City of New York

OFFICE OF THE COMPTROLLER

Scott M. Stringer
COMPTROLLER

FINANCIAL AUDIT

Marjorie Landa

Deputy Comptroller for Audit

Audit Report on the Oversight of the Financial Operations of South Bronx Charter School for International Cultures and the Arts

FM15-091A

February 29, 2016

http://comptroller.nyc.gov

THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, NY 10007

SCOTT M. STRINGER
COMPTROLLER

February 29, 2016

To the Residents of the City of New York:

My office has audited the South Bronx Charter School for International Cultures and the Arts ("the School") to determine whether the School exercised adequate oversight over its fiscal affairs; whether it maintained a system of internal controls sufficient to ensure that funds were appropriately expended, authorized, valid, and reasonable; whether transactions were accurately recorded and reported; and if potential conflicts of interest and related party transactions were adequately disclosed and approved. The audit covered funds and expenditures during the audit scope period of Fiscal Year 2013 (July 1, 2012 through June 30, 2013) and Fiscal Year 2014 (July 1, 2013 through June 30, 2014). We audit charter schools to increase accountability and ensure that funds are used appropriately and in the best interest of the public and children's education.

Our audit found that although the School has generally reported its revenue and expenses accurately and has correctly reported student enrollment to DOE, it did not consistently follow its established internal control procedures to ensure the proper oversight of all its financial activities. As a result of these deficiencies, we found that out of the sample of $876,016 in operating expenditures we reviewed, $104,915 were inadequately documented, and an additional $31,151 were not properly authorized, together comprising 15 percent of our sample. We also found that the School could not provide documentation to account for $16,000 in MetroCards that were recorded as having been purchased for distribution to parents. In addition, we found that the School's principal may have been overpaid $23,340 for her work related to an after school program. Further, the School incurred $5,374 in interest and penalties related to Internal Revenue Service payroll withholding tax filings. Finally, we found that the School employed a greater number of uncertified teachers than permitted under its charter agreement.

The audit makes nine recommendations including that the School should: update its written policies and procedures and ensure that the internal control weaknesses identified in this report are addressed; ensure that all expenditures are documented and invoices are properly approved prior to payment; refer the principal's after school payments to the School's Board of Trustees for review and recoupment of any overpayments, if necessary; and continue efforts to assist teachers to obtain certifications so that the School complies with its renewal agreement with DOE.

The results of this audit have been discussed with School officials and their comments have been considered in preparing this report. Their complete written response is attached to this report.

If you have any questions concerning this report, please e-mail my Audit Bureau at audit@comptroller.nyc.gov.

Sincerely,

Scott M. Stringer

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THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
FINANCIAL AUDIT

Audit Report on the Oversight of the Financial Operations of South Bronx Charter School for International Cultures and the Arts

FM15-091A

EXECUTIVE SUMMARY

The objectives of the audit were to determine whether South Bronx Charter School for International Cultures and the Arts (the School) exercised adequate oversight over its fiscal affairs; whether the School maintained a system of internal controls sufficient to ensure that funds were appropriately expended, authorized, valid, and reasonable; whether transactions were accurately recorded and reported; and if potential conflicts of interest and related party transactions were adequately disclosed and approved.

The School is a dual-language school that offers classes in English and Spanish for students in kindergarten through 5th grade. During school year 2012-2013 (also referred to as Fiscal Year "FY" 2013), the School enrolled an average of 390 students. At that time, the School shared space with traditional public schools operated directly by the New York City (the City) Department of Education (DOE) at two locations, 383 East 139th Street and 577 East 139th Street in the Bronx. In the 2013-14 school year (also referred to as Fiscal Year "FY" 2014), the School enrolled an average of 385 students in kindergarten through 5th grade, and operated in the same two locations as in the prior year.

According to the School's certified financial statements for FY 13 (July 1, 2012 through June 30, 2013) and FY 14 (July 1, 2013 through June 30, 2014), the School reported total revenue in the amounts of $5,762,130 and $5,673,722, respectively. The majority of the revenue ($5,237,829 in FY 13 and $5,212,061 in FY 14) was provided by the DOE. The School also received funds from New York State (State), local, and federal grants and other contributions totaling $524,301 in FY13 and $461,661 in FY14. The School reported expenses in the amount of $4,842,687 and $4,203,589 for FY 13 and FY 14, respectively. In FY13, program expenses totaled $3,804,619 and management and general expenses totaled $1,038,068. Similarly, in FY14, program expenses totaled $3,396,915 and management and general expenses totaled $806,674.

Audit Findings and Conclusion

Our audit found that although the School has generally reported its revenue and expenses accurately and has correctly reported student enrollment to DOE, it did not consistently follow its established internal control procedures to ensure the proper oversight of all its financial activities. Consequently, the School failed to maintain adequate internal controls over certain areas of its financial operations and specifically failed to properly segregate financial responsibilities, appropriately authorize financial transactions, properly document certain expenditures, and maintain an adequate inventory of assets.

As a result of these deficiencies, we found that out of the sample of $876,016 in operating expenditures that we reviewed, $104,915 were inadequately documented, and an additional $31,151 were not properly authorized, together comprising 15 percent of our sample. We also found that the School could not provide documentation to account for $16,000 in Metro Cards that were recorded as having been purchased for distribution to parents. In addition, we found that the School's principal may have been overpaid $23,340 for her work related to an after school program. Further, the School incurred $5,374 in interest and penalties related to Internal Revenue Service (IRS) payroll withholding tax filings. Finally, we found that the School employed a greater number of uncertified teachers than permitted under its charter agreement.

