

PERFORMANCE AUDIT

Johnsonburg Area School District Elk County, Pennsylvania

July 2017



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE
AUDITOR GENERAL

Mr. Dennis Crotzer, Superintendent
Johnsonburg Area School District
315 High School Road
Johnsonburg, Pennsylvania 15845

Mrs. Barbara Thorwart, Board President
Johnsonburg Area School District
315 High School Road
Johnsonburg, Pennsylvania 15845

Dear Mr. Crotzer and Mrs. Thorwart:

Our performance audit of the Johnsonburg Area School District (District) evaluated the application of best practices in the areas of finance and school safety. In addition, this audit determined the District's compliance with certain relevant state laws, regulations, contracts, and administrative procedures (relevant requirements). This audit covered the period July 1, 2012, through June 30, 2015, except as otherwise indicated in the audit scope, objective, and methodology section of the report. The audit was conducted pursuant to Sections 402 and 403 of The Fiscal Code (72 P.S. §§ 402 and 403), and in accordance with the Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Our audit found that the District complied, in all significant respects, with relevant requirements and applied best practices, except as detailed in our two findings noted in this audit report. A summary of the results is presented in the Executive Summary section of this audit report.

Our audit findings 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 relevant requirements. We appreciate the District's cooperation during the course of the audit.

Sincerely,

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

Eugene A. DePasquale
Auditor General

July 27, 2017

cc: **JOHNSONBURG 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 District. Our audit sought to answer certain questions regarding the District's application of best practices and compliance with certain relevant state laws, regulations, contracts, 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 July 1, 2012, through June 30, 2015, except as otherwise indicated in the audit scope, objectives, and methodology appendix of this report. Compliance specific to state subsidies and reimbursements was determined for the 2014-15 school year.

Audit Conclusion and Results

Our audit found that the District applied best practices and complied, in all significant respects, with certain relevant state laws, regulations, contracts, and administrative procedures, except as described in the two findings below.

Finding No. 1: The District's Operating Deficits Reduced the General Fund Balance by 60 Percent (\$2.4 Million) Over a Four-Year Period. Our review of the District's financial position over a four-year period showed that the District's General Fund balance decreased by over 60 percent to a level that is below the recommended financial industry guidelines, which should be concerning to taxpayers. The District experienced operating deficits in three of the

four years reviewed, and those deficits were the primary factor in the decrease in the General Fund balance. The operating deficits increased from \$400,450 in the 2012-13 fiscal year to \$1,065,808 during the 2014-15 fiscal year (see page 6).

Finding No. 2: The District's Real Estate Agreement with its Bus Contractor Lacked Board Oversight and May Place Future Financial Obligations on the District. On May 14, 2015, the Board of School Directors (Board) entered into a Real Estate Agreement with the District's current bus contractor that may not have been in the best financial interest of the District. The Real Estate Agreement allowed the bus contractor to build a work garage on district-owned property for a one-time lease payment of \$1. The bus contractor may occupy the garage as long as he provides transportation services to the District (see page 14).

Status of Prior Audit Findings and Observations. We conducted procedures to determine the implementation status of our prior recommendations to the District from an audit released on October 18, 2013. We found that the District had taken appropriate corrective action in response to our recommendations pertaining to maintaining an updated Memorandum of Understanding with local law enforcement (see page 20).

Background Information

School Characteristics 2015-16 School Year ^A	
County	Elk
Total Square Miles	167
Resident Population ^B	4,963
Number of School Buildings	2
Total Teachers	58
Total Full or Part-Time Support Staff	30
Total Administrators	4
Total Enrollment for Most Recent School Year	620
Intermediate Unit Number	9
District Vo-Tech School	n/a

A - Source: Information provided by the District administration and is unaudited.

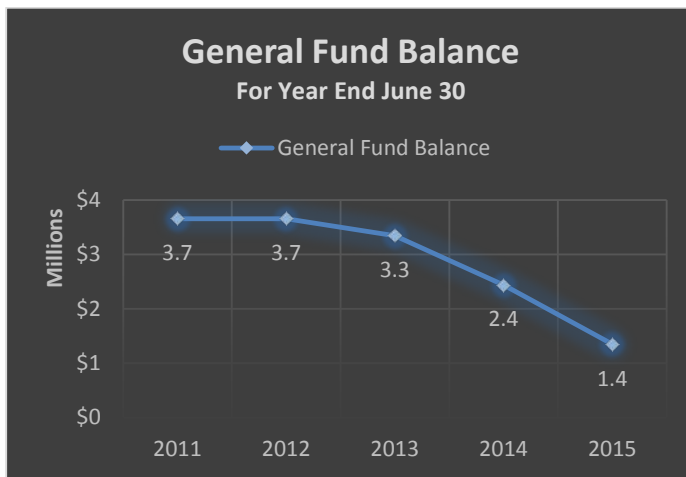
B - Source: United States Census
<http://www.census.gov/2010census>.

Mission Statement^A

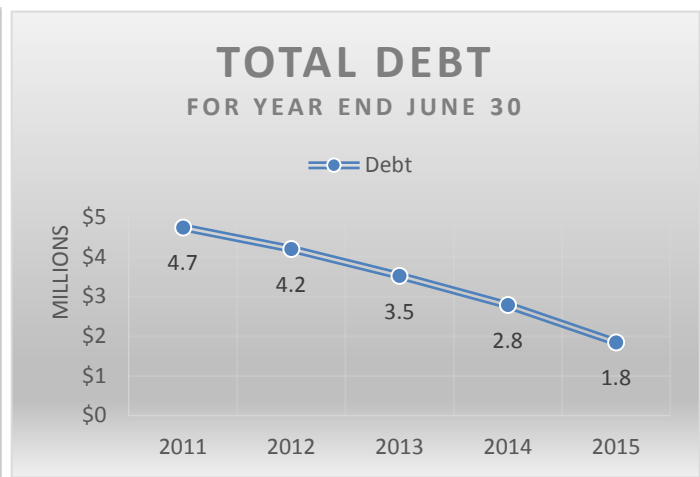
Expect, encourage, and enable students to excel at school and to live as responsible, productive citizens.

