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**OFFICE OF THE
NEW YORK STATE COMPTROLLER**

**DIVISION OF STATE
GOVERNMENT ACCOUNTABILITY**

**BEGINNING WITH
CHILDREN CHARTER
SCHOOL**

**FINANCIAL MANAGEMENT
PRACTICES**

Report 2006-N-4

AUDIT OBJECTIVE

Our objective was to determine whether the Beginning with Children Charter School (BwCCS) established and maintained an adequate system of internal control over the following areas of financial operation: financial oversight; disbursements and procurement; payroll; and equipment inventory.

AUDIT RESULTS - SUMMARY

We found that the internal controls established by BwCCS are generally adequate; however, compliance with the controls outlined in their Financial Policies Manual (manual) needs to be improved - particularly in the areas of disbursements and procurement.

We found that individuals were not always complying with established procedures before making cash disbursements. For example, we found that 8 of the 80 checks we tested (10 percent) were disbursed even though adequate supporting documentation was not available (e.g. missing invoices). If current practices are not improved, funds could be misappropriated. (See page 4)

To prevent unauthorized purchases, all purchases must be pre-approved in advance by the appropriate authority. However, we found that in 13 of the 80 transactions we tested, purchases were made without appropriate approval. As a result, there is an increased risk that some purchases may not be appropriate. (See pages 4-5)

BwCCS receives administrative support services from the Beginning with Children Foundation, which provides similar services to another charter school. BwCCS reimburses the foundation based on the estimated time foundation employees spend on BwCCS

work. We recommended that BwCCS and the foundation implement a system to verify the accuracy of the billings. (See pages 5-6)

To properly account for equipment, perpetual inventory records should be maintained. In addition, a physical inventory should be performed annually. We found that a complete inventory listing was not maintained and that a physical inventory was not conducted. We also found that formal policies and procedures had not been established. As a result, there is a significant risk that equipment may have been lost or stolen without detection. (See page 6)

Our report contains 6 recommendations to improve internal controls over financial management practices. BwCCS officials generally agree with our findings and have agreed to make changes and correct deficiencies. For example, BwCCS officials told us they will conduct additional staff training at the beginning of each school year and strengthen their purchasing and payroll processes. Further, BwCCS officials agreed to develop formal policies and procedures regarding equipment inventory.

This report, dated June 15, 2007, is available on our website at: <http://www.osc.state.ny.us>. Add or update your mailing list address by contacting us at: (518) 474-3271 or Office of the State Comptroller
Division of State Government Accountability
110 State Street, 11th Floor
Albany, NY 12236

BACKGROUND

In December 1998, the Legislature passed a law authorizing the creation of charter schools in New York State. This legislation is known as the New York Charter Schools Act of 1998. It authorized the establishment of charter schools as independent public schools governed by not-for-profit boards of trustees and managed according to the terms of a five-year performance contract or “charter.” Such schools provide opportunities for teachers, parents, community members, and not-for-profit organizations to establish and maintain schools that operate autonomously of existing schools and school districts.

BwCCS converted from a Department of Education (DoE) School to a charter school in September 2001. It is one of 23 schools currently chartered by the New York City DoE. The school was originally founded in 1992, through a unique public private partnership between the DoE, Pfizer Inc., the Beginning with Children Foundation and the United Federation of Teachers. Today BwCCS is located on two campuses in Brooklyn and serves approximately 450 students enrolled in kindergarten through the eighth grade.

According to BwCCS’s financial statements for the fiscal year ended on June 30, 2005, the school’s operating expenses totaled about \$4.75 million, of which \$3.79 million related to personal service costs (including fringe benefits) and about \$956,000 related to other than personal service costs. Revenues for the same fiscal year totaled about \$4.57 million, of which \$3.80 million was basic school aid provided by the DoE. BwCCS also received \$159,248 in Special Education Aid from DoE, \$398,821 in federal funding, \$183,608 in donations and fundraising, and \$18,768 in interest income. BwCCS incurred an

operating deficit that was funded by the accumulated fund balance.

In addition, DoE pays for the cost of food, transportation, and a portion of textbooks and special education services for BwCCS. DoE also provides safety, health services and space for the BwCCS middle school at no charge. The value of such services has not been quantified by the DoE.

