts. Audits of individual school districts assist the Department in its overall role of monitoring school district operations. These two audit units comprise more than 500 full time equivalent staff and have devoted significant resources to education in recent years. OAS tracks the audits and classifies findings.

The Department has an internal workgroup of executive managers and staff that reviews and identifies significant findings and trends for reporting to the audit subcommittee and referral to other subcommittees as appropriate for possible policy changes.

**Audit Report Abstracts  
 Regents Subcommittee on Audits/Budget and Finance  
 October 2010**

Audit	Payroll	Financial Reporting	Information Technology	Other
<b>Office of Audit Services</b>				
Oneida-Herkimer-Madison BOCES (2000-2005)	√	√		
Rome City School District (2000-2003)	√	√		
United Cerebral Palsy of Utica (2002-2004)	√	√		
<b>Office of the State Comptroller</b>				
** Eldred Central School District				
* Kinderhook (Ichabod Crane) Central School District (footnote 2)	√			√
Mexico Academy and Central School District		√	√	
* New York City Department of Education School Nutrition follow-Up Report (footnote 3)				√
* New York State Education Department and the Office of Children and Family Services Educators for Children, Youth and Families, Inc. Use of Contract Funds (footnote 1)				√
<b>October 2010</b>	<b>4</b>	<b>4</b>	<b>1</b>	<b>3</b>

\* Other:  
 1 Contract Funds  
 2 Medicaid Reimbursements  
 3 School Nutrition

\*\* No recommendations

The Department’s Internal Audit Workgroup met to review each of the audits being presented this month. The findings were considered of a routine nature and not of enough significance to bring to the Subcommittee. One of the findings was referred internally for assistance in resolution. Letters will be sent to the auditees reminding them of the requirement to submit a corrective action plan.



**Audit Report Abstracts  
 Regents Subcommittee on Audits/Budget and Finance  
 October 2010**

<b>Office of Audit Services</b>		
<b>Audit</b>	<b>Major Finding(s)</b>	<b>Recommendation/Response</b>
<p><b>Oneida-Herkimer-Madison BOCES                      Special Education                      Program Schedules -                      June 2000 through June                      2005                      CA-0410-1, CA-0410-2,                      CA-0901-1, CA-0901-2,                      CA-0901-3, CA-0901-4                      5th Judicial District</b></p>	<p><b>\$131,247 proposed adjustment</b></p> <p>These audits examined \$2.4 million in preschool special education expenses incurred over a six year period. They were conducted by an independent auditor through a contract with the County. Under Section 4410 of Education Law, the final report is issued by the Department.</p> <p>There were unsupported expenses found and time distribution records were not maintained to support other costs.</p>	<p><b>19 recommendations</b></p> <p>The recommendations focused on strengthening the policies and procedures.</p> <p><i>BOCES agreed with the recommendations.</i></p> <p>The Department's Rate Setting Unit reviews the recommended disallowances and adjusts tuition rates as needed. It has been determined that the rate setting methodology had already limited the costs of this program so no further adjustment to the tuition rate is required.</p>
<p><b>Rome City School                      District                      Special Education                      Program Schedules -                      June 2000 through June                      2003                      CA-0902-1, CA-0902-1,                      CA-0902-3, CA-0902-4                      5th Judicial District</b></p>	<p><b>\$43,130 proposed adjustment</b></p> <p>These audits examined \$2.6 million in preschool special education expenses incurred over a four year period. They were conducted by an independent auditor through a contract with the County. Under Section 4410 of Education Law, the final report is issued by the Department.</p> <p>There were unsupported expenses found, and salaries were charged in excess of the amount of time actually spent on the</p>	<p><b>12 recommendations</b></p> <p>The recommendations focused on strengthening the policies and procedures.</p> <p><i>The District agreed with the recommendations.</i></p> <p>The Department's Rate Setting Unit</p>

