



Fonda-Fultonville Central School District Payroll

Report of Examination

Period Covered:

July 1, 2013 — January 31, 2015

2015M-118



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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

September 2015

Dear School District Officials:

A top priority of the Office of the State Comptroller is to help school district officials manage their districts efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as districts' compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving district operations and Board of Education governance. Audits also can identify strategies to reduce district costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Fonda-Fultonville Central School District, entitled Payroll. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the New York State General Municipal Law.

This audit's results and recommendations are resources for district officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The Fonda-Fultonville Central School District (District) is located in seven towns¹ in Montgomery County, the Towns of Carlisle and Esperance in Schoharie County and the City and Town of Johnstown in Fulton County.

The District is governed by the Board of Education (Board), which comprises seven elected members. The Board is responsible for overseeing the District's financial and educational activities. The Superintendent of Schools (Superintendent) is the District's chief executive officer and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction. The Board annually appoints a District Treasurer (Treasurer) and a Deputy District Treasurer (Deputy) to assist with handling and overseeing the District's financial activities.

The District operates three schools with approximately 1,400 students and 158 employees. The District's 2014-15 budgeted appropriations were more than \$24.9 million, primarily funded through State aid and real property taxes. Budgeted appropriations for payroll and associated employee benefits for 2014-15 totaled \$14.9 million, about 60 percent the total budget.

Objective

The objective of our audit was to examine the District's payroll process. Our audit addressed the following related question:

- Are internal controls over payroll disbursements appropriately designed and operating effectively?

Scope and Methodology

We examined payroll disbursement records for the period July 1, 2013 through January 31, 2015.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit is included in Appendix B of this report.

Comments of District Officials and Corrective Action

The results of our audit and recommendations have been discussed with District officials, and their comments, which appear in Appendix A, have been considered in preparing this report. District officials generally agreed with our recommendations and indicated they planned to initiate corrective action.

¹ Towns of Amsterdam, Charleston, Florida, Glen, Mohawk, Palatine and Root

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a(3)(c) of the New York State Education Law, and Section 170.12 of the regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board of Education should make the CAP available for public review in the District Clerk's office.

Payroll Disbursements

The Board is responsible for establishing controls over payroll to safeguard District assets. Duties within the payroll process should be segregated to ensure no individual controls all phases of a payroll transaction. For instance, entering employee payroll information (e.g., pay rates, changes to pay amounts or withholdings), preparing and printing payroll checks and reconciling the payroll bank accounts should not be performed by the same individual. When segregating payroll duties is not feasible, District officials should implement compensating controls to reduce the associated risk. Such controls could include providing increased oversight or having an individual independent of the payroll process prepare the monthly bank reconciliations.

The District should improve controls over payroll disbursements. District officials did not adequately segregate payroll duties or establish sufficient compensating controls. The Deputy performed all steps in the payroll process, which included entering and modifying employee information, salary information, payroll deductions and withholding amounts in the District's accounting software program. In addition, the Deputy prepared the monthly payroll account bank reconciliations.

The Deputy processed the bi-weekly payrolls, prepared payroll checks, applied the Treasurer's signature to the checks and made direct deposits to employee designated bank accounts. The Deputy also remitted the amounts withheld for social security, federal and State income taxes and employee benefits to the appropriate entities and had full user access to the human resources and payroll sections of the accounting software program.² Furthermore, the Treasurer did not review payroll registers or checks prepared by the Deputy to verify that the amounts paid to District employees were accurate.

The Superintendent reviewed the payroll registers provided by the Deputy before the checks were printed to identify any gross pay amounts that appeared different from the previous pay period and performed this same review after the checks were printed. He also compared the net pay totals on the payroll and paycheck registers

² Effective internal control procedures over access rights to a financial software application should allow users access to those functions that are consistent with their job responsibilities, require monitoring of user activity on a periodic basis and prevent users from being involved in multiple aspects of financial transactions. While the Deputy's duties made it necessary for her to access these accounting software program modules, the District should implement compensating controls, such as preparing and reviewing payroll change reports.

to verify agreement and certified both documents. Direct deposit summary information was included on the payroll registers. However, no District officials reviewed the direct deposit upload document³ or compared this document with the certified payrolls. Further, while the District's software program has the capability to generate payroll change reports, these reports were not routinely prepared or reviewed.

