

# PERFORMANCE AUDIT

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## Western Beaver County School District Beaver County, Pennsylvania

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June 2015



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE  
AUDITOR GENERAL

The Honorable Tom W. Wolf  
Governor  
Commonwealth of Pennsylvania  
Harrisburg, Pennsylvania 17120

Mr. Patrick McGeehan, Board President  
Western Beaver County School District  
343 Ridgemont Drive  
Midland, Pennsylvania 15059

Dear Governor Wolf and Mr. McGeehan:

We conducted a performance audit of the Western Beaver 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 16, 2012 through August 8, 2014, except as otherwise stated in the report. Additionally, compliance specific to state subsidies and reimbursements was determined for the school years ended June 30, 2011 and June 30, 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 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 A. DePasquale  
Auditor General

June 11, 2015

cc: **WESTERN BEAVER COUNTY SCHOOL DISTRICT** Board of School Directors

## Table of Contents

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	Page
Executive Summary .....	1
Audit Scope, Objectives, and Methodology .....	2
Findings and Observations .....	6
Observation – The District Should Monitor Key Financial Indicators to Try to Prevent Further Fiscal Challenges .....	6
Status of Prior Audit Findings and Observations .....	15
Distribution List .....	16

## **Executive Summary**

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### **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 compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures.

Our audit scope covered the period March 16, 2012 through August 8, 2014, except as otherwise stated in the audit scope, objectives, and methodology section of the report. Compliance specific to state subsidies and reimbursements was determined for the 2010-11 and 2011-12 school years.

### **District Background**

The District encompasses approximately 34 square miles. According to 2010 federal census data, it serves a resident population of 5,428. According to District officials, the District provided basic educational services to 718 pupils through the employment of 65 teachers, 46 full-time and part-time support personnel, and 5 administrators during the 2011-12 school year. The District received \$7.5 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 matter unrelated to compliance that is reported as an observation.

#### **Observation: The District Should Monitor Key Financial Indicators to Try to Prevent Further Fiscal Challenges.**

During our audit of the District, we reviewed several financial indicators in an effort to assess the District's financial stability. Our review found that the District is potentially in a financially declining position (see page 6).

#### **Status of Prior Audit Findings and Observations.**

Our prior audit did not include any findings or observations.

## Audit Scope, Objectives, and Methodology

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### 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 16, 2012 through August 8, 2014.

Regarding state subsidies and reimbursements, our audit covered the 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:

- ü In areas where the District received transportation subsidies, was the District, and any contracted vendors, in compliance with applicable laws [24 P.S. § 25-2541] and procedures?

To address this objective:

- o The auditors reviewed a random selection of 7 of the 28 total District buses. For each bus in the sample, the auditors reviewed various data, including board approval of routes, manufacturer, serial number, year of

manufacture, and seating capacity as required under 24 P.S. § 25-2541.

- In addition, the auditors reconciled the transportation data the District submitted to PDE to the District's final formula allowance and/or contracted costs to ensure accuracy.

Ü Did the District ensure that bus drivers transporting District children at the time of the audit have the necessary license, physicals, training, background checks, and clearances as outlined in 24 P.S. § 1-111, 24 P.S. § 2070, 67 P.S. § 71.1, 22 *PA Code Chapter 8*, and 23 PA C.S. § 58-6354, and did they have written policies and procedures governing the hiring of new bus drivers?

To address this objective:

- The auditors initially selected 5 new drivers out of the 15 "new drivers" from the current school year and worked backwards to the last time the Bureau of School Audits audited the District and reviewed bus driver compliance. Auditors ensured that all of the new drivers not reviewed during the previous audit were selected for review and included both district-employed and contractor-employed drivers, as appropriate.
- The auditors also requested copies of the written policies and procedures governing the hiring of bus drivers to determine that these processes included requesting background checks and clearances.

Ü Were there any declining fund balances that may pose a risk to the District's fiscal viability?