**Audit Report Abstracts  
 Regents Subcommittee on Audits/Budget and Finance  
 October 2010**

	<p>program.</p>	<p>reviews the recommended disallowances and adjusts tuition rates as needed. It has been determined that the rate setting methodology had already limited the costs of this program so no further adjustment to the tuition rate is required.</p>
<p><b>United Cerebral Palsy and Handicapped Persons Association of the Utica Area                  Special Education Program Schedules - June 2002 through June 2004                  CA-0903-1, CA-0903-2, CA-0903-3                  5th Judicial District</b></p>	<p><b>\$178,484 proposed adjustment</b></p> <p>These audits examined \$19.1 million in preschool special education expenses incurred over a three year period. They were conducted by an independent auditor through a contract with the County. Under Section 4410 of Education Law, the final report is issued by the Department.</p> <p>There were unsupported expenses found, and salaries were charged in excess of the amount of time actually spent on the program.</p>	<p><b>11 recommendations</b></p> <p>The recommendations focused on strengthening the policies and procedures.</p> <p><i>The agency agreed with the recommendations.</i></p> <p>The Department's Rate Setting Unit reviews the recommended disallowances and adjusts tuition rates as needed. It has been determined that the rate setting methodology had already limited the costs of this program so no further adjustment to the tuition rate is required.</p>

**Audit Report Abstracts  
 Regents Subcommittee on Audits/Budget and Finance  
 October 2010**

<b>Office of the State Comptroller</b>		
<b>Audit</b>	<b>Major Finding(s)</b>	<b>Recommendation/Response</b>
<p><b>Eldred Central School District                      Virtual Desktops: Cost Savings and Energy Conservation                      2010M-81                      3rd Judicial District</b></p>	<p>It was found that the District has implemented a plan to replace 30 new computers in one of their computer labs in the summer of 2010. Instead of purchasing traditional computers, the District has decided to purchase virtual desktops because of the potential savings in cost, service and maintenance time. If the predicted amount of savings is achieved, the District will replace one additional lab (each containing 30 traditional desktop computers) per year with virtual desktops. If the District follows through with this three year plan, it is predicted that the District will achieve \$68,473 in cost savings.</p>	<p>There were no recommendations.</p>
<p><b>Kinderhook Central School District                      Cost Savings and Revenue Enhancements                      2010M-86                      3rd Judicial District</b></p>	<p>It was found that District procedures for managing overtime hours are not effective. The District incurred approximately \$428,000 of overtime costs, of which \$168,000 could be linked to a contract providing for overtime for certain employees. The District could have avoided up to \$260,000 in non-contractual overtime costs.</p> <p>Further, the District could realize net revenue enhancements of approximately \$57,250 in Medicaid reimbursements for Individual Education Plan services and Targeted Case Management by submitting claims for these services.</p>	<p><b>5 recommendations</b></p> <p>The report's recommendations focused primarily on strengthening the policies and procedures regarding the proper management of overtime hours, and the submission of claims for Medicaid reimbursements.</p> <p><i>The District agreed with the recommendations and has indicated that they plan to implement corrective action to address the findings.</i></p>

**Audit Report Abstracts  
 Regents Subcommittee on Audits/Budget and Finance  
 October 2010**

<p><b>Mexico Academy and Central School District Internal Controls Over Financial Operations Follow-up 2007M-197-F 5th Judicial District</b></p>	<p>A report that assessed the financial operations of the District was issued in October 2007. Certain conditions were identified that presented opportunities for improvement, and as a result, recommendations were made.</p> <p>The District was revisited in August 2009 to determine how much progress had been made with implementing the recommendations from the initial report. Eight recommendations were made, and from the follow-up report it was determined that the District had fully implemented four of the recommendations. The remaining four have been partially implemented.</p>	<p>The recommendations that were partially implemented were those pertaining to the segregation of financially-related duties involving the Treasurer and the payroll clerk, computer access controls, and the review of audit logs.</p> <p>The remainder of the recommendations have been fully implemented.</p>
<p><b>New York City Department of Education (NYCDOE) School Nutrition Follow-Up Report 2010-F-12 1st, 2nd, 11th, 12th, 13th Judicial District (Contract for Excellence)</b></p>	<p>A report was issued in June 2009, in order to examine whether the NYCDOE ensured that the food that was made available to students properly established nutritional guidelines.</p> <p>Following the initial report, a follow-up was conducted to assess the extent of implementation of the nine recommendations. It was determined that the NYCDOE made significant progress in implementing the recommendations.</p>	<p>The partially implemented recommendations were those pertaining to stopping the sale of competitive foods, electronically turning off vending machines until lunch has ended, and the frequency of bake sales.</p> <p>The remainder of the recommendations have been fully implemented.</p> <p>This report was shared with SED’s Child Nutrition Office which found the NYCDOE’s progress to be satisfactory.</p>