Financial Information

The following pages contain financial information about the District obtained from annual financial data reported to the Pennsylvania Department of Education (PDE) and available on PDE's public website. This information was not audited and is presented for **informational purposes only**.

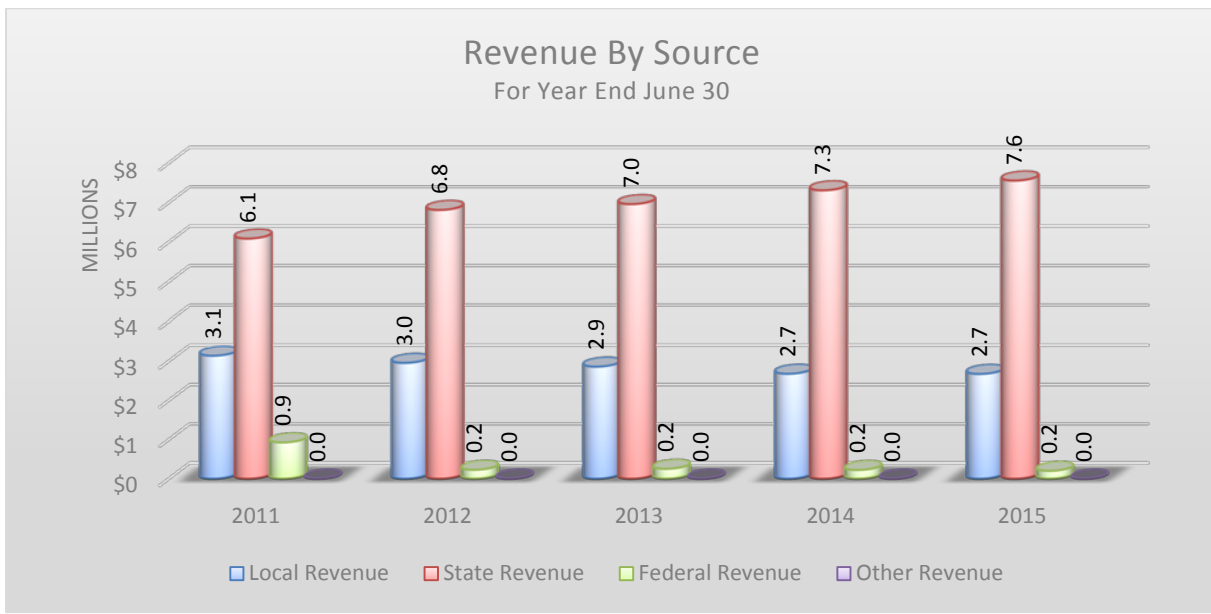
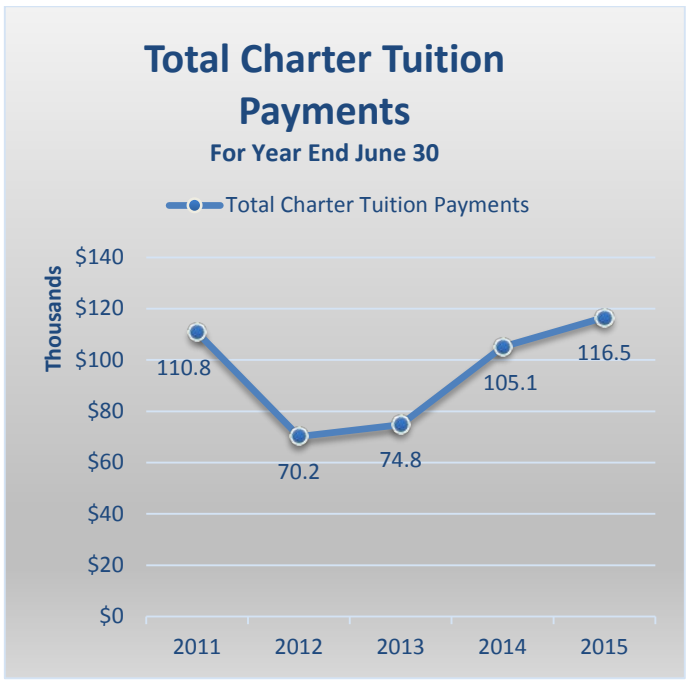
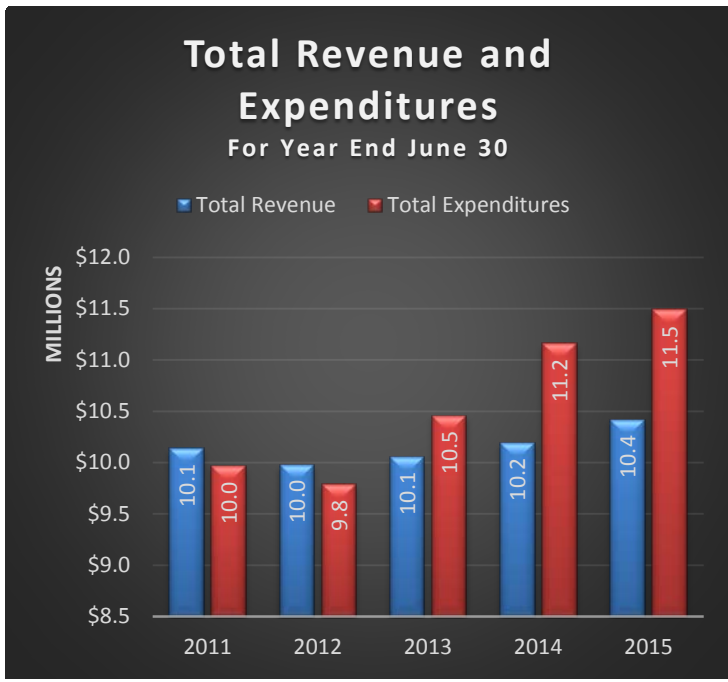


Note: General Fund Balance is comprised of the District's Committed, Assigned and Unassigned Fund Balances.



Note: Total Debt is comprised of Short-Term Borrowing, General Obligation Bonds, Authority Building Obligations, Other Long-Term Debt, Other Post-Employment Benefits and Compensated Absences.