In addition to preparing the monthly payroll bank reconciliations, the Deputy was responsible for making deposits in the payroll bank account and preparing a monthly reconciliation report, which provided additional information and was included in the Treasurer's monthly report to the Board. The monthly reconciliation report documented any adjustments made to the bank statement balance for outstanding transactions (i.e., deposits-in-transit and outstanding checks), reflected calculation of the month-end cash balance (by adding receipts and subtracting disbursements from the prior month's ending cash balance) and provided a comparison between the adjusted bank account balance and the report's ending cash balance. While the Treasurer certified this report, he did not verify that the reconciliations performed by the Deputy were accurate by tracing them to source records.

The District's payroll bank account is a clearing account used solely to disburse net pay to District employees. At the end of the month the adjusted bank and cash balance in this account should be cleared out and the reconciled account balance should be zero, because the deposits made to this account should equal the employees' net pay amounts each pay period. Thus, once the paychecks are cashed and direct deposits made, no funds should remain in this account.

We examined the June 30, 2013⁴ and January 31, 2015 payroll bank account reconciliation reports⁵ to determine if they were accurate and whether the reconciled bank account had a zero balance. We found these reconciliation reports were not accurate because a deposit of \$1,828, which was deposited in the bank in November 2012, was erroneously included on each report as a deposit-in-transit. Additionally, District officials could not provide an explanation for adjustments to the bank statement balance contained in these months' Treasurer's reports.

Because of these discrepancies, we prepared bank reconciliations for these months and found the payroll bank account had an adjusted bank

³ The upload document is used to convey direct deposit information (including the amounts to be disbursed to employees' bank accounts) to the District's bank.

⁴ We reviewed the June 30, 2013 bank reconciliation report to ensure that the July 1, 2013 cash balances were accurate.

⁵ See Appendix B for information on our sampling methodology.

balance of \$34,595 as of June 30, 2013 and \$60,834 as of January 31, 2015. District officials could not explain why the bank account had these balances or why the balance increased by more than \$26,000 during our audit period.

We also reviewed payroll transactions and bank account activity during the audit period to determine the reason for the increase in the account balance. Our review disclosed that for employees paid via direct deposit, the Deputy generally made one cumulative transfer from the District's payroll bank account to employees' bank accounts.

However, when a direct deposit was not made on time, the direct deposit to each bank had to be processed separately. We identified one instance where funds for the October 31, 2014 payroll direct deposit totaling \$18,045 were transferred from the trust and agency bank account rather than the payroll bank account. This occurred because the Deputy did not process the direct deposit for this payroll on time. As a result, the Deputy had to initiate separate electronic transactions to disburse direct deposit funds to three different banks and the \$18,045 electronic fund transfer to one of these banks was made from the trust and agency bank account instead of the payroll bank account. Neither the Deputy nor the Treasurer were aware that the funds for one direct deposit were paid from the wrong bank account. As a result, no correcting transactions were made to replenish the trust and agency bank account with funds from the payroll bank account.

The Deputy also paid two employees a total of \$5,526 more than they were entitled to.⁶ In both instances, the employees returned the entire amount paid (totaling \$12,275) to the District and the Deputy subsequently disbursed the correct amount (totaling \$6,749) to these employees. However, the Deputy deposited \$5,526 more in the payroll bank account than necessary because she had deposited the incorrect (higher) amount for the employees' net pay. The Deputy made these payroll corrections after the Superintendent had certified the payrolls and the Superintendent did not subsequently recertify the corrected payrolls.

We also identified one instance where the Deputy Treasurer voided 15 stale dated⁷ outstanding payroll checks totaling \$2,207 and one instance where the Deputy Treasurer voided a lost check totaling \$220. This caused a \$2,427 increase in the adjusted payroll bank account balance because the Deputy Treasurer did not subsequently return the voided amounts to the appropriate operating funds. The voided

⁶ One overpayment occurred on the November 8, 2013 payroll and the other occurred on the June 27, 2014 payroll.

⁷ A check is deemed stale, and the bank it is drawn on is not required to pay it, if it is presented more than six months after the date written on it.

transactions were also made without the Treasurer’s knowledge or approval.

The payroll disbursement discrepancies we identified occurred without the Treasurer’s knowledge or approval because District management did not properly segregate the Deputy’s duties or implement adequate compensating controls such as providing additional oversight. Because of these internal control weaknesses, we tested 100 payroll disbursements totaling \$185,248 from five payrolls⁸ during our audit period to determine if employees were paid the correct amounts, related payroll withholdings were correct and the individuals paid were bona fide District employees.

