A Special Investigation of

THE THADDEUS STEVENS COLLEGE OF TECHNOLOGY

June 2006

Auditor General Jack Wagner

Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, Pennsylvania 17120-0018

JACK WAGNER
AUDITOR GENERAL

June 2, 2006

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania
Harrisburg, Pennsylvania 17120

Dear Governor Rendell:

The Department of the Auditor General's Office of Special Investigations has completed a special investigation of the practices of the Business Office of the Thaddeus Stevens College of Technology in Lancaster, Pennsylvania. This investigation originated from a request by the Department of the Auditor General's financial auditors during this Department's financial audit of the College for the fiscal year ended June 30, 2004. Reports of this Department's financial audit and performance audit of the College were released on January 26, 2006.

During the course of this investigation, we found the following:

- The College made over $80,000 in payments from a separate Disbursement Account without adequate and appropriate supporting documentation. According to the Pennsylvania Department of Education, that agency was not aware of the balance in the Disbursement Account, which exceeded $653,000 at its height during the fiscal year ended June 30, 2003;

- The College lacked adequate policies, procedures, and internal controls for its Visa credit cards, which were used to make over $1.5 million in purchases from May 2003 through September 2004;

- The College lacked adequate policies, procedures, and internal controls for its fixed assets, which caused a systemic failure to track and record over $1.9 million worth of fixed assets for the period of July 1, 2003 to December 19, 2005; and

- The College's leave system permits employees to carry excessive leave balances, which, for three officials, could result in payments upon their termination and/or retirement estimated at $190,000.

We also have several additional concerns that are listed at the end of this report. Consistent with the policy and practice of the Department, this report is being forwarded to the State Ethics Commission for whatever further action it may deem appropriate.

We urge the College and the Board to implement all of the recommendations made in this report, as well as those made in the reports of the financial and performance audits. The Department of the Auditor General will follow-up at the appropriate time to determine whether the recommendations have been implemented.

This report is a public document and its distribution is not limited. Additional copies can be obtained on the Department of the Auditor General's website, *www.auditorgen.state.pa.us*.

Sincerely,

/S/

JACK WAGNER
Auditor General

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II. The College Lacked Adequate Policies, Procedures, And Internal Controls For Its Visa Credit Cards, Which Were Used To Make Over $1.5 Million In Purchases From May 2003 Through September 2004.	• Review all credit card purchases made since July 1, 2003 to ensure that all appropriate supporting documentation is available to justify each purchase; • Maintain a limited number of credit cards for appropriate purposes and implement policies, procedures, and internal controls governing their use; • Cancel and physically destroy all other credit cards; and • Re-evaluate the abilities of Business Office personnel and the adequacy of internal controls.
III. The College Lacked Adequate Policies, Procedures, And Internal Controls For Its Fixed Assets, Which Caused A Systemic Failure To Track And Record Over $1.9 Million Worth Of Fixed Assets For The Period Of July 1, 2003 To December 19, 2005.	• Update and maintain one consolidated fixed asset ledger for all fixed assets of value; • Retain a certified public accounting firm to assist in tracking, recording, and maintaining fixed assets; • Re-evaluate the fixed asset policies and procedures regarding computer peripherals; and

	• Tag each applicable item and discontinue the practices of tagging only one item of a bulk purchase, designating one tag for an entire room of assets, and placing fixed asset tags on items that are not included on fixed asset ledgers.
IV. The College's Leave System Permits Employees To Carry Excessive Leave Balances, Which, For Three Officials, Could Result In Payments Upon Their Termination And/Or Retirement Estimated At $190,000.	• Record, convert, and remove leave balances and address the issue of excessive leave balances in accordance with Commonwealth leave policy and with the assistance of a software program that reflects and implements that policy; • Establish a sick leave bank for employees to donate their excess sick leave for use by other employees who are in need of such leave; and • Require the President to report his leave usage to the Board chairperson or his/her designee and seek formal approval from that individual for his usage of leave.
Additional Concerns regarding the following three issues: • The use of a signature stamp to indicate the timely review and reconciliation of bank statements. • The hiring and employment of the wife and son of a College official. • A College official's approval of a payment to the official's spouse, who is also a College employee.	• Ensure that College employees provide accurate and complete information and documents in the course of audits and investigations by government agencies; • Reduce the number of bank accounts to the extent permitted by law if the number of accounts is determined to be excessive; • Ensure that bank statements are reviewed and reconciled in a timely manner by appropriate Business Office personnel; • Ensure that employees comply with the Public Official and Employee Ethics Act; • Consider adopting an anti-nepotism policy; and • Ensure that there is appropriate segregation of duties so that an employee cannot approve a transaction that may constitute a conflict of interest. Consistent with the policy and practice of the Department of the Auditor General, this report is being forwarded to the State Ethics Commission for whatever further action it may deem appropriate.

BACKGROUND AND INTRODUCTION

The Thaddeus Stevens College of Technology ("College") is a two-year technical college located in Lancaster, Pennsylvania. The College is accredited by the Pennsylvania Department of Education ("PDE") and the Middle States Association of Colleges and Schools. The College provides post-secondary education and training to indigent orphans, as well as to financially disadvantaged and non-scholarship students.

The Thaddeus Stevens College of Technology Act (Act 187 of 2002, effective on July 1, 2003) ("Act 187") removed the College from the direct control of PDE, thereby giving the College more administrative control over its day-to-day operations.[1] However, the College continues to be an instrumentality of the Commonwealth and state appropriations continue to be the College's primary source of funding.

Act 187 requires the College to maintain a Board of Trustees ("Board") consisting of nine members appointed by the Governor and confirmed by the State Senate. The Secretary of Education is an ex officio member of the Board.[2] The powers and duties of the Board include, but are not limited to, the following:

- maintaining general control of the property, personnel, and management of the institution;
- developing the institution's policies, bylaws, and regulations;
- electing the College's president and determining the salary, duties, and responsibilities of the president; and
- coordinating, reviewing, and approving the annual capital and operating budgets for the College.[3]

The Department of the Auditor General ("Department") has the authority and responsibility under The Fiscal Code to audit entities that receive state funds.[4] In addition, Act 187 provides that "[t]he activities of [the College] shall be subject to the audit of the Department of the Auditor General…."[5] In a letter dated February 26, 2003, the President of the College ("President") requested that the Department conduct a one-year financial audit of the College for the fiscal year ended ("FYE") June 30, 2004 pursuant to Act 187 ("FY 2003-04 Financial Audit"). The Department granted the College's request to conduct the audit, which commenced in June 2004.

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[1] 24 P.S. § 19-1901-B *et seq.*
[2] 24 P.S. § 19-1906-B.
[3] 24 P.S. § 19-1906.1-B.
[4] 72 P.S. § 403.
[5] 24 P.S. § 19-1915-B.

By correspondence dated November 15, 2004, the Department notified the College that it was compelled to withdraw from the audit engagement "until such time as the College is able to provide a trial balance and sufficient accounting documentation for [the Department] to reasonably continue the audit engagement for the purpose of expressing an opinion on the fairness of the financial statements." The Department re-engaged in February 2005.

On January 26, 2006, the Department issued an opinion that the financial statements for FYE June 30, 2004 fairly represented the College's financial position except for the lack of the prior year's cash flow statement, which the College did not have because it was in its first year of operation independent of PDE. Simultaneously, the Department issued a report of its routine performance audit of the College for the period of July 1, 2001 to August 13, 2004.

Prior to the Department's financial auditors re-engaging, they requested assistance from the Department's Office of Special Investigations ("OSI"). Specifically, the financial auditors were concerned about the number of Visa credit cards and transactions and the related controls. OSI's investigation commenced on January 6, 2005 and fieldwork was completed on January 6, 2006. The investigation focused on several issues in addition to the credit cards, based on allegations received by OSI during the course of the investigation.

It is important to understand that this report discusses the results of the Department's *special investigation*; this is not a report of the *financial audit* or a report of the *performance audit*, which, as previously discussed, resulted from separate engagements and have already been released. The College's staff and Board were provided with a draft copy of this investigation report for their review and comment. With the College's consent, relevant excerpts from the College's response are included verbatim at the end of each chapter of this report, followed by the Department of the Auditor General's comments on that portion of the College's response. In addition, the College provided a response to this section of the report (reproduced below), which is followed by our brief comments.

College's Response to Background and Introduction:

> Over the last 100 years, Thaddeus Stevens College of Technology evolved from a secondary school into a trade school and now has become a college. The pace of its evolution has hastened dramatically in the last ten years and understanding that dynamic force is important, to understanding the College's response to this [special investigation].
>
> After years of preparation and an initial failure, the College was granted accreditation in 1991. Central to the institution's long term viability is maintaining its accreditation by the Middle States Association of Colleges and Schools Commission's mandates on Higher Education. Upon

receiving accreditation in 1991, Middle States informed the College that it must have an independent financial audit with resulting financial statements and gain more autonomy from the Pennsylvania Department of Education (PDE).

Working with the General Assembly and the Governor's Office for several years, the College successfully gained the ability to comply with the Middle States' mandates with the passage of Act 187 in November of 2002. The Act which was effective July 1, 2003, separated the College from PDE and allowed the Board of Trustees to compel an independent financial audit of the institution.

During the year of transition (FY 2003-04) the College requested the Auditor General to conduct the institution's first ever financial audit. The Auditor General agreed and the audit was scheduled to begin June 15, 2004. Subsequently, the College was notified that its regularly scheduled Performance Audit had been moved up by six months and would precede the Financial Audit. Consequently, the Performance Audit began during the College's first year of transition on April 14, 2004, and ran simultaneous with the Financial Audit.

