



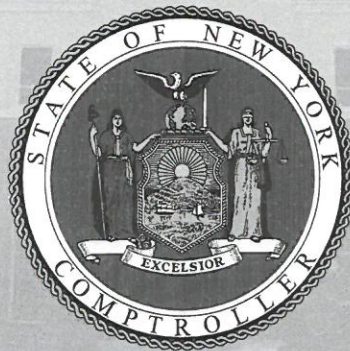
Morris Central School District Financial Operations

Report of Examination

Period Covered:

July 1, 2014 – August 31, 2015

2015M-251



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

January 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 Morris Central School District, entitled 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 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 Morris Central School District (District) is located in the Towns of Laurens, Morris, New Lisbon and Pittsfield in Otsego 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 (Superintendent) 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 Treasurer (Treasurer) and employees of the Otsego Northern Catskills Board of Cooperative Educational Services (ONC BOCES) share the responsibilities of maintaining accounting records, preparing financial reports and auditing claims.

The District operates one school building with approximately 500 students and 100 employees. The District's budgeted appropriations for the 2015-16 fiscal year are approximately \$9.5 million, which are funded primarily with State aid and real property taxes.

Objectives

The objectives of our audit were to evaluate the District's claims processing procedures and fund balance management. Our audit addressed the following related questions:

- Did District officials ensure claims were properly audited prior to payment?
- Did the Board and District officials ensure fund balances were reasonable?

Scope and Methodology

We examined the District's financial records for the period July 1, 2014 through August 31, 2015. To analyze the District's budgeting and financial trends, we extended our scope period back to July 1, 2011.

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 have begun 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.

Claims Audit

Education Law requires that the Board audit all claims before payment or appoint a claims auditor to assume the Board's powers and duties for examining and approving or disapproving claims. The Board may delegate the claims audit function by appointing a District employee, an independent contractor or an individual employed through an intermunicipal cooperative agreement or through shared services to the extent authorized by law. However, it may not be appropriate for a Board of Cooperative Educational Services (BOCES) to provide claims auditing services to its component districts because the districts could have material and significant contract payments¹ to that BOCES. When a claims auditor is appointed to assume the Board's claims auditing duties, the claims auditor must report directly to the Board.

An effective claims processing system ensures that every claim against the District contains enough supporting documentation to determine whether the goods or services purchased comply with statutory requirements and District policies and whether the amounts claimed represent actual and necessary District expenditures. The claims auditor's authorization to pay a claim should be documented with a signed statement on a warrant (listing 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.

District officials generally ensured claims were properly audited prior to payment. However, the ONC BOCES claims auditor approved all District payments including the payments made to the ONC BOCES. When a BOCES directly provides claims auditing services to a district using a BOCES employee while providing goods and other services to the same district, the arrangement puts the individual serving as claims auditor in the position of approving significant claims submitted by the BOCES, the individual's employer. Therefore, the claims auditor's objectivity and independence is compromised.

In addition, checks are printed with the Treasurer's electronic signature affixed prior to the claims audit, and the Treasurer does

¹ Contract payments include all payments to a BOCES for goods and services provided to the District, which, if significant or material, may impair the claims auditor's independence and result in a conflict of interest.

not directly supervise the application of her signature.² The District's independent auditors identified a control weakness in the District's claims audit process in the 2013-14 fiscal year. For example, they found several months in which claims were paid prior to certification from the claims auditor. For the 2015-16 fiscal year, the District contracted with ONC BOCES to perform the claims audit function.

Under this new claims audit process, District officials compile the claim packets³ and approve the packets before sending them to the accounts payable clerk, an ONC BOCES employee, who enters the claims into the financial accounting software. At this point, the claims auditor, also an ONC BOCES employee, uses a checklist⁴ while reviewing the claims to ensure they have adequate support and proper approvals and that purchases are for proper District purposes. If the claims auditor identifies an issue, he contacts the Treasurer to determine how to address it. For example, we found a voided check for an invoice containing sales tax which was later reissued for the correct amount, without the sales tax, in July 2015. Once all claims are considered satisfactory, the claims auditor initials each claim to show his approval and certifies the warrants, which are then sent back to the Treasurer. The Treasurer reviews the warrants and authorizes ONC BOCES officials to mail the checks. However, she does not compare the checks to the warrants.