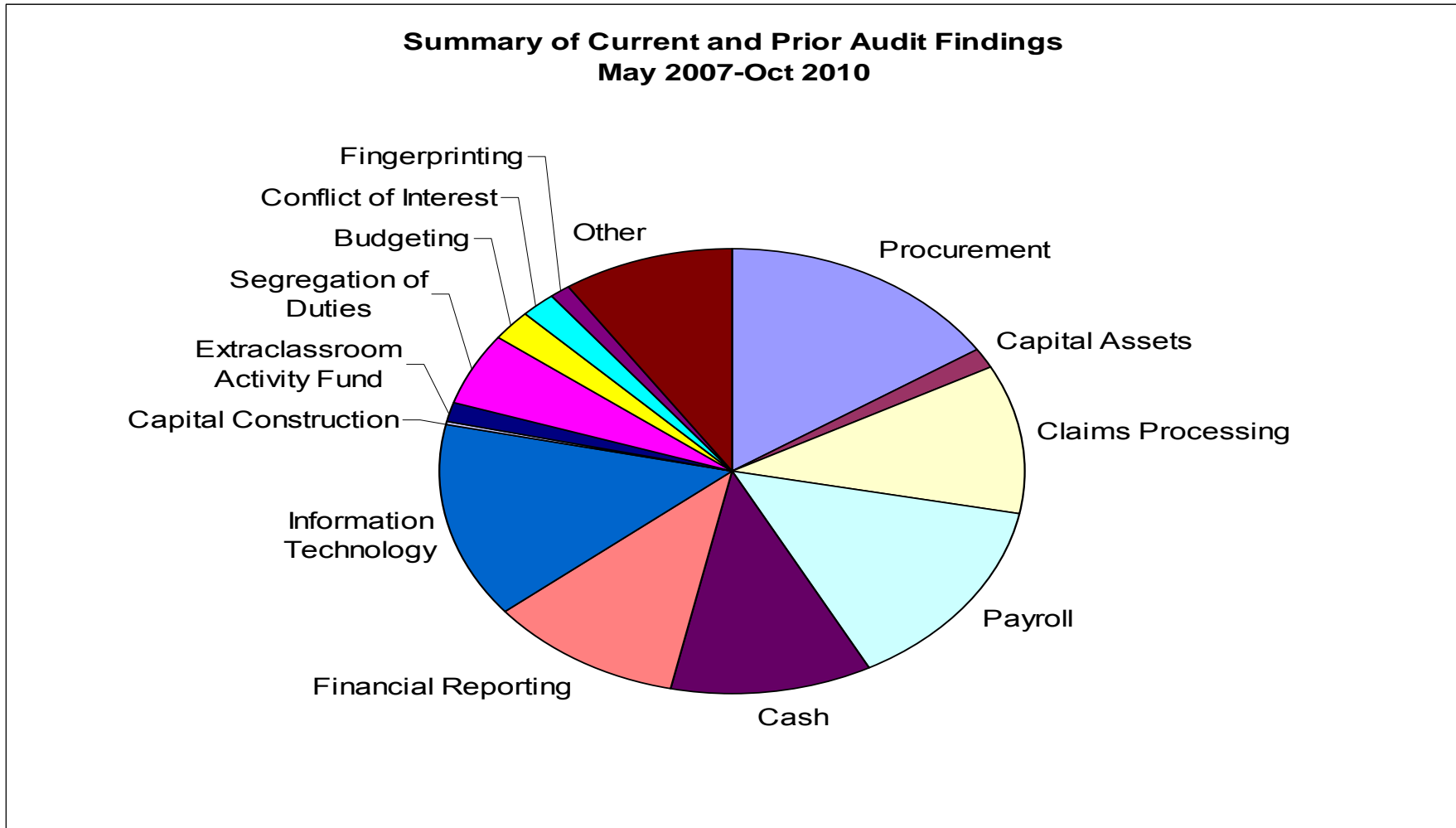
**Audit Report Abstracts**  
**Regents Subcommittee on Audits/Budget and Finance**  
**October 2010**