- To address this objective, the auditors reviewed the District's annual financial reports, budget, independent auditor's reports, summary of child accounting, and general ledger for fiscal years July 1, 2005 through June 30, 2013.

ü Did the District take appropriate steps to ensure school safety?

To address this objective:

- The auditors reviewed a variety of documentation including safety plans, training schedules, anti-bullying policies, and after action reports to assess whether the District followed best practices in school safety and 24 P.S. Sect. 13-1302, 1302.1A, 13-1303.1, and 13-1303 A. Generally, the auditors evaluate the age of the plan, whether it is being practiced through training and whether the school has an after action process for trying to improve on the results of its training exercises.
- In addition, the auditors conducted on-site reviews at the two school buildings to assess whether they had implemented basic physical safety practices based on national best practices.

## 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 state laws, regulations, 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 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, and comparative financial information.

Our audit examined the following:

- Records pertaining to pupil transportation, bus driver qualifications, and financial stability.
- 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

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### Observation

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### The District Should Monitor Key Financial Indicators to Try to Prevent Further Fiscal Challenges

*Criteria relevant to the observation:*

The Pennsylvania School Boards Association in its Annual Overview of Fiscal Health for the 2009-10 school year provided the following information relevant to the following fiscal benchmarks:

- 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).

Best business practices and/or general financial statement analysis tools require the following:

- A school district should maintain a trend of stable or increasing fund balances.
- The trend of current ratios should be at least two to one or increasing. Anything less calls into question the school district's ability to meet its current obligations with existing resources.
- A quick asset ratio or trend of ratios approaching one or less indicates a declining ability to cover obligations with the most liquid assets.

During the current audit of the District, we reviewed several financial indicators in an effort to assess the District's financial stability. Our review found that the District is potentially in a financially declining position.

We reviewed 22 financial benchmarks based on best business practices established by several agencies, including the Pennsylvania Association of School Business Officials, the Colorado State Auditor, and the National Forum on Education Statistics. The following were among the general areas we evaluated: (1) the level of the general fund – fund balance (assigned and unassigned), (2) the amount of total debt service, (3) the current ratio (current assets ÷ current liabilities) of all governmental funds, and (4) the trend of changes in financial position for the general fund.

If the District's financial indicators continue to decline, the District could be in risk of being added to PDE's financial watch list.

Act 141 of 2012 permits PDE to place a school district with serious financial problems on a financial watch list. This designation gives the District access to additional technical assistance from PDE. Likewise, if a school district's financial condition deteriorates to the point that it has to request an advance on its annual basic education subsidy, PDE may declare it to be in financial recovery status. School districts in financial recovery status have a PDE appointed chief recovery officer whose responsibilities include oversight of the district and the development of a district-wide financial recovery plan

Our testing found the District scored negatively on the following benchmarks:

**Decreasing Operating Position:** During the period 2006 to 2013, the District over expended its revenues five times, thereby decreasing its operating position.

*Criteria relevant to the observation (continued):*

- A debt-to-asset ratio or trend of ratios increasing towards one to one or greater is an indication that the school district's liabilities are approaching the level of the district's assets. This indicates the district has a debt level that may be too great for the district to adequately function.
- The costs for a school district student attending a charter school is paid out of the sending district's operating funds. This results in a reduction of the funds available for use in providing educational services to the district's students that remained in the traditional public school. This scenario continues until the number of students attending charter schools is so large that the district can reduce costs by closing a school building and reduces the number of staff employed by the district.
- The trend of effective tax rates as compared to levied tax rates should be stable or increasing to ensure the district has sufficient tax revenues to maintain its educational services at an appropriate level.

Each year that the District's expenditures exceed its revenues, a deficit is incurred. This deficit results in a decrease to the District's fund balance and could lead to a negative fund balance, which could impact the District's ability to maintain its educational services and put the District at greater risk of being placed on the financial watch list or declared to be in financial recovery status.