Financial Information Continued



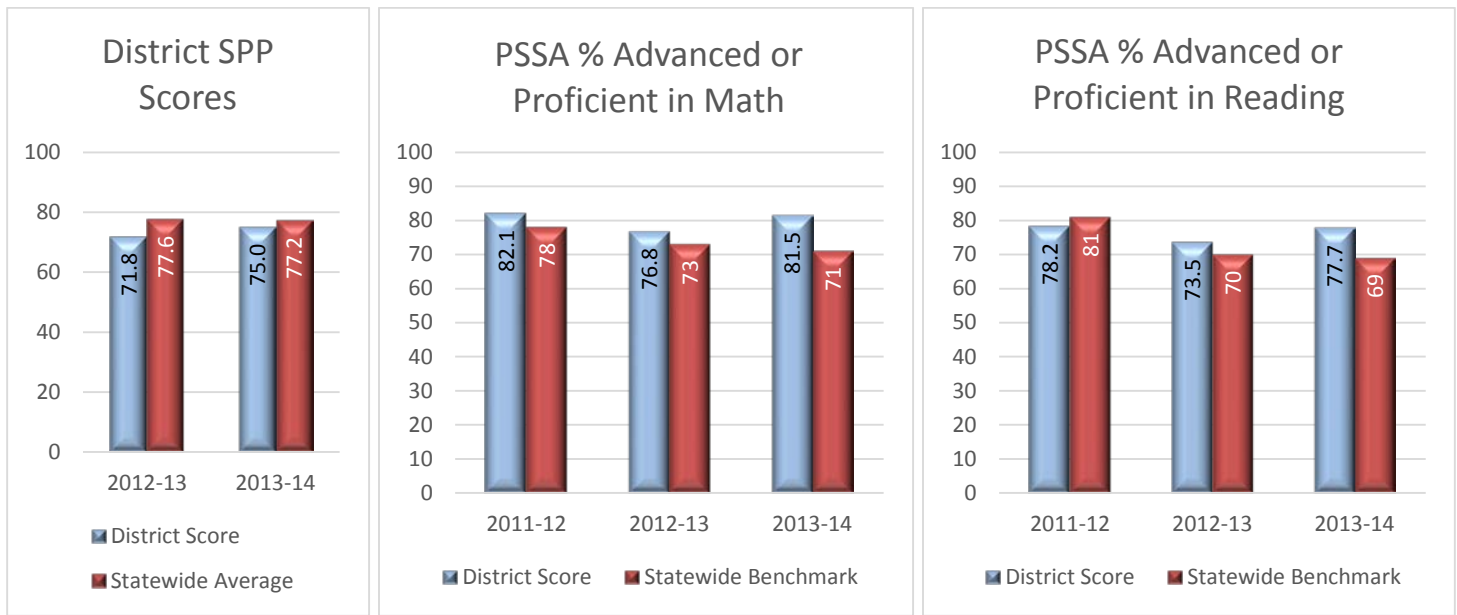
Academic Information

The following table and charts consist of School Performance Profile (SPP) scores and Pennsylvania System of School Assessment (PSSA) results for the entire District obtained from PDE's data files.¹ These scores are presented in the District's audit report for **informational purposes only**, and they were not audited by our Department.

SPP benchmarks represent the statewide average of all district school buildings in the Commonwealth.² PSSA benchmarks and goals are determined by PDE each school year and apply to all public school entities.³ District SPP and PSSA scores were calculated using an average of all of the individual school buildings within the District. Scores below SPP statewide averages and PSSA benchmarks/goals are presented in red.

Districtwide SPP and PSSA Scores

District	SPP Scores		PSSA % Advanced or Proficient in Math			PSSA % Advanced or Proficient in Reading		
	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
<i>Statewide Benchmark</i>	77.6	77.2	78	73	71	81	70	69
<i>Johnsonburg Area SD</i>	71.8	75.0	82.1	76.8	81.5	78.2	73.5	77.7
<i>SPP Grade⁴</i>	C	C						



¹ PDE is the sole source of academic data presented in this report. All academic data was obtained from PDE's publically available website.

² Statewide averages for SPP scores were calculated based on all district school buildings throughout the Commonwealth, excluding charter and cyber charter schools.

³ PSSA benchmarks apply to all district school buildings, charters, and cyber charters. In the 2011-12 school year, the state benchmarks reflect the Adequate Yearly Progress targets established under No Child Left Behind. In the 2012-13 and 2013-14 school years, the state benchmarks reflect the statewide goals based on annual measurable objectives established by PDE.

⁴ The following letter grades are based on a 0-100 point system: A (90-100), B (80-89), C (70-79), D (60-69), F (59 or below).

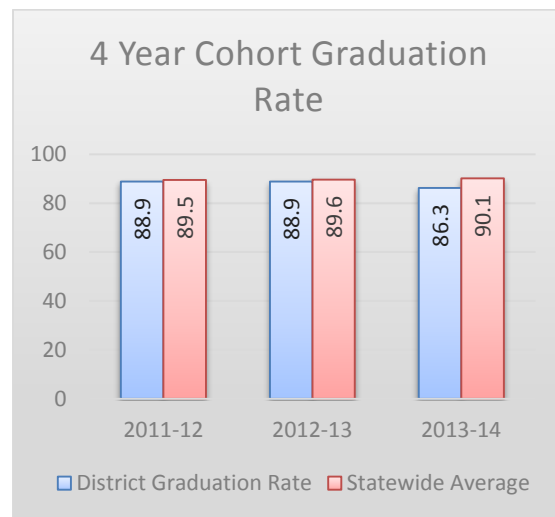
Individual School Building SPP and PSSA Scores

The following table consists of SPP scores and PSSA results for each of the District’s school buildings. Any blanks in PSSA data means that PDE did not publish a score for that school for that particular year.⁵

School Name	SPP Scores		PSSA % Advanced or Proficient in Math			PSSA % Advanced or Proficient in Reading		
	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
<i>Statewide Benchmark</i>	77.6	77.2	78	73	71	81	70	69
<i>Johnsonburg Area Elementary School</i>	73.1	86.7	87.2	78.3	81.7	76.9	76.5	76.4
<i>Johnsonburg Area High School</i>	70.4	63.2	77.0	75.4	81.3	79.5	70.4	78.9

4 Year Cohort Graduation Rates

The cohort graduation rates are a calculation of the percentage of students who have graduated with a regular high school diploma within a designated number of years since the student first entered high school. The rate is determined for a cohort of students who have all entered high school for the first time during the same school year.⁶



⁵ PDE’s data does not provide any further information regarding the reason a score was not published.

