



HANOVER AREA SCHOOL DISTRICT
LUZERNE COUNTY, PENNSYLVANIA
PERFORMANCE AUDIT REPORT

OCTOBER 2013

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL





Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen

EUGENE A. DePASQUALE
AUDITOR GENERAL

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania
Harrisburg, Pennsylvania 17120

Mrs. Evelyn Evans, Board President
Hanover Area School District
1600 Sans Souci Parkway
Hanover Township, Pennsylvania 18706

Dear Governor Corbett and Mrs. Evans:

We conducted a performance audit of the Hanover Area School District (District) to determine its compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures (relevant requirements). Our audit covered the period March 5, 2010 through January 31, 2013, except as otherwise indicated in the report. Additionally, compliance specific to state subsidies and reimbursements was determined for the school years ended June 30, 2010 and June 30, 2009. Our audit was conducted pursuant to Section 403 of The Fiscal Code, 72 P.S. § 403, and in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States.

Our audit found that the District complied, in all significant respects, with relevant requirements. However, we identified one matter unrelated to compliance that is reported as an observation. A summary of the results is presented in the Executive Summary section of the audit report.

Our audit observation and recommendations have been discussed with the District's management, and their responses are included in the audit report. We believe the implementation of our recommendations will improve the District's operations and facilitate compliance with legal and administrative requirements. We appreciate the District's cooperation during the conduct of the audit.

Sincerely,

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale".

EUGENE DEPASQUALE
Auditor General

October 1, 2013

cc: **HANOVER AREA SCHOOL DISTRICT** Board of School Directors

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Executive Summary

Audit Work

The Pennsylvania Department of the Auditor General conducted a performance audit of the Hanover Area School District (District). Our audit sought to answer certain questions regarding the District's compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures and to determine the status of corrective action taken by the District in response to our prior audit recommendations.

Our audit scope covered the period March 5, 2010 through January 31, 2013, except as otherwise indicated in the audit scope, objectives, and methodology section of the report. Compliance specific to state subsidies and reimbursements was determined for the 2009-10 and 2008-09 school years.

District Background

The District encompasses approximately 22 square miles. According to 2010 federal census data, it serves a resident population of 15,433. According to District officials, the District provided basic educational services to 2,125 pupils through the employment of 154 teachers, 128 full-time and part-time support personnel, and 14 administrators during the 2009-10 school year. Lastly, the District received \$11.2 million in state funding in the 2009-10 school year.

Audit Conclusion and Results

Our audit found that the District complied, in all significant respects, with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures. However, we identified one matter unrelated to compliance that is reported as an observation.

Observation: Questionable

Administrator Contract Provisions. Our audit of the Hanover Area School District's former Superintendent's and former Business Manager's contract found that the Board of School Directors agreed to a retirement incentive provision (see page 5).

Status of Prior Audit Findings and

Observations. With regard to the status of our prior audit recommendations to the Hanover Area School District (District) released on April 20, 2011, we found that the District had taken appropriate corrective action in implementing our recommendations pertaining to the general fund deficit (see page 8). However, the District had not taken appropriate corrective action in implementing our recommendations pertaining to errors in reporting membership for nonresident children placed in private homes (see page 9).

Audit Scope, Objectives, and Methodology

Scope

What is a school performance audit?

School performance audits allow the Pennsylvania Department of the Auditor General to determine whether state funds, including school subsidies, are being used according to the purposes and guidelines that govern the use of those funds. Additionally, our audits examine the appropriateness of certain administrative and operational practices at each local education agency (LEA). The results of these audits are shared with LEA management, the Governor, the Pennsylvania Department of Education, and other concerned entities.

Our audit, conducted under authority of Section 403 of The Fiscal Code, 72 P.S. § 403, is not a substitute for the local annual audit required by the Public School Code of 1949, as amended. We conducted our audit in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States.

Our audit covered the period March 5, 2010 through January 31, 2013, except for the verification of professional employee certification which was performed for the period July 1, 2012 through November 30, 2012.

Regarding state subsidies and reimbursements, our audit covered the 2009-10 and 2008-09 school years.