The following chart documents the District's decreasing operating position:

<b>Revenues v. Expenditures</b> <i>(Revenues - Expenditures)</i>				
Year Ended	Total		Total	Excess/
<u>June 30</u>	<u>Revenues</u>	-	<u>Expenditures</u>	<u>(Deficit)</u>
2006	\$10,040,055		\$ 9,990,518	\$ 49,537
2007	\$10,742,939		\$10,519,349	\$223,590
2008	\$10,753,186		\$11,005,337	(\$252,151)
2009	\$11,023,997		\$11,195,168	(\$171,171)
2010	\$11,288,392		\$11,656,793	(\$368,401)
2011	\$11,507,884		\$11,671,382	(\$163,498)
2012	\$10,968,758		\$11,548,679	(\$579,921)
2013	\$11,574,639		\$11,304,456	\$270,183

The District's Superintendent stated that the multiple fiscal years of deficits, with the resulting decreasing fund balance, are a result of the District's reduced revenues and increased costs due to the following reasons:

- Basic education revenue is at the same level it was in 2008-09.
- Declining enrollment caused over staffing and under-utilization of District buildings and buses.
- Increased pension costs caused by the increasing contribution rate for all school districts in Pennsylvania.

**Decreasing Fund Balance:** During the period 2006 to 2013, the general fund-fund balance decreased. A decreasing fund balance indicates the District's expenditures are exceeding its revenues. This reduction of the fund balance is an indicator that the District's financial position is declining and could possibly send the District into financial recovery status. Without the generation of additional revenues or the reduction of expenditures, the fund balance will continue to decrease. The District must make a concerted effort towards preventing their fund balance from falling below zero and being declared in

financial recovery status which could require PDE intervention.

The following chart documents the District's decreasing fund balance:

<b>Fund Balance</b>	
<u>Year Ended June 30</u>	<u>Fund Balance</u>
2006	\$1,968,494
2007	\$2,119,394
2008	\$1,828,244
2009	\$1,072,013
2010	\$ 688,035
2011	\$ 873,548
2012	\$ 261,376
2013	\$ 492,367

**Decreasing General Fund Current Ratio:** For the period 2006 to 2013, the general fund current ratio (current assets ÷ current liabilities) was decreasing. A decreasing trend towards one-to-one or even lower indicates that the District's financial solvency is decreasing toward a point where the District may not be able to pay its current debts without an infusion of cash. Potential creditors use this ratio to measure a district's ability to pay its short-term debts. A declining fund balance may also prevent the District from obtaining any new debt, such as loans, or increase the interest rate on the debt it can obtain, thereby costing the District more money.

The following chart documents the District’s decreasing current ratio:

<b>Decreasing General Fund Current Ratio</b>			
<i>(Current Assets ÷ Current Liabilities)</i>			
Year Ended June 30	Current Assets	÷ Current Liabilities	= Current Ratio
2006	\$3,177,842	÷	2.63 to 1
2007	\$3,441,082	÷	2.60 to 1
2008	\$3,249,815	÷	2.29 to 1
2009	\$2,432,960	÷	1.79 to 1
2010	\$2,007,470	÷	1.52 to 1
2011	\$2,262,223	÷	1.63 to 1
2012	\$1,937,868	÷	1.16 to 1
2013	\$2,051,807	÷	1.69 to 1

The District’s Superintendent stated that the trend in current ratios is decreasing due to level to declining state appropriations over the period and the expenditure of bond proceeds for building improvements.

**Decreasing General Fund Quick Ratio:** For the period 2006 to 2013, the general fund quick ratio ((cash + investments) ÷ current liabilities) was decreasing. This ratio assesses an organization’s short-term solvency. As a result, a decreasing trend can be an indicator of the District’s inability to pay its current debts without the disposal of other current assets. As with the current ratio, potential creditors also use this ratio to measure a District’s ability to pay its short-term debts. Therefore, a declining or unstable general fund quick ratio could also make it more difficult for the District to obtain a loan or other debt instruments at a competitive interest rate.