The Superintendent and Treasurer told us the ONC BOCES claims audit process is expected to be more efficient than doing it in-house. Further, the Superintendent told us they decided to use the ONC BOCES in part because of the findings in the last independent auditor's report regarding the deficiencies in the claims audit process. Although the change in process mitigates the concern raised by the independent auditors, the claims against the District for goods and services provided by the ONC BOCES should be audited by someone other than the ONC BOCES claims auditor. The Board, another District employee, an independent contractor or an individual employed through an intermunicipal cooperative agreement or through shared services should audit and approve the ONC BOCES' claims.

Because District officials have made changes to improve the claims audit process, we tested claims audited under this new process to ensure it was operating as intended. Out of 105 claims totaling

² The Treasurer emails ONC BOCES employees to authorize the payment of claims after checks have already been printed with her signature at the ONC BOCES facility.

³ Claim packets include the purchase order, invoice and preprinted checks with the Treasurer's electronic signature.

⁴ The checklist includes, but is not limited to, verifying the mathematical accuracy of each claim, ensuring each claim is not a duplicate payment, ensuring proper documentation is available to support each claim and ensuring that check numbers are in sequence.

\$484,134 issued from July 1, 2015 to date, we examined 10 randomly selected claims totaling \$28,962 and five higher risk claims⁵ totaling \$3,568 to determine if they were listed on the warrants and contained appropriate supporting documentation, if they were for proper District purposes and if the claims auditor approved the claims prior to payment. Although we identified minor deficiencies, which we discussed with District officials, we determined that all claims tested had proper claims auditor approval and adequate documentation to support that the disbursements were reasonable and proper District charges. Although District officials implemented a new claims audit process that adequately addressed the concerns of the independent auditors, the risk remains that an inappropriate check could be issued without the Treasurer's knowledge.

Recommendations

The Board should:

1. Ensure that ONC BOCES'claims for goods and services are audited and approved by someone other than the ONC BOCES claims auditor.

The Treasurer should:

2. Discontinue the practice of allowing her electronic signature to be affixed to checks without her direct authorization or supervision.
3. Compare the printed checks to the certified warrants of audited and approved claims prior to the checks being mailed.

⁵ See Appendix B for our sample selection methodology.

