

SALMON RIVER CENTRAL SCHOOL DISTRICT

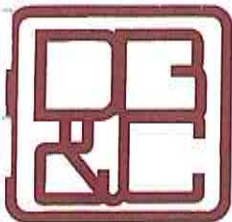
INTERNAL AUDIT RISK ASSESSMENT

2012-2013

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

TABLE OF CONTENTS

Executive Summary	1
Audit Scope, Objective, and Methodology	2
Results and Recommendations	3
Concluding Remarks	9



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Salmon River Central School District

Internal Audit Risk Assessment

School Year 2012-2013

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Executive Summary

In 2005, the Office of the New York State Comptroller (OSC) along with the New York State Education Department (SED) produced the "Five-Point School Financial Accountability Plan." The Plan promotes stronger internal controls, improves school district audits and strengthens the role of boards of education in conducting appropriate oversight. One component of the Five-Point Plan requires all districts to establish an internal audit function, which must include the development, annual updating, and reporting on a risk assessment of district operations.

The Salmon River Central School District (The District) outsourced its internal audit function and engaged Dragon Benware CPAs, P.C. (DBC) to serve as its internal auditor. Dragon Benware CPAs, P.C. performed the 2012-2013 risk assessment for the Salmon River Central School District on behalf of the District's Board of Education and to assist them in compliance with the NYS Five Point Plan for School District Accountability, and Commissioner's Regulations 170.12.

A risk assessment includes a review of a district's operations, including but not limited to, a review of financial policies and procedures and the testing and evaluation of a district's internal controls.

We separated the District's operations into nine auditable/functional units and assigned a risk rating of low, medium, or high to each unit through various methods such as questionnaires and discussions with district staff, and process walk-throughs.

Through this process, we conclude that the following six auditable/functional units present an elevated risk to the District's operations. As a result of the risk assessment we recommend the detailed testing of one of these areas to be completed for this year and one during each of the next two years for the Salmon River Central School District as determined by the Board.

- Extraclassroom Activity Fund
- Payroll and Personnel
- Purchasing and Expenditure - Purchasing
- Purchasing and Expenditure - Accounts Payable
- Revenue and Management - Cash Receipts and Revenue
- Governance, Control Environment & IT - Control Environment

This will place the District on a three year Audit Plan. Based on future updates to the risk assessment, this adaptable three year Audit Plan may need to change as a result of changes to the risk ratings.

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

Audit Scope, Objective, and Methodology

Scope

An annual risk assessment is required by the NYS Five Point Plan for School District Accountability, and Commissioner's Regulations 170.12.

The risk assessment for the Salmon River Central School District was conducted during March 2013 and August 2013.

Objective

To identify factors or conditions that threaten the achievement of a district's objectives. This involves identifying significant risks to the effectiveness and efficiency of operations, to the reliability of financial reporting, and compliance with policies, procedures, applicable laws and regulations.

Methodology

The internal audit function is governed by adherence to applicable AICPA *Generally Accepted Auditing Standards* and The Institute of Internal Auditors' *Code of Ethics*. The Institute's *International Standards for the Professional Practice of Internal Auditing* (Standards) constitutes the operating procedures for the function. The Institute of Internal Auditors' *Practice Advisories* were adhered to as applicable. In addition, we comply with applicable regulations promulgated by the State Commissioner of Education and the school district's policies and procedures.

Per New York Standards, the Internal Audit function is required to develop a risk assessment of a district's operations, including but not limited to, a review of financial policies and procedures and the testing and evaluation of internal controls, and an annual review and update of such risk assessment.

A risk assessment update includes a current year residual risk determination, follow-ups on any previous Internal Audit exceptions, as well as a follow-up on any corrective action plans and any external audit exceptions (financial statement, SED, OSC, etc.).

There are three categories of risk:

- **Inherent Risk** - The nature of some activities or assets makes them a greater risk than others. Some characteristics that generally increase inherent risk are opportunity, new activities, complexity, changes in operating environment, changes in personnel, and rapid growth. Inherent risk is a tool in determining the susceptibility of an entity, unit, or account to fraud, waste, or abuse assuming there were no related internal controls.
- **Control Risk** - The risk that material errors or fraud are not prevented or detected by the internal control system.
- **Residual Risk** - Remaining and assigned risk level calculated after evaluating control and inherent risk.

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

The assigned residual risk rating of low, medium, or high, is calculated after considering inherent and control risk. To establish a control risk rating, internal audit uses various testing methods such as questionnaires and discussions with district staff, and walk-throughs.

