
**Thomas P. DiNapoli
COMPTROLLER**



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**OFFICE OF THE
NEW YORK STATE COMPTROLLER**

**DIVISION OF STATE
GOVERNMENT ACCOUNTABILITY**

**OUR WORLD NEIGHBOR
CHARTER SCHOOL**

**FINANCIAL MANAGEMENT
PRACTICES**

Report 2007-S-56

AUDIT OBJECTIVE

Our objective was to determine whether Our World Neighbor Charter School (OWNCS) established and maintains an adequate system of internal control over the following areas of financial operation: financial oversight; cash disbursements and procurement; payroll and personal services, and equipment inventory.

AUDIT RESULTS - SUMMARY

We determined that OWNCS's controls can be strengthened to improve the school's financial management. The areas in need of strengthening included fingerprinting, cash disbursements, and procurement. Furthermore, the Board should monitor OWNCS's transactions more closely to ensure compliance with policies and procedures.

All personnel who work at the school are required to hold a valid fingerprint and background clearance from the Commissioner of Education. However, we found that four school employees and eight consultants did not have such clearances, as required. Moreover, 58 school employees began working at the school before receiving fingerprint and background clearances.

We found that school officials did not always use competitive bidding practices to ensure that they received the best prices for the goods and services they purchased. We found no evidence that competitive bidding practices were followed in seven instances that involved \$381,636 in vendor payments. For example, one vendor was paid \$135,142 for repair, security, and cleaning services; however, we found no documentation that a competitive bidding process had been used to select that vendor.

We found that the school was disposing of computer equipment without keeping any records of the discarded items. According to school officials, some parents had donated items of computer equipment that were now of little value. However, without written records, we cannot be assured that the items were indeed of little value or of the appropriateness of the method used to dispose of them.

This report, dated April 10, 2008, 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 New York State Legislature passed a Law authorizing the creation of charter schools in the State. This legislation is known as the New York Charter Schools Act of 1998 (Act). 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 performance contract or “charter” which may not exceed five years. Charter 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.

Opening in 2002, Our World Neighbor Charter School (OWNCS) is one of the 48 schools approved by the State University of New York (SUNY) and chartered by the Regents of the State of New York. In March 2007, the school was awarded a full-term five year charter renewal. Located in Astoria, Queens, the school, which consists of a grammar school and a middle school, offers instruction at the kindergarten through seventh grade. Under the Act, OWNCS is entitled to receive funding from local, State, and Federal sources. Such funding includes per-pupil payments for general operating support, additional State resources for special education, No Child Left Behind - Title 1 dollars, and in-kind services from the New York City Department of Education (DoE) - the school district in which OWNCS is located. During the school year that ended in June 2007, OWNCS had 672 students.

According to OWNCS’s financial statements for the fiscal year that ended on June 30, 2006, the school’s operating expenses totaled \$6.4 million, of which \$3.4 million was related to personal service costs (including

payroll taxes and fringe benefits). Revenue for the same fiscal year totaled about \$6.8 million, of which \$6.1 million was basic school aid provided by DoE.

During academic years 2001-02 through 2005-06, OWNCS was managed by Mosaica Education Inc. (MEI). MEI is a national corporation that manages a number of other public schools. MEI was responsible for all aspects of the school’s education and administrative operations. Their financial responsibilities included: personnel management, business administration, budgeting and financial reporting, and maintenance of financial records. For the school year that ended on June 30, 2006, OWNCS paid MEI a management fee of \$784,972.

OWNCS severed its relationship with MEI on July 31, 2006. School officials also negotiated a \$480,000 buy-out of the existing property lease from the New York City Economic Development Corporation. School officials stated that the fee was negotiated by their Board, their attorneys, the New York City Center for Charter School Excellence, and SUNY’s Charter School Institute (CSI). To facilitate the change from reliance on a management company to self-governance, the school prepared a Transition Plan and presented it to the CSI. On July 26, 2006, the Transition Plan was approved by the Board of Regents of the State of New York.

