
Audit Report

Genesee-Livingston-Steuben-Wyoming
Board of Cooperative Educational Services

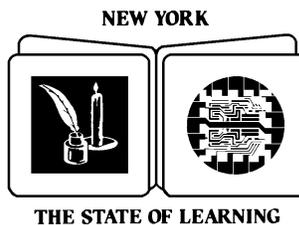
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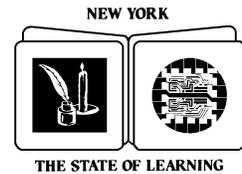
July 1, 1995 through June 30, 1996

BOC-0797-4

November 19, 1998

The University of the State of New York
THE STATE EDUCATION DEPARTMENT
Office of Audit Services
Albany, New York 12234





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November 19, 1998

Mr. Charles E. Moore
District Superintendent of Schools
Genesee-Livingston-Steuben-Wyoming Counties
Board of Cooperative Educational Services
27 Lackawanna Avenue
Mount Morris, New York 14510

Dear Mr. Moore:

The following is our final audit report (BOC-0797-4) on the Genesee-Livingston-Steuben-Wyoming Board of Cooperative Educational Services for the period July 1, 1995 through June 30, 1996. The audit was conducted pursuant to Sections 305 and 1950 of the Education Law in pursuit of Goal #5 of the Board of Regents/State Education Department Strategic Plan: "Resources under our care will be used or maintained in the public interest."

It is the policy of the State Education Department to consider for review matters of significant disagreement which result from the issuance of the final audit report. Appendix C describes the process to be followed in the event of such disagreement.

Ninety days from the issuance of this report, BOCES officials will be asked to submit a report on actions taken as a result of this audit.

I appreciate the cooperation and courtesies extended to the staff during the audit.

Sincerely,

Daniel Tworek

Enclosure

cc: Commissioner Mills
R. Cate
J. Kadamus
T. Sheldon
C. Foster (DOB)
R. Lindholm (OSC)
bcc: G. Illenberg
R. Kesper
S. Spear

Executive Summary

Genesee-Livingston-Steuben-Wyoming (GLSW) BOCES ranked as the 25th largest BOCES in the State, in terms of total general fund expenditures, for the 1995-96 school year (\$25,471,275).

The pie chart illustrates general fund expenditures by program area for the 1995-96 school year.

Background and Scope of the Audit

The audit examined management practices, records and documentation related to selected areas of GLSW BOCES operations for the period July 1, 1995 through June 30, 1996. These areas included Administration, Operations and Maintenance (O & M), Employment Preparation Education, Instructional Support, Other Services and Occupational Education. This was a financial related audit and the objectives were to: determine if cost allocations and transfers were accurate and reasonable; determine if services comply with Department approved specifications; verify that only reasonable and necessary costs were incurred; and verify that the budgetary process provides control over the expenditure of funds.

Audit Results

Below is a summary of the significant audit findings developed in response to the audit's objectives.

- Contact hours totaling \$188,237 were incorrectly claimed for EPE aid (page 5).
- Improvements can be made ensuring only necessary and reasonable expenditures are being made (page 7).
- Opportunities exist to improve management processes relating to inventory system, controls over vehicles, reporting tax information to IRS, budgeting and accounting, hiring retirees and employment contracts (pages 6-7).
- Improvements can be made in documenting O & M allocations (page 16-17).

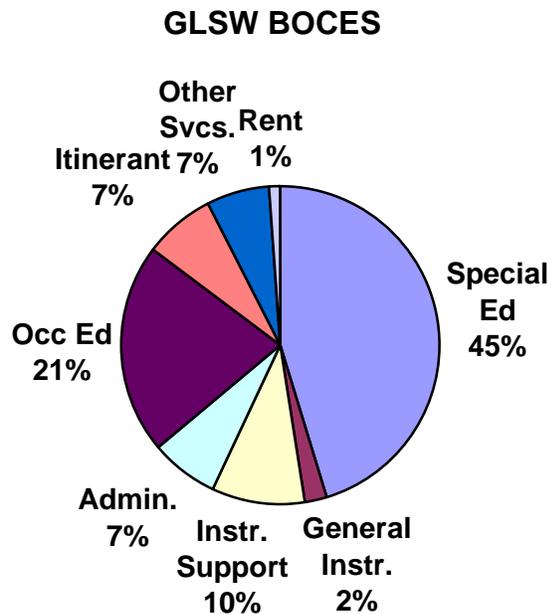


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Introduction

Background

Boards of Cooperative Educational Services (BOCES) are voluntary, cooperative associations of school districts that have joined together to provide educational programs or services more economically than each district could offer by itself. BOCES are organized under Section 1950 of the Education Law. Chapter 474 of the Laws of 1996 amended Section 305 of the Education Law to require the State Education Department (Department) to perform fiscal audits of BOCES at least once every three years.