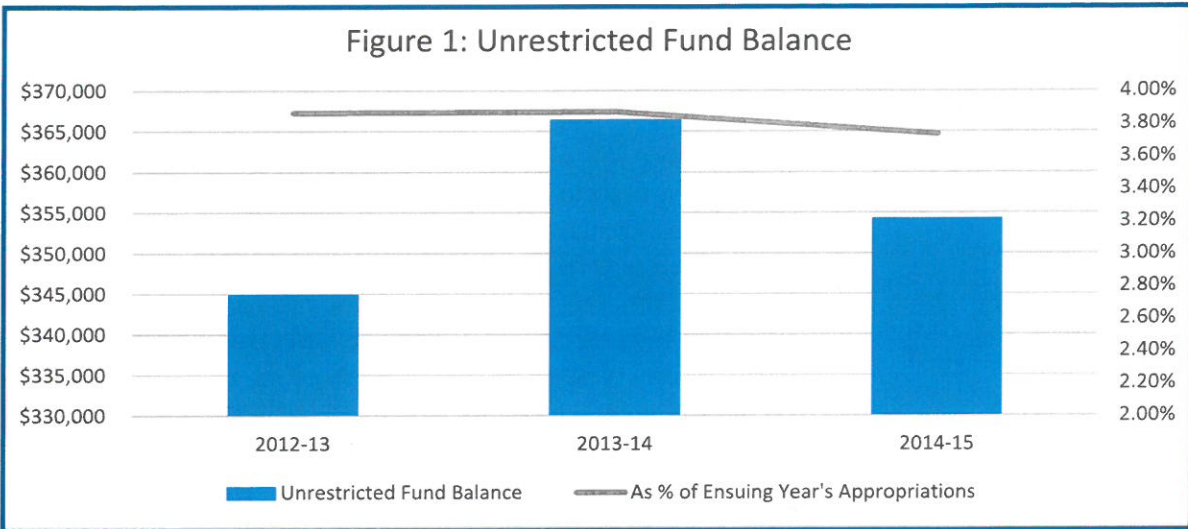
Fund Balances

Fund balance represents resources remaining from prior fiscal years that can be used to lower real property taxes for the ensuing fiscal year. A district may retain a portion of fund balance, referred to as unrestricted fund balance, within the limits established by New York State Real Property Tax Law. Accurate budget development, as well as budget monitoring and control, are effective ways to ensure fund balances are reasonable. Accordingly, it is essential that District officials develop reasonable, structurally balanced budgets to balance recurring expenditure needs with recurring revenue sources while providing desired services on a continuing basis and to manage fund balance responsibly. Combining a reasonable level of unrestricted fund balance with specific legally established reserve funds provides resources for unanticipated events and other identified or planned needs.

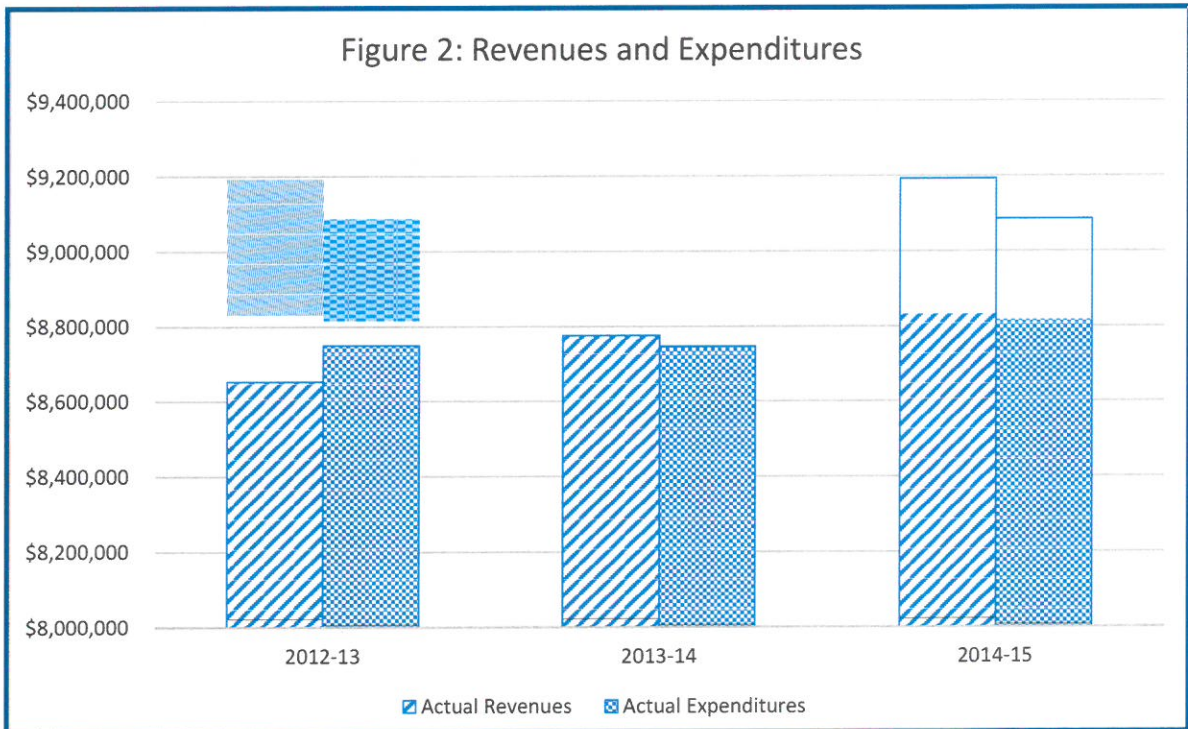
Districts may establish reserves to restrict a portion of fund balance for a specific purpose, also in compliance with statutory directives. However, reserve balances must be reasonable. Funding reserves at greater than reasonable levels contributes to real property tax levies that are higher than necessary because the excessive reserve balances are not being used to fund operations. The Board is responsible for developing a formal plan for the use of its reserves, including optimal or targeted funding levels and why these levels are justified. The Board must also ensure that District officials are maintaining appropriate documentation to account for and monitor reserve activity and balances.