Candidly, the overwhelming task of establishing all of the College's ERP [enterprise resource planning] systems from scratch, with existing employees, and supplying the requests of two audit teams put a tremendous strain on the College's resources. As a result, the desired level of supervision and control was not always present nor was there adequate time to prepare for the Financial Audit. However, the College contends and will show in its response that no funds were lost or any significant findings of inappropriate behavior identified.

The College fully acknowledges some of the problems that were identified in the course of the Special Investigation. However, these are issues of controls and human error that are certainly understandable within the context the College was operating. It must be noted that some of the problems identified are directly attributable to the work and directives of the financial auditors.

Few, if any, other agencies or instrumentalities of the Commonwealth could have achieved the successful total transformation that is occurring at Thaddeus Stevens College of Technology. The College should be commended for undertaking this incredibly difficult and complex effort for the benefit its students and the State of Pennsylvania.

Department of the Auditor General's Comments on the College's Response:

The Department acknowledges the College's transition from a trade school to a two-year college and from an entity under the direct control of PDE to a more independent instrumentality of the Commonwealth. We commend the College and its leadership for recognizing that changes were needed in order to serve students more effectively and for working to implement those changes.

However, even if the transition may explain some of the problems discussed in this report, the College must still address and correct those problems in order to improve its operations and protect public funds. Furthermore, the College cannot blame this Department, its staff, or its reports for the problems identified in the financial audit, performance audit, and, now, this special investigation. We completely reject any suggestion that this Department had in any way advised or instructed the College to operate in the manner cited in this report.

We encourage the College and the Board to correct all of the problems identified by promptly implementing the recommendations made by this Department in all three reports. We will follow-up at the appropriate time to determine whether the recommendations have been implemented.

FINDINGS AND RECOMMENDATIONS

Finding I: The College Made Over $80,000 In Payments From A Separate Disbursement Account Without Adequate And Appropriate Supporting Documentation; According To The Pennsylvania Department Of Education, That Agency Was Not Aware Of The Balance In The Disbursement Account, Which Exceeded $653,000 At Its Height During The Fiscal Year Ended June 30, 2003.

OSI reviewed the College's Disbursement Account for the period of July 1, 1998 through January 4, 2006. OSI received allegations that the sources, amounts, and uses of funds in the Disbursement Account were not fully disclosed to PDE and the Board, that the account was controlled directly by the President of the College and the Vice President for Finance Administration ("VPFA"), and that the funds in the account were not spent appropriately.

In a written response to OSI dated December 16, 2005, the President stated:

> As a result of a performance audit during the 1970's, the College established the Disbursement Account to maintain accounting records for various student activities as well as the Athletic Association. Prior to this time, shop instructors, coaches, etc. each had their own checking accounts for cash receipts and disbursements. At the recommendation of the auditors the College established a local checking account that was separate and apart from the College's Revenue Account. This account (Disbursement) consists of: student activity fees; athletic association revenues; shop funds; Home Board contributions; vending machine revenues; and other miscellaneous revenue.

The President also stated in his response that, "[a]lthough the Disbursement Account is a separate company [accounting software terminology] in [the College's accounting software], journal entries were posted in the main set of books to incorporate all activities in one complete set of books." During the FY 2003-04 Financial Audit, the Department's financial auditors were provided with eleven trial balances, of which eight did not contain the details of the Disbursement Account. During an interview on October 7, 2005, the VPFA stated that this omission was due to the College's lack of knowledge as to how to account for the funds in the Disbursement Account in the College's financial statements.

According to the VPFA during another interview on January 6, 2006, revenues in the Disbursement Account include student activity fees, athletic association revenues, shop funds, local contributions, vending machine revenues, and other miscellaneous revenues. The VPFA stated that these funds are unrestricted and used by the College at the President's discretion.

According to a representative of PDE's Bureau of Human Resources, PDE was aware of the existence of the Disbursement Account but did not know how much money was in the account, where the money came from, or how the money was used. Similarly, a representative of PDE's Bureau of Budget and Fiscal Management stated that PDE was unaware of the magnitude of the balance in this account.

OSI reviewed 60 monthly bank statements for the Disbursement Account in order to determine balances for the five fiscal years ending on June 30, 2001 through June 30, 2005.

Table 1
Disbursement Account's Highest and Average Balances

Fiscal Year Ended	Highest Monthly Ending Balance	Average Balance During Fiscal Year
June 30, 2001	$287,363.16	$242,307
June 30, 2002	$485,595.09	$402,489
June 30, 2003	$653,403.49	$581,121
June 30, 2004	$111,721.18	$23,428
June 30, 2005	$7,046.86	$5,470

As indicated in Table 1, the average balance in the Disbursement Account increased to $581,121 by FYE June 30, 2003, with the highest monthly ending balance (April 2003) reaching $653,403.49 during that same fiscal year. When the College became independent from PDE as of July 1, 2003, it began transferring funds from this account into investment accounts. The first "sweep" took place on July 3, 2003 and totaled $657,000. According to PDE's Bureau of Budget and Fiscal Management, the funds from the Disbursement Account should have been included in the College's annual augmentation that would then supplement its appropriation. Therefore, it is possible that the state appropriations authorized and distributed to the College could have been affected.

OSI reviewed the Disbursement Account ledger for the period of July 1, 1998 through June 30, 1999 and the College's accounting software for the period of December 19, 2000 through December 14, 2005. During the latter five-year period, 3,801 checks were written and $3,417,773.91 was disbursed from this account. OSI pulled a sample, or subset of the total population, consisting of 30 disbursements, including disbursements made as early as 1998 due to allegations of impropriety prior to the year 2000.[6]

[6] Payments from the Disbursement Account made before July 1, 2003 would have occurred while the College was still under the direct control of PDE.

We found that the College appears to have made the following payments from the Disbursement Account without adequate and appropriate supporting documentation at the time of payment:[7]

- **Information technology services totaling more than $77,000 in 2003 and 2005, without an approved contract.** The College has used a particular vendor since 1995, when he was tasked as lead engineer under state contract to implement the College's local area network. OSI reviewed payments made to this vendor totaling $37,092 in calendar year 2003 and $40,522 in calendar year 2005. OSI also reviewed a "Sole Source and Emergency Purchase Fact Sheet & Checklist for Services," dated September 22, 2005, in which the VPFA requested from the President an additional $25,000 to $50,000 in services from this vendor. The College has never sought competitive bids for any of the services provided by this vendor; in an interview on January 6, 2006, the VPFA stated that the College plans to bid out those services "in the future."

  Regardless of how the College *selected* this vendor (i.e., sole source or emergency procurement rather than competitive bidding), the College proceeded to *pay* the vendor without a contract. The VPFA stated that the College did not require a contract because the vendor's fee is "significantly less" than the state contract rate and he has a "proven competence and historical knowledge" of the College's network. OSI believes that the College has had ample time since 2003 to determine its information technology needs and should have engaged in procuring these services under contract to ensure that its needs are met.

- **Fee of $1,495 for a presenter for new students' orientation conducted on August 19-21, 1998, without an invoice.** In a written response received on January 6, 2006, the VPFA responded that the College's Vice President for Student Services ("VPSS") "was supposed to obtain an invoice before providing [the] check to Presenter. I cannot explain why the invoice was not attached or submitted to the Business Office." After reviewing a draft of this report, the College was able to locate and provide a copy of the invoice. However, we must still question why the College would pay for services that were not adequately supported by an invoice *at the time of payment*.

- **Payments totaling $1,255 for "Christmas Presents" or "Christmas Parties," without supporting documentation.** OSI requested the supporting invoices/receipts for all of the items in Table 2.

[7] As discussed in the "Additional Concerns" section of this report, we also found payments from the Disbursement Account that may be in violation of the Public Official and Employee Ethics Act.

<u>**Table 2**</u>
Unsupported Payments for Christmas Presents/Parties

Date	Payee	Amount	College's Description of Payment
Dec. 5, 2005	Retail Store #1	$ 700	Raffle prizes – Christmas party
Dec. 7, 2005	Retail Store #2	$ 380	Educational materials - Christmas presents
Dec. 7, 2005	Retail Store #3	$ 75	Educational materials - Christmas presents
Dec. 22, 2005	Person #1	$ 100	Christmas party
	TOTAL	**$ 1,255**	

According to the College, the expenditures listed in Table 2 were made by student organizations for holiday parties, including parties and gifts for underprivileged children in the community. The College stated that the students could not afford to make the purchases initially and then be reimbursed by the College later, so the College provided the students with checks written to the stores. In at least one case, the December 5, 2005 check listed in Table 2, the students used the College's check to purchase gift cards which were then used to purchase specific items.

After reviewing a draft of this report, the College provided a detailed analysis of these transactions. However, it has still not provided the actual receipts. We must question whether the College has such receipts and, if not, why the College would make payments without appropriate documentation at the time of payment or at least within a reasonable time thereafter. We also question why the College would issue payments for the gift cards rather than for the specific items that were subsequently purchased with the gift cards.

