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April 22, 1998

Mr. Carl T. Hayden
Chancellor
The University of the State of New York
State Education Building
Albany, NY 12234

Re: Report 97-F-47

Dear Mr. Hayden:

Pursuant to the State Comptroller's authority as set forth in Section 1, Article V of the State Constitution and Section 8, Article 2 of the State Finance Law, we reviewed the actions taken by State Education Department (Department) officials as of March 20, 1998, to implement the recommendations included in our prior audit report 96-S-31. Our prior report, which was issued October 4, 1996, examined the practices used by the Department to monitor and report on the fiscal status of Department operations.

Background

The Department is charged with the general management and supervision of all public schools and all of the educational work of the State. For fiscal year 1997-98, the State Legislature appropriated to the Department about $285 million for operations. This amount excludes appropriations for capital improvements and aid to school districts. Appropriations for Department programs generally include a combination of State, Federal, and Special revenue funds. For example, the Department's Office of Management Services program is funded by a State appropriation as well as charges against federally funded programs and Special Revenue operations for their share of Department overhead costs. These charges are a fixed percentage of the total personal service costs for Federal programs and Special Revenue operations and are accumulated in the Department's Cost Recovery account.

Funds for administering Federal programs are available to the Department to the extent that staff effort is used to administer such programs. The Department has developed a Time and Effort Allocation System (TEAS) to accumulate staff time expended on administering Federal programs. Information from this system is the basis for obtaining Federal reimbursement.

In November 1995, Department managers projected that the Cost Recovery account would end fiscal year 1995-96 with a deficit of $4.08 million. In March 1996, Department managers reported that the deficit for the Department would total $11.46 million for the fiscal year, if no corrective action was taken. Department records show that $5.04 million of the deficit occurred prior to April 1, 1995, while the remaining $6.42 million occurred during the 1995-96 fiscal year. In March 1996, the Commissioner of Education requested the State Comptroller to audit the Department's financial systems because of the size and fluctuations in the projected deficit. As a result of Department spending reductions and assistance from outside the Department, the deficit was closed on March 31, 1997.

Summary Conclusions

In our prior audit, we found that Department management had not established adequate financial reporting systems and controls and financial systems did not supply accurate or timely information to upper management. We identified weaknesses related to the Department's TEAS and found controls over journal vouchers were not adequate. In addition, the Department's deficit schedule did not include all obligations incurred. We also found that the Department needed to expand the use of technology to reconcile the TEAS with other accounting records, improve accuracy and timeliness of data for the Cost Recovery account, and to summarize employee separation costs.

In our follow-up review, we found that the Department has made progress implementing the recommendations contained in our prior report. For example, Department financial reporting systems and controls reflect some improvements, a new Human Resource/Fiscal Management System is being developed, and selected financial information is being provided more timely to management. The Department plans to use technology to improve TEAS and procedures for processing journal vouchers have been established, but controls are needed to ensure such procedures are properly followed. The full implementation of certain recommendations depends upon the development and implementation of the Department's new Human Resource/Fiscal Management System.

Summary of Status of Prior Recommendations

Of the 15 prior audit report recommendations, the Department has implemented five, partially implemented nine and has not implemented one.

Follow-up Observations

Recommendation 1

Continuously monitor financial condition and address deficits as they occur.

Status - Implemented

Agency Action - The Department now supplies the Board of Regents with a monthly financial report for their review, discussion and action. The report shows the financial status of the overall Department and each of its operating units.

Recommendation 2

Continue to update management reporting systems to ensure that relevant financial data is provided to managers timely.

Status - Implemented

Agency Action - Department management and the Board of Regents are provided with a monthly revenue and expenditure report. The Department plans to automate the reporting process and, as of February 1998, awarded a contract for development of a new Human Resources/Fiscal Management System to accomplish this and other objectives.

Recommendation 3

Ensure that major accounts, such as the Cost Recovery account, are properly automated so that managers can monitor activity on an ongoing basis.

Status - Partially Implemented

Agency Action - The status of the Cost Recovery account is included in the monthly financial report available to management and the Board of Regents. Department officials indicated they will include automation of this account in development of the new Human Resources/Fiscal Management System.

Auditors' Comment - Department officials should ensure that the automation of major accounts is included in the development of its new Human Resources/Fiscal Management System so that Department management can have accurate and timely expenditure reporting.