The Board and District officials generally ensured the unrestricted fund balance was within the 4 percent statutory limit. However, certain reserves had significant balances when compared to their respective liabilities. District officials have a five-year plan to reduce these reserves to reasonable levels.

Unrestricted Fund Balance – The District’s unrestricted fund balance at June 30, 2015 was within the statutory maximum of 4 percent of the ensuing year’s appropriations and has remained stable over the past three years.



This occurred because revenues generally kept pace with expenditures (see Figure 2) and District officials adopted realistic, structurally balanced budgets to ensure revenues were sufficient to cover expenditures.



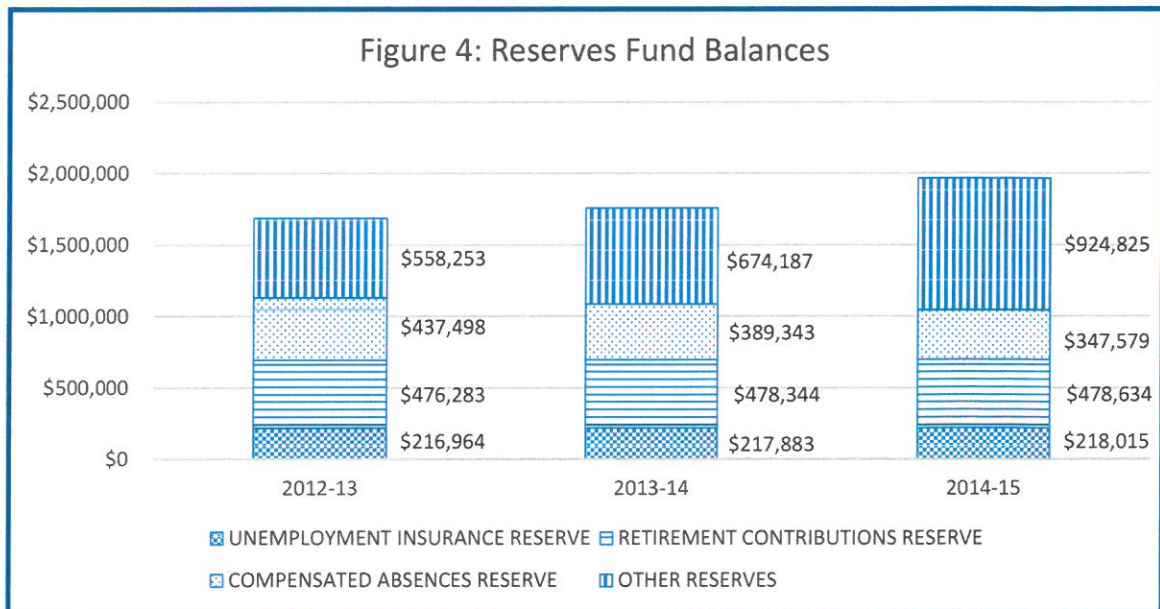
For example, the average expenditure and revenue variances were only 2.3 percent and 1.6 percent, respectively, from 2012-13 through 2014-15 (see Figure 3). While these variances are negligible on their own, in aggregate, they resulted in an increase in fund balance over the past several years. Although the Board adopted budgets that included an average planned use of more than \$330,000 in fund balance over

the last three years, the District's operations did not always use the fund balance and instead generated a surplus of \$39,000 over the three-year period.

Figure 3: Budget Variances

	2012-13	2013-14	2014-15	Average
Budgeted Revenues	\$8,451,389	\$8,629,643	\$9,134,394	\$8,738,475
Actual Revenues	\$8,653,941	\$8,775,983	\$9,192,501	\$8,874,142
Variance	\$202,552	\$146,340	\$58,107	\$135,666
Variance Percentage	2.4%	1.7%	0.6%	1.6%
Budgeted Appropriations	\$8,819,889	\$8,926,643	\$9,471,394	\$9,072,642
Actual Expenditures	\$8,749,796	\$8,747,426	\$9,085,784	\$8,861,002
Variance	\$70,093	\$179,217	\$385,610	\$211,640
Variance Percentage	0.8%	2.0%	4.1%	2.3%
Planned Use of Fund Balance	(\$368,500)	(\$297,000)	(\$337,000)	(\$334,167)
Results of Operations	(\$95,855)	\$28,557	\$106,717	N/A

Reserves – District officials have accumulated significant balances in three of the District's reserves. As of June 30, 2015, the District had nine reserves in the general fund totaling approximately \$2 million.