⁶ <http://www.education.pa.gov/Data-and-Statistics/Pages/Cohort-Graduation-Rate-.aspx>.

Findings

Finding No. 1

The District's Operating Deficits Reduced the General Fund Balance by 60 Percent (\$2.4 Million) Over a Four-Year Period

Criteria relevant to the finding:

The benchmarks used as criteria for this objective were based on best business practices established by several entities, including the Pennsylvania Association of School Business Officials (PASBO), the Colorado State Auditor, and the National Forum on Education Statistics. The following are some of the benchmarks used in our evaluation:

1. Operating position is the difference between actual revenues and actual expenditures. Financial industry guidelines recommend that the district operating position always be positive (greater than zero).
2. A school district should maintain a trend of stable fund balances.

Our review of the District's financial position over a four-year period showed that the District's General Fund balance decreased by over 60 percent to a level that is below the recommended financial industry guidelines, which should be concerning to taxpayers. The District experienced operating deficits in three of the four years reviewed, and those deficits were the primary factor in the decrease in the General Fund balance. The operating deficits increased from \$400,450 in the 2012-13 fiscal year to \$1,065,808 during the 2014-15 fiscal year.

In order to assess the District's financial stability, we reviewed several financial benchmarks to evaluate changes in its financial position over a period of four years from July 1, 2011, through June 30, 2015. Our evaluation raised concerns in the following areas of the District's finances:

- General Fund Balance
- Operating Position
- Revenues and Expenditures

General Fund Balance

As shown in Chart 1, the District's General Fund balance has steadily decreased during the period reviewed and was trending toward a negative balance by the fiscal year ending June 30, 2017.

Criteria relevant to the finding
(continued):

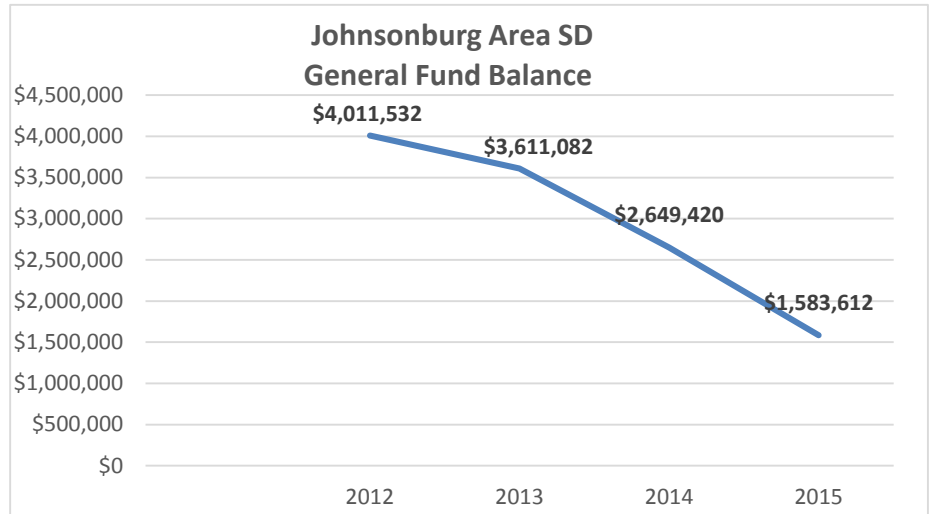
The Government Finance Officers Association (GFOA) has developed Budgeting Best Practices for School Districts. Among the best practices are:

General Fund Reserve. School districts should establish a formal process on the level of unrestricted/uncommitted/unassigned fund balance that should be maintained in the General Fund as a reserve to hedge against risk. The GFOA recommends, at a minimum, an unrestricted fund balance in their General Fund of no less than 10 percent of regular General Fund operating revenues or regular general operating expenditures.

The Pennsylvania School Boards Association in its Annual Overview of Fiscal Health for the 2013-14 school year provided the following information relevant to the following fiscal benchmarks:

- Financial industry guidelines recommend that fund balances be between 5 percent and 10 percent of annual expenditures.
- Operating position is the difference between actual revenues and actual expenditures. Financial industry guidelines recommend that the district operating position always be positive (greater than zero).

Chart 1



Of the District’s \$1.5 million General Fund balance as of June 30, 2015, only \$307,879 was classified as unassigned. This classification represents the spendable amount of the District’s General Fund, and it is significantly less than the fund balance recommended by GFOA (i.e. 10 percent of operating revenue or expenditures). The remaining \$1.2 million of the General Fund balance is classified as either assigned⁷ or non-spendable⁸ funds.

The operating deficits that occurred from the 2012-13 fiscal year through the 2014-15 fiscal year required the District to use their General Fund balance to pay for operating expenditures. While the District was able to employ this practice during our period reviewed, the current General Fund balance is not sufficient to continue this practice.

Just as individuals should have a “rainy day fund” to deal with emergencies or unforeseen needs, school districts should also have available reserve funds to deal with emergencies, unanticipated expenses, and disruptions to its revenues. The lack of available reserve funds could also lead to the District having no other options than borrowing money to maintain operations. Districts with low General Fund balances are considered higher risk borrowers and are more likely to be charged a higher interest rate when borrowing. Future borrowing costs could increase if the District’s General Fund balance doesn’t improve.

⁷ Assigned Fund Balance – are intended to be used by the District for specific purposes.

⁸ Committed Fund Balance – are funds that can only be used for the specific purposes as determined by a formal action of the District’s Board of School Directors.

Operating Position

A school district's operating position is determined by reviewing the total operating revenues compared to total operating expenditures. An operating deficit occurs when expenditures are greater than revenues. The following table shows the District's operating position for the four years reviewed and the increasing operating deficit that occurred during the period.