Recommendation 4

Ensure that established procedures for changing individual employee time allocations are followed. Modifications to time allocations should be made as they occur and not be made after the fact.

Status - Partially Implemented

Agency Action - Department officials have made some procedural changes to address the deficiencies cited in the prior audit. For example, staff receive a form every four weeks showing the TEAS codes to which their effort has been charged. This gives staff an opportunity to review a record of their activity before certifying their program activity

assignment sheets. In addition, formal quarterly reconciliations of TEAS are required to monitor the correctness of the recording of time allocations. Procedures still provide for retroactive changes to TEAS, but such changes require approval at the deputy commissioner and Chief Financial Officer level. Department officials indicated that at times these retroactive changes will be needed to correct errors and to account for certain delays in processes.

Auditors' Comments - We acknowledge that the Department procedural changes concerning TEAS improve controls. However, as we indicated in our prior report, retroactively changing the employees' time allocations makes the initial certifications meaningless. This could also raise questions about which activities the employees were actually carrying out.

Recommendation 5

Stop the practice of covering TEAS imbalances by rolling them forward to subsequent fiscal years.

Status - Implemented

Agency Action - In our follow-up review, Department officials indicated that they will not allow TEAS imbalances to be rolled into subsequent fiscal years in the future.

Recommendation 6

Develop procedures to ensure that all outstanding obligations are accounted for at all times.

Status - Partially Implemented

Agency Action - Department officials can now identify certain of the previously unaccounted for obligations through their data warehouse. However, the Department still does not have systems in place for identifying all types of outstanding obligations. Department officials provided documentation indicating that the Department's proposed Fiscal Management System will have the ability to provide daily extracts of obligations made against Department funds but not encumbered on the OSC central accounting system.

Auditors' Comments - Department management needs to ensure that the Fiscal Management System will provide for the identification of all outstanding obligations.

Recommendation 7

Improve controls over the processing of journal vouchers by requiring that they be authorized at appropriate levels and requiring that large dollar value transactions be approved by Department management.

Status - Partially Implemented

Agency Action - Department officials have adopted new procedures for processing journal vouchers. Requests for journal vouchers must be made in writing to Fiscal Management. Journal vouchers must contain appropriate documentation and be approved by both Budget Coordination and Fiscal Management. In addition, Fiscal Management approval responsibilities for various types of journal voucher transactions have been assigned to separate individuals. However, the Department has not sufficiently limited the number of staff who can approve journal vouchers. We identified 33 individuals who could approve journal vouchers including 15 clerks of various salary grades. In addition, requirements for higher management approvals for large dollar vouchers have not been established.

Auditors' Comments - Limiting the number of staff who approve journal vouchers and requiring higher management approvals for large dollar journal voucher are still needed to implement the recommendation.

Recommendation 8

Prepare periodic reports for Department management that summarize the number, value and the fiscal impact that journal vouchers have on specific programs.

Status - Implemented

Agency Action - In response to our prior audit, the Department's Fiscal Management Unit has developed a report that will allow program offices to obtain the charges processed against any particular account.

Recommendation 9

Ensure that appropriate documentation is maintained to support the journal vouchers that are processed.

Status - Partially Implemented

Agency Action - As noted in Recommendation number 7, Department officials have established procedures for processing journal vouchers. These procedures indicate that each request must provide the reason for the transfer, the cost centers to be credited, the cost centers to be charged, the amount per cost center and sufficient detail to identify the specific expenditures. During our follow-up review, we reviewed a sample of 14 processed journal vouchers to determine if they contained adequate supporting documentation. We identified two journal vouchers that Fiscal Management staff had approved for which sufficient documentation was not provided. Department officials agreed that the documentation on file should have provided more clarification to provide for an adequate audit trail. Officials indicated that steps will be taken to ensure sufficient documentation is provided in the future.

Auditors' Comments - Continued efforts to strengthen documentation in support of journal vouchers is necessary.

Recommendation 10

Ensure that those authorizing journal vouchers do not approve these transactions unless sufficient justification and explanations are provided.

Status - Partially Implemented

Agency Action - As previously noted, Department officials have established procedures for strengthening the processing of journal vouchers. As indicated in recommendation number 9, we identified two journal vouchers with inadequate supporting documentation. When we discussed one of these two vouchers with the Department staff who approved it, the staff could not explain why the transaction was processed. We also reviewed one journal voucher processed regarding the quarterly TEAS reconciliation. Department officials had to obtain additional documentation to explain the nature of certain transactions on this journal voucher. Department officials indicated that the problems we noted with the TEAS journal voucher occurred because reconciliation memos from program offices could not be fully processed on one document. They indicated that they will take steps to provide a better audit trail for future reconciliations.

