



East Moriches Union Free School District

Claims Processing

Report of Examination

Period Covered:

July 1, 2014 – May 31, 2016

2016M-273



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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

October 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 East Moriches Union Free School District, entitled Claims Processing. 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 East Moriches Union Free School District (District) is located in the Town of Brookhaven, Suffolk County. The District is governed by the Board of Education (Board), which is composed of five elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools is the District's chief executive officer and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction.

The District operates two schools for kindergarten through 8th grade, with approximately 730 students and 110 employees. Approximately 365 District students attend 9th through 12th grade at Center Moriches Union Free School District, Eastport-South Manor Central School District or Westhampton Beach Union Free School District. The District's budgeted expenditures for the 2015-2016 fiscal year were approximately \$25.8 million, including \$8.4 million in tuition costs for the 9th through 12th grade students, funded primarily with State aid, real property taxes and grants.

The Board has delegated its claims auditing responsibility to a claims auditor. The claims auditor reports directly to the Board and is responsible for formally examining and allowing or rejecting all accounts, charges, claims or demands against the District. The Board has appointed a District Treasurer (Treasurer) who is responsible for the receipt, custody and disbursement of District funds, including the signing of District checks. The Board has authorized the District Clerk to sign checks in the Treasurer's absence.

Objective

The objective of our audit was to examine claims processing. Our audit objective addressed the following related question:

- Did the Board ensure that claims were adequately audited and approved before payment?

Scope and Methodology

We examined the internal controls over claims processing for the period July 1, 2014 to May 31, 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 agreed with our recommendations and indicated that they are initiating 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.

Claims Processing

An effective system for claims processing ensures that every claim against the District contains enough supporting documentation to determine whether the amounts claimed represent actual and necessary expenditure and whether the goods or services billed for were actually received. New York State Education Law (Education Law) requires the Board to audit all claims before they are paid, or to appoint a claims auditor to assume the Board's powers and duties to examine and approve or disapprove claims. The claims auditor should review detailed receipts to determine whether the claims are properly itemized and supported and whether the District received the goods or services.

The claims auditor's authorization to pay a claim should be documented with a signed statement on a warrant (list of claims) authorizing the Treasurer to pay the claimants. The Treasurer should compare the signed checks with the warrant to verify their accuracy and consistency before authorizing the checks to be issued. If the Board allows the Treasurer to use an electronic or facsimile signature to sign District checks, the signature must be affixed by the Treasurer or under the Treasurer's direct supervision. During our audit period, the District paid 4,422 general fund claims by check, totaling \$31,882,857.

The Board and District officials have established many controls over the claims processing function to ensure that claims are audited adequately and properly supported. Specifically, the Board's purchasing policy requires that a purchase order properly approved by the purchasing agent accompany each purchase or else the person placing the order may be held personally responsible for the cost.

Once a purchase is made, the account clerk typist assembles the claims package, which includes the purchase order, invoice, appropriate supporting documentation and the check signed by the Treasurer. The claims auditor generally conducts a thorough and deliberate audit of each claim before authorizing the Treasurer to pay, using specific claims approval procedures developed by the District's internal auditors. Upon completing the audit, the claims auditor stamps each claim "approved" and initials the corner of the check and the remittance. She also signs the warrant authorizing the Treasurer to pay the claims and prepares a monthly report to the Board outlining audit dates and details, including any findings or inquiries.

We selected and reviewed 45 claims totaling \$225,049¹ to determine whether the claims were adequately audited and approved. The Board generally ensured that claims were audited and approved before payment. However, the claims auditor did not properly identify and report all confirming purchase orders to the Board, and the Treasurer did not supervise an account clerk typist's use of her electronic signature to sign the District's checks.

Confirming Purchase Orders

Purchase orders should be issued prior to purchasing goods or receiving services. Using purchase orders helps control District expenditures by ensuring that purchases are properly authorized and preapproved and that adequate funds are available. A confirming purchase order is a purchase order issued after the goods or services have already been ordered or received. District officials must strictly control and limit the use of confirming purchase orders to emergency purchases because such purchases circumvent the approval and price verification features of the normal purchasing process. There is limited assurance that confirming purchases are made at the best price and quality and are for legitimate and authorized District purposes.

The claims auditor's monthly reports to the Board identified instances of confirming purchase orders. We also reviewed the selected claims to determine whether the claims auditor had properly identified whether purchase orders were issued prior to the ordering of the goods and services. Six of the claims we reviewed contained confirming purchase orders totaling \$22,293. Two of these claims totaling \$6,949 were not stamped as audited, including one claim for \$1,984 with no support attached and another claim totaling \$43,390, which was audited but was missing an invoice for \$12,252. The claims auditor noted in the monthly reports that three of these claims totaling \$11,857 contained confirming purchase orders.

Although all of these purchases appeared to be reasonable and legitimate, the use of confirming purchase orders circumvents internal controls and weakens the procurement and budget control process. Furthermore, when the claims auditor does not properly identify all instances of confirming purchase orders or other deficiencies in the claims, there is an increased risk that the District could pay improper claims.

Check Signing

Education Law requires the Treasurer to sign all checks issued on behalf of the District. The Board, at its discretion, may require that checks be countersigned by another District officer, including a Board member. In addition, the Board may, by resolution, designate a Deputy Treasurer or Board member, (other than a Board member

¹ See Appendix B for detailed information on our selection process.

authorized to countersign) to sign checks in lieu of either the Treasurer or other official whose signature is required, in case of their absence or inability to sign. The Board may also authorize the use of an electronic or other facsimile signature on District checks.