Table 1

Johnsonburg Area SD General Fund Operating Position			
Year Ended June 30	Total Revenues and Other Financing Sources⁹	Total Expenditures and Other Financing Uses¹⁰	Operating Surplus/ (Deficit)
2012	\$9,985,007	\$9,791,216	\$193,791
2013	10,063,585	10,464,035	(\$400,450)
2014	10,202,197	11,163,859	(\$961,662)
2015	10,422,865	11,488,673	(\$1,065,808)
Total:	\$40,673,654	\$42,907,783	(\$2,234,129)¹¹

The District's financial decline during the period reviewed can be attributed to the District's increasing expenditures, which outpaced steady revenues. Rising instructional expenditures, mainly retirement and healthcare costs, were the primary cause of the District's increasing expenditures.

Revenues

The District relies heavily on revenue from the Commonwealth. Revenue from the Commonwealth comprised 72 percent of the District's total revenues in the 2014-15 fiscal year. Another 26 percent of total revenues were derived from local revenues while federal revenue was the source of the remaining 2 percent.

⁹ Information obtained from the District's Independent Auditor's Report, *Statement of Revenue, Expenditures and Changes in Fund Balance*, fiscal years ending 2011 through 2015.

¹⁰ Ibid.

¹¹ The difference between the District's cumulative operating deficit (\$2,234,129) and the decrease in the General Fund balance (\$2,427,920) is \$193,791. This amount can be attributed to prior period adjustments that occurred during the audit period.

The District's total revenues increased by 4 percent from July 1, 2011, through June 30, 2015. During this same time period, the District's largest revenue component (Commonwealth funding) increased by 10 percent. However, during the same time period, local revenues actually decreased 9 percent from \$2,952,446 in the 2011-12 fiscal year to \$2,671,898 in the 2014-15 fiscal year.

The District's millage rate remained constant at 30.08 during the period reviewed. The District believed that their tax base could not handle an increase in the millage rate and that an increase in the millage rate would be counterproductive and result in less revenue collected due to an increase in tax delinquencies. Local tax revenue collected decreased by almost \$20,000 from the 2011-12 fiscal year to the 2014-15 fiscal year. The District attributed this to a decreasing population during the period.

Due to the current financial situation of the District and in particular the low General Fund balance, the District's Board did raise taxes from 30.08 to 30.90 mills in the 2015-16 fiscal year and from 30.90 to 31.50 mills in the 2016-17 fiscal year.

Expenditures

The District's total expenditures increased by 17 percent during the period reviewed. This increase was over four times the rate that total revenues increased over the same time period. The increase in expenditures occurred mainly due to rising retirement and healthcare costs that the District experienced.

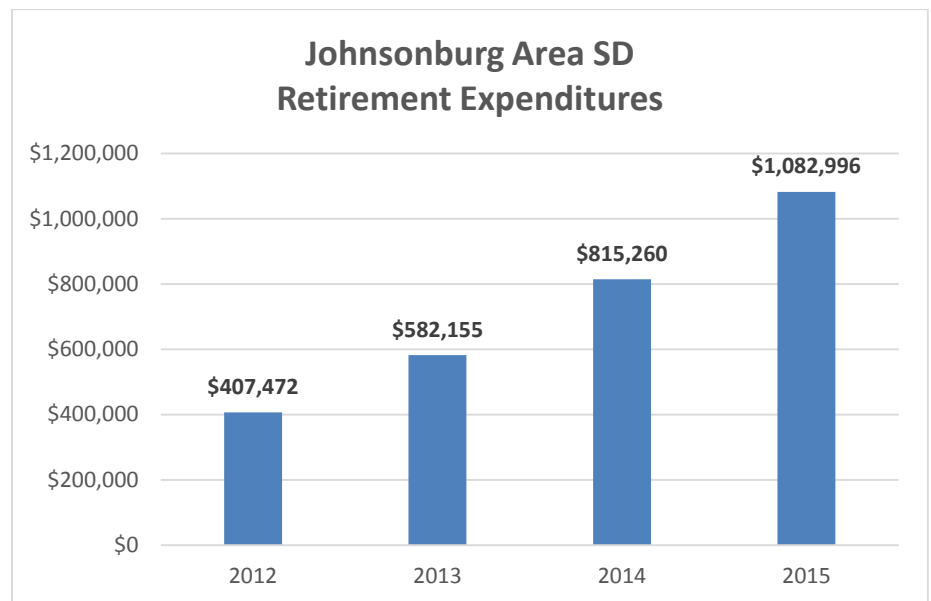
Increased Retirement Costs

The District's required contribution to the Public School Employees' Retirement System increased from 8.65 percent of payroll in the 2012-13 fiscal year to 21.4 percent in the 2014-15 fiscal year. While this is a significant increase, the Commonwealth communicated these increases well in advance in order to give school districts the opportunity to prepare for the increases.

While the District made efforts to reduce operational expenses where possible, those efforts still weren't enough to cover total expenditures with available revenue. Rather than raise taxes, the District chose to spend down the General Fund balance. The District's General Fund balance is currently too low to continue this practice of using the General Fund to pay for excess expenditures over revenues. Further, the District has been notified that the retirement contribution rates will continue to escalate, which will place even more of a financial burden on the District. The District expects rising retirement and healthcare costs to outpace the additional revenue the District hopes to achieve with the tax millage increases.

The chart below illustrates the increase in the District's required retirement expenditures.

