



**EASTERN LEBANON COUNTY
SCHOOL DISTRICT**

LEBANON COUNTY, PENNSYLVANIA

PERFORMANCE AUDIT REPORT

JUNE 2014

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL





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EUGENE A. DePASQUALE
AUDITOR GENERAL

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

Mr. Leon Moll, Board President
Eastern Lebanon County School District
180 Elco Drive
Myerstown, Pennsylvania 17067

Dear Governor Corbett and Mr. Moll:

We conducted a performance audit of the Eastern Lebanon County 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 4, 2011 through May 24, 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, 2009, 2010, 2011, and 2012. 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 did identify one (1) 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 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 A. DEPASQUALE
Auditor General

June 12, 2014

cc: **EASTERN LEBANON COUNTY 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 Eastern Lebanon County School District (District) in Lebanon County. Our audit sought to answer certain questions regarding the District's compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures.

Our audit scope covered the period March 4, 2011 through May 24, 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 2008-09, 2009-10, 2010-11, and 2011-12 school years.

District Background

The District encompasses approximately 75 square miles. According to 2010 federal census data, it serves a resident population of 20,724. According to District officials, the District provided basic educational services to 2,512 pupils through the employment of 177 teachers, 101 full-time and part-time support personnel, and fourteen (14) administrators during the 2011-12 school year. The District received \$8.5 million in state funding in the 2011-12 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 (1) matter unrelated to compliance that is reported as an observation.

Observation: The District is Facing an Increasingly Precarious Financial Situation Including a Declining General Fund Balance and Rapidly Increasing Charter School Costs. Our review of the Eastern Lebanon County School District's (District) financial situation found that the District's general fund balance has decreased nearly 77 percent over the four-year period we examined, to a fund balance of \$190,035, as of June 30, 2012 (see page 5).

Status of Prior Audit Findings and Observations. There were no findings or observations in our prior audit report.

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 4, 2011 through May 24, 2013, except for the verification of professional employee certification, which was performed for the period July 1, 2012 through April 18, 2013.

Regarding state subsidies and reimbursements, our audit covered the 2008-09, 2009-10, 2010-11, and 2011-12 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 payroll (e.g. Social Security and retirement), did it follow applicable laws and procedures?

- ✓ Did the District, and any contracted vendors, ensure that current bus drivers were properly qualified, and did they have written policies and procedures governing the hiring of new bus drivers?
- ✓ 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 contracts contain adequate termination provisions?
- ✓ Were votes made by the District's Board of School Directors free from apparent conflicts of interest?
- ✓ 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?
- ✓ Were there any declining fund balances that may pose a risk to the District's fiscal viability?
- ✓ 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 there any other areas of concern reported by independent auditors, citizens, or other interested parties?

Methodology

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

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 state laws, regulations, contracts, grant requirements, and administrative procedures.

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 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.

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.

Findings and Observations

Observation

The District is Facing an Increasingly Precarious Financial Situation Including a Declining General Fund Balance and Rapidly Increasing Charter School Costs

Our review of the Eastern Lebanon County School District's (District) annual financial reports, independent auditor's reports (IAR), and general fund budgets for the fiscal years ended June 30, 2009, 2010, 2011, and 2012 found that although the District had an \$823,298 general fund surplus as of June 30, 2008, its balance decreased to a general fund balance at the end of the 2011-12 school year of \$190,035—nearly a 77 percent decrease over that four-year period. The IAR reported the following:

<u>Year</u> <u>Ending</u> <u>June 30</u>	<u>Revenue</u>	<u>Expenditures</u>	<u>Expenditures</u> <u>(Over)/Under</u> <u>Revenues</u>	<u>Other Financing</u> <u>Sources/</u> <u>(Uses)</u>	<u>Adjustments</u>	<u>General Fund</u> <u>Surplus/</u> <u>(Deficit)</u>
2008	-	-	-	-	-	\$ 823,298
2009	\$ 28,547,462	\$ 25,153,441	\$ 3,394,021	\$ (3,746,392)	\$ 14,978	485,905
2010	30,850,789	26,344,015	4,506,774	(4,547,213)	(41,330)	404,136
2011	31,559,303	27,422,706	4,136,597	(4,420,948)	(2,507)	117,276
2012	31,972,256	27,427,428	4,544,828	(4,256,537)	(215,533)	190,035

Our review identified the following factors that contributed to the District's financial deterioration:

Continued Construction Projects without Certainty as to when Reimbursements will be Received:

The District embarked on an extensive construction project in 2009 and completed all Pennsylvania Department of Education (PDE) required PlanCon applications necessary to receive reimbursement. Due to PDE constraints, PlanCon reimbursements are backlogged, and a moratorium has been placed on all new PlanCon applications effective for the 2012-13 school year. Therefore, it is unknown as to when these reimbursements will be available to cover current expenditures.