Audit Recommendations

To address these issues, we make nine recommendations including that the School should:

- Update its written policies and procedures and ensure that the internal control weaknesses identified in this report are addressed.
- Ensure that all expenditures are documented and invoices are properly approved prior to payment.
- Refer the principal's after school payments to the School's Board of Trustees (the Board) for review and recoupment of any overpayments, if necessary.
- Continue efforts to assist teachers to obtain certifications so that the School complies with its renewal agreement with DOE.

Agency Response

School officials generally agreed with the report's recommendations and represented that the School has accordingly improved its internal controls and accounting procedures. Further, they reported that the Board recognized the need for improved controls in 2013 and began to revise its Accounting and Finance Manual, which is currently under review by the finance committee and should be approved by the end of the fiscal year. However, School officials did not specifically address the report's findings, except stating that the Board was aware of and previously approved the Principal's after school earnings.

AUDIT REPORT

Background

In December 1998, the New York State Legislature passed the Charter Schools Act (the Act), which became Article 56 of the New York State Education Law. The Act authorized the establishment of charter schools as independent not-for-profit public schools governed by boards of trustees and managed under contracts, also known as “charters.” Each charter had to be approved by one of three possible approving entities: the Board of Trustees of the State University of New York, the New York State Education Department and, for schools operating within the five boroughs of the City of New York, DOE. [1]

Charters allow the establishment of public schools that receive funds through local school districts but operate independently from the school districts. Accordingly, by design, charter schools are not subject to most of the pedagogical oversight and regulation that govern traditional public schools. A substantial portion of charter schools’ revenue comes from per-pupil payments made by the local school districts.[2] Charter schools also receive federal and State funding under various programs as well as revenue from fundraising and other school activities. DOE’s operating budget for the 2015-16 school year includes $1.5 billion for charter schools.

At the start of the 2015-16 school year, there were 205 charter schools operating in New York City, with 82 charter schools in Brooklyn, 59 in the Bronx, 45 in Manhattan, 15 in Queens and 4 in Staten Island. These schools collectively serve over 95,000 New York City students, representing approximately 8.6 percent of the City’s 1.1 million public school student enrollment. Approximately 6 percent of charter school students are English Language Learners and 16 percent receive special education services.

All charter schools are 501(c)(3) tax-exempt not-for-profit education corporations. The Act imposes responsibility for oversight over the school’s administrative, fiscal and operational affairs on the school’s board of trustees. Accordingly, each board is responsible for setting policy, operations, and the fiscal management of the schools. Approximately half of all New York City charter schools contract with separate management companies to perform the school’s administrative and pedagogical functions. Services provided by management companies vary from school to school and responsibilities range from having full operational control of the school’s daily functions to back office services.

South Bronx Charter School for International Cultures and the Arts (the School) is a charter school located in the Bronx. The charter for the School was approved by DOE in 2005 and renewed by DOE in 2010 for an additional three years. In April 2013, DOE and the School entered into a second renewal agreement that extended the school’s charter for another five years, until June 18, 2018. (The two charter renewal agreements applicable to the scope period are hereinafter referred to as the “renewal agreements.”) The School’s charter and its renewal agreements set forth numerous operational, organizational, academic, and regulatory requirements applicable to the School. Among other things, the School is required to “at all times maintain appropriate

[1] According to Section 2852 (9-a) of the NYS Education law, after July 1, 2015, all charters will be issued by the New York State Education Department’s board of regents upon applications directly to the board of regents or on recommendations of the board of trustees of the State University of New York pursuant to a competitive process. In addition, effective July 1, 2015, no more than fifty charters shall be granted to a charter for a school located in New York City

[2] Charter schools receive per-pupil funding based on student enrollment. The per-pupil amount is calculated based on a rate as determined by the New York State Education Department and is based on a formula used for all traditional public school districts.

management and financial controls.” The School’s Board, which cannot consist of less than five and no more than nine trustees, is specifically responsible for the oversight of the school’s operations including formulating the general policy to be followed in managing the school’s administrative, pedagogical and fiscal affairs.

The School is a dual-language school that offers classes from kindergarten to 5th grade in both English and Spanish. During school year 2012-2013 (FY 2013), the School enrolled an average of 390 students. The school at that time shared space with traditional DOE public schools at two facilities located at 383 East 139th Street and 577 East 139th Street in the Bronx. In the 2013-14 school year (FY 2014), the School enrolled an average of 385 students in kindergarten through fifth grade. While the School was located at the two public schools, it was not responsible for rent, custodial services, and maintenance and school safety services other than the security needed after public school hours.

According to the School’s certified financial statements for FY 13 (July 1, 2012 through June 30, 2013) and FY 14 (July 1, 2013 through June 30, 2014), the school reported total revenue in the amount of $5,762,130 and $5,673,722, respectively. The majority of the revenue ($5,237,829 in FY 13 and $5,212,061 in FY 14) was provided by the DOE. The School also received funds from State, local, and federal grants and other contributions totaling $524,301 in FY13 and $461,661 in FY14. The School reported expenses in the amount of $4,842,687 and $4,203,589 for FY 13 and FY 14, respectively. In FY13, program expenses totaled $3,804,619 and management and general expenses totaled $1,038,068. Similarly, in FY14, program expenses totaled $3,396,915 and management and general expenses totaled $806,674.