- **Hotel charges of $693.60 for four rooms at a hotel in King of Prussia, Pennsylvania on April 2 and 3, 2004, without supporting documentation**. In a written response received on January 6, 2006, the VPFA acknowledged: "Supporting documentation is required; however, I cannot explain why it is not attached to the copy of the check." During the course of this investigation, the VPFA was able to obtain a copy of the invoice from the hotel and provide it to OSI. After reviewing a draft of this report, the College stated that it believes that it did have an invoice at the time of payment but that the invoice was misfiled. It is impossible for us to confirm that assertion. Again, we would be concerned about the payment for items that were not adequately supported by an invoice at the time of payment.

- **Cellular telephone bills/purchases of $653.24, without adequate supporting documentation.** Cellular telephone bills provided to OSI by the College during the course of this investigation contained no detailed information such as the telephone user, how many calls were made, and when calls were made. Table 3 lists the information contained on the purchase order for a monthly bill from a cellular telephone service provider, totaling $319.35 for two phones.

Table 3
October 2002 Purchase Order Description of Cell Phone Charges

Description	Charges
Monthly Access	$ 35.00
Monthly Access	$ 20.00
Home Usage & Charges	$ 254.00
Taxes/other	$ 10.35
TOTAL	**$ 319.35**

Although the purchase order listed the items on Table 3, the bill attached was only the "Account Summary" page 1 of 30, containing the total amount of $319.35. When OSI requested additional support, the VPFA stated that the College's security officers used the two phones. The College has not provided OSI with supporting documentation for the "Home Usage & Charges" of $254. Without such documentation, we cannot determine whether the phones were used appropriately or whether the College itself made such a determination at the time of payment.

OSI also questioned the lack of supporting documentation for a $333.89 charge to another cell phone service provider. The VPFA explained that the charge was to purchase a new cellular telephone for her that would function as both a telephone and personal digital assistant ("PDA") and also would permit the recording of handwritten notes that could be transferred to a desktop computer. The VPFA further explained that she would discontinue her other wireless communications device when the contract ends if she were able to use the telephone/PDA as intended. She decided to pay the greater undiscounted price for the telephone/PDA rather than enter into a multi-year contract.

After reviewing a draft of this report, the College provided a copy of a bill from the provider listing $333.89 under "One Time Charges" without any additional explanation or documentation. The College has not provided OSI with adequate supporting documentation for this expense or any confirmation that it had such documentation at the time of payment.

- **Mirror for President's car for $126, without an invoice from the dealer.** OSI received a copy of an invoice from the College's repair shop dated February 4, 2002 for repairs to the side view mirror on the President's personal car totaling $191.26. OSI also received a copy of a check from the President dated February

27, 2002 for $250, which included additional personal funds from the President representing a contribution to the repair shop. Despite other documentation maintained by the College and provided to OSI, the College's Business Office did not have an invoice from the automobile dealer for $126, seeking payment for the part purchased by the College's repair shop. Instead, the College's Business Office had only an estimated quote from the repair shop for the purchase.

During an interview on January 6, 2006, the VPFA acknowledged that the dealer's invoice would have been the correct supporting documentation for this expense, rather than the estimated quote provided by the College's repair shop. After reviewing a draft of this report, the College was able to provide a copy of the dealer's invoice to OSI that was maintained by the College's repair shop. However, based on the VPFA's statement during the investigation, it is not clear whether the College's Business Office had this invoice at the time when it issued the payment for the mirror.

Conclusions and Recommendations:

Based on our review of the transactions in our sample, OSI questions whether the monies in the Disbursement Account have been appropriately managed by the College and whether the payments made from the account were appropriate. We also question whether PDE and the Board had sufficient knowledge about the Disbursement Account, the amount of monies in the account, and how those funds were being used.

We recommend that the Board conduct its own thorough review of the Disbursement Account and ensure that the College implements policies, procedures, and internal controls that address allowable and authorized expenditures and the need for adequate and appropriate supporting documentation at the time when funds are disbursed from the account.

The College must also ensure that information regarding the Disbursement Account is fully disclosed to PDE and other appropriate agencies of the Commonwealth to the extent that such information may affect the College's annual appropriation from the Commonwealth.

College's Response to Finding I:

> [Special investigation] Finding Number One is based on the [Department] of the Auditor General's contradictory advice and its investigators' refusal to acknowledge the College's fully substantiated purchases from its Disbursement Account. The finding is mistaken for the following reasons: A) the OSI Team has refused to acknowledge the [Department of the] Auditor General's…prior advice confirming the use of a Disbursement Account; B) the OSI Team has refused to acknowledge the over eighty (80) pages of documentation provided to substantiate the College's

payment of all funds from the Disbursement Account; C) the OSI Team has failed to find any wrongdoing or misappropriation of funds.

***Department of the Auditor General's Comments on the College's Response*:**

We will address the three points of the College's response in the order in which they were presented: A) We completely reject the suggestion that this Department had, in any way, advised or instructed the College to maintain or use the Disbursement Account in the manner cited in this finding; B) Despite the number of pages of documents provided both during this investigation and after the College received a draft copy of this report, the College did not provide any information or documentation to change the main points of this finding; and C) While we do not claim to have found any "wrongdoing or misappropriation of funds" in the transactions in our sample, we did find internal control problems that create an environment in which waste, fraud, or abuse of funds can occur – and certainly could have occurred in transactions outside of our sample. The fact that we did not find any evidence of misconduct does not eliminate the need for the College to improve internal control practices and processes.

With some revisions to the discussion based on information and documentation provided by the College after it reviewed a draft report, this finding will remain. We encourage the College and the Board to implement promptly the accompanying recommendations. We will follow-up at the appropriate time to determine whether the recommendations have been implemented.

<u>Finding II</u>: The College Lacked Adequate Policies, Procedures, And Internal Controls For Its Visa Credit Cards, Which Were Used To Make Over $1.5 Million In Purchases From May 2003 Through September 2004.

OSI reviewed the College's Visa credit card transactions for the months of May 2003 through September 2004.[8] OSI's review of these transactions found serious deficiencies in the College's ability to adequately monitor purchases made, obtain supporting documentation needed to justify expenditures, and reconcile credit card statements to accounting records.

The College engaged in 3,143 credit card transactions with 691 different vendors, totaling $1,560,889.13. In order to put these transactions into context, we present the following data about the College's usage of its Visa credit cards:[9]

- The College used 155 different Visa credit cards for these transactions and maintained a total of 204 total credit cards in the VPFA's office. The College has stated that this excessive number of credit cards was needed "to track each cost center and provide a clear audit trail." However, as demonstrated in this finding, such a passive approach to fiscal oversight did not work.

- In an interview on July 7, 2005, the VPFA told OSI that credit card transactions constitute 25% of the College's annual total expenditures.

- 34 different vendors were paid $10,000 or more for aggregate purchases. The three highest vendors accounted for $71,039.18, $59,303.70, and $48,247.13 in purchases, respectively.

- 11 different single purchases were made for $5,000 or more, in excess of the College's allowable ceiling amount for single purchases (noted in its policy and procedure manual as $4,999.99), including one purchase totaling $9,736.20.

- College credit card usage by card number revealed that Operations or Maintenance Buildings, Warehouse, and General Administration card activity accounted for $119,909.99, $92,882.11, and $83,969.03 in purchases, respectively.

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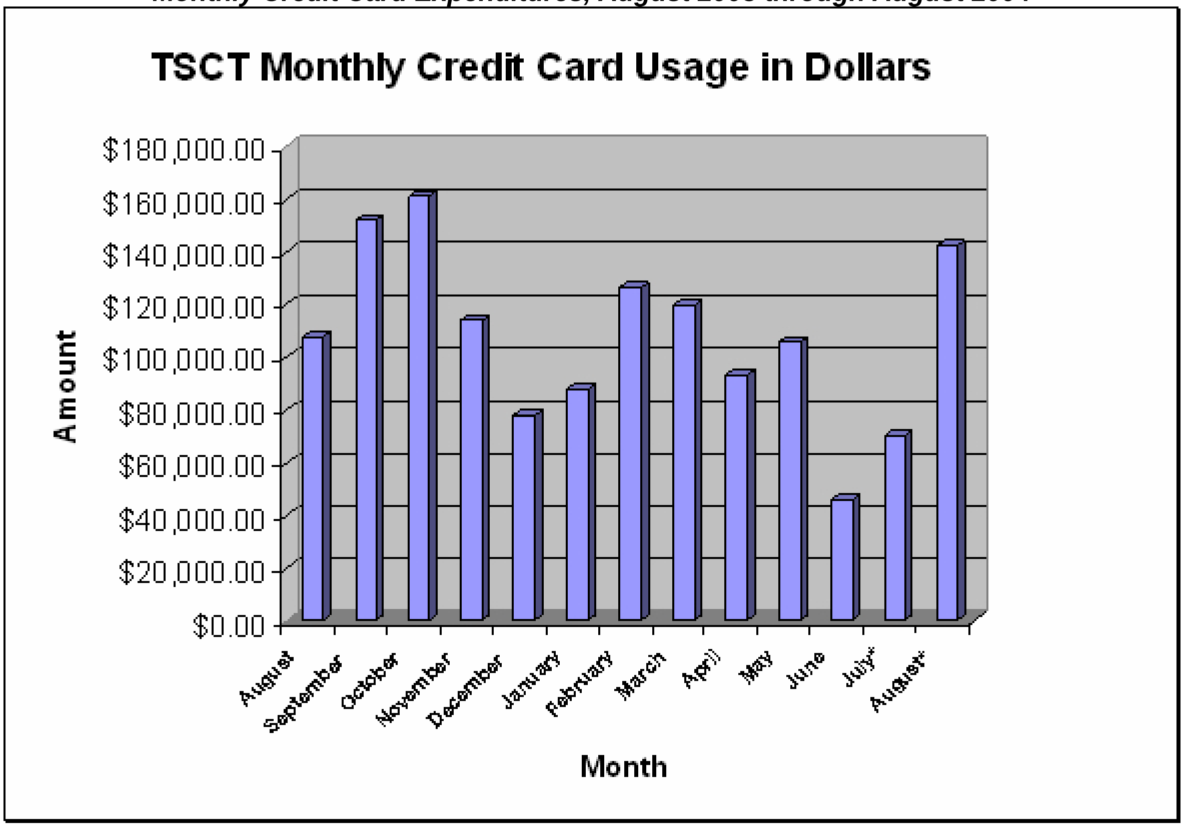
[8] OSI's review did not include complete credit card statements for the months of May 2003, July 2004, and August 2004, or any statements for the month of July 2003. The data discussed in this report includes only information actually reviewed by OSI. Credit card transactions that occurred before July 1, 2003 would have occurred while the College was still under the direct control of PDE.