Not all risks are equal. Some are more likely than others to occur, and some will have a greater impact than others if they occur. Once risks are identified, their probability and significance must be assessed. Upon identifying and assessing risk, the District must decide on how to deal with it. Based on a cost/benefit analysis, in some cases, the decision may be to control it; in others, it may be to accept it.

Results and Recommendations

DBC has separated the District into nine auditable areas/control cycles. Using the methodology explained above, the residual risk ratings for the Salmon River Central School District have been determined and assigned to the nine units as follows:

Auditable Areas/Control Cycles	Residual Risk
Governance, Control Environment, & IT	Medium
Accounting and Reporting	Low
Revenue and Cash Management	Medium
Purchasing and Expenditures	Medium
Payroll and Personnel	Medium
Extraclassroom Activity Fund	High
Assets and Inventory	Low
Facilities Maintenance and Construction	Low
Student Services and Data	Low

Per New York State Standards, the internal audit function is required to recommend changes for strengthening controls and reducing identified risks, and to specify time frames for implementation of such recommendations. In addition, the recommendations are provided to assist the District in managing and reducing risk. It should be noted that the enhancements recommended are not the only contributing factors to the ratings of medium or high risk. As explained above, many areas are inherently riskier than others, regardless of their internal control structure.

I. Extraclassroom Activity Fund

Situations Noted and Recommendations:

- Per District's Activity Treasurer's Job Description no. 4, "The Activity Treasurer of each extraclassroom activity fund shall be responsible for determining which of the activities of his/her organization is subject to sales tax. As appropriate, the New York State sales tax should be collected and identified by the amount included in each deposit". This appears to be the responsibility of the Faculty Advisor. We recommend that the Student Activity Treasurer's Job Description no. 4 be removed to properly reflect his/her responsibilities.

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

- We noted that faculty advisors do not indicate the sales tax on their deposit forms. Per District's Job Descriptions, the Faculty Advisor of each extraclassroom activity fund shall be responsible for determining which of his organizations are subject to sales tax. As appropriate, the New York State sales tax should be collected and identified by the amount included in each deposit. We recommend following what was indicated in the job description since this conforms to the Regulations of the Commissioner of Education for the control of extraclassroom funds.
- We noted that no Faculty Auditor was appointed for the extraclassroom activity funds. The District found it difficult to find a staff member interested to volunteer for that role. Though some of the faculty auditor's tasks are being done by the Deputy Central Treasurer, it's still important to appoint a person to do the Faculty Auditor role. According to "Finance Phamplet 2, The Safeguarding, Accounting and Auditing Extraclassroom Activity Funds", the function of the auditor shall be distinct and separate from the duties of the other officers. The person appointed shall have no part in the approval of payments, planning of income, or in the keeping of records and forms.
- According to the District's Faculty Advisor's Job Description no. 9, "the books for the graduating class be closed six months after graduation". This appears to be inconsistent with Policy 5520 which states there that "Funds of discontinued extraclassroom activities, those inactive for one year and of graduating classes shall revert to the account of the general student organization or student council and shall be expended in accordance with the organization's constitution". We recommend updating the Faculty Advisor's Job Description to be consistent with Policy 5520.
- We noted that Activity Treasurers do not indicate the receipt no. when recording a deposit transaction to their ledgers. Indicating the receipt no. to the ledger will provide more complete information of the document and tracing of the deposits to the ledgers or vice versa can easily be done.
- We obtained a listing of the District's extraclassroom activity funds and made a selection of 5 activity clubs to verify that internal controls are properly implemented. Per our test work, 4 of the selected activity clubs do not maintain student ledgers.
- We selected 5 samples each for the student deposit (SD) form and student activity fundraiser request (SAFR) form to verify that internal controls are properly implemented. Per our test work we noted the following:
 - 2 of the selected SD forms were not signed by the activity treasurer.
 - 1 of the selected SD form was not signed by the faculty advisor.
 - 2 of the selected SAFR forms were not signed by the activity treasurer.
 - All of the selected SAFR forms were not signed by the central treasurer
 - 4 of the selected SAFR forms indicate the principal's approval after the activity date.