All the disbursements we reviewed were made to bona fide District employees and accurately calculated in accordance with applicable collective bargaining agreements and Board-approved pay rates. Generally, payroll withholdings were accurate, except for minor discrepancies, which we discussed with District officials. However, because District officials did not establish adequate internal controls over payroll and allowed the Deputy to control all facets of the payroll process without appropriate oversight, there remains a risk that errors or inappropriate transactions could occur and not be detected or corrected in a timely manner. Furthermore, the failure to correctly reconcile the payroll bank account increases the risk that discrepancies will not be detected or resolved in a timely manner.

Recommendations

The Board should:

1. Require District management to authorize and fully document the reasons for all payroll disbursement changes.

District officials should:

2. Segregate the Deputy’s payroll duties so that this individual does not control all aspects of payroll transactions. If it is not feasible to adequately segregate the Deputy’s duties, District officials should establish compensating controls to routinely monitor and review the Deputy’s work or have an individual independent of the payroll process perform the monthly bank reconciliations.

⁸ See Appendix B for information on our sampling methodology.

The Treasurer should:

3. Routinely generate and review payroll change reports to promptly identify, investigate and resolve any payroll discrepancies before the payrolls are submitted for certification.
4. Review the direct deposit upload document each pay period and forward it to the Superintendent for certification.
5. Identify the source of all excess money in the payroll bank account and return the funds to the appropriate operating accounts.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



Fonda-Fultonville

CENTRAL SCHOOL DISTRICT

August 6, 2015

Mr. Jeffrey P. Leonard
 Chief Examiner
 One Broad Street Plaza
 Glens Falls, New York 12801-4396

Dear Mr. Leonard:

Please accept this letter as the official response from the Fonda-Fultonville Central School District Board of Education and Administration regarding the draft Report of Examination of "Payroll" conducted by your office. This response summarizes our position regarding your draft findings and recommendations.

Payroll Disbursements

We recognize the importance of establishing controls over payroll to safeguard District assets, including proper segregation of duties within all phases of the payroll function. District Administration will carefully examine the recommendations presented in your draft report, and will develop and implement a Corrective Action Plan (CAP) to ensure that duties within the payroll function are properly segregated. Compensating controls will be identified and implemented in those instances where segregating duties is not feasibly. Based on your recommendations, the District has already taken steps to ensure that the direct deposit upload and the payroll change report is reviewed and compared to the payroll register.

We appreciate the fact that your examination determined that all of the payroll disbursements reviewed were made to bona fide District employees, and were accurately calculated in accordance with applicable collective bargaining unit agreements and Board approved pay rates.

We would like to thank your office for the recommendations and the cordial, beneficial approach taken by your staff. Your review has provided the District with the opportunity to enhance our internal control structure so we may continue safeguarding District assets.

Sincerely yours,

Thomas Ciaccio
 Superintendent of Schools

Matt Sullivan
 President to the Board of Education

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Data Coordinator

A Legacy of Families First

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

The objective of our audit was to examine the District's payroll process for the period July 1, 2013 through January 31, 2015. To accomplish our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed District officials and reviewed Board minutes and the District policy manual to determine and document the internal controls over the payroll process and the processes used to prepare and review the Treasurer's reports.
- We examined user permissions provided by the Capital Region BOCES Northeastern Regional Information Center to gain an understanding of each user's access permissions for the human resources and payroll modules of the District's accounting software program.
- We examined general ledger trial balances, monthly Treasurer's reports and bank statements for the payroll related accounts.
- We examined the June 30, 2013 and January 31, 2015 payroll bank account reconciliation reports prepared by the Deputy for the payroll clearing account (clearing account) to determine if they were accurate and whether the reconciled clearing account had a zero balance. We selected June 30, 2013 because it provided the balance as of the beginning of our audit period on July 1, 2013, and we selected January 31, 2015 because it was the end of our audit period. Because the reports were inaccurate for each month, we prepared bank reconciliations for these months to determine the ending balances in the clearing account at month-end. We also reviewed payroll transactions and bank account activity during the audit period to determine the reasons for any clearing account balance variances.
- We reviewed 100 payroll disbursements to 20 District employees during five payroll periods during our audit period. We used a random number generator to select 15 employees in each pay period and judgmentally selected an additional five employees. We judgmentally selected the five pay periods and five employees based on increased risk. We reviewed the certified payrolls on the selected pay dates and compared gross pay with salary notices, collective bargaining agreements and Board minutes to determine if the employees were paid the correct amounts, related payroll withholdings were correct and the individuals paid were bona fide District employees.

We conducted this performance audit in accordance with GAGAS. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

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AND SCHOOL ACCOUNTABILITY

Andrew A. SanFilippo, Executive Deputy Comptroller
Gabriel F. Deyo, Deputy Comptroller

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