[9] According to the VPFA during an interview on January 6, 2006, the College also possessed and used two credit cards for retail stores and approximately nine credit cards for gasoline companies. She told OSI that those cards were used sparingly. OSI did not find any evidence to the contrary. This finding relates only to the College's Visa credit cards.

Monthly Credit Card Expenditures, August 2003 through August 2004



**OSI's review did not include complete credit card statements for the months of July 2004 and August 2004.*

<u>The College's Use of Credit Cards Generally</u>

Authorization for the use of credit cards for purchasing at the College dates back to 1998. A letter dated June 24, 1998 from the College's President to PDE's comptroller requested permission for the College to participate in the Commonwealth's Purchasing Card Program. In a letter dated October 27, 1998 to the campus community, the VPFA notified the campus community that the College was approved to participate in the program. However, according to the College, the credit cards were not actually used until 1999.

OSI asked the College to provide policies and procedures governing the use of the credit cards. The VPFA provided OSI with the Commonwealth's "Visa Purchasing Card Manual for Cardholder and/or Authorized Users" ("Manual") issued by the Department of Education's Bureau of Management Services and dated December 4, 2000.[10] The College was still part of PDE when this policy was issued. The Manual states that "the purpose of this credit card program is to simplify and streamline the payment process as opposed to a more traditional accounts payable system." In her October 27, 1998 letter, the VPFA stated that "the purpose of this program at [the College] was to streamline the

[10] This Manual implemented the Commonwealth's Purchasing Card Program, which was established by Management Directive 310.23 Amended (Mar. 24, 1997).

payment process for purchase orders totaling less than $1,500." After the College received its independence from PDE on July 1, 2003, it cancelled the credit cards at the direction of PDE and obtained new Visa credit cards as replacements.

OSI's review of the College's policies and procedures governing the use of the credit cards indicated that the Manual had an issue date of December 4, 2000. The section regarding procurement and payment procedures was dated July 1998. The Manual has not been updated since the College received its independence from PDE and is no longer applicable. The only update to the Manual occurred when the College increased purchase card limits from $1,500 to $4,999.99 on July 1, 2003. In addition, OSI found no official document in the Manual announcing the College's formal adoption and acceptance of all policies and procedures identified in the Manual.

When asked during an interview on July 7, 2005 why no changes had been made to the College's policies and procedures governing the usage of credit cards at the College, the VPFA stated that the College was "in the midst of a transition period" and was "rewriting procedures." OSI notes that the College received its independence from PDE as of July 1, 2003, and our review of credit cards took place two years later, with the College using policies and procedures that were outdated, incomplete, and never officially adopted.

During an interview on August 18, 2005 about the problems surrounding credit card usage, the President and the VPFA agreed that OSI had found many discrepancies during testing (discussed later in this finding). They agreed that the policies and procedures in place at the time were not updated and effective, the processing format did not provide effective audit trails and control, credit card batch processing was taking four months on average, warehouse "Receiving Reports" (verifying that the items were actually received) did not include the necessary information, and there were control issues with the credit cards. The President also stated that he would discuss split purchases with College employees.

In a "Presidential Update" dated September 19, 2005 that was disseminated to all College employees, the President stated, "The College was advised by the Auditor General's [Department] to eliminate, or dramatically reduce, the use of purchasing cards." During an interview on January 6, 2006, the VPFA stated that Visa cards were still active but had not been used since August 2005. We want to emphasize that our concern is not with the fact that the College uses credit cards but rather the excessive number of cards used and the lack of adequate internal controls over those cards. When used and managed properly, credit cards can provide an efficient means of making purchases.

OSI's Review of Credit Card Transactions

As discussed below, OSI performed two separate reviews of specific credit card transactions in an attempt to evaluate the College's monitoring process and overall management of credit card usage.

Test #1 –- Sample of 155 Transactions

As already discussed, OSI reviewed the College's Visa credit card transactions during the period of May 2003 through September 2004. From that total population of 3,143 transactions, OSI selected a sample, or subset, of 155 credit card transactions, totaling $184,335.35 in purchases. For all 155 transactions in the sample, OSI obtained or attempted to obtain vendor invoices to reconcile the purchases made by the College. OSI's review of these transactions focused on determining whether purchase order dates and numbers were recorded and corresponded to actual credit card purchases; whether signatures, dates, and purchase order numbers were present on Receiving Reports; whether invoice dates and numbers matched those on invoices received from vendors; whether purchases were pre-approved; and whether credit card statements were reconciled and posted in a timely fashion. A review of these 155 transactions revealed the following:

- 71 Receiving Reports were unavailable or did not include dates received;
- 22 purchase orders were either unavailable or missing signatures;
- 19 invoices were missing, unavailable, or did not contain all relevant information;
- 11 instances of missing dates and/or signatures for the reconciliation of transactions in the batch processing;
- 9 instances of missing dates for the posting of transactions in the batch processing;
- 4 instances of missing dates for the approval of the entire batch processing;
- On average, the College took 114 days from the transaction date to the reconciliation date of the purchases;
- On average, the College took 124 days from the reconciliation date to the posting date of these transactions to its ledger accounts;
- One purchase indicated that sales tax was paid in the amount of $48, even though the College is exempt from paying such taxes;
- Dollar amounts differed when listed on the Receiving Report and purchase order for the same transaction;
- Receiving Reports contained little or no detail as to actual quantity and description of items received and contained no purchase order numbers or signatures;

- Purchase orders listed dates that were anywhere from four to six months after the transaction date; and

- Purchase orders were split to avoid bidding requirements and single-purchase dollar limitations.

<u>Test #2 – Sample of 21 Transactions</u>

OSI selected another sample of 21 credit card transactions totaling $5,620.54 in purchases. OSI's focus with regard to this sample was to test specific transactions that appeared to be Internet purchases and travel-related purchases. According to the President and the VPFA, the College does not use credit cards for travel and individual employees do not have access to credit card numbers so the employees could not make Internet purchases. Furthermore, in an interview on July 7, 2005, the President stated that the VPFA and two employees in the Business Office have lists of all of the College's credit cards and that the VPFA is the only individual who has access to the physical cards.

However, OSI's review of these 21 credit card transactions found the following:

- 11 of 21 transactions were Internet purchases made at retail stores;

- 10 of 21 transactions were travel-related purchases, including airfare;

- One purchase order contains a handwritten note that appears to indicate that a non-Business Office employee was given the credit card number to pay for a hotel room ($179.82), while the documentation submitted to OSI with another purchase order includes an e-mail from a different non-Business Office employee that appears to indicate that he would use the credit card to purchase a lamp ($148.39) online as a replacement for a damaged item; and

- A total of $330.58 total in state sales tax was paid by the College, a tax-exempt institution.

<u>Conclusions and Recommendations</u>:

The College's failure to adequately monitor its credit card usage is a serious internal control issue that creates an environment conducive to waste, fraud, and abuse. We are concerned about the outdated policy and procedure manual followed by the College, which was never formally adopted, as well as the large number of exceptions, discrepancies, and unavailable documentation noted during our testing.

Furthermore, the fact that the College did not obtain the necessary invoices for many of the items purchased using the credit cards is reason for concern. By not having a valid invoice on file, the College does not have vital information to determine if the items received were exactly what was ordered and ultimately paid for. While OSI found no specific examples of the College's purchasing inappropriate or questionable items, there were many instances in which an opinion regarding an item's legitimacy could not be offered because adequate and appropriate supporting documentation was missing.

We recommend the following:

- The College should review all credit card purchases made since July 1, 2003 to ensure that all appropriate supporting documentation is available to justify each purchase.

- The College should maintain a limited number of credit cards for appropriate purposes and implement appropriate policies, procedures, and internal controls governing their use. Those credit cards that are to remain active at the College should be limited to use by the Purchasing Office and/or President's Office. In addition, before a credit card is actually charged for any reason, either to purchase an item or for travel expenses, the College should require dual signatory approval for all transactions and prior receipt of all invoices.

- The College should immediately cancel and physically destroy all other credit cards. The remaining cards left active should remain locked in the College's safe and should never leave the safe without proper authorization and documentation.

- For its non-credit card purchases, the College should continue using a purchase order, reimbursement, and/or other alternative accounts payable type system.

- In implementing and monitoring its purchasing systems, the College should re-evaluate the abilities of Business Office personnel and the adequacy of internal controls and correct any weaknesses found.