While all districts have the same school years, some have different fiscal years. Therefore, for the purposes of our audit work and to be consistent with Pennsylvania Department of Education (PDE) reporting guidelines, we use the term school year rather than fiscal year throughout this report. A school year covers the period July 1 to June 30.

Objectives

What is the difference between a finding and an observation?

Our performance audits may contain findings and/or observations related to our audit objectives. Findings describe noncompliance with a statute, regulation, policy, contract, grant requirement, or administrative procedure. Observations are reported when we believe corrective action should be taken to remedy a potential problem not rising to the level of noncompliance with specific criteria.

Performance audits draw conclusions based on an evaluation of sufficient, appropriate evidence. Evidence is measured against criteria, such as laws and defined business practices. Our audit focused on assessing the District's compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures. However, as we conducted our audit procedures, we sought to determine answers to the following questions, which serve as our audit objectives:

- ✓ Were professional employees certified for the positions they held?
- ✓ In areas where the District received state subsidies and reimbursements based on pupil membership (e.g. basic education, special education, and vocational education), did it follow applicable laws and procedures?

- ✓ Did the District have sufficient internal controls to ensure that the membership data it reported to PDE through the Pennsylvania Information Management System was complete, accurate, valid, and reliable?
- ✓ In areas where the District received state subsidies and reimbursements based on payroll (e.g. Social Security and retirement), did it follow applicable laws and procedures?
- ✓ Did the District, and any contracted vendors, ensure that their current bus drivers were properly qualified, and did they have written policies and procedures governing the hiring of new bus drivers?
- ✓ Were there any declining fund balances that may pose a risk to the District's fiscal viability?
- ✓ Did the District pursue a contract buy-out with an administrator and if so, what was the total cost of the buy-out, what were the reasons for the termination/settlement, and did the current employment contract(s) contain adequate termination provisions?
- ✓ Did the District take appropriate steps to ensure school safety?
- ✓ Did the District have a properly executed and updated Memorandum of Understanding with local law enforcement?
- ✓ Were votes made by the District's Board of School Directors free from apparent conflicts of interest?
- ✓ Were there any other areas of concern reported by independent auditors, citizens, or other interested parties?
- ✓ Did the District take appropriate corrective action to address recommendations made in our prior audit?

Methodology

What are internal controls?

Internal controls are processes designed by management to provide reasonable assurance of achieving objectives in areas such as:

- Effectiveness and efficiency of operations.
- Relevance and reliability of operational and financial information.
- Compliance with certain relevant laws, contracts, grant requirements, and administrative procedures.

Government Auditing Standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our results and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our results and conclusions based on our audit objectives.

The District's management is responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the District is in compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures (relevant requirements). In conducting our audit, we obtained an understanding of the District's internal controls, including any information technology controls, as they relate to the District's compliance with relevant requirements that we consider to be significant within the context of our audit objectives. We assessed whether those controls were properly designed and implemented. Any deficiencies in internal control that were identified during the conduct of our audit and determined to be significant within the context of our audit objectives are included in this report.

In order to properly plan our audit and to guide us in possible audit areas, we performed analytical procedures in the areas of state subsidies and reimbursements, pupil transportation, pupil membership, and comparative financial information.

Our audit examined the following:

- Records pertaining to pupil transportation, pupil membership, bus driver qualifications, professional employee certification, state ethics compliance, financial stability, reimbursement applications, tuition receipts, and deposited state funds.
- Items such as board meeting minutes and policies and procedures.

Additionally, we interviewed select administrators and support personnel associated with the District's operations.

Lastly, to determine the status of our audit recommendations made in a prior audit report released on April 20, 2011, we performed additional audit procedures targeting the previously reported matters.

Findings and Observations

Observation

Criteria relevant to the observation:

Section 1073(a) of the Public School Code, 24 P.S. § 10-1073(a), requires school districts to enter into three-to-five-year employment contracts with their superintendents.

Questionable Administrator Contract Provisions

Our audit of the Hanover Area School District's (District) former Superintendent's contract found that the Board of School Directors (Board) and the former Superintendent agreed to a retirement incentive provision as part of the former Superintendent's contract, which was effective February 1, 2009 through February 1, 2014.