As one of five charter schools created by the conversion of a pre-existing public school, BwCCS is required to pay its staff in accordance with the terms of the prevailing public school teacher contract. Under the contract, staff salaries, fringe benefits and pension contributions have escalated since BwCCS converted in September 2001. These escalating costs have resulted in fiscal stress. According to BwCCS’ annual independent audits, the school operated at a deficit in one of its first five years of operation. However, the audit report for the year ended June 30, 2005 indicated that, after five years of operation, BwCCS had accumulated an operating surplus of \$773,861, which represents about 16.3 percent of its annual operating expenditures.

At the time of our audit, BwCCS was in the process of renewing their charter with the New York State Board of Regents.

AUDIT FINDINGS AND RECOMMENDATIONS

Financial Oversight

Board Oversight

Charter schools are to be governed by a board of trustees (Board). BwCCS’s Board is composed of 13 members and is responsible for overseeing school operations. The Board

consists of four representative groups: BwCCS staff, parents of BwCCS students, Foundation representatives, and community members. According to BwCCS' charter, the Board is required to meet at least six times during the year.

We reviewed the minutes of the Board's meetings during the 2004-05 school year to determine whether the Board was adequately overseeing school operations. We found that the Board met nine times during the 2004-05 period and was actively involved in the schools operations and was providing adequate oversight.

Annual Independent Audit

Pursuant to Section V of the BwCCS charter, each year a fiscal audit of the school should be conducted by a Certified Public Accountant. New York State Education Department further requires that all such audits be conducted in accordance with the government auditing standards issued by the United States Government Accountability Office.

We reviewed the work performed by BwCCS's auditing firm. We found that the school had been audited annually. The audit was conducted in accordance with government auditing standards and the results of the audit were discussed by the Board.

Disbursements and Procurement

Disbursements

According to the BwCCS Financial Policies and Procedures Manual (Manual), adequate supporting documentation must be obtained before disbursing a check for payment. Supporting documentation generally includes a copy of the purchase order, an invoice, and a packing slip or receiving report. In

addition, the Senior Accountant should review the supporting documentation, prepare a check, and forward the check with support to the school Principal for signature. If the check is over \$5,000, the check must also be signed by an authorized Board member.

To determine whether BwCCS officials were following the Manual, we reviewed a judgmental sample of 80 transactions (checks). This sample was selected from a population of 722 checks totaling \$1.06 million that were issued during the period July 1, 2004 through December 31, 2005. The sample included a variety of transactions and amounts, e.g., payments to individuals, businesses, contractors and credit card companies. Our review of the 80 checks, which had a total value of \$226,247, did not disclose any improper use of school funds. However, we found eight instances totaling \$36,431 of payments for which certain of the required supporting documentation was not present (e.g. missing invoices and/or packing slips). BwCCS officials told us they will ensure full compliance with the Manual in the future by conducting additional staff training at the beginning of each school year.

Approval of Purchases

The Manual requires all purchases to be pre-approved prior to placing an order. BwCCS procedures require varying levels of approval, depending upon the dollar value of the item being purchased. The Administrative Assistant can approve purchases for less than \$250 while the Principal's approval is required for purchases greater than \$250, but less than \$5,000. Purchases valued at more than \$5,000 require the approval of an authorized Board member and the Principal.

To determine whether BwCCS officials were complying with the policy regarding purchase approvals, we tested for compliance the same

transactions pertaining to the previously discussed sample of 80 checks. We found that pre-approvals were not obtained in 13 instances totaling \$19,995. Of the 13 instances: 3 were for purchases less than \$250; 9 were for purchases of more than \$250; and 1 was for a purchase of more than \$5,000. When required approvals are not obtained, there is increased risk that some purchases may not be appropriate.

Recommendations

1. Ensure that supporting documentation is obtained before disbursing a check.
2. Ensure that all required pre-approvals have been obtained before making purchases.

(BwCCS officials have accepted these recommendations and have implemented procedures to address them.)

Payroll

Salary Allocation

The Foundation has approximately ten employees that provide various support and administrative services to BwCCS and another charter school affiliated with the Foundation. The Foundation provides business support services, technology related services, and performance testing of BwCCS students. A Memorandum of Understanding (MOU) between the Foundation and BwCCS outlines the reimbursement arrangements for this relationship. For fiscal year 2004-05, the Foundation charged BwCCS \$399,240 for administrative employee salaries. The percentages charged to BwCCS ranged anywhere from 20 percent to 80 percent of the employee's salary.