The following chart documents the District’s decreasing quick ratio:

<b>Decreasing Quick Ratio</b>				
<u>((Cash + Investments) ÷ Current Liabilities)</u>				
<u>Year Ended June 30</u>	<u>Total Cash + Investments</u>	<u>÷</u>	<u>Current Liabilities</u>	<u>= Quick Ratio</u>
2006	\$1,869,725		\$1,209,348	1.55 to 1
2007	\$1,966,044		\$1,321,689	1.49 to 1
2008	\$2,292,427		\$1,421,570	1.61 to 1
2009	\$1,508,780		\$1,360,947	1.11 to 1
2010	\$ 714,758		\$1,319,435	0.54 to 1
2011	\$1,009,886		\$1,388,675	0.73 to 1
2012	\$ 722,435		\$1,676,492	0.43 to 1
2013	\$ 852,685		\$1,210,845	0.70 to 1

The District’s Superintendent stated that the overall decrease in the quick ratios is due to level to declining state appropriations over the trend period.

**Increasing Debt-to-Asset Ratio:** For the period 2006 to 2013, the general fund debt-to-asset ratio (current liabilities ÷ current assets) is increasing. An increasing trend towards one-to-one or more is an indication that the District may not be able to pay its current liabilities with current assets on hand. This trend could require the District to liquidate non-current assets or wait for an inflow of revenues. As a result, the District might have to increase the time it holds invoices prior to making payment. This action could impede the District’s ability to obtain a loan or other debt instrument. It could also result in a higher cost for any new debt that is obtained.

The following chart documents the District’s increasing debt-to-asset ratio:

<b>Increasing Debt-to-Asset Ratio</b>					
<b>(Current Liabilities ÷ Current Assets)</b>					
<u>Year Ended June 30</u>	<u>Current Liabilities</u>	÷	<u>Current Assets</u>	=	<u>Current Ratio</u>
2006	\$1,209,348		\$3,177,842		0.38 to 1
2007	\$1,321,689		\$3,441,082		0.38 to 1
2008	\$1,421,570		\$3,249,815		0.44 to 1
2009	\$1,360,947		\$2,432,960		0.56 to 1
2010	\$1,319,435		\$2,007,470		0.66 to 1
2011	\$1,388,675		\$2,262,223		0.61 to 1
2012	\$1,676,492		\$1,937,868		0.87 to 1
2013	\$1,210,845		\$2,051,807		0.59 to 1

The District’s Superintendent stated that the debt-to-asset ratio is increasing because the District has taken on additional debt for capital improvement, while state appropriations have declined.

**Increase in Charter School Students:** During the period 2006 to 2012, the number of District students attending charter schools has increased by over 300 percent. This enrollment growth has simultaneously increased the District’s charter costs. Further, the charter school costs as a percentage of revenues increased. Consequently, the amount of District funds available for in-house educational services has been reduced. This could cause the District to reduce services to the students that remained in the District’s schools. Specifically, unless the number of students attending charter schools is significant enough to reduce the number of staff or the number of school buildings, the District cannot reduce its operating costs, even though it is educating fewer students due to its students transferring to charter schools.

The following charts document the District's increasing charter school costs over the period:

<b>Charter School Membership Growth</b>			
<i>(As a Percentage of Total District Membership)</i>			
Year Ended June 30	Charter School ADM	÷	Total District ADM = Charter School/District ADM
2006	14.216		912.145 = 1.56%
2007	19.048		856.294 = 2.22%
2008	34.929		851.180 = 4.10%
2009	40.393		837.067 = 4.83%
2010	40.110		862.741 = 4.65%
2011	45.058		841.039 = 5.36%
2012	50.351		801.999 = 6.28%