AUDIT FINDINGS AND RECOMMENDATIONS

We determined that OWNCS’s controls can be strengthened to improve the school’s financial management. The areas in need of strengthening included fingerprinting, cash disbursements, and procurement. Furthermore, the Board should monitor OWNCS’s transactions more closely to

ensure compliance with policies and procedures.

Financial Oversight

Board Oversight

Like all of New York's charter schools, OWNCS is governed by a Board of Trustees (Board). The Act gives the Board final authority for policy, operational decisions, and fiscal management of the school. In addition, Board members have a fiduciary responsibility for school assets and finances.

Accordingly, the Board should design, adopt, and monitor policies and procedures for safeguarding the school's resources from misappropriation and improper use.

We found that the Board met a total of 22 times between July 2005 and May 2007. The Board's agendas for these meetings indicated that the school's financial statements and other related financial documents (e.g. bank reconciliations) were presented and discussed at many of the meetings. However, our review of the minutes found that the Board minutes did not deal specifically with all the topics listed in the agendas. For example, the minutes contained no specific wording that documented discussions on the budget, revenues, and cash disbursements, even though the agendas mentioned that these items would be discussed. School officials agreed that, in the future, they will provide more thorough documentation of the financial discussions that take place during Board meetings. We also found the Board did not have a quorum for 5 (23 percent) of the 22 Board meetings.

Fingerprinting

According to Article 56, Section 2854(3)(a-2)(i) of the Act a criminal history record

check must be performed for all prospective charter school employees who do not already hold a valid clearance from the Commissioner of Education. Part 87 of the Commissioners' Regulations defines a prospective employee as anyone, including Board members, consultants, and vendors, who will reasonably be expected to provide services to the school or which involve direct contact with students under the age of 21. Employees who cannot be or have not been cleared in advance of the start of their employment can be cleared to start work through the use of an Emergency Conditional Clearance (ECC) process. To comply with this process, the Board must pass a resolution stating that the employee has been recommended by the Board Chairman for an ECC and that the employee is granted clearance for 20 business days before it must be renewed by the Board.

We reviewed the personal files of all 71 school employees for the pay-period that ended April 30, 2007 to determine whether the school was in compliance with the Act and found no fingerprint clearance forms for 4 of the school's 71 employees. School officials showed us documentation indicating that two of the four had applied to SED for the clearances; however, the applications were still pending. Although the Board may have granted an ECC for these employees, we found no evidence that the Board did so. We also noted that 58 (81 percent) of the 71 employees began working at the school - for periods ranging from one week to three years before receiving their fingerprint and background clearances.

In addition, we found no fingerprint clearance forms for eight contractors who had regular access to students. School officials provided us with supplementary background-screening documentation for four of the eight contractors; however, the background screening had not been performed by the

Commissioner of Education, as required by the Act. The lack of screening for the contractors was due, at least partially to a lack of procedures on the part of OWNCS.

School officials told us that they are in the process of obtaining the required fingerprinting and background screenings for all employees and contractors who have regular access to their students.

Annual Independent Audit

According to Section 2854(1)(c) of the Act and OWNCS's charter, a certified public accountant is to conduct an annual audit of the school. SED also requires that the annual audit be conducted in accordance with generally accepted government auditing standards issued by the United States Government Accountability Office.

We reviewed the reports provided by OWNCS's auditing firm for the 2005-06 fiscal year. The reports provided by the auditing firm indicate that the audit was conducted in accordance with generally accepted government auditing standards. The firm provided all of the required auditor's reports and the audit results were discussed with the Board.

Recommendations

1. Require the Board to include more details in its meeting minutes to reflect topics listed in the agendas and discussed at the meetings.
2. Ensure a quorum of the Board is present before conducting business.
3. Comply fully with the Act, Commissioner's Regulations, and the OWNCS's charter regarding fingerprinting and background checks.

