



ALIQUIPPA SCHOOL DISTRICT
BEAVER COUNTY, PENNSYLVANIA
PERFORMANCE AUDIT REPORT

NOVEMBER 2013

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. Edward Palombo, Board President
Aliquippa School District
100 Harding Avenue
Aliquippa, Pennsylvania 15001

Dear Governor Corbett and Mr. Palombo:

We conducted a performance audit of the Aliquippa 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 April 23, 2010 through May 18, 2012, except as otherwise indicated in the report. Additionally, compliance specific to state subsidies and reimbursements was determined for the school years ended June 30, 2010 and June 30, 2009. Our audit was conducted pursuant to Section 403 of The Fiscal Code, 72 P.S. § 403, and in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States.

Our audit found that the District complied, in all significant respects, with relevant requirements, except as detailed in the finding noted in this report. A summary of the results is presented in the Executive Summary section of the audit report.

Our audit finding 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

November 21, 2013

cc: **ALIQUIPPA 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 Aliquippa School District (District) in Beaver 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 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 April 23, 2010 through May 18, 2012, except as otherwise indicated in the audit scope, objectives, and methodology section of the report. Compliance specific to state subsidies and reimbursements was determined for the 2009-10 and 2008-09 school years.

District Background

The District encompasses approximately four (4) square miles. According to 2010 federal census data, it serves a resident population of 9,438. According to District officials, the District provided basic educational services to 1,171 pupils through the employment of 115 teachers, 87 full-time and part-time support personnel, and nine (9) administrators during the 2009-10 school year. Lastly, the District received \$12.1 million in state funding in the 2009-10 school year.

In July 2012, the General Assembly passed Act 141 of 2012, which required the Pennsylvania Department of Education (PDE) to develop and implement an early warning system for identifying financially declining school districts. PDE places those districts detected through the early warning system in Financial Watch Status, which permits them to receive additional technical assistance to improve their financial condition (see Finding on page 6).

Under Act 141 of 2012, PDE may also declare school districts to be in financial recovery status. This designation occurs when a school district's financial condition deteriorates to the point that it requires multiple advances on its annual state basic education subsidy and has numerous negative financial indicators. PDE can find school districts to be in moderate or severe financial recovery status. Such designations result in PDE appointing a chief recovery officer whose responsibilities include oversight of the district and the development of a district-wide financial recovery plan.

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, except for one (1) compliance related matter reported as a finding.

Finding: The District Is Facing Serious Financial Challenges, including a \$928,556 General Fund Deficit. Our audit of the Aliquippa School District's (District) annual financial reports, independent auditor's reports, and general fund budgets for fiscal years ended June 30, 2012, 2011, 2010, 2009, 2008, and 2007 found that the District has a deteriorating general fund balance, with a \$928,556 deficit for the fiscal year ended June 30, 2012. This decline was due primarily to its failure to control expenditures in accordance with its general fund budgets. In addition, we found that the Pennsylvania Department of Education has placed the District in Financial Watch Status because of its poor fund balance ratio and several other negative financial indicators (see page 6).

Status of Prior Audit Findings and Observations. With regard to the status of our prior audit recommendations to the Aliquippa School District's (District), released on December 13, 2010, we found that the District had taken appropriate corrective action in implementing our recommendations pertaining to a certification deficiency (see page 12).

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 April 23, 2010 through May 18, 2012, except for the following:

- Verification of professional employee certification, which was performed for the period April 1, 2010 through April 30, 2012.
- Review of the District's annual financial reports, independent auditor's reports, and general fund budgets, which covered fiscal years 2006-07 through 2011-12.

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

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

Objectives

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?

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.

- ✓ 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?
- ✓ 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?
- ✓ Were there any declining fund balances that may pose a risk to the District's fiscal viability?
- ✓ Did the District pursue a contract buy-out with an administrator and if so, what was the total cost of the buy-out, what were the reasons for the termination/settlement, and did the current employment contract(s) contain adequate termination provisions?
- ✓ Did the District take appropriate steps to ensure school safety?
- ✓ Did the District have a properly executed and updated Memorandum of Understanding with local law enforcement?
- ✓ Were 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 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

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.