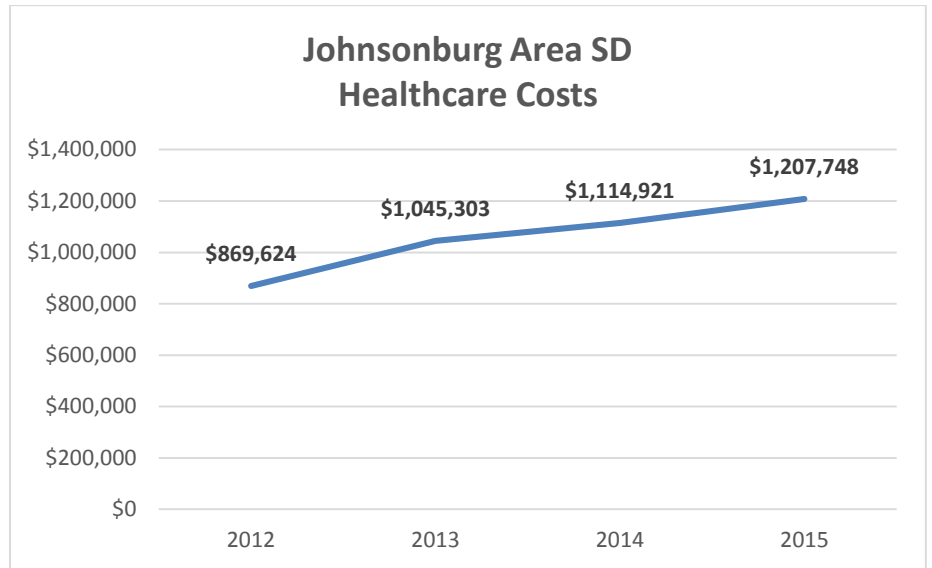
Chart 2



Increasing Healthcare Costs

The District's increasing costs for employees' healthcare was the second largest component of the increase in instructional expenditures. Chart 3 shows the 39 percent increase in healthcare costs over the period reviewed:

Chart 3



To help control costs in 2016-17, the District modified the employee health insurance plan to include higher deductibles than previously required. The District estimates this change will save over \$138,000 per year.

When we asked specifically about the District's future plans to address the operating deficits and declining fund balance, District officials responded as follows:

Our only choice is to continue to look for ways to lessen District expenditures. The District is getting smaller and will continue to look for ways to share services with neighboring school districts, reviewing professional positions for possible elimination and any other costs that can be cut without hurting District's commitment to their students and community.

While the District has been able to sustain operations to this point, the District cannot continue to operate for the next five years with expenditures outpacing revenues. While we acknowledge that the District has taken actions to reverse its financially declining position, until operating revenues exceed operating expenditures, the District's financial position will remain tenuous.

Recommendations

The *Johnsonburg Area School District* should:

1. Develop and implement a long-term strategic plan that will assist the District in replenishing and then stabilizing the General Fund.
2. Prepare a multi-year budget that adequately reflects annual commitments to help ensure the District is prepared to meet future obligations.
3. Review the tax collection percentages during the 2015-16 and 2016-17 fiscal years to determine the optimal balance between raising the millage rate and actual amount collected.

Management Response

District management provided the following response:

The District disagreed with the finding, stating, "While the District agrees with the facts that the District is in financial decline due to increasing expenditures outpacing steady revenues, and that the need for a long term strategic plan is necessary, the Board has been aware of the issue and has made many decisions to reduce operating expenses. At the end of the 2017-18 fiscal year our outstanding debt payment will have been satisfied and that will save the District over \$500,000 per year. The District's goal is to begin to build the fund balance to a prudent amount.

The District has a dwindling population and therefore not robust tax base and does depend heavily on state funding. This is a multifaceted problem and the Board is doing everything they can to keep this school system operational and provide the best education for its students as possible. Special Education costs have also increased tremendously as well as payments to charter schools which are not always

known from year to year. The budget impasse in 2014 was especially hard on the District and the Board was forced to draw on its investments before actually relying on a line of credit that had to be paid back.”

Auditor Conclusion

We are encouraged that the District has taken steps to reduce expenses. While we acknowledge that the District has a declining population base and increasing fixed costs, we continue to stress the importance of having revenues exceed expenses. We will determine the effectiveness of the District’s actions during our next cyclical audit of the District.

Finding No. 2

The District's Real Estate Agreement with its Bus Contractor Lacked Board Oversight and May Place Future Financial Obligations on the District

Criteria relevant to the finding:

Chapter 23 of the State Board of Education regulations provides, in part:

“The board of directors of a school district shall be responsible for all aspects of pupil transportation programs, including the following:

(7) The negotiation and execution of contracts or agreements with contractors . . .” See 22 Pa. Code § 23.4(7).

On May 14, 2015, the Board entered into and approved at a public meeting a Real Estate Agreement (Agreement) with the District's current bus contractor (Contractor) that may not have been in the best financial interest of the District. The Agreement allowed the Contractor to build a work garage on district-owned property for a one-time lease payment of \$1. Under the Agreement, the Contractor may occupy the garage as long as it provides transportation services to the District.

Our review of the Agreement indicates that the District did not receive any compensation for allowing the Contractor to build a garage on its property except for the \$1 lease payment. Instead, the District will most likely incur additional costs in the future if and when it ends its relationship with the Contractor. Refer to the Criteria Box for information on the contract's termination provisions.

In addition, we found that the Agreement lacked terms requiring the Board to approve the physical structure and costs for the garage that it may have to buy from the Contractor in the future. The Agreement also lacked deadlines for the Contractor to obtain the necessary land survey and appraisal and a requirement for the Contractor to provide these documents to the Board. Consequently, the land survey was completed but not provided to the Board, and the appraisal documenting the fair market value of the District's property wasn't obtained until requested during our audit, which was more than a year after construction was complete. Without this information, the Board did not know the value of the district-owned land before the work garage was built, a figure that was also important to the termination provisions of the Agreement (see Criteria Box).

Lastly, while the Board considered the financial implications of this Agreement at the time it was signed, it does not appear that potential long-term costs were analyzed for the period after the current transportation contract expires on June 30, 2018. The District could be subject to long-term costs that could result from the building of this garage, including but not limited to, future environmental damages. Ultimately, the Board is

*Criteria relevant to the finding
(continued):*

Termination Provisions of Agreement

The Agreement is to remain in effect as long as the Contractor is providing transportation services to the District. However, if the District opts to go with a different bus contractor in the future, the Agreement outlines two termination options that are both based on a land appraisal required by the Agreement.

1. The Board can elect to retain ownership of the property and purchase the facility from the current Contractor. Under this option, the Contractor is responsible for obtaining an appraisal of the land and building at the time of termination. Then, the Board would pay the difference between the land only appraisal originally required by the Agreement and the land and building appraisal required at the time of termination.
2. If the Board does not wish to retain ownership of the property, the Contractor can purchase the land from the District. Under this option, the Contractor would purchase the land from the Board using the land only appraisal originally required under the Agreement, and the Board would be responsible for the cost of executing a deed for the land.

responsible for all aspects of student transportation, including the execution and oversight of contracts and agreements.