We found that neither BwCCS nor the Foundation has kept track of the actual number of hours of service Foundation employees provided to BwCCS; instead, estimates were used for billing purposes. Although an elaborate time-tracking system would not be warranted, BwCCS should validate the percentage allocations through other means. For example, the Foundation could track its employees' time for selected periods to validate the percentages. BwCCS officials stated they would implement the use of time sheets for tracking time charged to the charter schools.

Substitute Teachers

BwCCS policy requires that teacher leave be recorded on the school secretary's calendar and also written in a log that lists the names of the substitute teacher hired as well as the regular teacher. After the substitute teacher provides services, they are required to complete a timecard that specifies their identification numbers and the date(s) they worked.

To determine whether BwCCS officials were complying with the policy, we selected a sample of 40 instances where substitute teachers were hired. The sample was selected from a population of 209 teaching substitutions, including 77 from the 2004-05 school year and 132 from the 2005-06 school year. We selected our sample using those months with the highest substitute teacher activity. Of the 40 instances tested, we found the substitute teacher timecards were not available in 35 instances. In addition, we found 23 instances in which the name of the regular teacher, who was on leave, was not documented in the log. As a result, management lacks adequate assurance that the leave accruals of the regular teachers had been properly charged.

Recommendations

3. Determine and record the time and services provided by Foundation staff and charge BwCCS accounts accordingly, based on actual expenses rather than estimates.
4. Revise the recordkeeping system for teacher substitution and ensure that all required documents are maintained properly.

(BwCCS has accepted these recommendations and has implemented changes to address recommendation number 4. For recommendation number 3, BwCCS officials are reviewing implementation options.)

Equipment Inventory

To account for equipment properly, BwCCS should maintain a perpetual inventory record of all equipment and perform an annual physical inventory of the equipment belonging to the school. The inventory record should include the equipment's acquisition date, cost, serial number, and disposition date, if appropriate. Further, each item should be tagged to denote BwCCS's ownership. For fiscal year 2005, BwCCS's financial statements indicated that its inventory was worth \$514,922, or 28 percent of the school's total assets.

We found that BwCCS does not maintain a perpetual inventory of equipment and does not perform an annual physical inventory. Instead, we found that various departments within BwCCS maintain separate equipment inventory listings. These are neither complete nor tested.

In response to our audit, BwCCS officials agreed to develop formal equipment inventory

policies. In addition, they said they would expand their current asset listing to include all appropriate information (e.g. cost and serial number) and perform an annual physical inventory.

Recommendations

5. Develop and implement formal inventory policies and procedures for the recording, control, valuation, and disposition of equipment.
6. Ensure all inventory items are properly tagged and inventoried annually.

(BwCCS has accepted these recommendations and is in the process of implementing procedures to address them.)

AUDIT SCOPE AND METHODOLOGY

We conducted our audit in accordance with generally accepted government auditing standards. We audited the BwCCS's controls over selected financial management practices for the period July 1, 2004 through May 23, 2006. To accomplish our objective, we interviewed officials of BwCCS and reviewed applicable laws and policies and procedures related to the financial operations of the school. We also examined the financial operating records of BwCCS and the work performed by the firm of certified accounts engaged to audit BwCCS's financial statements. Our review included BwCCS's Financial Policies and Procedures Manual, which sets out criteria for financial practices.

To determine whether disbursement, procurement, and contracting practices were in compliance with the Manual, we selected a sample of 80 checks to review and confirm pre-approvals and other supporting documentation.

To determine whether payroll and personnel services were being processed accurately, we reviewed allocation methodologies and selected a sample of 40 instances of teacher substitution and compared them to substitute teacher timecards and logs maintained by the school.

To assess the accuracy of the schools' equipment inventory, we reviewed and tested available inventory records and addressed the adequacy of accounting practices.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State, several of which are performed by the Office of Operations. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these management functions do not affect our ability to conduct independent audits of program performance.

AUTHORITY

The audit was performed according to the State Comptroller's authority under Article V, Section 1, of the State Constitution; and Section 33 of the General Municipal Law.

REPORTING REQUIREMENTS

We provided a copy of this report in draft to BwCCS officials for their review and comment. A copy of their response to the draft report is contained in Appendix A. Their comments were considered in preparing this draft report. BwCCS officials agree with our recommendations and either have already implemented them or will be implementing them.

Within 90 days after the final release of this report, we request the Chairman of the BwCCS Board to report to the State Comptroller advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons why.