Article V of the contract states:

“The Superintendent shall be entitled to all benefits that are stated in Board Policy 4140.01 – Administrative Compensation and Related Benefits during the Term of this Agreement with the following adjustments: . . .

b . . . Retirement after thirty (30) years . . . the Superintendent shall collect a bonus of eighty (80%) of his salary . . .”

The prior Management Team Compensation Plan (Act 93) effective July 1, 2004 through June 30, 2009, stated the following:

“ . . . Retirement after thirty (30) years – If an administrator, upon reaching the age of fifty-three (53), desires to retire and so notifies the Board of Education by May 1 of this intent, he/she will collect a bonus of seventy-five percent (75%) of his/her salary.”

The current Management Team Compensation Plan (Act 93) effective July 1, 2009 through June 30, 2012, which was extended to June 30, 2013, eliminated the 75 percent Retirement Bonus, except for two administrators that were grandfathered due to their closeness to retirement.

On October 4, 2012, the Board approved the Letter of Intent to Retire from the Superintendent effective June 30, 2013. The Superintendent's salary, per contract, as of July 1, 2012, is listed as \$104,500 per annum. Based on the retirement incentive payout of 80 percent, the former

Superintendent received a payment of \$83,600 upon his retirement.

Furthermore, the former Business Manager's Employment Contract (Contract) was effective July 1, 1986 through June 30, 1991. Article V, of this Contract, Fringe Benefits stated:

“ . . . Retirement after thirty (30) years – If the Business Manager intends to legally retire (at the end of 30 years of service) so notifies the Board of Education by May 1 of this the year of retirement, said employee shall receive an annual salary increment for the last year of service in the amount of \$750.”

However, the Contract also notes under Article V, if the District increases the provisions of any fringe benefits of any District personnel in excess of those set forth in the Contract, or increases the provisions or benefits of any or all District Administrators or Personnel, the Fringe Benefits, as set forth in the Contract, shall be automatically and correspondingly increased to the same or similar level of the District Personnel and/or Administrators.

The former Business Manager retired effective April 5, 2010. The Board had not officially renewed his contract in fifteen years. Instead it updated the contract to include a termination clause and compensation in line with the Management Team Compensation Plan (Act 93). Nevertheless, on January 26, 2010, the Business Manager requested payment of 80 percent of his current salary upon retirement. He based his request on the provision included in the Superintendent's contract. On April 9, 2010, the Superintendent signed a memo approving the payment. The former Business Manager's salary, per board minutes, as of July 1, 2009, was listed as \$94,787.50 per annum. Based on the retirement incentive payout of 80 percent, the former Business Manager received a payment of \$75,830 upon retirement.

As noted above, the Act 93 contract effective July 1, 2009, eliminated a 75 percent retirement bonus. The former Business Manager was not listed as an administrator grandfathered for purposes of the retirement bonus. Although, the Superintendent's contract, effective

February 1, 2009, allowed for an 80 percent retirement bonus at the time of the former Business Manager's retirement, the Board should have considered the cost to the taxpayers and reviewed the legality of this payment. The Board should have reviewed and approved the contract of the former Business Manager at regular intervals to avoid costly payouts and any misunderstanding of allowable benefits.

The taxpayers have the right to expect that their hard earned money will be spent on the education of the District's students and not on excess benefits to individuals.

Furthermore, the information in these agreements should be more transparent to the public so that the taxpayers can consider such information when determining whether the Board has made decisions in the best interest of the District, the taxpayers, and the students.

Recommendations

The *Hanover Area School District* should:

1. Consider the taxpayers' expectation that their money will be used for the education of the District's students when negotiating employee agreements.
2. Ensure all of the District's employment agreements are as transparent as possible, so that the District's taxpayers can evaluate their appropriateness.
3. Ensure contracts are renewed on a regular basis to eliminate confusion and/or unnecessary payouts.

Management Response

Management stated the following:

"The provision of the 80% of salary at retirement for the current and former Superintendent's contract was standard language at the time at Hanover Area School District. This practice will be discontinued going forward as the service provided by PSBA will preclude this as of July 1, 2013. The lack of contract or renewal of the former Business Manager has not continued as there is a signed and dated contract on file for the current Business Manager."