<p><b>New York State Education Department (Department) and the Office of Children and Family Services Educators for Children, Youth and Families, Inc. Use of Contract Funds 2007-S-128</b></p>	<p><b>\$883,530 adjustment</b></p> <p>In a prior audit of grants awarded by the Office of Children and Family Services (OCFS) to selected New York City-based child care centers, it was found that many of these Centers, including Educators for Children, Youth and Families, Inc. (Educators), misused the government funds they received, in a potentially fraudulent manner. Educators is a now defunct nonprofit community-based organization, that offered after-school services to children. In the prior audit, Educators were unable to document the appropriate use of the entire \$47,251 it received from those grants. Four of the seven contracts from which Educators received significant funding were administered by the Department, and three were administered by the OCFS.</p> <p>Between October 2002 through July 2007, Educators received almost \$3.2 million in contract payments from the Department and OCFS. It was determined that Educators could not support or justify almost half of the sampled payments reviewed (\$883,530). Of this amount, \$687,360 was paid on Department-awarded contracts, and \$196,170 was paid on OCFS-awarded contracts.</p> <p>Time and effort records were not provided, and thus there was no evidence that the \$65,733 that was paid to employees, should have been charged to the contracts.</p> <p>Further, Educators requested the Department reimburse it for \$20,137 paid to vendors for which Educators had already</p>	<p><b>3 recommendations</b></p> <p>The report's recommendations focused primarily on strengthening the policies and procedures pertaining to the recovery of payments made to Educators for the unsupported and inappropriate claims, the investigation of the support and propriety of the \$1.4 million expenditures paid to Educators that were not included in the report, and the review of contract oversight procedures for grant recipients. These recommendations were directed at both the Department and OCFS.</p> <p><i>When the findings were discussed with Educators' officials, they stated that all government funds were used appropriately, and it was only a matter of missing paperwork. The Department and OCFS officials both agreed with the recommendations and have stated that they have begun to implement them.</i></p> <p>The Department has referred this</p>
---	--	--

**Audit Report Abstracts**  
**Regents Subcommittee on Audits/Budget and Finance**  
**October 2010**

	<p>been reimbursed. Supporting documentation was also not provided for \$196,170 claimed on expenditure reports.</p> <p>The findings, regarding Educator’s conduct, have been referred to the Office of the State Comptroller’s Investigations Unit for review, as well as to law enforcement agencies for possible criminal prosecution.</p>	<p>matter to the New York State Attorney General’s Office for assistance in recouping the funds.</p>
--	---	--

October 2010 Regents Audits/Budget and Finance Subcommittee Meeting  
 Final Report on the Results of the School District Accountability Initiative



The Chart depicts the distribution of audit findings by type. The findings are for the most part found in the audits issued by the Office of the State Comptroller (OSC) as part of the five-year audit initiative. As a result of the audits:

- OSC has issued pertinent guidance and provided statewide training,
- SED has participated in statewide training on the significant findings,
- Corrective Action Plans have been received and follow-up has occurred on some instances.

October 2010 Regents Audits/Budget and Finance Subcommittee Meeting  
Final Report on the Results of the School District Accountability Initiative

### **Definitions of Categories**

Procurement – includes findings related to lack of a contract, failure to competitively bid, failure to use purchase orders, lack of segregation of duties, no approval of the purchase and a lack of documentation.

Capital Assets – includes failure to have a manager responsible, lack of policy, and inappropriate disposal.

Claims Processing – includes claims being paid without adequate documentation, failure to audit the claim, an untrained claims auditor, and a claims auditor that lacks independence.

Payroll – includes a lack of segregation of duties in the payroll process; no policy and procedures and inappropriate payments to district administrators including leave accruals and health benefits; improper classification of employees; insufficient policies and procedures for the employee retirement system; improper contractual benefit payments; and improper longevity payments to the former superintendent.

Cash – includes poor control of cash, failure to prepare bank reconciliations, and weaknesses in the treasurer's duties.

Financial Reporting – includes inaccurate accounting statements, such as, an overstated fund balance, fund balance exceeding the legal limit, general fund transfers without voter approval, and improper use of accrued liability reserve funds.

Information Technology – includes lack of a disaster recovery plan, failure to back up information, inappropriate or undocumented user rights, inappropriate or missing password protection, and no policy and procedures.

Capital Construction – includes a lack of detailed accounting records related to a capital project, undocumented expenses, inappropriate and unapproved change orders.

Extraclassroom Activity Fund – includes poor accounting over funds and no documentation of expenses.

Segregation of Duties – includes weakness in control caused by individuals having responsibility for incompatible functions.

Budgeting – includes budget reviews required for school districts that have received approval for deficit financing, poor revenue projections and use of fund balance.

Conflict of Interest – includes personal conflicts of board members, district officials, and district employees where they have an interest in a contract, where they have the power, or may appoint someone who has the power to negotiate, authorize, approve, prepare, and make payment or audit bills or claims of the contract.

Fingerprinting – includes failure to fully comply with fingerprinting requirements.