In 2005, the School entered into a management agreement with Victory Schools, Inc. (Victory). Pursuant to the management agreement, Victory was responsible for overseeing the major operations of the School, including design of the curriculum, acquisition of education materials, hiring all staff, and providing all financial and accounting functions. Among other things, Victory was to be paid a management fee in connection with its work for the School.

In February 2013, the School and Victory reduced Victory’s responsibilities at the School and replaced the management agreement with a “service agreement.” Under the service agreement, Victory was no longer responsible for managing the operations of school. However, the service agreement still required Victory to provide academic advice, operational support, financial and accounting services, and other administrative assistance to the School. In compensation for services rendered under the service agreement, Victory was to be paid a service fee $537,000 for FY 13 and a service fee of $280,000 for FY 14. In both years, the School was required to pay the service fee to Victory in 24 installments on a bi-monthly basis. Late payments were subject to interest as provided by the service agreement.

Based on the service agreement in effect in FY 13 and FY 14, expenses incurred by Victory and its employees in performing its services were included in Victory’s fee structure. However, the service agreement further provided that the School would also specifically reimburse Victory for certain additional expenses incurred on behalf of the School. Any additional reimbursement owed to Victory would be billed separately from the service fees and if not paid, would be subject to payment of late fees. Although there were no late payments during the scope period, the service agreement provided that any portion of the bi-monthly service fee not paid within thirty (30) days of its due date would accrue interest at an annualized rate of seven percent (7 percent), provided that such past due payments did not result from DOE’s failure to timely remit the district funding to the School or due to causes beyond the control of the School. Failure to pay on time will result in a liability to the school which will accumulate interest until paid.

As of the close of FY 14, the School reported on its certified financial statement that it owed Victory $528,896 in loan payables that were comprised of deferred management fees incurred prior to the creation of the service agreement and unreimbursed miscellaneous expenses. When asked about this loan, School officials stated that at Victory's request in 2010, the then deferred management fee payments (from FY 07 through FY 2009) were converted to a loan at the rate of 5.125 percent per annum. According to School officials, the deferred management fees resulted from the financial difficulties initially faced by the School as a start-up in 2005, together with the costs incurred by the School for the operation of classes at three different buildings and its purchase of the current School location in 2007. The loan that was based on the deferred management fees was reported as fully paid by the School in June 2015.

During the audit scope period, the School was in the process of constructing its own building. To finance the construction of a dedicated building to be used by the School, in June 2013 the School obtained financing with the assistance of New York City Build NYC Resource Corporation through the issuance of $21,650,000 in Tax-Exempt Revenue Bonds (the "Series 2013A Bonds), bearing interest at variable rates (2.75 to 5 percent) to maturity. The bonds mature on April 15, 2043. The school also received $620,000 in Taxable Revenue Bonds (the "Series 2013B Bonds"), bearing a term fixed rate of 6 percent annually to maturity on April 15, 2017.

As disclosed in the School's certified financial statements, the proceeds of the Series 2013 A Bonds and the Series B Bonds were used in connection with refinancing past liabilities and the construction of a five-story building, located at 164-166 Bruckner Boulevard, Bronx, NY. The property was purchased by the School in 2007 with a combination of equity and loans secured by mortgage liens on the property. As part of the 2013 financing, the existing mortgages were paid in full. The new building is used by the school as its primary location. It contains classrooms, a cafeteria, a kitchen, and space for art, music and administrative activities. In connection with this financing, in FY 2014, the School reported an outstanding long term liability in the amount of $22,270,000 representing future principal bonds payments.

Objectives

The objectives of this audit were to determine whether:

- the School exercised adequate oversight over the School's fiscal affairs;
- the School maintained a system of internal controls sufficient to ensure that funds were appropriately expended, authorized, valid, and reasonable;
- transactions were accurately recorded and reported; and
- potential conflicts of interest and related party transactions were adequately disclosed and approved.

Scope and Methodology Statement

We conducted this audit in accordance with generally accepted government auditing standards. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The scope of this audit covered FY 2013 (July 1, 2012 through June 30, 2013) and FY 2014 (July 1, 2013 through June 30, 2014). Please refer to the Detailed Scope and Methodology at the end of this report for the specific procedures and tests that were conducted.

Discussion of Audit Results

The matters covered in this report were discussed with School officials during and at the conclusion of this audit. A preliminary draft report was provided to School officials, and discussed at an exit conference held on December 21, 2015. On January 19, 2016, we submitted a draft report to the School with a request for comments. We received a written response from School officials on February 1, 2016.

School officials generally agreed with the report's recommendations. In their response, School officials stated, "The Reports [sic] recommendations for improved internal controls and accounting procedures has [sic] merit." Further, they stated that the Board recognized the need for improved controls in 2013 and began to revise its Accounting and Finance Manual, which is under review by the finance committee and should be approved by the end of the fiscal year. School officials did not specifically address the report's findings, except stating that the Board was aware of and previously approved the Principal's after school earnings.