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.

Lastly, to determine the status of our audit recommendations made in a prior audit report released on December 13, 2010, we performed additional audit procedures targeting the previously reported matters.

Findings and Observations

Finding

The District Is Facing Serious Financial Challenges, including a \$928,556 General Fund Deficit

Criteria relevant to the finding:

Section 609 of the Public School Code (PSC) provides, in part:

“No work shall be hired to be done, no materials purchased, and no contracts made by any board of the school directors which will cause the sums appropriated to specific purposes in the budget to be exceeded.”

PSC Section 6-611-A provides:

“1) The department shall develop and implement an early warning system under which the department shall:

- (i) Compile financial data and maintain accurate and current information and data on the financial conditions of school districts. Each school district shall provide its financial data and information to the department within 15 days of a request by the department.
- (ii) Regularly analyze and assess school district budget reports, data and other information directly related to the financial conditions of school districts.
- (iv) Notify any school district identified for financial watch status.
- (v) Offer technical assistance to school districts in financial watch status to correct minor financial problems and to avoid a declaration of financial recovery status under Section 621-A.”

Our audit of the Aliquippa School District’s (District) annual financial reports (AFR), independent auditor’s reports (IAR), and general fund budgets for fiscal years ended June 30, 2012, 2011, 2010, 2009, 2008, and 2007 found that the District has a deteriorating general fund balance, with a \$928,556 deficit for the fiscal year ended June 30, 2012. This decline was due primarily to its failure to control expenditures in accordance with its general fund budgets.

In addition, we found that the Pennsylvania Department of Education (PDE) has placed the District in Financial Watch Status because of its poor fund balance ratio and several other negative financial indicators. This designation gives the District access to additional technical assistance from PDE, aimed at improving its fiscal condition. If the District’s financial position does not improve it could be placed 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.

As shown in the following chart, the District has had a general fund deficit for the last two fiscal years:

Trend: Declining General Fund Balance				
Fiscal Year End	Revenue	Expenditures	Difference in Expenditures/Revenues	General Fund Surplus/Deficit
June 30 2007	-	-	-	\$1,908,314
2008	\$21,396,155	\$22,055,812	\$(659,657)	1,248,657
2009	20,317,688	21,229,931	(912,243)	336,414
2010	21,301,254	20,772,786	528,468	864,882
2011	19,842,948	20,854,998	(1,012,050)	*(139,875)
2012	19,045,496	19,834,177	(788,681)	(928,556)

*In 2010, the independent auditors made an error by not including the athletic funds in the general fund balance for the 2010 IAR. This resulted in an understatement of \$7,293 to the general fund.

The most significant factor impacting the deterioration of the District’s general fund balance was its failure to control expenditures in accordance with its general fund budgets. The following table details actual expenditures in excess of budgeted expenditures:

Expenditures: Budget vs. Actual			
<u>Fiscal Year</u> <u>Ended June 30</u>	<u>Budgeted</u> <u>Expenditures</u>	<u>Actual</u> <u>Expenditures</u>	<i>(Over)/Under</i> <i>Budgeted</i>
2008	\$20,377,783	\$22,055,812	<i>\$(1,678,029)</i>
2009	21,662,995	21,229,931	<i>433,064</i>
2010	21,732,486	20,772,786	<i>959,700</i>
2011	20,056,827	20,854,998	<i>(798,171)</i>
2012	19,696,655	19,834,177	<i>(137,522)</i>

The District’s largest variance in actual to budgeted expenditures occurred in its costs for capital outlay, regular programs, special programs, and other instructional programs.

The District’s inability to control its spending within the confines of its budget violates Section 609 of the Public School Code. In addition, these over expenditures indicate that the District’s budgets are based on unstable assumptions and are poorly monitored. For example, the District’s administration and its Board of School Directors (Board) should adopt budgets that estimate beginning fund balances based on historical indicators and on realistic expectations for future available funding during the budgetary period. Furthermore, they should use monthly budget status reports to scrutinize proposed expenditures for the current operations and limit them to revenues received and the amount appropriated.