Cash Disbursements and Procurement

Cash Disbursement

According to the OWNCS Accounting Manual (Manual), school employees requesting to purchase an item must complete a purchase order and all such purchase orders must be approved by the Principal. Original copies of all invoices, purchase orders, rental agreement, and any other financial documentation should be retained. Receiving reports should be obtained before payments are authorized. For the period of July 6, 2005, through February 27, 2007, the school issued 1,199 checks for expenditures that totaled \$5.5 million.

To determine whether school officials were in compliance with the Manual's procedures, we selected a judgmental sample of 41 cash disbursements totaling \$253,884. Our sample was drawn from expenditures that totaled \$500 or more and covered various types of expenditures, including meals, travel, field trips, staff training, personal service, repairs, and supplies. We found that OWNCS's internal controls related to cash disbursements were not operating as stated in the Manual. We found a total of 18 discrepancies associated with 15 of the 41 disbursements, totaling \$86,022. Purchase orders were missing in 13 of the disbursements while receiving reports were missing for five of the disbursements.

Procurement

A good system of internal controls includes a comprehensive procurement policy that outlines procedures for the purchasing of goods and services. The appropriate use of competition provides school officials with the greatest assurance that goods and services are being acquired at a reasonable price and purchases are not influenced by favoritism,

extravagance, or fraud. The Manual states that a competitive bidding process should be used for all major purchases exceeding \$5,000. The Manual also stipulates that requests for goods or services, that require competitive bidding be forwarded to the Business Manager who will then compile the appropriate information and procure the necessary bids. Once the bids are received, the Business Manager must forward them, with a recommendation, to the Principal for review and submission on to the Board for evaluation. Based on the Board's decision, the vendor of choice is to be notified and the goods procured. During July 1, 2006, through February 27, 2007, the school paid more than \$5,000 each to 37 vendors - a total of \$1.91 million.

To determine whether school officials were procuring goods and services in an appropriate manner, we selected a judgmental sample of 18 vendors, who had been paid a total of \$700,927 during fiscal year 2006-07. Our sample consisted of various types of disbursements (e.g. office equipment and personal services) and payments of at least \$5,000 to each of the vendors during fiscal year 2006-07. We found no documentation to verify that a proper bidding process had been followed in 7 of the 18 instances. In total, the school paid \$381,636 to these 7 vendors. For example, the school had paid \$135,142 to a cleaning company for maintenance, cleaning, and security services and \$92,524 to a food provider without any competitive bidding.

School officials told us they could not locate three contracts totaling \$41,930 related to this sample. They also told us that they could not locate four sets of bid documents that had been originally obtained by their former management company (MEI). As a result, there was no assurance that the school received the best value for its purchases.

Bank Reconciliations

Good accounting practices require that the school reconcile the bank and book balances of all cash accounts to determine the reasons for any differences and to correct any errors in the accounts. According to the school's Manual, bank statements must be reconciled by the eighth business day of the new month. In addition, a copy of the original bank statement is to be maintained on file at the school.

School officials are not following the policies and procedures as set forth in the Manual. When we reviewed bank reconciliations for the 21-month period between July 2005 and March 2007, we found no indications that bank reconciliation had been completed for 4 of the 21 months: July 2005, August 2005, September 2005, and June 2006. This non-compliance could result in inaccurate account balances, entry errors, and the failure to detect and prevent misuse of school funds.

School officials explained that such reconciliations had been prepared by their former management company but confirming documentation could not be found. They added that according to their accounting system, reconciliations were completed. However, without copies of those bank reconciliations, we have no assurance that they were performed or were performed in a timely manner.

Recommendations

4. Comply with established cash disbursement policies and procedures.
5. Comply with established policies and procedures for bidding.

6. Establish an adequate recordkeeping system for retaining bidding documentation.
7. Ensure that bank reconciliations are performed in a timely manner and establish an adequate recordkeeping system for retaining such reconciliations.