Increased Charter School Obligations and Discontinued State Reimbursement for said Costs:

Tuition paid to charter schools has increased rapidly at the District, as the table below illustrates. In addition, the District is facing growing financial pressure as a result of the elimination of the state reimbursement paid to all districts for a portion of their charter costs. While the District’s charter costs have risen, the issue is compounded by the fact that, since 2011, the Commonwealth has not funded the District reimbursement for charter school tuition costs. If this reimbursement were still in place, the District would have received at least \$90,000 in additional revenue for 2010-11 and 2011-12.

School Year	Tuition Paid to Charter Schools	State Reimbursement Paid to District
2007-08	\$ 212,568	\$ 58,933
2008-09	352,073	82,247
2009-10	455,122	88,344
2010-11	593,140	No Funding
2011-12	639,070	No Funding
Four-Year Increase:	<u>200%</u>	

Annual Payback of Overpaid Taxes:

The District’s finances are further stressed by a settlement agreement that requires the District to make annual payments back to the local tax bureau. The District was overpaid \$1,171,006 in local property taxes between the years 2004 and 2007. This overpayment was incurred because of a wide-ranging fraud and theft-of-funds by the former executive director of the Lebanon County Earned Income Tax Bureau, where money being shifted around resulted in some school districts being underpaid, and some being overpaid. This was confirmed by an independent investigation. The settlement agreement requires the District to pay the total overpayment back in equal installments (\$61,631.87) over a nineteen-year period beginning September 30, 2012.

Recommendations

The *Eastern Lebanon County School District* should:

1. Use monthly budget status reports to scrutinize proposed expenditures for current operations and limit them to revenues received and the amounts appropriated.
2. Open a dialogue with the District's community to keep stakeholders informed of the financial status and health of the District.
3. Conduct a survey of parents sending children to a charter school to determine the reason why the District is losing more students to charter schools.

Management Response

Management stated the following:

“The district has experienced a declining fund balance for several reasons.

- First, Cyber Charter School tuition increased significantly during the time of the audit and state reimbursement ended.
- Second, special education costs increased significantly, due in large part to move-ins, and state reimbursement has been flat during that same time period.
- Third, Lebanon County experienced serious problems including embezzlement and problems with distribution of funds with its local earned income tax collections during this audit period.
- And, fourth, the district embarked on a construction project in 2009, received approvals on PlanCon A through G, submitted H in July, 2009 and a second H in spring 2010 and is still awaiting action by PDE to receive reimbursement on debt payments since 2009. We followed the rules of PlanCon but as of June 30, 2013, it is estimated the state owes ELCO School District over \$388,000 on the debt payments

the district has made while waiting for PDE to process PlanCon H.

A prior period adjustment was made June 30, 2012 removing a \$215,000 receivable the district carried for the debt payments made in prior years and for which reimbursement was not received. Had that prior period adjustment not been made *and* had we booked a receivable for the reimbursement due for payments made during 2011-12, the fund balance would have been more than twice what it was at June 30, 2012.

The district has been working to reverse the declining fund balance trend and in fact, grew the fund balance slightly at June 30, 2012 in spite of the adjustments described above concerning debt reimbursements. The fund balance is projected to grow an estimated \$200,000 at the close of the 2012-13 fiscal year, again in spite of not receiving reimbursement on some debt payments made during 2012-13.”

Auditor Conclusion

The purpose of this observation is to inform the District and its stakeholders about its financial situation. We are encouraged that the District is actively working to reverse its General Fund balance trend. We will follow up on the District’s financial position during our next cyclical audit.

Status of Prior Audit Findings and Observations

Our prior audit of the Eastern Lebanon County School District resulted in no findings or observations.

Distribution List

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

The Honorable Tom Corbett
Governor
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The Honorable Carolyn Dumaesq
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1010 Harristown Building #2
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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.