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

II. Payroll and Personnel:

Situations Noted and Recommendations:

- We noted that as of the date of this report, the district does not have written procedures detailing the time and attendance and payroll process. Additionally, there are no written procedures describing the employment process (advertising/posting, interview, reference/credential check, offer, acceptance, starting, etc.). We recommend that these procedures be completed, as indicated by the School Business Executive, by the end of the school year.
- We noted that as of the date of this report, the district does not have an employee manual/handbook for those who are not teachers. We recommend that an employee manual/handbook be created and completed by the end of the school year, as indicated it will be by the School Business Executive.
- We obtained a listing of all employees active for the February 15, 2013 pay period and made a selection of 5 employees to verify that the internal controls are operating effectively. Per our testwork, 1 of the selected employees was not calculated correctly. For employees without contracts, where the Teacher's Salary Schedule is used, we recommend verifying that the step up rate has been changed for the current year. In the case of Shelley Phillips, her longevity rate was not updated for the July 1, 2011 effective date.

III. Purchasing and Expenditures

A. Purchasing and Accounts Payable

Situations Noted and Recommendations:

- Although the Board has appointed a purchasing agent to be responsible for developing and administering the purchasing function and committing the district for purchases by approving purchase orders, the purchasing agent has not established a purchasing calendar. The majority of the District's purchasing is done over the summer on BOCES cooperative purchasing bids; however, per General Municipal Law, section 104-b, a purchasing calendar identifies dates on which certain classes of items will be bid or otherwise purchased. This type of planning helps coordinate the purchasing process on a weekly, monthly, and annual basis. In addition, the use of an orderly purchasing calendar will also help ensure that established procurement policy and procedures are followed and goods and services are received in a timely manner. We recommend that a purchasing calendar be considered.
- We noted that the district participates in cooperative purchasing through BOCES but does not make purchases through the State Office of General Services (OGS), through county governments, from correctional institutions, or from the State contracts/organizations that serve the disabled, where possible, to avoid the cost of bidding. We also noted that preferential vendors, such as the OGS, Corcraft and Blind, are not used. State laws make it

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

possible for school districts to purchase supplies and equipment through the OGS without competitive bidding. Generally, lower prices are available through this method of purchasing. The costs of advertising, developing bid specifications and quality control of the items are not borne by the local district. We recommend the participation in county contracts, purchasing products made by the blind and disabled, purchasing prison-made goods, and other agencies to take advantage of State contracts without competitive bidding.

- We noted that blanket orders used for specific local vendors do not have a fixed monetary limit. In addition, we also noted that not all purchases have purchase orders. We recommend looking for the best pricing among competing supplier bids and setting a fixed monetary limit. As the forecast quantity can be difficult to get with blanket orders, it is important to discuss with the supplier a monetary limit and quantity to keep in stock. We also recommend that all purchases have purchase orders.
- We noted that as of the date of the report, there are no formal written policies in regards to accounts payable. We recommend formal policies be completed by the end of the school year as indicated by the School Business Executive. In districts, paying bills is an important function to maintain an adequate cash flow. Guidance should be provided to districts.

B. Cash Disbursements:

Situations Noted and Recommendations:

- We noted that for those checks over a certain dollar amount, two signatures are not required by the district. It is useful to require two signatures on checks, especially for purchases over a certain amount. This amount will vary with the district budget. Even though two signatures are required, three or four people might have check signing authority to ensure that two signers are available to make disbursements.

IV. Governance and Planning

A. Control Environment

Situations Noted and Recommendations:

- We noted that the District has no designated individuals for the following positions:
 - a. Designated Educational Official (DEO) to receive court notification regarding a student's sentence/adjudication in certain criminal cases and juvenile delinquency proceedings.
 - b. School Pesticide Representative
 - c. Reviewing Official, Hearing Official and Verification Official for participation in the federal Child Nutrition Program (the Hearing Official may not be the same person as the Reviewing and/or Verification Official).

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

Per Policy 1330, the above designations shall be made by the Board of Education at the Annual Organization Meeting. We recommend that such policy be followed. However, if those designations are not applicable to the District, we recommend updating the District's Policy 1330.

- We noted that there is no indication that Policy 2340 was performed during the school year. According to this policy, "The board shall review the effectiveness of its internal operations at least once annually and will formulate a plan for improving its performance. The Superintendent and others who work regularly with the Board may be asked to participate in this review and to suggest ways by which the Board can improve its functioning as a legislative body". We recommend that such policy be performed.