Background Information Regarding the Agreement

The District’s current transportation contract covers the period July 1, 2011, through June 30, 2018. In October 2014, the Contractor expressed an interest in buying district-owned property in order to build a work garage and administrative office. The District wasn’t interested in selling its land, but it agreed to allow the Contractor to build a work garage on its property for maintenance of vehicles used to transport District students, as long as the Contractor incurred all associated costs.

As such, the parties entered into an Agreement on May 14, 2015, allowing the Contractor to lease the District’s land at no cost and to build a work garage at the Contractor’s expense. The Agreement required the Contractor to obtain a land survey and appraisal at his expense, but the Agreement lacked specific deadlines for these activities to be completed. Additionally, the Contractor was responsible for all costs associated with constructing, maintaining, and insuring the work garage, as well as paying any resulting property taxes. The garage was built and operational for the start of the 2015-16 school year. The Contractor is entitled to occupy the garage for the duration of the current contract and through any extensions thereof.

Board’s Failure to Stipulate Construction Terms and Be Informed of Building Costs

The Agreement lacked terms requiring the Board to approve the physical structure and costs associated with the work garage that the Contractor wanted to build on district-owned property. While the Contractor outlined the size of the building, what would be in it, and the anticipated completion date in a letter to the District dated October 14, 2014, neither a budget or anticipated costs were provided. None of these specifics or reference to this letter were included in the Agreement. Therefore, the District did not have any control over the physical building and construction costs on its property.

In fact, the District didn't know: 1) the value of its land prior to construction; 2) the costs associated with the construction; or 3) the value of the building after completion until we inquired about these amounts during our audit. Similarly, the Board wasn't informed of existing costs associated with the upkeep of the work garage, such as maintenance and insurance costs that the District could incur if it buys the building from the Contractor.

After we requested this documentation, the District contacted the Contractor and provided a **land and building** appraisal dated November 10, 2016, which indicated the value of the District's land was \$30,000 and the building was \$150,000. This appraisal wasn't obtained by the Contractor until more than one year after the work garage was completed, so a land only appraisal prior to construction never occurred.

Since the District owns the land that the work garage was built on and it may have to buy the building if and when it terminates services with the Contractor, it would have been prudent to include construction terms in the Agreement to protect the District's land asset and potential financial obligations.

Concerns Regarding the Agreement and Future Costs

If the District eventually terminates the transportation contract with the Contractor and purchases the building (the first termination provision in the Criteria Box), using the numbers from the 2016 appraisals by way of example, the District would have to pay the Contractor \$150,000 for the building (i.e., land and building appraisal of \$180,000 minus the land only appraisal of \$30,000). However, it's important to note that a new land and building appraisal would have to be obtained at the time of termination of the transportation contract, so the estimated value of the building could potentially be higher at that time, which would increase the buy-out costs for the District.

Alternatively, if the Board does not wish to retain ownership of the property (the second termination provision in the Criteria Box), the Contractor can purchase the land from the District using the land only appraisal originally required under the Agreement.

Because the land only appraisal amount of \$30,000 remains in place for both termination provisions, it appears that the District would not be compensated for any appreciation in the value of the land during the period of the Agreement under either termination option despite being the owner of the land. Instead, all of the appraised land appreciation would be a gain for the Contractor.

Summary

Transportation costs are a large part of the District's budget. The Board is responsible for all aspects of student transportation, including contracting and ensuring contract oversight.

The Board's lack of construction stipulations in the Agreement and oversight of the construction and costs allowed the Contractor considerable freedom while building on district-owned land. Without placing stipulations on the construction project and staying informed of construction costs and completion values, it does not appear that necessary safeguards were in place to protect the District's future financial interests.

The District essentially agreed to allow the Contractor to use its land for free while the Contractor provided transportation services to the District. The Contractor is paid for the transportation services that are provided to the District. In addition, upon termination of transportation services with the Contractor, the District will have to choose between either selling the land without any appreciation from date of the Agreement or purchasing the building based on an appraised value and becoming responsible for the related maintenance costs as well as any other costs that resulted from the construction of the garage. It is important that the Board have knowledge of these potential costs in order to make an informed decision regarding future transportation contracts.

As shown in Finding No. 1 of this report, the District is experiencing a declining financial position; therefore, it is essential that the District carefully evaluate potential contractual agreements to determine whether they are in the best financial interests of the District. All precautions should be made to protect the taxpayers' funds for the future of the District and its students.

Recommendations

The *Johnsonburg Area School District* should:

1. Thoroughly evaluate the terms of any significant contracts being negotiated and ensure that all agreements are in the best financial interest of the District.
2. Obtain building-related costs (e.g. utilities, insurance, maintenance, etc.) from the bus contractor.

Management Response

District management provided the following response:

The District disagreed with the finding, stating, “The board felt confident that the decision to allow the bus contractor to erect a building on the District’s land was in the best interest of the school district and its taxpayers. The solicitor for the school district had reviewed the request and was in agreement. The Board did not want to sell any of the District’s land for several reasons, one of them being that if the current contractor was not the successful bidder on a new transportation contract, and they owned the land, they would be able to sell that land to whomever they wanted. Since we do not own our busses and do not plan on owning the busses, the Board felt that any new transportation company would need a building to house busses and perform maintenance. The space that was occupied previously was not adequate for maintaining the busses and was an eyesore. The District will thoroughly evaluate all future agreements and ensure they are in the best financial interest of the District. Any contractor bidding on a transportation contract with the District would be 100% responsible for building related costs such as utilities, insurance, maintenance, etc.”

Auditor Conclusion

The current agreement has the potential to lead to a future financial liability for the District. This agreement allowed the Contractor to use district-owned land for free while the Contractor provided transportation services to the District. This agreement will eventually force the District to either sell the land without any appreciation from the date of the Agreement or purchase the building and the associated known and unknown costs that come with that purchase.