BOCES may provide such services as special education for students with disabilities, occupational education, academic and alternative programs, summer schools, staff development, computer services, educational communications and cooperative purchasing. There are 38 BOCES in New York State and all but 13 of the 705 operating school districts in the State are members.

Each BOCES submits an annual Cooperative Services Application (CO-SER) to the Department for approval for each program and service offered to districts. After the BOCES obtains approval and determines budgeted program costs, it notifies the districts of available programs and the applicable rates.

Districts that belong to a BOCES are called component districts and are required to pay a share of the BOCES' administrative costs. Only districts that actually use the programs offered by a BOCES, called participating districts, are required to pay for the program costs. Costs charged to the districts for administration and programs are based on budgeted costs and are adjusted at year-end to reflect actual costs. Typically, a refund is issued to the districts to reconcile differences.

Genesee-Livingston-Steuben-Wyoming (GLSW) BOCES was established to be a means for the school districts of Genesee, Livingston, Steuben and Wyoming counties to cooperatively carry out studies, develop specialized facilities and to offer shared educational programs and services. Shared programs allow districts to offer opportunities to students and staff that might not

otherwise be economically possible.

GLSW BOCES, headquartered in Mount Morris, New York, serves 22 component districts. GLSW BOCES ranked as the 25th largest in the State, in terms of total general fund expenditures, for the 1995-96 school year.

Objectives, Scope and Methodology

Pursuant to Sections 305 and 1950 of the Education Law, we audited management practices, records and documentation related to selected operations of GLSW BOCES for the period July 1, 1995 through June 30, 1996. This was a financial related audit and the objectives were to:

- determine if cost allocations and transfers between funds and among CO-SERs are accurate and reasonable;
- determine if CO-SERs comply with Department approved specifications;
- verify that only reasonable and necessary costs were incurred;
- verify that the budgetary process provides control over the expenditure of funds; and
- verify the accuracy and reliability of data reported to the Department for Employment Preparation Education aid.

To accomplish our objectives, we reviewed applicable laws, regulations, policies and procedures; interviewed Department and GLSW BOCES management and staff; examined records and supporting documentation; sampled transactions on a non-statistical basis; and reviewed GLSW BOCES' audited financial statements.

There is no State or BOCES process to assess whether CO-SERs result in measurable cost savings to school districts. As a result, the audit was notable to complete this portion of the scope.

We conducted the audit in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. An audit includes examining, on a test basis, evidence supporting

transactions recorded in the accounting and operational records and applying other audit procedures considered necessary in the circumstances. An audit also includes assessing the estimates, judgments and decisions made by management. We believe that the audit provides a reasonable basis for our findings, conclusions and recommendations.

Comments of GLSW BOCES Officials

GLSW BOCES officials generally agreed with the findings and recommendations in this report. Their response is included as Appendix B.

Employment Preparation Education (EPE)

GLSW BOCES operates an Employment Preparation Education (EPE) Program. This categorical aid program serves students over 21 years of age who have not received a high school or equivalency diploma.

Part 168.4 of the Regulations of the Commissioner of Education states that EPE Program funds may be spent for personal services, employee benefits, equipment, supplies and materials, contractual services, travel expenditures, staff development and training, and other expenditures approved by the Commissioner. These expenditures are to be used only for EPE Program purposes.

GLSW BOCES received a total of \$888,896 in EPE aid for the period July 1, 1995 through June 30, 1996 based on reported contact hours. The audit found that GLSW BOCES did not have an effective system for identifying, documenting and accumulating certain EPE contact hours and, as a result, contact hours were inaccurately reported.

Education Law 3602 states that when total revenue received exceeds the entire cost of such program, State aid payable in the following year will be reduced by the amount of such excess. This means that BOCES must refund the larger of revenues disallowed or expenditures disallowed, but not both. The audit report will be used by the Department to adjust future aid received by GLSW BOCES.