Status of Prior Audit Findings and Observations

Our prior audit of the Hanover Area School District (District) released on April 20, 2011, resulted in two findings. The first finding pertained to a general fund deficit, and the second finding pertained to errors in reporting membership for nonresident children placed in private homes. As part of our current audit, we determined the status of corrective action taken by the District to implement our prior audit recommendations. We performed audit procedures and interviewed District personnel regarding the prior findings. As shown below, we found that the District did implement our recommendation related to the general fund deficit. However, the District did not implement our recommendations related to membership for nonresident children placed in private homes.

Auditor General Performance Audit Report Released on April 20, 2011

Finding No. 1: **District has a General Fund Deficit of \$1,315,398 as of June 30, 2009**

Finding Summary: Our prior audit of the District's annual financial reports, independent auditor's report, and general fund budgets for fiscal years ended June 30, 2008 and 2009, found that the District's previous general fund surplus of \$413,763 as of June 30, 2007, had decreased over the last two fiscal years leaving a general fund deficit of \$379,756 and \$1,315,398, respectively.

Recommendation: Our audit finding recommended that the District:

Provide for systematic reduction of the fund balance deficit in the general fund by utilizing monthly budget status reports to scrutinize proposed expenditures for current operations and limit them to revenues available and the amounts appropriated.

Current Status: During our current audit, we found that the District did implement our prior recommendations. The District resolved the general fund deficit resulting in a general fund balance of \$299,814 for the school year ending 2009-10. The general fund balance for the 2010-11 school year was \$1,358,431.

Finding No. 2: Errors in Reporting Membership for Nonresident Children Placed in Private Homes Resulted in Reimbursement Overpayments of \$113,302

Finding Summary: Our prior audit of the District's pupil membership reports submitted to the Pennsylvania Department of Education (PDE) for the 2007-08 and 2006-07 school years found District personnel incorrectly reported nonresident membership for students in both years resulting in overpayments of \$113,302.

Recommendations: Our audit finding recommended that the District:

1. Provide regular in-service training to staff responsible for recording and reporting membership. This training should emphasize the importance of maintaining accurate records and the relationship of membership data to state subsidies and reimbursements.
2. Strengthen controls to ensure pupil membership is reported in accordance with PDE guidelines and instructions.
3. Implement controls to verify actual membership days to computer generated reports.
4. Perform an internal review of membership reports and summaries prior to submission of final reports to PDE.
5. Review subsequent year reports and if errors are found, submit revised reports to PDE.

We also recommended that PDE:

6. Adjust the District's allocations to resolve the overpayments in the amount of \$113,302 for the 2007-08 and 2006-07 school years.

Current Status: During our current audit, we found that the District did not implement our prior recommendations. In addition, District personnel incorrectly reported nonresident membership for one student during the 2008-09 school year. This error did not have a significant effect on the District's subsidy. Therefore, a verbal comment was issued. The District did not educate any nonresident students in the 2009-10 school year. We again recommend that the District take steps to strengthen its membership reporting process to ensure it is following PDE's guidelines and instructions.

Distribution List

This report was initially distributed to the District's Superintendent of Record, the Board of School Directors, our website at www.auditorgen.state.pa.us, and the following stakeholders:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania
Harrisburg, PA 17120

The Honorable Carolyn Dumaesq
Acting Secretary of Education
1010 Harristown Building #2
333 Market Street
Harrisburg, PA 17126

The Honorable Robert M. McCord
State Treasurer
Room 129 - Finance Building
Harrisburg, PA 17120

Ms. Lori Graham
Acting Director
Bureau of Budget and Fiscal Management
Pennsylvania Department of Education
4th Floor, 333 Market Street
Harrisburg, PA 17126

Dr. David Wazeter
Research Manager
Pennsylvania State Education Association
400 North Third Street - Box 1724
Harrisburg, PA 17105

Mr. Tom Templeton
Assistant Executive Director
School Board and Management Services
Pennsylvania School Boards Association
P.O. Box 2042
Mechanicsburg, PA 17055

This report is a matter of public record and is available online at www.auditorgen.state.pa.us. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 231 Finance Building, Harrisburg, PA 17120; via email to: news@auditorgen.state.pa.us.