The full text of the School's response is included as an addendum to this report.

FINDINGS

Our audit found that although the School has generally reported its revenue and expenses accurately and has correctly reported student enrollment to DOE, it did not consistently follow its established internal control procedures to ensure the proper oversight of all its financial activities. Consequently, the School failed to maintain adequate internal controls over certain areas of its financial operations and specifically failed to properly segregate financial responsibilities, appropriately authorize financial transactions, properly document certain expenditures, and maintain an adequate inventory of assets.

As a result of these deficiencies, we found that out of the sample of $876,016 in operating expenditures that we reviewed, $104,915 were inadequately documented, and an additional $31,151 were not properly authorized, together comprising 15 percent of our sample. We also found that the School could not provide documentation to account for $16,000 in Metro Cards that were recorded as having been purchased for distribution to parents. In addition, we found that the School's principal may have been overpaid $23,340 for her work related to an after school program. Further, the School incurred $5,374 in interest and penalties related to IRS payroll withholding tax filings. Finally, we found that the School employed a greater number of uncertified teachers than permitted under its charter agreement.

Internal Control Weaknesses

The School failed to consistently adhere to the internal controls outlined in its "Principal's Manual 3: Accounting and Finance," dated 2009 (the Accounting and Finance Manual). Although the Accounting and Finance Manual has not been updated since 2009, it does set forth adequate fiscal policies and procedures to ensure the proper oversight of the School's financial activities, when followed. However, we found that the School did not consistently follow those procedures, as detailed in the following sections of this report.

Improper Use of School-Based Checking Account

The School bypassed fiscal controls that mandate specific documentation and levels of authorization by using the school-based checking account to make certain expenditures. According to the Accounting and Finance Manual, the "purpose of this [school-based] checking account is for small purchases, petty cash replacement, and other minor, necessary purchases." However, we found that the School used the school-based checking account to process payments that, because of the amounts involved, should have been handled through the main checking account. These payments included $4,725 spent for a teacher training workshop and eight recurring payments for off-site storage units used to store school records and equipment, totaling $33,149.

Because the school-based checking account does not require purchase orders or check request forms, the only evidence of approvals for expenditures was the signatures on the checks themselves. According to the School's existing procedures, all disbursements should have the proper authorization levels. For example, purchases between $500 and $1,000 must be approved by the principal and purchases of less than $500 require the approval of only the business manager. However, our audit identified 8 instances in FY 13, totaling $4,039, where checks ranging from $135 to $1,000 were signed by the Director of Human Resources, but were there was no evidence of the required approvals having been given.

In addition to the expenditures described above, out of the $126,211 in expenses made during the audit period from the school-based checking account that we sampled, we found that $5,923 in transactions were inadequately documented. Among them, we identified two payments totaling $1,525 where the invoices were dated well after the checks were issued. For one of the two payments, we found that an invoice dated February 12, 2013 was provided as backup for a check issued on September 1, 2012.

We also found three payments totaling $1,775 for ice cream and ices where two of the invoices provided as backup did not match the check amounts and did not include a business address or contact information for the payee. Further, a review of the general ledger identified another seven payments made in addition to the sampled expenditures to the same vendor totaling an additional $4,286 that similarly did not contain the vendor's business address, phone and fax number and taxpayer ID. Had these payments been processed through the School's main checking account, however, the required check request form would have identified a business address which would have provided sufficient detail to ascertain the validity of the payment.

In addition, we found that the School did not properly segregate responsibilities related to processing payments through the school-based checking account. Specifically, we found that the School's business manager was responsible for both recording journal entries and signing the checks issued through the school-based checking account. To help ensure proper controls over payments, these two functions should have been separate so that the person issuing a payment undertakes an independent review to ensure that all of the required approvals and documentation are in place before payment is made.

Key duties and responsibilities need to be divided or segregated among different staff members to reduce the risk of error or fraud. This should include segregating the responsibilities for processing and recording transactions and handling cash. Since the School used the school-based checking account to process regular payments rather than only for payments of small incidental expenses, it is especially important that such controls be in place.

Lack of Oversight Over Credit Card Expenditures

We found that the School had inadequate oversight over its credit card expenditures. Of the $40,263 in credit card transactions we sampled from the two-year scope period, we found that $10,194 (25 percent) had insufficient documentation. Of this $10,194, the School could not provide *any* backup to support $2,095 in charges. These charges included $230 for an unexplained car rental on the principal's credit card (which was repaid after the audit was initiated) and phone bills, meals, and shipping charges. According to the Accounting and Finance Manual, originals and copies of receipts must be retained when credit cards are used to place orders with vendors.

In addition, for $7,129 of the $10,194 in inadequately documented charges, the School only provided the customer charge receipts that reflected the amounts charged to the credit card; the School did not produce any itemized receipts that identified what the funds were actually spent on. Almost all of these insufficiently documented expenditures, a total of $6,473, were for meals. Per the Accounting and Finance Manual, food allowances are permissible. However, the Accounting and Finance Manual also states that meals are to be kept to reasonable costs. Without itemized bills, we could not determine whether these expenditures were reasonable.