<u>College's Response to Finding II</u>:

In this finding, OSI has criticized a practice in which the College engaged while it was part of the Commonwealth. Furthermore, OSI found absolutely no evidence of any wrongdoing.

<u>Department of the Auditor General's Comments on the College's Response</u>:

As already explained in our comments on the College's response to the previous finding, the fact that we did not find any "wrongdoing" or "misappropriation" of assets in the transactions in our sample does not eliminate the need for the College to improve internal control practices and processes. With some revisions to the discussion based on information and documentation provided by the College after it reviewed a draft report, this finding will remain. We encourage the College and the Board to implement promptly the accompanying recommendations. We will follow-up at the appropriate time to determine whether the recommendations have been implemented.

<u>Finding III:</u> The College Lacked Adequate Policies, Procedures, And Internal Controls For Its Fixed Assets, Which Caused A Systemic Failure To Track And Record Over $1.9 Million Worth Of Fixed Assets For The Period Of July 1, 2003 To December 19, 2005.

As part of OSI's review of the College's Visa credit card usage, we tested a sample of credit card purchases (specifically, computers and computer peripheral devices due to their higher dollar value) to determine if the purchased items could be physically located and if they were accounted for on the College's fixed asset ledger. A fixed asset ledger, which is also referred to as a "fixed asset register" or "fixed asset schedule," is used to keep track of assets (i.e., land, equipment, machinery, etc.) from acquisition to disposal. A ledger's key components are the asset's cost, purchase date, useful life, rate of depreciation, location, and purchase order number.

OSI conducted four separate tests of fixed assets. OSI selected an original sample of 76 items purchased with the College's Visa credit cards to review for physical existence and inclusion on the fixed asset ledger if appropriate. This test was conducted at the College in August 2005. OSI then conducted three separate tests of fixed assets during a final review in January 2006. The testing that occurred in January 2006, in which a sample of 24 fixed assets was chosen, focused on physical existence of the assets, the availability of supporting documentation, and the effectiveness of changes made by the College throughout the course of this investigation in the area of fixed asset tracking and recording. The results of these tests are described later in this finding.

Generally, the College failed to adequately manage, track, and record numerous fixed assets on its fixed asset ledger because the College's policies and procedures were antiquated and not effective. If even available, the invoices for items purchased were not systematically stored, managed, or easily retrieved when requested. The College's accounting for fixed assets was incorrect or nonexistent and its internal controls over assets purchased were weak or nonexistent. As demonstrated in Table 4, the College continually revised its fixed asset ledger during the course of this investigation to include items that were not previously recorded.

Table 4
College's Revisions to Fixed Asset Ledgers

Fixed Asset Ledger Period	Date OSI Received Fixed Asset Ledger	Total "Book Value" of Fixed Assets Listed on Ledger[11]	Total "Book Value" of Fixed Assets Added From Each Previous Ledger Received by OSI
FYE June 30, 2004	July 7, 2005	$1,113,548.41	N/A[12]
FYE June 30, 2004	Aug. 3, 2005	$1,541,965.04	$428,416.63
FYE June 30, 2004	Dec. 6, 2005	$2,270,030.40	$728,065.36
FYE June 30, 2005	Dec. 19, 2005	$2,713,013.69	$442,983.29
7/1/05-12/19/05	Dec. 19, 2005	$3,091,535.65	$378,521.96
		CUMULATIVE TOTAL	**$1,977,987.24**

Table 4 illustrates the numerous fixed asset ledgers received from the College and their respective total "book values" of assets tracked according to the College. Note that each succeeding fixed asset ledger provided by the College to OSI includes additional assets, therefore increasing book value dollar totals. Furthermore, the fixed asset ledgers for FYE June 30, 2005 and for the period of July 1, 2005 to December 19, 2005 were created by the College during the course of this investigation and were not previously in existence. Based on changes to fixed asset policies and procedures, the College is now tracking over $1.9 million worth of additional fixed assets.

Policies and Procedures

The policies and procedures governing the College's fixed asset management in place at the start of the investigation were largely antiquated and ultimately ineffective. OSI initially received the College's "Policy for Fixed Assets" on August 3, 2005. However, throughout the course of this investigation, the College significantly revised its fixed asset policy to reflect necessary changes brought to its attention by OSI. The College ultimately adopted what are essentially new policies and procedures to correct problems encountered during OSI's review and testing of fixed assets. The College provided OSI with a new and completely revised version toward the end of our investigation in December 2005.

[11] The dollar amounts listed do not reflect any revisions (additions or subtractions) that the College may have made to the fixed asset ledgers since providing them to OSI.

[12] The fixed asset ledger for FYE June 30, 2004 was the initial fixed asset ledger reviewed and tested by OSI. However, the Department's financial auditors received previous fixed asset ledgers that were revised to include additional assets and subtract duplicate assets that were listed.

The effect of the College's original way of handling its fixed assets is demonstrated by the College's inability to respond in a timely manner to requests made by OSI during this investigation. For example:

- On July 21, 2005, OSI sent the College a sample of 76 assets to test and verify their physical existence. The College responded with the location of all of the assets 28 days later on August 18, 2005.

- On October 7, 2005, OSI requested a fixed asset ledger for FYE June 30, 2004. The College responded on December 6, 2005, 60 days later, by providing an inaccurate fixed asset ledger.

- On October 7, 2005, OSI requested a current and comprehensive fixed asset ledger from the College. The College responded on December 19, 2005, 73 days later, by providing a fixed asset ledger for FYE June 30, 2005, and a fixed asset ledger for the period July 1, 2005 to current, periods that were not captured on previous fixed asset ledgers.

- On November 15, 2005, OSI requested copies of all invoices from a particular computer vendor, specifically those related to the College's fixed asset purchases. The College responded on January 20, 2006, 66 days later, by faxing 16 invoices to OSI that were not found when OSI conducted our final review of fixed assets in January 2006. It appears that the College paid for those purchases without the invoices.

The College's provision of requested documents and records was slow and resulted in considerable delays in the fieldwork and testing portion of this investigation. In interviews and formal responses, College management acknowledged that the information provided was incorrect and that it took the College a long period of time to gather. As the College submitted revised ledgers, the problems persisted and, in some cases, became worse.

It is important to note that, as a result of problems identified during the course of this investigation, the College made the following positive changes to its original policy:

- Both submissions of the College's policy governing fixed assets are entitled "Financial Management, number 310, General Capital Assets and Other Fixed Asset Accounting and Reporting in MIP [accounting software]." The new policy indicates that it was revised on October 20 and November 22, 2005. While the prior policy listed no effective date, the new policy lists the "effective date" as July 1, 2003. The prior policy indicates only "By the Direction of the President," while the new policy states that it was "Approved by Thaddeus Stevens College of Technology Board of Trustees."

- The College's new policy includes numerous additions and explanations for the treatment of specific items that were not addressed in the prior policy.

These additions and explanations include the "Thaddeus Stevens Collection" of antiques and artifacts, inventory, library books, other fixed assets, and prepaid expenses.

- The College's new policy includes a section on what the asset record will include, which was not mentioned in the prior policy. The new policy states the "asset record will include: item description, serial or service tag numbers, asset number, purchase price or fair market value, asset location, asset class, and fund from which asset was purchased."

- The College's new policy includes a more detailed and expanded listing of MIP asset class numbers, titles, asset life, and asset valuation thresholds.

- The new policy also includes expanded definitions and criteria for "Low Value Assets," which were not included in the prior policy.

- Most important, the College's new policy includes a designated section relating to the treatment and criteria applied to "General Capital Assets and Low Value Assets" by time period. This section provides specifics for such assets acquired during the periods prior to July 1, 2003 (when the College became independent from PDE) and those acquired during FYE June 30, 2004 and stated changes for FYE June 30, 2005 and FYE June 30, 2006. This section references specific "Low Value Assets" including computers, computer peripherals, donated assets, equipment, and computer software, along with their respective dollar-value thresholds for each designated period. An all-inclusive definition for computer peripherals is also included in this section.

Fixed Asset Testing

OSI conducted four separate tests of fixed assets during this investigation. The original test of fixed assets was conducted in August 2005. However, because numerous discrepancies were noted during this testing, including many items selected that were not listed on the College's fixed asset ledger, three additional tests of fixed assets and the College's revised fixed asset ledgers were conducted in January 2006.

Test #1 – Sample of 76 assets

This test consisted of a sample of 76 items purchased with the College's Visa credit cards, totaling $97,941.12. The majority of these purchases occurred during FYE June 30, 2004. As part of this sample, OSI attempted to focus on those low value assets, such as computers, computer peripherals, equipment, and other electronic equipment, that have a tendency to be easily transferred or stolen. This sample also included 24 laptop or desktop computers.

In an interview on July 18, 2005, the VPFA acknowledged that the fixed asset ledger that she had previously provided was "incorrect and incomplete," explaining that the employee in the College's Business Office who had prepared it was "a young kid" who "obviously did not know what he was doing." She also acknowledged that there were clear inaccuracies in the information reported on the fixed asset ledger, such as lack of appropriate tag numbers, check dates listed that occurred before the dates of actual purchase, depreciation calculated incorrectly, asset location not listed, and overall lack of assets listed as whole. Consequently, OSI requested that the College prepare an updated fixed asset ledger that included the necessary revisions and listed all computer purchases because not all computer purchases made with the Visa credit cards were listed on the College's fixed asset ledger.