EPE Contact Hours Were Overstated

Part 168 of the Regulations of the Commissioner of Education and Department policy govern the determination of contact hours eligible for EPE. Hours claimed by BOCES must be for eligible students and adequately documented.

GLSW BOCES was not able to provide documentation to support the number of contact hours they claimed. As a result, the audit requested GLSW BOCES to reconstruct the claimed hours. However, GLSW BOCES could not fully account for 27,208 contact hours claimed. In addition, 13,101 hours claimed did not

meet all criteria for eligibility. This included 811 hours for classes that were not approved for EPE; 11,050 hours that were not adequately explained; and 1,240 hours that were not supported by tested attendance records. As a result of these conditions, the audit reduced claimed contact hours by 40,308 hours.

There were several conditions related to these reductions. Several documents provided did not contain student names; therefore the audit could not ensure that these hours were not already included in other documents provided. Some documents revealed that services were provided to students under 21 years of age. Also, the contact hours for the non-traditional program (GRASP) were miscalculated.

GLSW BOCES has recognized that there are problems with the 1995-96 EPE contact hours and has retained the services of a CPA to review the subsequent year's data. GLSW BOCES agrees that eligible contact hours documented are 40,308 less than the number of hours claimed. The audit applied an average rate of \$4.67 per contact hour thereby reducing EPE revenues by \$188,237.

Expenditures

The audit requested supporting documentation for \$291,277 in claimed EPE expenses. GLSW BOCES provided documentation to support \$198,381, or \$92,896 less than claimed. As a result, the audit reduced EPE expenses accordingly.

GLSW BOCES officials do not agree that \$92,896 in expenses was not related to the EPE Program. However, they are unable to provide documentation to prove these expenses were EPE related.

Recommendations

1. Ensure that all claimed contact hours are appropriate and adequately documented.
2. Ensure that EPE funds are only spent on EPE related expenses and are adequately documented.

Comments of GLSW BOCES Officials

GLSW BOCES officials agreed with these recommendations.

Opportunities to Improve Management Processes

Management is responsible for establishing effective management processes or controls. In its broadest context, management controls include the plan of the organization, methods and procedures adopted by management to ensure that its goals are met. These processes include such areas as planning, organizing, directing and controlling program operations. They include systems for measuring, reporting and monitoring program performance. The audit reviewed several processes that it determined significant to the audit objectives and found several opportunities for improvements. These areas include inventory control, reporting to tax authorities, unnecessary and unreasonable expenses, and improving budgeting and accounting for year-end transactions.

Inventory System Needed Improvement

Adequate internal controls over valuable assets should include a system to track the location and use of the assets and controls in place to ensure that the assets are used only for authorized purposes. In addition, the controls should include assurances that the assets are disposed of properly.

During the 1995-96 fiscal year, GLSW BOCES did not have in place a fixed asset inventory system. According to GLSW BOCES officials, this was due to the recent completion of a merger of two BOCES which stretched the staff among several tasks. As such, creating a unified inventory system was determined to be a lower priority and was not completed. GLSW BOCES has since hired an outside firm to perform a physical inventory and create a computerized inventory system.

GLSW BOCES officials agree that the inventory system in effect during 1995-96 was inadequate and have taken several steps to improve the system. GLSW BOCES will reconcile the physical inventory to records of assets that should be present. GLSW BOCES had a complete inventory of assets performed and is awaiting the results. Also, internal procedures were prepared for Business office staff and other program managers who deal with the perpetuation of the inventory. GLSW BOCES conducted training on the new procedures in February 1998.

Controls Over Vehicles Need Improvement

Adequate internal controls over valuable assets should include a system to track the location and use of the assets and controls in place to ensure that the assets are used only for authorized purposes. For vehicles, BOCES should control the use by requiring vehicle logs for each of its vehicles. These logs should be reviewed for evidence of unauthorized use. Vehicle logs can also be used for scheduling periodic maintenance.

Internal Revenue Code, Section 614, requires employers to report the value of personal use of employer-provided vehicles. Publication 17 describes the recordkeeping requirements. The mileage must be recorded and identified as business or personal use for each trip.

GLSW BOCES requires vehicle logs for all but two of its vehicles, which are operated by the District Superintendent and an Assistant District Superintendent. However, GLSW BOCES has since changed this requirement to include these vehicles. The logs now used require the driver to record only the business use of the vehicle, not any personal use. As a result, this new control is incomplete since it does not quantify the amount nor identify the nature of non-business use of a GLSW BOCES vehicle.