B. Qualified Individuals

Situations Noted and Recommendations:

- We noted that CSEA employees are not currently evaluated because the evaluation tool has not been agreed by both parties at this time. One of the most important responsibilities of a district is to provide each employee with an outline of his/her areas of responsibility and the specific duties/tasks he/she is expected to perform within those areas. It is good business practice for each employee to be evaluated, at least yearly, by his/her immediate supervisor and a written report made. Emphasis should be placed on quality of work desired, focusing on both areas of strength and areas of suggested improvement. It is also essential that employees be equipped for new challenges. Ongoing education and training must prepare employees to keep pace and deal effectively with change.

V. Revenue and Cash Management

A. Cash Receipts and Revenue

Situations Noted and Recommendations:

- For the Extraclassroom Activity Fund, we noted that individuals who collect cash do not each have a cash box. We recommend that each individual collecting cash be provided his or her own cash box to be held responsible for. This control significantly reduces the risk of theft, as each individual is accountable for the contents of their cash box.
- We noted that the individual responsible for the accounts receivable billings is not prohibited from completing cash receipts and disbursement duties. We recommend a segregation of duties. The individual responsible for the billings should be independent of cash receipt and disbursement duties.
- For the Extraclassroom Activity Fund, we noted that receipt forms, cash registers, or log of tickets sold are not used to account for miscellaneous revenues. Through the interviewing process we found there to be a lack of accountability over miscellaneous revenues. Good

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

business practice requires that accountability be established upon receipt of the funds through the use of a receipt form, cash register, log of tickets sold, etc. The funds should be turned over to the treasurer and deposited in a timely manner. Someone independent of the operation should periodically verify the reasonableness and completeness of all deposits. We recommend the use of these suggested methods and the funds deposited as soon as practicable.

- We noted that the District does not have a written policy for collecting delinquent receivables. Clear policies and procedures are necessary for effective accounts receivable management. This will prevent the risk of financial loss due to nonpaying customers. Written policies will also insure that the accounts are all handled in a consistent manner.

VI. Student Services

A. Safety and Security:

Situations Noted and Recommendations:

- We noted that the District's Mohawk School has 10 scheduled fire drills for the current school year which does not comply with the required number of fire drills. According to Education Law §807, instruction and training in fire drills must be held in all public and private schools. Such drills or rapid dismissals shall be held at least 12 times in each school year (8 between September 1 and December 1; 2 during summer [one in the first week]; 2 in the other periods). According to EL §3623(1) and CR §156.3(f)(2), 3 fire drills per year are required on each bus. CR §155.17 requirements include annual testing of sheltering and early dismissal drills.

VII. Assets and Inventory

A. Inventory Controls:

Situations Noted and Recommendations:

- During our interviewing process, we noted that the District does not periodically perform a physical inventory of all property and equipment. Inventory controls are needed over all assets in order to properly safeguard against loss, establish effective utilization, determine needs, and identify any surplus items. Adequate controls include maintaining complete and accurate records, tagging assets with ownership and identification labels, and periodically conducting physical inventories. We recommend that the District periodically perform a physical inventory of all property and equipment and create detailed property records. This should include the fine arts and athletic departments. In connection with this inventory, tags should be placed on each asset with numbers that are recorded in the detail property records. Detailed property records should, at a minimum, include a description of the asset, asset number, and location, the acquisition cost and date of purchase. This will help improve the

**Salmon River Central School District
Internal Audit Risk Assessment
School Year 2012-2013**

tracking of assets for disposal and impairment purposes. Written procedures should be developed to ensure all fixed assets are captured as well as a method for reflecting disposals. Additionally, any supplemental schedules such as the computer records kept by the computer technicians and disposals in all departments should be periodically reconciled to these records.

Concluding Remarks

In order to assist the Salmon River Central School District in mitigating the risk of fraud, waste or abuse, and to comply with the NYS Five Point Plan, DBC recommended areas for detailed testing based on the initial risk assessment results. The Board of Education determined the following areas for detailed testing for this year and the next two years.

- Governance and Control Environment – SY 2012-2013
- Payroll and Personnel – SY 2013-2014
- Information Technology – SY 2014-2015

This will place the District on a three year Audit Plan. Based on future updates to the risk assessment, this adaptable three year Audit Plan may need to change as a result of any changes to the risk ratings.

We wish to convey our thanks and appreciation to the management and staff of the District for the courtesy and cooperation extended to us during the performance of our internal auditing services.

Respectfully submitted,

Dragon Benware CPAs, P.C.

Dragon Benware CPAs, P.C.
September 12, 2013