The College should have known what assets it had purchased and therefore needed to be included on its fixed asset ledger. However, OSI had to visit the College on three separate occasions (August 3, 10, and 18, 2005) in order to physically verify all 76 items included in our sample. OSI noted the following:

- The College allows employees to maintain College-owned laptop computers, printers, and other electronic devices at their homes if they so choose. However, the College does not track – and therefore does not know – the *specific* locations of *specific* items.

- Several computers that had been purchased with the College's Visa credit cards were not listed on the fixed asset ledger.

- Invoices were not available at the College to determine which items had actually been ordered and paid for, and Receiving Reports were not completed or were incorrectly completed.

- Several items had been damaged, out for repair, and/or returned for credit, yet the old items' serial numbers and invoices were still used for tracking purposes. It was not until OSI requested documentation for those items during the course of this investigation that the College discovered these discrepancies.

- The actual location of fixed assets, if even listed, was not accurate.

- Many fixed assets were not tagged with the College's fixed asset control tags.

- Only one fixed asset tag existed, and only one entry was made on the fixed asset ledger, for a purchase that included multiples of the same item (i.e., purchase of ten computer monitors).

- College employees expressed concerns about the lack of controls over computers, especially laptops, and the manner in which equipment was tracked.

- The College's fixed asset tags were found on equipment that was not recorded on fixed asset ledgers.

- During OSI's inspection of items, the door to the "Data Center" room, containing more than $9,000 worth of assets and all incoming telephone lines for the entire campus, was not locked and was left wide open without an employee monitoring the area.

In an interview on August 18, 2005, the President and the VPFA discussed the discrepancies that OSI noted during the physical verification of our sample of 76 fixed assets and their relationship to the College's fixed asset schedule. OSI expected that the same discrepancies would not be found when further testing of fixed assets and the fixed asset ledger was conducted, because the College was aware of them and would make the necessary changes. OSI decided to again test the College's fixed assets for physical existence, as well as for inclusion on the newly revised fixed asset ledger that had been provided to OSI in December 2005. The College assured OSI that the newly revised fixed asset ledgers included all fixed assets in its possession and relevant to its new policies and procedures. However, discrepancies of the same nature were found.

OSI conducted three tests from January 4 through 6, 2006, to determine if the College's fixed assets existed and if the fixed asset ledgers were accurate, as discussed below:

<u>Additional Test #1: Sample of 24 assets</u>

Based on the newly revised fixed asset ledger provided by the College to OSI on December 6 and 19, 2005, we noted 24 assets for which OSI had obtained invoices from vendors that were not listed on the ledgers. Ten of the assets noted from invoices should have been included on the College's fixed asset ledger for FYE June 30, 2004 and 12 of the assets noted from invoices should have been included on the College's fixed asset ledger for FYE June 30, 2005. The purpose of the test was to determine why these assets were not included on fixed asset ledgers and to verify their physical existence.[13] OSI noted the following:

- 21 out of 24 items were physically verified and/or adequate documentation was provided to illustrate a duplicate shipment or cancelled order. The three items not physically verified were computers, which, as previously explained, were maintained at the homes of College employees without the College's specific knowledge until this investigation.

- For the 12 assets not listed on the College's ledger for FYE June 30, 2005, 7 were indicated by the President as not required to be included because they were computer peripheral devices not listed in the College's new fixed asset policy. However, based on the criteria listed in the policy, OSI believes that these items should be included on the ledger because many of them cost the College more than $700 each.

[13] For two of the 24 assets, the College indicated prior to our visit that one was a duplicate shipment and the other was a canceled order. For these two instances, OSI only requested supporting documentation and did not conduct a physical inspection of the item.

- The College agreed to add the remaining assets to its fixed asset ledgers, with the exception of two computers originally listed in our sample. In this instance, OSI received two identical invoices from the vendor, listing different order dates, for what turned out to be only one purchase. Therefore, the College could only show two computers on its fixed asset ledger, not four.

Additional Test #2

This test was conducted to determine if the College maintained all of the necessary supporting documentation needed to justify its computer purchases. OSI cross-referenced invoices received from a computer vendor against the College's purchase records for those assets. We noted the following:

- 12 instances in which OSI had the vendor's invoices in support of fixed assets listed on the ledgers, but the College did not have the invoices in its supporting documentation. To the College's credit, there were also 29 instances in which the College had invoices to support fixed assets purchased, but the invoices were not sent to OSI by the vendor.

- 32 instances in which neither the College nor OSI had an invoice to support a fixed asset listed on the College's fixed asset ledgers. This included one instance in which the College purchased 105 computers on July 27, 2005 for a total cost of over $116,000, but did not have an invoice for the purchase. During an interview on January 6, 2006, the VPFA stated that she assumed that her staff always received an invoice for purchases and she attributed the missing invoices to human error.

Additional Test #3

This test was conducted in order to evaluate the adequacy of the College's supporting documentation available for all fixed assets. We noted the following:

- A College employee compiled "Fixed Asset Binders" containing the supporting documentation for the fixed asset ledgers in response to OSI's request to review fixed asset support documentation. This information was not retained in a single comprehensive source, but rather was broken down by the fiscal year in which the asset purchase was made.

- Ten instances in which the College marked the "Fixed Asset Cover Sheet" with a note "need paperwork." In all ten instances, the College did not have a purchase order, invoice, Receiving Report, and/or quote to support the purchase.

- Six instances in which fixed assets and supporting documentation were retained in the "Fixed Asset Binder" for both FYE June 30, 2004 and FYE June 30, 2005, which should have been in the binder for only FYE June 30, 2005. In all six instances, the fixed assets were not duplicated on the fixed asset ledger.

Computers and Computer Peripherals

During an interview on August 18, 2005, the VPFA stated that two College employees had conducted a complete inventory of all computers. Based on the timing of when one of these employees left employment at the College, we believe that the inventory would have been conducted during the summer of 2005. Furthermore, the President stated that he knows where "90%" of the computers are at the College. However, based on our detailed testing, OSI questions whether the College, even after all of the revisions and updates to its fixed asset ledgers and policies and procedures and extensive searching, truly knows exactly how many computers and items of computer peripheral equipment are the property of the College. This concern is based upon the following:

- During the interview with the VPFA on August 18, 2005, OSI asked for a listing of all computers available at the College, but such a listing was never provided and still has not been provided as of this date of this report. Based on statements made during our interviews, the College's position appears to be that all computers of value are now tracked on the newly revised fixed asset ledgers. However, because of the numerous discrepancies noted in testing, OSI simply cannot validate this claim. The only reason that the College started tracking all of its computers in the first place is because of this investigation. Had the College provided OSI with a list of all computers at the start of the investigation, even with some discrepancies, such a list would have been better than not providing any list at all. Without a list at the start of the investigation, OSI did not know exactly how many computers existed and had to be tested.

- When OSI interviewed the College's former Systems Engineer on August 16, 2005, he stated that purchasing procedures for computers were not in writing and that many College staff could have purchased computers by bypassing him. Although the College had designated this employee as one of two individuals to answer our questions about the College's computers, he could not provide a definitive answer on how many computers were in the College's possession. He estimated the number of computers at the College to be approximately 650 units with an estimated dollar value around $750,000, which is a reasonable estimate based on OSI's review of the College's revisions to its fixed asset ledgers. The College's information technology vendor (discussed in Finding I), the other individual designated by the College, provided an estimate of 300-500 computers. Unfortunately, these estimates are the best information that we were able to obtain during the course of our investigation; as of the date of this report, we have still not received a complete, definitive list of the College's computer inventory.

- Based on invoices received from the College's computer vendors and additional invoices reviewed during the testing conducted in January 2006, OSI noted that the College added 203 computers from the first fixed asset ledger received by OSI on July 7, 2005 for FYE June 30, 2004 (showing 150 computers) to the last ledger received by OSI on December 6, 2005 for that same fiscal year (showing 353 computers). Furthermore, the College has now recorded and listed a total of 546 computers on all current fixed asset ledgers, provided to OSI on December 6 and 19, 2005. By e-mail dated December 23, 2005, the President provided OSI with a listing of 302 "older computers that were transferred to the College from PDE." He also stated that "these computers are past their useful life in terms of depreciation and do not appear on any of our Fixed Asset Ledgers."

- During the January 2006 testing of fixed assets, after the College had assured OSI that all fixed assets were included on the revised ledger for FYE June 30, 2004, OSI noted that one computer valued at $2,878 was not listed.[14]

Conclusions and Recommendations:

The College is seriously deficient in the tracking, locating, recording, and monitoring of fixed assets purchased. Additionally, the College's policies, procedures, and controls governing fixed assets were not effective, as evidenced by the fact that the College tracked and recorded over $1.9 million worth of additional fixed assets during the course of this investigation. While OSI commends the College for its efforts in attempting to update and track fixed assets, those efforts would have been unnecessary if the College had taken a more proactive role from the outset. Furthermore, how many additional assets remain untracked is still not known, as well as whether any assets have been misplaced or stolen from the College due to the lack of internal controls. OSI cannot offer an opinion in this regard, because the College is unable to report with certainty exactly how many assets are in its possession.

We recommend the following:

- The College should continue to track down and record, on revised fixed asset ledgers, those assets that were previously unrecorded, particularly those assets that are maintained and utilized by employees at their homes. Furthermore, the College should record fixed assets immediately upon receipt, as opposed to periodically or after conducting an inventory.