Vehicle logs should document all miles driven and be monitored for scheduled maintenance. For vehicles assigned to employees, the mileage log is needed to comply with Internal Revenue Service (IRS) Regulations.

GLSW BOCES officials recognized that the controls in place during 1995-96 were incomplete and took immediate action to correct the problem. GLSW BOCES officials state that the new vehicle logs adequately record personal use of GLSW BOCES vehicles.

BOCES Paid Expenses of Spouses

Article 8 of the New York State Constitution states that no school district shall give or loan any money or property in aid of any individual. This includes advancing funds for later reimbursement by the individual.

GLSW BOCES paid the expenses for the spouses of two employees attending a conference. GLSW BOCES has expended public funds for the benefit of individuals. In addition, the Business office did not request reimbursement of this expense. As a result, GLSW BOCES has inappropriately expended \$218.

GLSW BOCES officials recognize that they failed to request reimbursement from two employees for spouse expenses and will be requesting reimbursement of the \$218. GLSW BOCES officials believe that GLSW BOCES has adequate procedures in place to prevent this from occurring again.

Report All Required Wage and Tax Information to the IRS

The IRS sets rules and regulations regarding the reporting of information for the administration of the federal tax system. According to Internal Revenue Code, Section 614.027(a), the value of personal use of an employer-provided vehicle must be included in income. Additionally, the instructions for completing the W-2 (Wage and Tax Statement) require the employer to report all taxable fringe benefits on the employees' W-2s.

GLSW BOCES failed to properly report the value of personal use of GLSW BOCES-owned vehicles for two employees. In addition, GLSW BOCES did not report payments to another employee for a monthly allowance for business use of a personal car. Each of these amounts is required to be reported to the IRS on the employees' W-2 Wage and Tax statements.

GLSW BOCES officials acknowledge that the value of personal use of GLSW BOCES-owned vehicles was not reported properly in compliance with IRS regulations. GLSW BOCES officials state that the monthly allowance to an individual is not fully taxable. The audit agreed that it is not fully taxable, but it is fully reportable on the individual's W-2. The individual is then responsible to file the appropriate tax forms to claim only the personal use value.

GLSW BOCES officials state they have taken several steps to ensure compliance in the future. These steps include new policies for reporting the taxable portion and personal use of GLSW BOCES-owned vehicles. GLSW BOCES also stated the taxable

portion for each individual was calculated, documented and included on the W-2, as appropriate.

BOCES Exceeded the Approved Budget for Certain Expense Accounts

According to the Uniform System of Accounts for BOCES (System of Accounts), 1988 edition, page 5, issued by the Office of the State Comptroller, “if a proposed purchase exceeds the appropriation available, the encumbrance cannot be entered and must be returned without approval.” In addition, the Financial Management Guide prepared by the Office of the State Comptroller states that “budgetary control requires that appropriations be available prior to incurring an obligation.”

Good internal controls require the preparation of a budget to serve as an operating plan, which besides forming the basis for policy decisions, provides a framework for operations and a method of controlling expenditures.

A system that tracks the amount appropriated, the amount encumbered, year-to-date expenditures and the unencumbered balance is essential to guard against the creation of liabilities in excess of appropriations approved by the Board. Budgets prepared on a line item basis enable an entity to track and monitor the cost of operations.

The accounts within the administration budget exceeded the available appropriations throughout the year. The audit found that at least 11 of 99 accounts (11%) within administration were over budget by over \$189,395 out of \$2,071,957 (9%).

GLSW BOCES officials acknowledge problems with the accounting software package they were using. They have changed to a different budget software system which requires appropriations be available by line item before an encumbrance can be placed.

Properly Account for Year-End Encumbrances

According to the System of Accounts, outstanding encumbrances for which materials have not been delivered as of the end of the year should be recorded as a liability, not an expense.

Specifically, the Comptroller requires BOCES to record the transaction as a credit to account A600 Accounts Payable and a debit to the specific expense account. The payment transaction in the subsequent year should be a debit to accounts payable and a credit to cash.

GLSW BOCES recorded \$672,000 in expenses of the prior year as an expense in the prior year. However, GLSW BOCES did not properly record the subsequent year's journal entry. Specifically, GLSW BOCES recorded a credit to Account 001-1310-300 and a debit to A600 Accounts Payable. While the net effect of this entry would be zero, GLSW BOCES did not comply with the prescribed accounting method for this activity.