Payroll and Personal Services

OWNCS's payroll expenditures were approximately \$3.4 million during fiscal year 2005-06. Effective controls over payroll operations require that appropriate policies and procedures be in place and monitored. However, we found that OWNCS lacks policies and procedures for various internal control areas related to the payroll process, such as segregation of duties and removing employees from payroll.

Separation of Duties

The personnel function should be responsible for initiating, calculating, and documenting all payroll changes. The payroll function should process all of these changes and ensure that they are executed properly. Such separation of duties ensures the integrity of the payroll cycle. Proper supervision is also necessary to ensure adequate and timely reporting of employee attendance and the prevention or detection of abuses.

OWNCS has limited staff and resources to fully separate payroll functions. However, we determined that OWNCS officials must review their processes to determine to what extent they can better separate these duties with the school's available resources.

For example, we found that OWNCS's Administrative Operations Coordinator has many responsibilities in the areas of both payroll and human resources. She enters the

payroll data for new employees into the payroll system, verifies the accuracy of payroll, signs for the payroll register, and counts the manual paychecks. She also adds and removes employees from the payroll and maintains all personnel files as well as the monthly administrative attendance sheets.

Further, the Administrative Operations Coordinator provides the only level of approval of the payroll before the data is sent electronically to the payroll vendor. Further, no other school employee periodically reviews her work as a compensating control. Therefore, none of these functions is subjected to adequate checks and balances exposing the school to a potential risk that inappropriate and undetected payroll transactions may occur.

OWNCS officials agreed with our findings and told us they will implement a plan for ensuring that these functions are more effectively separated.

Recommendation

8. Separate key internal control duties and/or institute compensating controls when duties cannot be separated. Such compensating controls should include independent periodic checks on payroll and personnel functions.

Equipment Inventory

Good internal controls over equipment inventory require school officials to maintain a perpetual inventory record and perform an annual physical inventory of all equipment belonging to the school. Each equipment item should be tagged to denote school ownership. In addition, the equipment listing should indicate the equipment's acquisition date, cost, serial number, tag number, and disposition date. Furthermore, effective

controls should include the establishment of detailed written policies and procedures for the inventory process. The total value of the school's furniture, fixtures, and equipment was \$752,720 for the fiscal year that ended on June 30, 2006.

We found that school officials had no evidence to support that physical inventories were performed in fiscal years 2005-06 and 2006-07 to account for all items of equipment. In addition, when school officials provided us with a copy of their equipment inventory listing, we determined that it did not include acquisition dates or the cost of equipment. Further, we found that the listing is updated only twice a year - at the beginning and end of the academic year. Therefore, the equipment listing is not necessarily updated at the time of equipment purchase or disposal.

While interviewing school officials, we found that one of the school's employees was disposing of computer equipment without maintaining a record of what items were discarded. The employee explained that he had not yet created a method for tracking disposals, but that he had donated the equipment to a recycling facility. In addition, there are no inventory records for donated items. Therefore, it is not possible to confirm that these items have little value.

The lack of established written policies and procedures over equipment inventory contributed to the problems we identified. School officials have already taken corrective action and have created an asset disposal form that must be completed in the future when equipment is discarded.

Recommendation

9. Develop and implement detailed written equipment policies and procedures to

address the conditions identified in this report.

AUDIT SCOPE AND METHODOLOGY

We conducted our audit in accordance with generally accepted government auditing standards. We audited OWNCS' controls over selected financial management practices for the period July 1, 2005, through August 23, 2007. To accomplish our objective, we interviewed OWNCS officials and reviewed both the school's Accounting Manual and its laws, policies, and procedures related to the financial operations of the school. We also examined the financial operating records of OWNCS' and the work performed by the firm of certified public accountants engaged to audit OWNCS's financial statements.

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. 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 functions do not affect our ability to conduct independent audits of program performance.

AUTHORITY

The audit was performed pursuant 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 draft copy of this report to Our World Neighbor Charter School officials for their review and comments. Their comments are attached to this final report as Appendix A. Our World Neighbor Charter School officials agreed with our recommendations and have implemented changes to address them.