We also found an additional $7,215 in travel expenses that were not approved by the Board in accordance with the principal's employment agreement. In particular, we identified credit card expenditures related to trips by the principal to Boston, Albany, and Las Vegas that lacked documentation establishing prior Board approval. According to the principal's employment agreement, "All conferences attendance [*sic*] must be approved by the Board of Trustees at least 60 days prior to the conference date." We did find that this process was followed and prior approval by the Board was given in connection with other travel and conferences, including trips to San Antonio, San Diego, and New Orleans.

During the audit period, we also found that there were no independent approvals of the principal's credit card usage for two of the four credit card statements we reviewed. These unapproved expenditures included the unapproved travel expenses described above, specific purchases made in connection with otherwise approved travel, catering expenses, and purchases on Amazon and at Home Depot. The Accounting and Finance Manual states that each time a credit card is used, the principal or business manager must fill out a Credit Card Charge Form and obtain the appropriate approvals. However, the School did not use the Credit Card Charge Form during the scope period.

Lack of Documentation and Unapproved Expenditures

Of the $876,016 in payments we sampled for the scope period, we found that the School failed to provide adequate supporting documentation for 19 payments totaling $86,258, nearly 10 percent. Invoices should have been retained for proper record keeping. Twelve of the 19 payments represent AT&T and Verizon phone bills in the amount of $1,317 that were paid monthly directly to the providers from the school's checking accounts without adequate supporting documentation. As a result, we cannot determine whether the cell phone expenses were appropriate or accurately paid.

In addition, our review found four payments totaling $23,936 made from the main checking account that were not properly approved according to the Accounting and Finance Manual. These payments were for insurance, art supplies, cell phone service, and professional services. According to the Accounting and Finance Manual, "There are four escalating authorization levels for purchases." However, three of these purchases did not contain any documentation indicating approval and the other purchase was missing the principal's approval.

Assets Were Not Adequately Inventoried

The School did not maintain an adequate inventory of its assets, as required by its charter renewal agreements with DOE. In addition to this requirement contained in the charter renewal requirements, the Accounting and Finance Manual states that "all fixed assets purchased at the School must first be tagged or identified in accounting records by a control number. Victory Schools will issue pre-numbered tags." Fixed assets are defined in the Accounting and Finance Manual as durable goods that cost $500 or more.

In connection with the audit, the School provided us with a fixed asset schedule that it represented was used for financial accounting purposes. However, this schedule did not contain a breakdown of the specific assets, but rather only presented an aggregate amount associated with specific purchases. The School also provided us with computer inventory lists for FY 13 and 14. However, those lists were missing essential information, such as the asset control numbers and serial numbers. Such information is required by the Accounting and Finance Manual. Moreover, as a result of these omissions, it was not possible for us to test the accuracy of the lists by matching specific items on the list with items found in the School.

In a meeting held on October 28, 2015, the School and Victory officials provided us with a comprehensive list of inventory for computer equipment including approximately 300 items. This list was created after the audit was initiated. In addition, on December 3, 2015, the School provided us an additional list of inventory of non-computer assets.

School Could Not Account for MetroCards It Purchased

The School was unable to account for its purchase of 143, 30-day unlimited MetroCards with a total value of approximately $16,000. Our review found that between July 1, 2012, and June 30, 2014, the School purchased 180 MetroCards for a total of $20,935, which reflected 30 cards purchased every quarter.

According to School officials, the MetroCards were provided to parents whose children did not qualify for the school buses provided by DOE or who were in locations that posed logistical issues for the School's school bus service. However, the School was only able to provide signed receipts for 37 of the 180 MetroCards. Without documentation to support the MetroCards' distribution, we question the appropriateness of the purchase of the remaining 143 MetroCards.

Potential Overpayments to Principal Totaling More Than $23,000

During FY 13, the School's principal received compensation of $11,400 beyond her annual salary of $163,240. Similarly, in FY 14, the School's principal received an additional $11,940 above her $173,240 annual salary. This additional compensation was classified on payroll records for both years as "after-school earnings." According to the School, the additional compensation was paid because the principal was listed as the supervisor for an after-school program which was funded through a federal Title 1 grant. In FY 13, according to payroll records, the principal charged 228 hours for the after-school program and was paid $50 per hour. In FY 14, the principal charged 199 hours for the after-school program and was paid $60 per hour.

Although the School's employee manual allows the principal to receive additional pay for summer programs, it does not specifically allow additional payments to be made to the principal for school-year after-school programs. In addition, the principal's employment agreement states "[i]t is expected that the Principal will devote at least forty (40) hours each week to his/her duties and professional responsibilities." According to the employment agreement, the principal is required to "direct the staff, School functions and programs, student activities and management and building care." Further, our review of budget documents submitted to the Board for review and approval did not identify additional compensation to the principal for the after school program. Since managing school programs is part of the principal's contractual responsibilities and she is required to work at least 40 hour each week, there does not appear to be adequate justification in the School's records for the additional compensation paid to her for the after-school program.

> **School Response: "**The Board of Trustees has reviewed this matter and has determined that it was informed of all payments made to the School's Principal and had previously approved all such expenditures. Accordingly, no overpayment was made to the Principal and no recoupment is warranted."
>
> **Auditor Comment:** Our review of the School's budget documentation or Board minutes did not indicate the Board was aware of or approved these payments. All such decisions should be duly noted in the Board minutes or otherwise documented and the failure to do

so calls into question when and by whom undocumented decisions were made. We are nevertheless pleased that School officials stated that the Board will review its employment contracts for clarification to ensure that all sources of compensation are clearly outlined.