Status of Prior Audit Findings and Observations

Our prior audit of the District released on October 18, 2013, resulted in one finding, as shown below. As part of our current audit, we determined the status of corrective action taken by the District to implement our prior audit recommendations. We reviewed the District's written response provided to PDE, interviewed District personnel, and performed audit procedures as detailed in each status section below.

Auditor General Performance Audit Report Released on October 18, 2013

Prior Finding: **Memorandums of Understanding with Local Law Enforcement Not Updated Timely**

Prior Finding Summary: During our prior audit of the District, we found that the Memorandum of Understanding (MOU) between the District and the local law enforcement agencies had not been updated timely. The Public School Code requires public schools to update and re-execute MOUs with local law enforcement every two years.

Prior Recommendations: We recommended that the District should:

1. Continue to review, update, and re-execute the current MOUs between the District and all the local law enforcement agencies having jurisdiction over school property.
2. Adopt an official board policy requiring District administration to biennially update and re-execute the MOUs with local law enforcement agencies having jurisdiction over school property and file a copy with PDE's Office of Safe Schools on a biennial basis as required by law.

Current Status: The District did implement our prior recommendations. The District currently has two updated MOUs. The MOUs with the Johnsonburg Borough Police Department and the Pennsylvania State Police were both updated February 1, 2017.

In addition, on May 9, 2013, the District updated Board Policy No. 805, regarding Emergency Preparedness. The policy requires District administration to biennially update and re-execute all MOUs with local law enforcement agencies having jurisdiction over school property and to file a copy with PDE's Office of Safe Schools on a biennial basis as required.

Appendix: Audit Scope, Objectives, and Methodology

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, PDE, and other concerned entities.

Our audit, conducted under authority of Sections 402 and 403 of The Fiscal Code,¹² is not a substitute for the local annual financial 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. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit.

Scope

Overall, our audit covered the period July 1, 2012, through June 30, 2015. In addition, the scope of each individual audit objective is detailed on the next pages.

The District's management is responsible for establishing and maintaining effective internal controls¹³ to provide reasonable assurance that the District is in compliance with certain relevant state laws, regulations, contracts, and administrative procedures (relevant requirements). In conducting our audit, we obtained an understanding of the District's internal controls, including any information technology controls, which 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 controls 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.

¹² 72 P.S. §§ 402 and 403.

¹³ 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; and compliance with certain relevant state laws, regulations, contracts, and administrative procedures.

Objectives/Methodology

In order to properly plan our audit and to guide us in selecting objectives, we reviewed pertinent laws and regulations, board meeting minutes, academic performance data, annual financial reports, annual budgets, new or amended policies and procedures, and the independent audit report of the District's basic financial statements for the fiscal years July 1, 2012, through June 30, 2015. We also determined if the District had key personnel or software vendor changes since the prior audit.

Performance audits draw conclusions based on an evaluation of sufficient, appropriate evidence. Evidence is measured against criteria, such as laws, regulations, third-party studies, and best business practices. Our audit focused on the District's efficiency and effectiveness in the following areas:

- ✓ Financial Stability
- ✓ Transportation Operations
- ✓ Bus Driver Requirements
- ✓ School Safety

As we conducted our audit procedures, we sought to determine answers to the following questions, which served as our audit objectives:

- ✓ Based on an assessment of financial indicators, was the District in a declining financial position, and did it comply with all statutes prohibiting deficit fund balances and the over expending of the District's budget?
 - To address this objective, we reviewed the District's annual financial reports, General Fund budgets, independent auditor's reports, and summary of child accounting for fiscal years 2011-12 through 2014-15. The financial and statistical data was used to calculate the District's General Fund balance, operating position, charter school costs, debt ratio, and current ratio. These financial indicators were deemed appropriate for assessing the District's financial stability. The financial indicators are based on best business practices established by several agencies, including PASBO, the Colorado Office of the State Auditor, and the National Forum on Education Statistics. Finding No. 1 describes the results of our review of this objective.
- ✓ Did the District ensure compliance with applicable laws and regulations governing transportation operations, and did the District receive the correct transportation reimbursement from the Commonwealth?¹⁴
 - To address this objective, we randomly selected 4 out of 14 vehicles for the District's largest contractor during the 2014-15 school year. We obtained information that supported data reported to PDE to ensure that the District reported the correct information and received the appropriate transportation

¹⁴ See 24 P.S. §§ 3-1301, 13-1302, 13-1305, 13-1306; 22 Pa. Code Chapter 11.

subsidies from PDE. This information obtained included: odometer readings, daily mileage sheets, student rosters, and weighted calculations. In addition, we reviewed both contracts with the District's bus contractor to ensure they were current, properly obtained, approved, executed, and monitored. Finding No. 2 describes the only reportable issues noted during our review of this objective.

- ✓ Did the District ensure that bus drivers transporting District students had the required driver's license, physical exam, training, background checks, and clearances as outlined in applicable laws?¹⁵ Also, did the District have written policies and procedures governing the hiring of new bus drivers that would, when followed, provide reasonable assurance of compliance with applicable laws?
 - To address this objective, we randomly selected five of the nine new bus drivers hired by the District's bus contractor during the period September 12, 2013, through October 7, 2016, and reviewed documentation to ensure the District complied with the requirements for bus drivers. We also determined if the District had written policies and procedures governing the hiring of bus drivers and if those procedures, when followed, ensure compliance with bus driver hiring requirements. Our review of this objective did not disclose any reportable issues.

- ✓ Did the District take actions to ensure it provided a safe school environment?¹⁶
 - To address this objective, we reviewed a variety of documentation including safety plans, training schedules, and anti-bullying policies. Due to the sensitive nature of school safety, the results of our review of this objective are not described in our audit report. The results of our review of school safety are shared with District officials and, if deemed necessary, with PDE.

¹⁵ 24 P.S. § 1-111, 23 Pa.C.S. § 6344(a.1), 24 P.S. § 2070.1a *et seq.*, 75 Pa.C.S. §§ 1508.1 and 1509, and 22 *Pa. Code Chapter 8*.

¹⁶ 24 P.S. § 13-1301-A *et seq.*

Distribution List

This report was initially distributed to the Superintendent of the District, the Board of School Directors, and the following stakeholders:

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