We analyzed these reserves for reasonableness and adherence to statutory requirements and found the funding of the property loss, liability, insurance, tax certiorari, repair and capital reserves to be reasonable. However, the reserves for retirement contributions, compensated absences and unemployment insurance, with balances totaling approximately \$1 million, were significant when compared to the amounts necessary for their stated purposes.

- Retirement Contributions Reserve – This reserve is used to pay the District’s retirement contribution to the New York State and Local Retirement System (NYSLRS). The District’s 2014-15 NYSLRS expenditure was \$155,464. The reserve balance as of June 30, 2015 was \$478,634, three times higher than the 2014-15 annual contribution. However, the 2015-16 adopted budget and the District’s five-year plan call for the annual use of \$40,000 from this reserve over the next five years.
- Compensated Absences Reserve – This reserve must be used only for cash payments for accrued and unused sick, vacation and certain other leave time owed to employees when they leave District employment. As of June 30, 2015, we determined the District’s liability for compensated absences was approximately \$281,000. However, the reserve balance was \$347,579. Therefore, the reserve was overfunded by approximately \$67,000.
- Unemployment Insurance Reserve – This reserve is used to pay unemployment insurance claims under the “benefit reimbursement” method. The District’s expenditures for unemployment insurance totaled \$9,956 over the past four years. However, the \$218,015 reserve balance as of June 30, 2015 was more than 43 times higher than the average annual expenditure.⁶

Reserve fund balances have accumulated to significant levels because, prior to our audit period, District officials transferred funds to them without using them. However, District officials have a formal five-year plan for reserve balance levels and usage. We reviewed the plan and found it to be reasonable.

During our audit period, District officials have raised taxes to be within the Real Property Tax Cap, barring override.⁷ In addition, the District has budgeted a 1 percent decrease in real property taxes for the 2015-16 fiscal year. By evaluating reserve balances and developing a five-year plan, the District is ensuring reserves are used for their intended purpose while avoiding financial stress.

Recommendation

4. The Board should continue to evaluate reserve fund balances and follow its five-year plan regarding the funding and use of such reserves.

⁶ In calculating the average annual expenditure over the last four years, we included only the years in which expenditures were made (2011-12 and 2012-13).

⁷ The law precludes a school district from adopting a budget that requires a tax levy that exceeds the prior year’s tax levy by more than 2 percent or the rate of inflation, whichever is less, with certain exclusions permitted by law, unless at least 60 percent of District voters approve a budget that requires a tax levy that exceeds the statutory limit.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

BOARD OF EDUCATION
MARGARET CAEZZA
President
MICHAEL WALLING
Vice President
BRIAN PAGE
STEPHEN PHELPS
WENDY MOORE



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ADMINISTRATION
MATTHEW SHELDON
Superintendent
KATHARINE SMITH
Principal
DEBORAH CHICORELLI
Director of Pupil Personnel

December 22, 2015

H. Todd Eames, Chief Examiner
Office of the State Comptroller
Division of Local Government and School Accountability
Binghamton Regional office
State Office Building, Suite 1702
44 Hawley Street
Binghamton, NY 13901-4417

Dear Mr. Eames:

This letter is the official response from the Morris Central School District to the Report of Examination of Financial Operations for the period of July 1, 2014 to August 31, 2015.

The district would like to express our appreciation for the time, insight and thoughtfulness your staff dedicated to our district. Your auditor was on site for several weeks and always maintained the upmost professionalism and willingness to work with and answer any questions that district staff had.

Through the information gathering process, the auditor developed two objectives in an attempt to help the district remain financially sound while meeting its obligations to the taxpayers of our district. The objectives developed were "to evaluate the District's claims processing procedures and fund balance management."