GLSW BOCES officials state that part of the reason the situation was handled that way was due in part to limitations of the software package in use during 1995-96. The other primary reason was the amount of staff time required to re-enter all the data the subsequent year. For these reasons, GLSW BOCES officials stated they used one budget code and only one credit entry was made. GLSW BOCES officials believe the new budget software package will assist in future year-end transactions.

The Administrative Budget was Increased and the Original Budget was Exceeded

There currently is no mechanism for BOCES to increase the administrative budget once the original budget has been approved by vote of the component school districts. However, GLSW BOCES increased the administrative budget from \$2,107,894 to \$2,485,346, or \$377,452 (18%).

This increase was possible due to additional revenue derived from sources other than component district charges. Therefore, the charges to the districts were not increased even though GLSW BOCES expended \$2,254,137, or \$146,243 more than the original approved budget.

GLSW BOCES has not complied with Education Law by unilaterally increasing the administrative budget. The component districts did not have an opportunity to approve all administrative expenses.

GLSW BOCES officials agree that they increased the administrative budget contrary to Education Law. They state they will not amend the administrative budget in the future.

Obtain Approval to Hire a Retired Teacher

Section 211 of The New York State Retirement and Social Security Law states that no retired person may be employed in a position in public service except upon approval of the State Civil Service Commission, the Commissioner of Education or other official, depending upon the circumstances.

GLSW BOCES employs a retired teacher to coordinate an athletic association. Since this employee was retired and receiving a pension from the Teachers' Retirement System (TRS), the employee was subject to limitations on income from public service totaling \$8,880 for the 1995-96 fiscal year. Should the employee exceed this amount, the employee's retirement benefits would be reduced.

In order to retain this employee, GLSW BOCES agreed to enter into a deferred compensation agreement. This agreement stated that the employee would earn \$14,000 per year, but be paid \$8,880 per year. The remaining amount would be deferred until after the employee could accept the payment without loss of retirement benefits.

GLSW BOCES hired an attorney to research the legality of this agreement and received an opinion that this would be acceptable. However, GLSW BOCES did not notify the TRS, the State Civil Service Commission or the Commissioner of Education for approval. As a result, GLSW BOCES has not complied with State Retirement and Social Security Law.

GLSW BOCES officials state they made an oral inquiry to the Department to obtain a waiver for the retired teacher under Section 211, but it was denied. They then obtained an opinion from their legal counsel that the deferred compensation route could be taken and not violate the law. GLSW BOCES officials state the TRS told them that the employee has the obligation to request approval under Section 212, not GLSW BOCES.

The TRS has stated that deferred compensation is not a legal way to avoid the requirement of the Law. The TRS has ruled the employee owes the retirement system for the amount earned above the legal limit.

GLSW BOCES officials state they will no longer enter into any new deferred compensation agreements. They further state that salary offers for retirees will be limited to a maximum amount allowed under Section 212.

Contract Allows Excessive Personal Leave

Section 1950 of Education Law states that District Superintendents may not accumulate vacation or sick leave credits in excess of the vacation or sick leave credits for management confidential employees....nor may any District Superintendent, at the time of separation from service, be compensated for accrued and unused vacation credits or sick leave at a rate in excess of the rate permitted management confidential employees.

According to the employment contract between GLSW BOCES and the District Superintendent, the District Superintendent may earn five personal leave days per year and accumulate a balance up to 30 days. Upon separation, the District Superintendent may be compensated for up to 30 days of unused personal leave.

Management confidential employees earn up to five personal leave days per year. They are not permitted to accumulate any unused leave days and are not compensated for these days upon separation. Therefore, this contract provides for benefits in excess of those permitted by Education Law. The District Superintendent has not exercised this clause of his contract.

GLSW BOCES officials explained that the District Superintendent has five personal days in his contract because the merger order from the Commissioner of Education stated that no employee should lose any benefit in place until such time as new benefits were finalized. They claim that the District Superintendent lost five sick days in his contract and the personal days were added to offset this loss. GLSW BOCES officials further state that technically Section 1950 addresses sick and vacation days only and is silent on

personal days. However, the audit maintains the contract is not in compliance with the intent of the Education Law.