Auditors' Comments - Documentation must be sufficient to explain the justification for journal vouchers and to be a basis for approval of the voucher.

Recommendation 11

Include information concerning unpaid obligations in financial reports prepared for management.

Status - Partially Implemented

Agency Action - During our follow-up review, Department officials indicated that information concerning unpaid obligations will be available in the future through their newly created data warehouse and the Fiscal Management System that they are developing.

Auditors' Comments - The current monthly report provided to management and the Board of Regents contains data on actual and projected expenditures. The report does not, however, identify the types of unpaid obligations that our prior audit determined were necessary to estimate the deficit. Department officials should ensure that they have the ability to identify and accumulate all Department expenditures through either their data warehouse and/or the Fiscal Management System currently being developed.

Recommendation 12

Revise the current system for allocating costs associated with employee effort to the appropriate funding sources.

Status - Partially Implemented

Agency Action - Department officials indicated that they are limited by the inability to split payrolls on the State Accounting System. Department officials also indicated that they are attempting to do a better job in matching the payroll to areas of staff effort which should help reduce the number of adjustments needed. There have been no other substantive changes to the process since the prior audit. Department officials indicated that it can still take as long as three months to complete a quarterly reconciliation and have these results reflected on the Department's financial management system. During this time, program managers do not have current and accurate information concerning the fiscal status of their programs.

Documentation supplied by Department officials regarding their proposed Financial Management System indicated that it will have the ability to handle multiple fund codes for employee salaries. Department officials indicated that the State's new payroll system and the Department's new Human Resources/Fiscal Management System may help eliminate the problems noted in our prior audit.

Auditors' Comments - As we indicated in our prior audit, the current process for allocating the costs associated with employee effort to the appropriate funding source is time consuming, difficult to track, and does not provide timely information to Department program managers. Department officials should continue their efforts to develop a more efficient system to allocate costs associated with employee effort to the appropriate funding sources.

Recommendation 13

Ensure that revised procedures take advantage of available automation so that the process is streamlined.

Status - Partially Implemented

Agency Action - Department officials indicated they have agreed to purchase software to streamline the TEAS process. Department officials intend to fully automate as much of this process as possible. This will include creating an electronic program activity assignment form and certification as well as automation of reconciliation reports. If practical, the automation will include the preparation of adjusting transactions. However, our review of the proposed Financial Management System indicates that it does not appear that the system will be able to allocate employee costs to the appropriate funding sources, produce the necessary journal vouchers to complete the transaction or calculate appropriate fringe benefit and indirect cost charges and immediately reflect them in the appropriate

program accounts as we suggested in our prior audit report.

Auditors' Comments - The Department needs to perform more comprehensive systems planning to ensure all necessary aspects of automation are accounted for.

Recommendation 14

Automate the revenue calculation and collection process for the Cost Recovery account.

Status - Not Implemented

Agency Action - Department officials indicated that if improvements can be made in this process as a result of developing the Department's Human Resource/Fiscal Management System they will be made.

Auditors' Comments - We believe that automating the process would provide management with more accurate and timely information and, therefore, should be pursued. For example, through automation, revenues could be collected biweekly rather than quarterly resulting in additional annual interest earnings for the State General Fund. In addition, more timely financial analysis of the status of the Cost Recovery account would be possible, more accurate data would be available for staff to use when preparing revenue projections and less staff time would be needed to calculate revenues.

Recommendation 15

Automate the process for identifying and accumulating employee separation costs.

Status - Implemented

Agency Action - Department officials provided documentation indicating the current financial system can produce reports of lump sum payments. These reports show lump sum payments by bargaining unit for each pay period and on a year to date basis. Department officials also indicated that the new Financial Management System will also be capable of identifying and accumulating such costs.

Major contributors to this report were Frank Russo, Robert Lindholm, Jack Dougherty and Thomas Kulzer.

We would appreciate your response to this report within 30 days, indicating any action planned or taken to address any unresolved matters discussed in this report. We also thank the management and staff of the Department for the courtesies and cooperation extended to our auditors during this review.

Yours truly,

Jerry Barber
Audit Director

cc: Robert L. King, DOB
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