School Incurred IRS Penalties and Interest on Payroll Withholding Taxes

In July 2012, the School was required to pay to the IRS additional withholding taxes that were related to tax filings in the prior fiscal year. According to Victory, the additional assessment of taxes resulted from issues that arose when the School changed payroll vendors. However, the IRS charged the School $5,374 in interest and penalties due to the additional assessment. Pursuant to Victory's agreement with the School, Victory is responsible for overseeing the payroll process, which includes vendor management. Consequently, the School should not be responsible for the $5,374 and should seek to recoup the interest and penalties from Victory.

School Employed A Greater Number of Uncertified Teachers Than Allowed

During FY 2013 the School employed 9 teachers who were not certified, and in FY 2014 it employed 7 uncertified teachers. Section 4.3 of the School's DOE renewal agreements provides that the School "shall employ or utilize in instructional positions only those individuals who are certified in accordance with the requirements applicable to other public schools." Section 4.3 further allows the School to employ up to five teachers who are not certified. However, it states that teachers who are exempted from certification "shall not comprise more than thirty percent (30%) of the instructional employees of the Charter School, or five (5) teachers, whichever is less." Thus, the School's teaching staff exceeded the limit of five uncertified teachers by four in FY 2013 and two in FY 2014.

According to the School's principal, the School was not able to hire enough certified teachers to meet the requirement because it is a bilingual school and there is a limited pool of bilingual teachers with certifications. We also note that the School did make an effort to comply and assist its teachers to obtain the certification. Specifically, in May 2014, the School paid for teachers to participate in the New York City Charter School Center certification services program. The purpose of the program was to provide "technical assistance to schools and teachers to ensure that charter schools comply with all teacher certification regulations."

OTHER ISSUE

The School did not update its website to include its FY13 and FY14 annual reports as required. According to the Charter School Act of 1998, "Each charter school shall submit to the charter entity and to the board of regents an annual report. Such report shall be issued no later than the first day of August of each year for the preceding school year and shall be made publicly available by such date and shall be posted on the charter school's website." In addition, our review found that the School did not post its Board minutes after January 2013, and audited financial statements after FY 2012. At the end of our audit fieldwork, on December 3, 2015, the School updated its website to include the annual reports, Board minutes, and audited financial statements.

RECOMMENDATIONS

We recommend that the School:

1. Update its written policies and procedures and ensure that the internal control weaknesses identified in this report are addressed.

   School Response: "[W]e understand the need for good internal controls and have recently developed a new manual to document our financial accounting policies and procedures which is currently being reviewed by the Finance Committee of the Board of Trustees. We expect that this manual will be approved and the policies and procedures will be implemented by the end of the current school year."

2. Maintain itemized receipts of all expenditures that include vendor contact information and addresses. In addition, in connection with any meal expenditures, document the purpose for each meal and identify the specific individuals in attendance.

   School Response: "The School is currently implementing this recommendation and has included these policies and procedures in the new accounting and finance manual."

3. Use the Credit Card Charge Form or some other similar mechanism for each credit card purchase to ensure that school funds are only used school purposes.

   School Response: "The School is currently implementing this recommendation and has included these policies and procedures in the new accounting and finance manual."

4. Ensure that all expenditures are documented and invoices are properly approved prior to payment.

   School Response: "The School is currently implementing this recommendation and has included these policies and procedures in the new accounting and finance manual."

5. Refer the principal's after school payments to the Board for review and recoupment of any overpayments, if necessary.

   School Response: "The Board of Trustees has reviewed this matter and has determined that it was informed of all payments made to the School's Principal and had previously approved all such expenditures. Accordingly, no overpayment was made to the Principal and no recoupment is warranted. Nonetheless, the Board of Trustees will review its employment contracts for clarification that all sources of compensation made to the School employees with employment contracts are clearly outlined in the agreements."

   Auditor Comment: During the course of the audit, we were not provided with any written documentation to substantiate that these payments were approved by the Board.

6. Ensure that all sources of compensation made to the School employees with employment contracts are clearly outlined in the agreements.

   School Response: "The Board of Trustees will review its employment contracts for clarification that all sources of compensation made to the School employees with employment contracts are clearly outlined in the agreements."

7. Ensure that adequate records are maintained to support the purchase and distribution of MetroCards.

   School Response: "We appreciate the audit findings relating to this matter. However, we believe that proper records for the MetroCard distribution during the audit periods were misplaced during the School's relocation from its two former locations to its new facility in September 2014. We agree on the need for proper documentation and have implemented procedures to improve recordkeeping by migrating to electronic filing of such records."

8. Seek to recoup from Victory the interest and penalties assessed to the School by IRS.

   School Response: "The Board of Trustees greatly appreciates the findings of the auditors relating to this matter. The Board had requested that Victory review the findings and, if appropriate, provide reimbursement back to the School. We are pleased to report that a payment of $6,322.16 was made by Victory to the School in January 2016."

9. Continue efforts to assist teachers to obtain certifications so that the School complies with its renewal agreement with DOE.