CONTRIBUTORS TO THE REPORT

Major contributors to this report were Kenrick Sifontes, Stephen Lynch, Tom Trypuc, Altagracia Rodriguez, Hu Zhang and Elaine Yu.

APPENDIX A - AUDITEE RESPONSE



March 13, 2007

Mr. Steven Sossei, Audit Director
Office of the State Comptroller
Division of State Services
State Audit Bureau
110 State Street, 11th Floor
Albany, New York 12236

Re: **Beginning with Children Charter School
Report 2006-N-4**

Dear Mr. Sossei:

The Beginning With Children Charter School (BwCCS) administration and Board of Trustees wants to thank you for the professionalism of your staff and the respectful manner in which the audit was conducted. The process was ably supervised by Tom Trypuk, and Altagracia Rodriguez. The audit team was considerate of the daily operations of the school and the children we serve.

At the time of the audit, BwCCS was undergoing the renewal process with its authorizer the New York City Department of Education (DoE). I am pleased to inform you that the DoE recommended BwCCS receive a full five year renewal until August 31, 2011 and the State Board of Regents approved the renewal on April 25, 2006. To receive its renewal BwCCS demonstrated that the school was academically successful, organizationally viable and in compliance with applicable laws and regulations pertaining to its charter.

As one of the first charter schools audited by the Office of State Comptroller, we believe the process was informative for all involved. Our expectation is to run a high performing, fiscally sound accountable school that protects the use of public funds; complies with all appropriate laws and regulations; and aligns financial resources to achieve the greatest academic and programmatic outcomes for our students. This audit process has helped us achieve this goal and provided valuable insights and opportunities for reflection.

Below please find our response to the draft report's findings and recommendations.

Disbursements and Procurement

Beginning in September 2006, BwCCS implemented several new procedures in the area of pre-approval and maintenance of supporting documentation. During

Beginning with Children Charter School

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the fall of 2006, BwCCS also conducted staff training in order to better implement the new procedures.

BwCCS accepts recommendations 1 and 2 and has implemented procedures to reflect these recommendations.

Salary Allocation

While the Beginning with Children Foundation employees perform services at two different charter schools, each year during the budget process, careful consideration is given to the needs of each school and the allocation of Foundation staff to support these needs. While timesheets are not maintained, Foundation staff has defined roles and responsibilities at each school and can monitor their time individually to meet the needs of each school. During the year, the percentage allocation to each school by the ten employees whose time is shared is reviewed by Foundation officials to ensure that no school is overcharged.

Please note that the Foundation has spent additional personnel time in the areas of compliance, oversight and facilities without allocation of costs to BwCCS.

BwCCS accepts recommendations 3 and 4. Regarding recommendation 3, BwCCS is currently in the process of investigating time sheet programs that both effectively and efficiently meets the needs of the school. Procedures have been implemented to reflect recommendation 4.

Equipment Inventory

The report indicates for fiscal year 2005, \$514,922 or 28% of the schools total assets, were not properly inventoried. Of the total fixed assets of \$514,922, \$350,599 or 68% of total fixed assets consists of playground equipment and related land improvements which cannot be inventoried. These items are permanently attached to the property.

The balance of fixed assets consists of \$75,184 of computer equipment and \$89,139 of other school equipment and furniture and fixtures.

An overall asset listing for each of the above mentioned areas is maintained by BwCCS. Although BwCCS recognizes that improvements are needed in the maintenance of the overall asset listing in terms of serial numbers, disposition dates, tags on equipment and physical counts, the most at-risk, costly computer equipment has been monitored and counted regularly.



The technology department is the only department which maintains a separate listing of computer equipment. This separate computer equipment inventory contains more detail such as serial numbers and location of assets, however, all the equipment on this listing is also included on BwCCS' overall asset listing. The computer equipment inventory is and has been counted on a regular basis.

BwCCS accepts recommendations 5 and 6 and is in the process of implementing procedures to reflect these recommendations.

In summary, BwCCS implemented recommendations 1, 2 and 4. As for recommendations 3, 5 and 6, BwCCS is in the process of investigating appropriate procedures and systems to effectively and efficiently meet the recommendation requirements.

If you have any questions regarding our responses to either the findings or recommendations, please do not hesitate to contact us. Thank you.

Sincerely,

John R. Day
Chairman of the Board

Cc: Mr. Kenrick Sifontes, Office of the State Comptroller
Ms. Cynthia Bailey, Principal
Mr. Curtis Palmore, Lower School Director
BwCCS Board of Trustees