- The College should retain a certified public accounting firm to assist in tracking, recording, and maintaining fixed assets. The firm will also be able to evaluate the College's policies and procedures; determine asset values, depreciation, and useful life; and implement an improved fixed asset tracking system and ledger.
- The College should discontinue its practice of maintaining separate fixed asset ledgers broken down by fiscal year. Instead, the College should update and maintain one consolidated fixed asset ledger for all fixed assets of value. Furthermore, as assets depreciate, the College should maintain a separate

[14] Although this type of problem further illustrates the need for improved management oversight of internal controls as noted on page 32 of the FY 2003-04 Financial Audit report, the $2,878 error would not have been material to the financial statements for that period.

ledger that includes the date on which the asset was placed out of service and the asset's salvage or scrap value, if applicable.

- The College's fixed asset policies and procedures, with respect to computer peripherals, should be reevaluated and the class of assets listed should be expanded, specifically to include servers and network devices.

- When tagging and recording assets, the College should tag each applicable item, and discontinue its practice of tagging only one item of a bulk purchase or designating one tag for an entire room of assets.

- The College should assign sequentially numbered fixed asset tags to every item received in a bulk purchase; when the assets are received, the College should record the items on ledgers. This will allow the College to improve its management and tracking of assets purchased.

- The College should discontinue its practice of placing fixed asset tags on items that are not included on fixed asset ledgers. However, if the College feels the need to track other items (e.g., calculators or chairs), it should implement a separate tracking system to do so.

<u>College's Response to Finding III</u>:

> Despite the dramatic terms framing this finding, there was no systemic failure to track assets. The College acted in accordance with well-established practice (which was also adopted by the Pennsylvania State System of Higher Education). Any confusion on this point was caused by the Financial Audit Team's contrary and contradictory advice regarding the treatment of low value assets. There is no evidence of any wrongdoing nor any misappropriation of any College-owned asset.

<u>Department of the Auditor General's Comments on the College's Response</u>:

We must briefly reiterate the points made in our comments on the College's responses to other findings. The fact that we did not find any "wrongdoing" or "misappropriation" of assets in the transactions in our sample does not eliminate the need for the College to improve internal control practices and processes. We also completely reject the suggestion that this Department in any way advised or instructed the College to track or record fixed assets in the manner cited in this finding.

With some revisions to the discussion based on information provided by the College after it reviewed a draft report, this finding will remain. We encourage the College and the Board to implement promptly the accompanying recommendations, particularly the recommendation that the College retain a certified public accounting firm to assist in tracking, recording, and maintaining fixed assets. We will follow-up at the appropriate time to determine whether the recommendations have been implemented.

Finding IV: The College's Leave System Permits Employees To Carry Excessive Leave Balances, Which, For Three Officials, Could Result In Payments Upon Their Termination And/Or Retirement Estimated At $190,000.

During the course of this investigation, OSI received allegations that the President and the VPFA do not accurately report their usage of paid leave. In fulfilling our obligation to investigate those allegations, we did not question whether those officials or any other College employees used leave that they had earned and to which they were entitled. Rather, our concern was whether employees took time off without deducting that time from their leave balances, particularly in light of the impact of leave balances on the College's finances. Although OSI did not find specific instances in which leave was used and not recorded against leave balances, we do have several related concerns that are discussed in this finding.[15]

In an interview on January 6, 2006, the VPFA stated that the College adheres to the Commonwealth leave policy that covers all employees. According to the Commonwealth's Personnel Rules, unused annual and sick leave is carried over to the next calendar year if such leave does not exceed the maximum carryover amount. The maximum accrued annual leave (i.e., vacation time) carryover is 45 days (337.5 hours). Unused annual leave is converted to sick leave until the sick leave maximum amount is accrued. The maximum accrued sick leave carryover is 300 days (2,250 hours). Once sick leave reaches the maximum, the leave is to be removed from the records. Although leave is encouraged to be used in the year in which it is earned, there is a seven-pay-period extension before it will be converted, if annual leave, or removed, if sick leave. By June of each year, the leave from the prior calendar year should be converted or removed.[16]

OSI conducted a review of annual leave accrued and used for the period of January 1, 2003 through November 11, 2005 by the President, VPFA, and VPSS to determine if such leave had been recorded properly.[17] OSI found that the excess annual leave for 2003 for the President (112 hours) and the VPFA (195 hours) was not converted to sick leave as required.[18] The College's leave records also indicated that the VPFA used zero hours of annual leave in a three-year period, while the President used 65 hours and the VPSS used 358 hours during that same period.

Due to our concern about the impact of leave balances on the College's finances, we estimated the future annual leave payouts with the assistance of PDE. At the 337.5-hour maximum allowable annual leave balance carryover plus the additional hours that

[15] The recording and use of leave before July 1, 2003 would have occurred while the College was still under the direct control of PDE.

[16] Management Directive 505.7 Amended, "Personnel Rules" (Feb. 24, 1998), as further amended.

[17] The three-year period included the two full calendar years 2003 and 2004 and records from January 1, 2005 through November 11, 2005 for the calendar year 2005.

[18] The excess annual leave for 2003 for the VPSS and the 2004 excess annual leave for all three officials was converted. It is not clear whether the 2005 excess annual leave has been converted, as those hours were still available for use until the seventh pay period in 2006.

can be accrued and paid out at retirement, we conservatively estimated that future annual leave payouts for the three officials could exceed $20,000 each. Specifically, we estimated the President's payout at $26,500, the VPFA's at $23,000, and the VPSS's at $22,500. Because we calculated these payouts using a 2004 hourly rate, our estimates are likely to be lower than the actual payouts upon termination and/or retirement.

OSI also reviewed the three officials' sick leave balances for the period of January 1, 2003 through November 11, 2005. We found the following cumulative balances: 1,045 hours for the President, 1,961 hours for the VPFA, and 2,421 hours for the VPSS. The College's leave records indicated that the President and the VPFA used no sick leave in a three-year period, while the VPSS used 173 hours during that same period. According to PDE, the VPFA did not use any sick leave for at least eight years. The VPFA stated that she reports all of her leave to the President.

The sick leave balance for the VPSS was 81 hours more than the allowable maximum amount of sick leave permitted to be carried on the books.[19] By way of explanation, the VPFA stated that the sick leave *payout* is capped at 2,250 hours but the sick leave *accrued* can exceed this and is not capped. However, OSI confirmed with PDE that the excess accrued sick leave is to be removed each year after the seven-pay-period extension. Therefore, the VPSS has been allowed to carry sick leave balances in excess of the maximum of 2,250 hours for calendar years 2003, 2004, and 2005. Upon OSI's suggestion that a sick leave bank be established for employees to donate their excess leave, the VPFA stated that she would consider the idea.

Based on these sick leave balances, we conservatively estimated the President's future sick leave payout as $24,000, the VPFA's at $42,000, and the VPSS's at $52,000. Again, because we calculated these payouts using a 2004 hourly rate, our estimates are likely to be lower than the actual payouts upon termination and/or retirement.

Combining both the annual and sick leave payouts, we conservatively estimated the payouts to these officials upon their termination and/or retirement for all accrued leave to total $190,000: $50,500 for the President; $65,000 for the VPFA; and $74,500 for the VPSS. After reviewing a draft of this report, the College stated that its failure to properly limit and convert leave balances is the result of a technical problem in its payroll software program that affects *all* College employees, not just these three officials. Although the College has asserted that it can manually override this technical problem and that, therefore, such payments will not be made to these three officials or any other similarly situated employee, we are obligated to raise this issue in order to ensure that the College fixes this problem.

However, in doing so, it is not our intent to suggest that the three officials themselves have acted inappropriately or that the College has made any improper leave payouts. We reviewed the leave balances for these three officials because, although the

[19] The 81 hours is derived from the 2,421 total hours less the maximum amount to be carried of 2,250 plus the 90 hours accrued for the calendar year 2005, as of November 11, 2005.

College stated that the technical problem affects all employees, they were the only employees with excess annual leave that should have been converted as of June 30, 2004.

Finally, OSI reviewed the President's 12 leave slips submitted between July 1, 2003 and November 11, 2005. We noted three instances when the President's leave slips were not signed by anyone and nine instances when they were signed by the VPFA rather than by a Board member. Prior to July 1, 2003, a PDE representative signed the President's leave slips. After reviewing a draft of this report, the College stated that, following the College's separation from PDE, the President originally did not have anyone sign his leave slips because of the absence of any individual on campus with the authority to approve or disapprove his leave, but then, upon further reflection, the President chose to have the VPFA sign his leave slips as a type of verification.

We commend the President for recognizing on his own the need to have someone sign his leave slips. However, we believe that the appropriate individual to sign and, more important, to *approve* the President's leave slips is the chairperson of the Board or his/her designee. This practice would serve as an internal control mechanism to ensure that all leave is reported, although we want to note that we did not find any evidence that the President of the College acted inappropriately in using his leave.

Conclusions and Recommendations:

The College should record, convert, and remove leave balances, as well as address the issue of excessive leave balances, in accordance with Commonwealth leave policy and with the assistance of a software program that reflects and implements that policy. As we have already recommended informally to the VPFA, the College should establish a sick leave bank so that employees can donate their excess sick leave for use by other employees who are in need of such leave. Finally, the President should report his leave usage to the Board chairperson or his/her designee and seek formal approval from that individual for his usage of leave.