   School Response: "The School will continue to provide a pathway to certification for our diverse dual language teachers. However, the Board of Trustees will establish a specific timeframe (3-5 years) after which a teacher must be certified in order to continue teaching at the School. In addition, the School will look into the possibility of providing in-service courses to help uncertified teachers attain certification. Finally, a professional bulletin board will be prominently displayed showing the availability of college courses and programs available locally (within NYC) to help teachers attain certification."

DETAILED SCOPE AND METHODOLOGY

We conducted this audit in accordance with generally accepted government auditing standards. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The scope period of this audit was July 1, 2012, to June 30, 2014.

To achieve our audit objectives, we reviewed the New York State Charter Schools Act of 1998, the School's charter renewal agreements with DOE, Victory's Modified Charter School Services Agreement, the School by-laws, Board minutes, federal tax forms 990, certified financial statements, the School's Accounting and Finance Manual and the Employee Manual. To gain an understanding of the school's financial practices, we interviewed the School's Principal, Director of Operations, Director of Human Resources, and the Business Manager. In addition, we interviewed Victory's Chief Financial Officer and payroll team. The results were documented in memoranda and flowcharts.

To determine the reliability of the School's financial information, we reconciled the School's general ledger and trial balances to the financial statements for FY13 and FY14. To determine whether the general ledger was complete, we judgmentally selected two months per fiscal year with the largest number of disbursements, as recorded in the bank statements, and traced those disbursements to the general ledger.

To determine whether the School properly recorded per pupil funding obtained from DOE, we traced each invoice over the two year period to the School's general ledger. In addition, we verified the total payments made by DOE by reviewing the payment information in the NYC Financial Management System. To determine the accuracy the invoices, we reviewed DOE's Automate the Schools (ATS) reports and the School's student Full-Time Equivalent (FTE) end of the year reconciliation for FY14. In addition, we randomly selected 40 student case files out of 387 and reviewed certain documents such as admission or discharge forms (where applicable) to determine the accuracy of the enrollment data reported to DOE. Finally, we selected the three students who, per ATS reports, moved out of state and verified whether the School reported the discharge timely.

We identified 226 disbursement transactions from the School's general ledger that had no description during the scope period. To determine whether those expenses were appropriate, we randomly selected 25 transactions each year and reviewed their supporting documents. We also reviewed payments that were issued from the school main checking account and school-based checking account. For the main checking account, we stratified our population of expenditures based on dollar threshold ($0 through $999, $1,000 through $4,999, $5,000 through $9,999, and $10,000 and above) and randomly selected 15 expenditures in each category. For each transaction sampled, we requested and reviewed supporting documentation to determine whether payments were documented, authorized, and appropriate.

In addition, as a part of our sampled expenditures, we reviewed payments made to Victory in connection with its service agreement. For each expenditure sampled, we verified that the expense was properly documented and paid in accordance with the terms of the service agreement.

For the school-based checking account, we judgmentally selected the two highest months of expenses each year. For each transaction sampled, we requested and reviewed supporting documentation to determine whether payments were documented, authorized and appropriate. To determine whether the School's credit cards were being used in accordance with the Accounting and Finance Manual, we judgmentally selected the two highest months of expenses each year and reviewed supporting documentation.

For payroll expenditures, we requested and reviewed payroll registers and employee W-2s for the entire audit scope period. To test the accuracy of the payroll register information, we reconciled the wages reported on the employee W-2s to the School's payroll journal. To determine whether the salaries paid were in accordance with the Board approved budget, we compared the payroll register to the approved budget for FY 13 and FY 14. In addition, we also reviewed the Principal's employment contract to determine whether the School compensated the principal in accordance with her contract. We also determined whether the School teachers had the appropriate certification by conducting a search on each employee through the New York State Education Department website.

Finally, to determine whether the school was properly recording its assets, we requested and reviewed the School's inventory list for FY 13 and FY 14. We reviewed the list for completeness and accuracy. To determine whether the School conducted background checks on school employees, we randomly selected 20 out of the entire school's staff of 54 employees and reviewed their personal file for background checks.

South Bronx Charter School for International Cultures and the Arts

January 29, 2015

Via First Class Mail

Marjorie Landa
Deputy Comptroller for Audit
City of New York
Office of the Comptroller
1 Centre Street, Room 1100
New York, NY 10007

Dear Ms. Landa:

We are in receipt of the Financial Audit Report ("Report") on the Oversight of the Financial Operations of the South Bronx Charter School for International Cultures and the Arts (the "School") issued by the Office of the Comptroller (the "Comptroller" or the "Auditors") for the City of New York dated January 19, 2016. This letter responds to the findings and recommendations set forth in the Report.

As you know, the School is a model of excellence providing its students with a constructivist and child centered curriculum. The School's intellectually challenging and standards based curriculum is enriched by our international perspective, the arts, and dual language program. Our students receive a well-rounded education that uses the arts to promote excellence in all areas, including cognitive, social, emotional, and moral. Our School meets or exceeds New York State Learning Standards, aligns student learning to those standards and supports teachers with professional development opportunities. Our community, our parents, and staff are empowered to participate meaningfully in our school to strengthen its potential for success.

The School's Board of Trustees ("Board") has carefully reviewed the Report's findings and recommendations. Our responses to the recommendations are set forth in Attachment 1. The Reports recommendations for improved internal controls and accounting procedures has merit. We note, however, that the Board recognized this in 2013 and began implementing steps to improve in the administrative functions. We continue those improvements, but also note that the Auditors did not determine there were any intentional acts which affected the School's finances. We also note the recommendations and findings of non-financial matters, which we believe were outside the scope of the audit and Report.