Within 90 days after the final release of this report, we request the Chairman of the Our World Neighbor Charter School Board of

Trustees 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, Joan Williams, Orin Ninvalle, Teeranmattie Mahtoo-Dhanraj, Hu Zhang, Akande Ojo, and Paul Khor.

APPENDIX A - AUDITEE RESPONSE



Our World Neighborhood Charter School
36-12 35th Avenue
Astoria, NY 11106

March 6, 2008

Kenrick A. Sifontes
Audit Manager
Office of the State Comptroller
Division of State Government Accountability
123 William Street- 21th Floor
New York, NY 10038

Background Information

The \$480,000 payment to MEI pertains to the buy-out of the existing lease from the Economic Development Corporation. The amount was not a severance fee. Please change the language in your draft report.

*
Comment

Board Oversight

As discussed, the financial status of the OWNCS is discussed at the board meetings. OWNC has implemented a process where by all issues pertaining to the financial statements is documented in the monthly minutes. In regards to lack of quorum, OWN has adhere to the 10 meetings in the fiscal year as required by the State University of New York. While there were meetings that lack a quorum at no time did OWN voted on any business without a quorum.

Fingerprint

All fingerprint and clearance background information were subsequently obtained for staff members and independent contractors. OWN recognizes that the process of background check and clearance for employees take awhile as they are processed by the NYS Education Department. In most cases, staff members start the work prior to the completion of this background check. As part of our process, the board will implement a resolution for an emergency conditional clearance pending NYS Education Department final clearance in order for prospective employees to begin employment.

Tel: (718) 392-3405 Fax: (718) 392-2840 www.owncs.org

* State Comptroller's Comment: Changes were made to the final report to address this matter.

Cash Disbursements

OWNC continues to tighten its internal controls. As part of the newly implemented procedures, all purchases that require purchase orders are attach to invoices, packing slips and/or other receiving reports. Receiving slips are now stamped and initial by an administrative staff upon receipt of all items.

Procurement

OWN is a charter school, as such, purchases are often-times based on an area of study and hence, vendors may be the sole source for particular materials. In these cases, OWN will clearly document a vendor as "sole source" when other bids cannot be obtained. With regards to general office supplies, the school often obtains more competitive or lower prices from recurring vendors as compared to other vendors due to our on-going procurement history. Nevertheless, OWNCS continues to seek competitive prices for all purchases. In cases where purchases are greater than \$5,000.00 all bidding materials are currently obtained and maintain in our records.

Bank Reconciliation

As noted, all reconciliations have been completed as reflected in our accounting system. The business office has taken the necessary steps to ensure that all hard copies of the bank reconciliations are filed and maintained in our office on a monthly basis.

Payroll and Personal Services

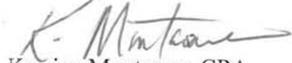
Due to the size of operation and funding restrictions, segregation of duties sometimes become an issue as in the case of OWNCS where the Administrative Operations Coordinator provides one level of approval before the payroll is sent electronically to our payroll vendor. As a compensatory control, OWNCS has forwarded a copy of all employee contracts to the business office to ensure that all employees on payroll are authorized to be paid. In addition, the payroll register from the payroll vendor goes directly to the business office for review. All payments made to employees are subsequently verified by the business office via the monthly general ledger entry with the corresponding payments from OWNCS's bank account.

Equipment Inventory

As noted, an asset disposal form was instituted and is currently being used to record all disposals. In addition, the asset list was updated. Acquisition dates and costs are also included. Prior to the disposal approval forms, disposals were made only for previously donated items. Currently, all equipment is tagged and denotes the property of OWNCS.

For any further questions or comments, please contact me at 718 392-3405 Ext. 207.

Sincerely,



Karrine Montague, CPA
Business Manager
Our World Neighborhood Charter School

Cc: Brian Ferguson, Executive Director, OWNCS