College's Response to Finding IV:

> [Special investigation] Finding Number Four is incorrect and extremely misleading. In addition, the allegations cited by OSI under this finding are baseless and unsubstantiated. The clear inference contained in the text of this Finding is the College President and the Vice President of Financial Affairs used their positions to gain a financial advantage through improperly accounting for leave and engaged in practices of not recording leave that was actually taken.
>
> Even though OSI states…that "Although OSI did not find specific instances in which leave was used and not recorded against leave balances…," it still implies throughout this Finding that the College President and the VPFA and VPSS somehow were engaged in fraudulent behavior from which they benefited at the expense of the Commonwealth.

> It remains to be seen why, if the Auditor General's [Department] could find no evidence of wrongdoing, that this allegation by implication would be retained in this Report. The inclusion of this finding in a publicly published report is improper and unsubstantiated.

Department of the Auditor General's Comments on the College's Response:

During the course of this investigation, OSI received allegations that certain College employees used leave without recording such use against their leave balances. We were obligated to follow-up on those allegations and we fulfilled that obligation. As clearly stated in the finding, we did not find any evidence confirming the truth of those allegations.

However, we did find other related problems on which we are compelled to report. In its response, the College is overreacting to our recommendation to correct a systemic problem that, by its own admission, may affect all employees. Again, the fact that we did not find any "wrongdoing" or "fraudulent behavior" does not eliminate the need for the College to improve internal control practices and processes. The issue of excessive leave balances must be addressed and corrected in order to reduce the potential financial burden on the College and the Commonwealth.

With some revisions to the discussion based on information provided by the College after it reviewed a draft report, this finding will remain. We encourage the College and the Board to implement promptly the accompanying recommendations. We will follow-up at the appropriate time to determine whether the recommendations have been implemented.

ADDITIONAL CONCERNS

OSI has the following additional concerns based on evidence gathered during the course of this investigation:

- ***The use of a signature stamp to indicate the timely review and reconciliation of bank statements:*** During the FY 2003-04 Financial Audit, financial auditors from the Department asked the College to produce bank statements and corresponding reconciliations for selected months of 2004. The College provided bank statements and reconciliations for 14 different bank accounts, some of which had been stamped with the name of a College official and dated to indicate that they had been reconciled in a timely manner. The College must ensure that its employees provide accurate and complete information and documents in the course of audits and investigations by government agencies. In addition, the College appears to maintain too many bank accounts and should reduce the number of accounts. The College should also ensure that the statements for those accounts are reviewed and reconciled in a timely manner by the appropriate Business Office personnel so that the reconciliations are accurate and effective.

- ***The hiring and employment of the wife and son of a College official:*** This official's wife received at least $12,170 in payments from the Disbursement Account. The official's son worked as a part-time student intern for over four years, at a rate of $6.50 to $9.96 per hour. The College should ensure that its employees comply with the Public Official and Employee Ethics Act[20] ("Ethics Act"), which generally prohibits conflicts of interest, and consider the adoption of an anti-nepotism policy in employment.

- ***A College official's approval of a payment to the official's spouse, who is also a College employee:*** This payment was made from the Disbursement Account for reimbursement of $281.78 incurred at a local restaurant in May 2003. In addition to implementing the same recommendations as in the previous bullet, the College should ensure that there is appropriate segregation of duties so that an employee cannot approve a transaction that may constitute a conflict.

Consistent with the policy and practice of the Department, this report is being forwarded to the State Ethics Commission for whatever further action it may deem appropriate.

[20] 65 Pa.C.S. § 1101 *et seq.*

<u>College's Response to Additional Concerns</u>:

The College has and continues to contend that all of its bank accounts were reviewed and reconciled. It acknowledges that during the period in question, due to the extenuating circumstances detailed previously in this report[,] reconciliations were not done in as timely a manner as is desirable. That is not to say that they were not performed – they were.

* * *

OSI also asserted the College maintained too many bank accounts. There is simply no basis for that statement. The attached chart will explain why each account exists.

<u>Bank Account</u>	***<u>Justification for Separate Account</u>***
Pell Checking	To comply with Cash Management Regulations outlined in the U.S. Department of Education's Blue Book
FFELP Checking	To comply with Cash Management Regulations outlined in the U.S. Department of Education's Blue Book
Payroll	To maintain payroll transactions separately from other operating expenditures and to assist in the reconciliation of payroll transactions.
Revenue Checking	To ensure effective control over and accountability for all non-appropriated receipts and to disburse federal grants and other financial aid to students.
Revenue Sweep	To more efficiently transfer funds from our checking account to invest it or move it to a money market account thereby allowing the College to earn interest on our business checking accounts. Banks are not allowed to give interest on business checking accounts.
Local Disbursement Checking	To maintain student organizations and shop fund receipts and disbursements separately from operating funds.
Local Disbursement Sweep	To more efficiently transfer funds from our checking account to invest it or move it to a money market account thereby allowing the College to earn interest on our business checking accounts. Banks are not allowed to give interest on business checking accounts.
Appropriation Checking	To ensure effective control over and accountability for all state-appropriated funds.

Appropriation Money Market	Funds in this account were moved to the Appropriation Sweep. This account is no longer active.
Appropriation Sweep	To more efficiently transfer funds from our checking account to invest it or move it to a money market account thereby allowing the College to earn interest on our business checking accounts. Banks are not allowed to give interest on business checking accounts.
Child Care Checking	To maintain restricted funds which are donated to the College for child care expenditures entitled to eligible students.

*   *   *

The College official referred to [in the second bullet] was the College President. The circumstances that led to the temporary employment of his wife resulted from the sudden departure of an employee in the College's Business Office.

At the time, it took an average of nine to twelve months to fill a position with all of the approvals required by PDE and [the Governor's Office of Administration]. The process to fill the position with a permanent employee was initiated immediately. Since the job functions were critical, the College President requested his wife to fill-in until a permanent employee could be hired. The College President selected his wife based on the following qualifications:

(1) She was a college graduate who had graduated with honors;

(2) She had an excellent working knowledge of Microsoft Works that was being used to maintain student accounts (the primary function of the vacant position); and

(3) She did not require a criminal background check because she had been employed by the Federal Bureau of Investigation (FBI) for several years and had a "Top Secret" security clearance.

The College President's wife was not an employee of the College; she was an independent contractor who was paid $10.00 per hour and received no benefits. This pay rate was significantly less than the employee she replaced and the permanent employee who was hired to fill the vacant position….She was paid with <u>non-Commonwealth funds</u> and the College's Board of Trustees was fully aware of this situation. When a regular permanent employee was hired, her employment ceased. She has never been employed by the College in any manner since that time….

The circumstances that led to the employment of the President's son resulted from the College's lack of an adequate website and the high cost of having a fully functional website developed in the private sector. At the time, the College's website consisted of one single page and was for all intent and purposes useless. The President's son was selected based on the following qualifications:

(1) He had previously been selected and served in the FBI's internship program at the end of his junior year in high school. He worked in the Agency's I.T. department.

(2) He had been designing websites since his junior year in high school. He was compensated at $25.00 per hour for websites he developed and maintained in the private sector.

(3) He was enrolled in the Computer Science program at Millersville University. The College used Millersville University students as interns to perform work at Thaddeus Stevens College[, a] program approved by PDE.

The President asked his son to develop and maintain a fully functioning website for the College as part of the internship program. During the President's son's employment, the College's website was totally redesigned; added program descriptions; model schedules; numerous photographs; grew to over a hundred pages; added online applications; and was kept current. PDE was fully aware of the employment of the President's son as an intern. The rates of pay for interns were set by PDE.

The College President was concerned with the appearance of nepotism in the employment of his wife and son. However, due to the circumstances at the time and the College's limited financial resources, he felt that their qualifications and willingness to work at basic pay rates, justified their employment. Neither his wife, son nor any other relative of the College President work at the College and none will be employed in the future. The College agrees it should develop a Conflict of Interest policy that includes an article on nepotism.

*　　*　　*

In April of 2003, the College…was…requested…to sponsor a dinner table….[The requester] stated that this would be an excellent opportunity for a representative of the College and a guest to share information about the College and the value Stevens provides the Commonwealth….

> The President agreed and selected the VPFA and her husband, a faculty member at the College.….The total bill was $281.78, which the VPFA's husband placed on his personal credit card….All of the appropriate supporting documentation accompanied the transaction. The funds used were non-Commonwealth funds. In the future, the VPFA will not approve any transactions involving her spouse. The College believes that this is the only time this has occurred in the 30 years these individuals have been employed at the College.

Department of the Auditor General's Comments on the College's Response:

We appreciate the College's acknowledgement that bank statements were not reviewed and reconciled in a timely manner. With regard to the number of different bank accounts, it is not clear whether some or all of the accounts are truly needed because the College is prohibited by law from commingling certain funds or whether, similar to the College's use of its credit cards, the College is simply maintaining an excessive number of accounts as a passive form of fiscal oversight. The Board should review this issue and take appropriate action.

We commend the College for recognizing, in response to this investigation, the necessity of having policies prohibiting nepotism in employment and requiring appropriate segregation of duties. In particular, a public official's hiring of his/her immediate family members is never in the best interest of a public institution, even under the best of circumstances and even if, as appears to be the case here, the hiring resulted from an honest mistake of judgment.

With some revisions to the discussion based on information provided by the College after it reviewed a draft report, this section will remain. We encourage the College and the Board to implement promptly the accompanying recommendations. We will follow-up at the appropriate time to determine whether the recommendations have been implemented.

DISTRIBUTION LIST

This report was distributed initially to the College's Board of Directors and President, as well as the following:

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The Honorable Robert P. Casey, Jr.
State Treasurer

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