To adequately safeguard and prevent unauthorized use, the Treasurer and other District officials should maintain custody of their signatures and directly supervise the check signing process for disbursement and payroll checks. District officials are responsible for establishing procedures to ensure that the electronic signature process is in compliance with Board policies.

The Board has not adopted a check signature policy that authorizes the use of electronic or other facsimile signatures to imprint District checks with the required signatures. The Board has authorized the District Clerk to sign checks in the Treasurer's absence. However, the District Clerk uses the Treasurer's signature flash drive and does not use her own signature. Furthermore, the Treasurer does not maintain custody of her signature flash drive or supervise the disbursement and check signing process. The account clerk typist prints checks with the Treasurer's electronic signature affixed prior to the claims audit, and the Treasurer does not directly supervise the application of her signature. The account clerk typist borrows the signature flash drive and inputs the user name and password for the flash drive to imprint the checks with the Treasurer's signature, without the Treasurer being present.

As a result of this weaknesses, we reviewed all 213 canceled checks totaling approximately \$4 million attached to the bank statements for the sample months of October 2014, May 2015 and February 2016 to determine if checks were for legitimate District purposes. Although we found no exceptions, when the Treasurer does not retain control of her electronic signature, there is an increased risk that an inappropriate check could be issued without the Treasurer's knowledge.

Recommendations

The claims auditor should:

1. Properly identify and report to the Board all instances of confirming purchase orders.
2. Disapprove any claims that do not contain sufficient supporting documents.

The Board should:

3. Enforce its policy of not allowing confirming purchase orders.
4. Develop and adopt a check signature policy that includes the

authorization of the use of a signature flash drive by designated signees to imprint District checks with the required signatures.

The Treasurer should:

5. Discontinue the practice of allowing her electronic signature to be affixed to checks without direct authorization or supervision.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



East Moriches Union Free School District

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Dr. Charles T. Russo
Superintendent of
Schools

Mr. Michael Carlson
Middle School Principal

Mr. Edward Schneyer
Elementary School
Principal

Ms. Michele Pepey
Director of Special
Education/PPS
Supervisor

September 28, 2016

Mr. Ira McCracken
Chief Examiner
Division of Local Government and School Accountability
The New York State Comptroller’s Office
250 Veterans Highway
Room 3A10
Hauppauge, New York 11788

Dear Mr. McCracken:

The East Moriches Schools Board of Education and the superintendent have reviewed the findings of The New York State Comptroller’s Office for the period including July 1, 2014, to May 31, 2016. We are in agreement with the findings and recommendations included in the report. Also, this audit response letter serves as the Corrective Action Plan to address those recommendations.

As you know, each year the East Moriches District proposed school budget is audited by your office, and I can say without hesitation that throughout those reviews and this audit, your staff is always professional and flexible when working with the East Moriches business office staff. We appreciate your work and the reviews that you perform.

If there is any other information or supporting documentation needed, please advise.

Sincerely,

Charles T. Russo, Ed.D.
Superintendent of Schools

Enc.

cc: Board of Education
Donna LaRocca, Nawrocki Smith, LLP
Peter Rodriquez, Coughlin Foundotos Cullen & Danowski, LLP

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Ms. Janet Miglino
Treasurer

Ms. Jacqueline Franke
District Clerk

Corrective Action Plan to Address July 1, 2014, to May 31, 2016, OSC Claims Audit

OSC Recommendations:

1. Properly identify and report to the Board all instances of confirming purchase orders.
2. Disapprove any claims that do not contain sufficient supporting documents.
3. Enforce its policy of not allowing confirming purchase orders.

Actions to Address Recommendations 1, 2, and 3.

The Board's internal auditing firm is going to audit the claims auditor's function and processes starting October 2016 to June 2017 to ensure that all instances of confirming purchase orders are reported to the Board of Education in the monthly claims auditors report to the Board as well as ensuring that all claims have supporting documentation.

OSC Recommendations:

4. Develop and adopt a signature check policy that includes the authorization of the use of a signature flash drive by designated signees to imprint District checks with the required signatures.
5. Discontinue the practice of allowing her electronic signature to be affixed to checks without direct authorization or supervision.

Actions to Address Recommendations 4 and 5.

The Superintendent working with the internal auditor and the Board's legal counsel will develop a policy to recommend to the Board by the regular October 2016 meeting date for their review and adoption.

The electronic signature will not be affixed to checks unless direct authorization or supervision is given or provided by the District Treasurer. The action will be monitored by the Superintendent and by a sign out procedure implemented when the disk is used.

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

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

- We reviewed applicable laws and the District's policies and procedures over claims auditing and purchasing.
- We interviewed key personnel to obtain an understanding of the claims processing and purchasing procedures, as well as the check signing process.
- The District paid 4,422 claims totaling \$31,882,857 during our audit period of July 1, 2014 through May 31, 2016. We selected three months from each calendar year in our audit period (October through December 2014, April through June 2015 and January through March 2016). We judgmentally selected a sample of five claims to test from each month, for a total of 45 claims, excluding but not limited to demand payments, Board of Cooperative Educational Services payments, tuition payments and other claims less than \$1,000.
- We requested and obtained the claims payment packets, vendor history files, warrants and the claims auditor reports for all claims selected in order to determine whether internal controls over claims processing were designed appropriately and operating effectively to adequately safeguard District assets.
- We randomly selected three of the nine months included in our claims processing test for which we reviewed the bank statements and all 213 canceled checks to determine if the checks contained the Treasurer's signature.

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

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