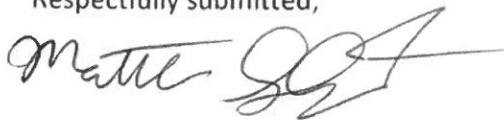
Concentrating on the two objectives and the review of the District's finances, the audit contains two findings with four different recommendations that the District will consider to improve our overall financial operations. The two findings were:

- "Although District officials implemented a new claims audit process that adequately addressed the concerns of the independent auditors, the risk remains that an inappropriate check could be issued without the Treasurer's knowledge.
- "By evaluating reserve balances and developing a five-year plan, the District is ensuring reserves are used for their intended purpose while avoiding financial stress.

The school district is in agreement with these findings and the included Corrective Action Plan details how we plan to address the four recommendations that have been suggested in the audit.

The Board of Education and Administration of the Morris Central School District wish to express their appreciation for the recommendations provided through the audit process to help the district strengthen its financial operations and to continue to fulfill our obligations to the taxpayers of the school district.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Matt Sheldon", with a stylized flourish extending to the right.

Matthew L. Sheldon
Superintendent

BOARD OF EDUCATION
MARGARET CAEZZA
President
MICHAEL WALLING
Vice President
BRIAN PAGE
STEPHEN PHELPS
WENDY MOORE



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ADMINISTRATION
MATTHEW SHELDON
Superintendent
KATHARINE SMITH
Principal
DEBORAH CHICORELLI
Director of Pupil Personnel

Unit Name: Morris Central School District

Audit Report Title: Morris Central School, Financial Operation, Report of Examination, Period
Covered: July 1, 2014-August 31, 2015

Audit Report Number: 2015M-251

For each recommendation included in the audit report, the following is our corrective action(s) taken or proposed. For recommendations where corrective action has not been taken or proposed, we have included the following explanations.

1. **Audit Recommendation:** The Board should: Ensure that BOCES claims for goods and services are audited and approved by someone other than the BOCES claims auditor.

Implementation Plan of Action(s): The District has approximately twelve checks a year that are for BOCES claims or goods. The District will have a Morris employee audit those claims and goods before a check to BOCES is printed and signed.

Implementation Date: This will commence February 1, 2016

Person Responsible for Implementation: Matthew Sheldon (Superintendent)

2. **Audit Recommendation:** The Treasurer should: Discontinue the practice of allowing her electronic signature to be affixed to checks without her direct authorization or supervision.

Implementation Plan of Action(s): The District will investigate the options available to have the treasurer pre-approve the warrants and checks prior to her electronic signature being placed on the checks. This may include the use of the school's financial program [REDACTED] to authorize payment.

Implementation Date: February 1, 2016

Person Responsible for Implementation: Kristina Hand (Treasurer)

3. **Audit Recommendation:** The Treasurer should: Compare the printed checks to the certified warrants of audited and approved claims prior to the checks being mailed.

Implementation Plan of Action(s): The District will investigate ways to ensure that the treasurer is able to approve claims without creating an undue delay in the checks being mailed out.

Implementation Date: February 1, 2016

Person Responsible for Implementation: Kristina Hand (Treasurer)

4. **Audit Recommendation:** The Board should continue to evaluate reserve fund balances and follow their five-year plan regarding the funding and use of such reserves.

Implementation Plan of Action(s): The Board of Education, in conjunction with the superintendent, shall review the reserve fund balances and five-year plan at a minimum of two times a year. This review will occur once during the budget process to determine possible use of reserves and secondly at the end of a budget year to determine present levels of reserves and future needs.

Implementation Date: February 1, 2016

Person Responsible for Implementation: Matthew Sheldon (Superintendent)

Signed:



Name: Matthew Sheldon

Title: Superintendent

12/22/15
Date

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

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

- We interviewed District and ONC BOCES officials to gain an understanding of the claims audit process and plans for reserve fund balances and usage.
- We selected a sample of five disbursements based on payee names and an additional random sample of 10 disbursements to determine if the controls over the claims audit process were adequate.
- We compared reserve balances to planned uses or, in the absences of such plans, to the historical use of those reserves to determine reasonableness. We compared the unrestricted fund balance to the following year's appropriations to determine if the District was within statutory requirements.
- We analyzed revenues, expenditures and budgets to identify trends in funding and use of reserve balances.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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