<b>Charter School Cost Growth</b>			
<i>(As a Percentage of Total District Expenditures)</i>			
Year Ended June 30	Tuition Paid to Charter Schools	÷	Total District Expenditures = Charter Costs/Total Costs
2006	\$126,419		\$ 9,990,518 = 1.27%
2007	\$205,926		\$10,519,349 = 1.96%
2008	\$365,061		\$11,005,337 = 3.32%
2009	\$450,411		\$ 11,195,168 = 4.02%
2010	\$460,496		\$11,656,793 = 3.95%
2011	\$529,842		\$11,671,382 = 4.54%
2012	\$538,719		\$11,548,679 = 4.66%
2013	\$455,203		\$11,304,456 = 4.03%

The District's Superintendent stated the increase in charter school students and charter school costs is caused by the following.

- The opening of new charter schools, including a performing arts charter school in the vicinity of the District.
- 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.

- Declining enrollment which increases the percentage of students attending charter schools.

**Decreasing Effective Tax Rates:** For the trend period 2006 to 2013, the trend of effective tax rates (actual property tax revenue ÷ assessed taxable property value) compared to the levied tax rates is decreasing. This indicates that the rate of tax collections is decreasing even though the levied tax rate is increasing or staying the same. This is an indicator of the relative fiscal health of the taxpayers and the support available to the District. As a result of the decreasing effective tax rates, the District cannot expect an increase in property taxes to provide increased revenues to the District. Therefore, the District’s ability to generate additional resources is very slight or dependent on additional funding from the state.

The following chart documents the decreasing effective tax rate as compared to levied tax rate over the trend period:

<b>Trend: Decreasing Effective Millage Rate</b>					
(As a Percentage of the Actual Assessed Millage Rates)					
<u>Year Ended June 30</u>	<u>Effective Millage Rate</u>	÷	<u>Assessed Millage Rate</u>	=	<u>Tax Collection Percentage</u>
2006	\$33.83		\$41.00		82.51%
2007	\$35.23		\$41.00		85.93%
2008	\$30.48		\$41.00		74.34%
2009	\$38.07		\$41.00		92.85%
2010	\$37.38		\$41.00		91.17%
2011	\$32.68		\$42.50		76.89%
2012	\$33.68		\$43.30		77.78%
2013	\$36.84		\$46.85		78.63%

The business manager stated that there is a fairly regular group of taxpayers that pay their taxes late and after they become delinquent. These taxpayers, in addition to those that, for one reason or another, cannot pay their taxes timely, or at all, caused the tax collection rate to decline.



## **Recommendations**

The *Western Beaver County School District* should:

1. Provide the Board of School Directors standard monthly updates on key financial benchmarks so that policy changes can be made before the District's financial condition worsens significantly.
2. Monitor and maintain budgetary control over expenditures so that expenditures do not exceed revenues.
3. Explore potential options for increasing revenues and/or decreasing expenditures.
4. Consider the current and potential future economic conditions prior to taking on additional debt for capital projects. Additionally, analyze the District's ability to generate the necessary revenues to pay the future debt service costs.
5. Conduct a survey of parents sending their children to a charter school to determine why the District is losing students to charter schools.
6. Take a more aggressive approach to collecting property taxes before they become delinquent and for collecting delinquent property taxes.

## **Management Response**

Management stated the following:

“The District has, over the course the last 5 years, restructured its business plan to reduce staff, maintain current programs, and started an on-line academy. This restructuring has resulted in 2012-13 and 2013-14 financial position to be positive. Our latest Financial Report indicated a fund balance of \$621,000.”

## **Auditor Conclusion**

We commend the District for making improvements in their financial condition recently and recommend that they continue to monitor and try to improve the financial condition of the District.

## **Status of Prior Audit Findings and Observations**

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**O**ur prior audit of the District did not include any findings or observations.

## **Distribution List**

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

The Honorable Tom W. Wolf  
Governor  
Commonwealth of Pennsylvania  
Harrisburg, PA 17120

The Honorable Pedro A. Rivera  
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