South Bronx Charter School for International Cultures and the Arts

On behalf of the Board, I wish to thank the Comptroller and its Auditors for the diligent, thorough and professional approach to the audit and Report. We believe that by its recommendations, the Comptroller has assisted the School in fulfilling its mission while concurring in the School's efficient operation, quality and integrity.

Very truly yours,

The Board of Trustees of the
South Bronx Charter School for
International Cultures and the Arts

BY:____________________
Pricilla Ocasio, Chair

Attachment 1

AUDIT RECOMMENDATION	**SCHOOL RESPONSE**
1. Update its written policies and procedures and ensure that the internal control weaknesses identified in this report are addressed.	**SBCSICA RESPONSE**: This Audit Report covers fiscal years 2013 and 2014 which were periods of transformational activity and transition at the School. As noted in the Background section of this Audit Report, during the audit scope period (1) the School shared space with and operated out of two traditional public school facilities, (2) School administrators were involved with overseeing construction of a new school building and obtaining over $22 million in long-term financing and (3) management of the School's day-to-day operations was being transitioned from Victory, the School's external management company, to internal administrative resources at the School. The School successfully relocated to its new building at the beginning of fiscal year 2015. In light of the activity described above, it is not surprising that documentation and evidence of authorization could not be located for a relatively small percentage of expenditures subject to the audit sample. Furthermore, we are pleased that the audit found no evidence of wrongdoing or inappropriate spending. Nonetheless, we understand the need for good internal controls and have recently developed a new manual to document our financial accounting policies and procedures which is currently being reviewed by the Finance Committee of the Board of Trustees. We expect that this manual will be approved and the policies and procedures will be implemented by the end of the current school year.
2. Maintain itemized receipts of all expenditures that include vendor contact information and addresses. In addition, in connection with any meal expenditures, document the purpose for each meal and identify the specific individuals in attendance.	**SBCSICA RESPONSE:** The School is currently implementing this recommendation and has included these policies and procedures in the new accounting and finance manual. As noted in comment no. 1 above, the Finance Committee of the Board of Trustees is currently reviewing this manual. We expect the manual will be approved by the end of the current fiscal year.

3. Use the Credit Card Charge Form or some other similar mechanism for each credit card purchase to ensure that school funds are only used school purposes.	**SBCSICA RESPONSE**: The School is currently implementing this recommendation and has included these policies and procedures in the new accounting and finance manual. As noted in comment no. 1 above, the Finance Committee of the Board of Trustees is currently reviewing this manual. We expect the manual will be approved by the end of the current fiscal year.
4. Ensure that all expenditures are documented and invoices are properly approved prior to payment.	**SBCSICA RESPONSE**: The School is currently implementing this recommendation and has included these policies and procedures in the new accounting and finance manual. As noted in comment no. 1 above, the Finance Committee of the Board of Trustees is currently reviewing this manual. We expect the manual will be approved by the end of the current fiscal year.
5. Refer the principal's after school payments to the Board for review and recoupment of any overpayments, if necessary.	**SBCSICA RESPONSE**: The Board of Trustees has reviewed this matter and has determined that it was informed of all payments made to the School's Principal and had previously approved all such expenditures. Accordingly, no overpayment was made to the Principal and no recoupment is warranted. Nonetheless, the Board of Trustees will review its employment contracts for clarification that all sources of compensation made to the School employees with employment contracts are clearly outlined in the agreements.
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7. Ensure that adequate records are maintained to support the purchase and distribution of MetroCards.	**SBCSICA RESPONSE**: We appreciate the audit findings relating to this matter. However, we believe that proper records for the MetroCard distribution during the audit periods were misplaced during the School's relocation from its two former locations to its new facility in September 2014. We agree on the need for proper documentation and have implemented procedures to improve recordkeeping by migrating to electronic filing of such records.

8. Seek to recoup from Victory the interest and penalties assessed to the School by IRS.	**<u>SBCSICA RESPONSE</u>**: The Board of Trustees greatly appreciates the findings of the auditors relating to this matter. The Board had requested that Victory review the findings and, if appropriate, provide reimbursement back to the School. We are pleased to report that a payment of $6,322.16 was made by Victory to the School in January 2016.
9. Continue efforts to assist teachers to obtain certifications so that the School complies with its renewal agreement with DOE.	**<u>SBCSICA RESPONSE</u>**: As discussed with the Auditors on several occasions, as a bi-lingual school, SBCSICA has encountered difficulty in engaging certified teachers who can teach in dual languages. Accordingly, as the authorizers are aware, the Board of Trustees have provided an opportunity for teachers with diverse backgrounds to commence employment at the School and assist them in the path to certification. For example, of the 7 teachers identified as being uncertified in FY 2014, 6 have subsequently received their teaching certificates. The School will continue to provide a pathway to certification for our diverse dual language teachers. However, the Board of Trustees will establish a specific timeframe (3-5 years) after which a teacher must be certified in order to continue teaching at the School. In addition, the School will look into the possibility of providing in-service courses to help uncertified teachers attain certification. Finally, a professional bulletin board will be prominently displayed showing the availability of college courses and programs available locally (within NYC) to help teachers attain certification.