Recommendations

3. Improve inventory system and reconcile the physical inventory to records of assets.
4. Ensure all vehicles use mileage logs and record all personal mileage.
5. Ensure personal expenses are not reimbursed.
6. Report all required wage and tax information to the IRS.
7. Ensure that individual accounts do not exceed budgeted amounts.
8. Properly account for year-end encumbrances.
9. Ensure the administrative budget is not increased once approved by the component districts.
10. Ensure approval is obtained to hire retired teachers and the salary paid does not exceed that allowed by Section 212.
11. Ensure the District Superintendent employment contract complies with Education Law.

Comments of GLSW BOCES Officials

GLSW BOCES officials agreed with these recommendations.

Good Practice Identified

Governments must ensure that public funds are used effectively at all times. Changes in need should be considered when incurring contractual obligations.

GLSW BOCES included cancellation clauses in their leases of classroom space. These clauses stated that if GLSW BOCES found that the space is no longer needed due to enrollment declines, then the lease would end.

The auditor notes that another BOCES incurred rental costs for space it was no longer using. This resulted from long-term leases that did not include similar cancellation clauses. This practice helps ensure that public funds are not wasted on unnecessary classroom space.

Cost Allocations and Transfers

The Education Law requires that the net cost of operating a BOCES service be allocated among participating districts. The System of Accounts facilitates such allocations by requiring a separate accounting of revenues and expenditures for each service program.

Expenditures should be charged directly to the pertinent service involved and expenditures related to more than one service should be prorated accordingly. Interservice program transfers are used to record charges in other service programs.

Section 1950 (4)(d) of the Education Law states those component districts that do not participate in a cooperative service are not required to pay any share of the expenditures for such service. In order to ensure that components pay only for services received, cost allocations between funds and among CO-SERs should be accurate and reasonable.

The audit reviewed a limited number of transfers and found that GLSW BOCES needs to improve documentation to ensure that the net cost of operating BOCES services is accurately allocated among participating programs.

Documentation of Operations and Maintenance Allocation Needs Improvement

Good internal controls include adequately documenting certain calculations of costs. These documents should include, at a minimum, documentation of the basis of the calculation and an audit trail to the actual charges.

GLSW BOCES allocated operations and maintenance (O & M) charged to the programs that received the services based upon the square-footage occupied by that program. GLSW BOCES could not adequately document the square-footage used in this calculation. As a result, the audit recalculated the charge for these services.

This recalculation determined that the original calculation by BOCES was reasonable, therefore the audit does not recommend adjustments to the program expenses. However, GLSW BOCES

needs to improve and maintain documentation of this calculation in the future.

GLSW BOCES officials agree that the documentation of square-footage used in this calculation needs improvement, but they do not believe the calculation was incorrect. They state that steps have already been taken to improve documentation including re-measuring or comparing each room to original blue prints, improving the spreadsheet used to determine share percentages, and adding a verification step to the process for the 1999-2000 budget development.

Recommendation

12. Improve documentation of O & M allocations.

Comments of GLSW BOCES Officials

GLSW BOCES officials agree with the finding and have already taken steps to implement the recommendation.

Genesee-Livingston-Steuben-Wyoming BOCES
Contributors to the Report

- Calvin Spring, Audit Manager
- Dan McCarthy, Associate Auditor (Auditor-in-Charge)
- Ronald Talarico, Senior Auditor

**NEW YORK STATE EDUCATION DEPARTMENT
OFFICE OF AUDIT SERVICES
AUDIT REVIEW PROCEEDINGS**

Requests for Audit Review

It is the policy of the State Education Department to consider for review matters of significant disagreement which result from a final audit report issued by the Office of Audit Services.

An organization requesting an audit review must make a written application to the Associate Commissioner for Planning and Policy Development within 30 days of receiving the final audit report. An organization may request a review of an audit whenever the final audit report directs the recovery of funds from the organization and one or more of the following conditions is met:

- Recovery of funds would cause immediate and severe financial hardship to the organization, thereby affecting the well-being of program participants;
- The organization's violation was caused by erroneous written guidance from the State Education Department;
- The State Education Department failed to provide timely guidance on the matter or condition when the organization had previously requested such guidance in writing; and/or
- The report contains errors of fact or misinterpretation of laws, statutes, policies or guidelines.

Organizations requesting an audit review must submit a written application describing how one or more of the above conditions have been met. This application must include all evidence and information the organization believes are pertinent to support its position.

An audit report which recommends improvements in internal controls of administrative or financial systems, but has no material financial impact on the organization, will not be considered for an audit review proceeding.