As a result of the District’s general fund deficits and several other financial factors, on March 15, 2013, PDE placed the District on the Commonwealth’s financial watch list (see report background for additional information). As previously discussed, the watch list was created by Act 141 of 2012, as part of an “early warning system” for identifying school districts that were struggling to maintain fiscal stability. By detecting these districts when they are initially beginning to deteriorate, the General Assembly hoped to provide them with assistance that would prevent them from experiencing severe fiscal problems, which could cause them to fall into financial recovery status.

As part of this effort, PDE offers all districts on the financial watch list technical assistance to help them improve. This work involves PDE employees and consultants evaluating the districts' policies and procedures, assessing their programs, providing best practice recommendations, and serving as liaisons with PDE. However, these districts are not eligible for any additional funding under the financial watch status designation.

According to a letter from PDE dated March 15, 2013, the following financial indicators led to the District's financial watch list designation:

Financial Indicators Leading to Financial Watch Status	
<i>Indicator</i>	<i>District Performance</i>
Fund Balance Ratio	-4.4% fund balance ratio (2011-12 AFR).
Debt Ratio	11.53% debt ratio (3-year average 2009-10, 2010-11, and 2011-12).
Basic Education Funding Advance	District was provided an advance of \$1,000,000 in July 2012 to enable the District to make payroll; advance was recovered in August 2012.
Market Value/Personal Income Aid Ratio	For 2012-13, it was .7727.
Aliquippa City's Financial Designation	The City was declared financially distressed pursuant to Act 47 of 1987.
Ability to Acquire Tax Anticipation Note	District was unable to acquire a tax anticipation note during the summer of 2012, which necessitated the request for the Basic Education Funding advance in 2012.
Outstanding Debt	District's outstanding debt was 228% of expenditures at the end of the 2011-12 fiscal year.
Delinquent Tax Rate	District had a high delinquent real estate tax rate of 23.3% in the 2011-12 fiscal year.
Cash Shortfall Projection	District projecting a \$725,000 cash shortfall in June 2013; anticipates having cash flow issues and having difficulty meeting payroll obligations during the 2012-13 fiscal year.

In addition, the District is facing growing financial pressure as a result of an increase in tuition being paid to charter schools. While the cost of tuition is rising—nearly 34 percent over four years—the issue is compounded by the fact that, since 2011, the Commonwealth has not funded the school district reimbursement for charter school tuition costs. If this reimbursement were still in place, the District would have received at least \$172,000 in additional revenue in 2009-10.

Trend: Growth in Charter Costs		
<u>School Year</u>	<u>Tuition Paid to Charters</u>	<u>State Reimbursement</u>
2008-09	\$ 770,825	\$181,401
2009-10	709,558	172,754
2010-11	1,013,476	n/a
2011-12	1,031,007	n/a

In summary, the District is facing severe financial challenges. As a result, it may be forced to eliminate certain educational services and decrease its professional staff in order to account for its reduced revenues. The likelihood that the District will have to curtail its educational offerings is increased by the fact that it has a poor local tax base, as evidenced by its high rate of delinquent tax payments. If the District’s financial situation continues to degrade, it is possible that PDE may declare it to be in financial recovery status.

Recommendations

The *Aliquippa School District* should:

1. Monitor and maintain budgetary control over expenditures in compliance with Section 609 of the Public School Code.
2. Provide the Board standard monthly updates on key financial benchmarks so that policy changes can be made before the District’s financial condition worsens.
3. Use monthly budget status reports to scrutinize proposed expenditures for the current operations and limit them to revenues received and the amount appropriated.

4. Adopt budgets estimating beginning fund balances based on historical indicators and realistic expectations of the amount that will actually be available for the budgetary period.
5. Provide for systematic reduction of the general fund deficit.
6. Conduct a survey with parents sending their children to a charter school to determine the reason why the District is losing students.
7. Monitor the costs to the District related to charter schools on a continuous basis.
8. Open a dialogue with the community to keep stakeholders informed of the financial status and health of the school district.
9. Accept technical assistance offered by PDE to help the District with its financial challenges.

Management Response

Management stated the following:

“Management is working to address the General Fund deficit by reviewing all operations of the school district for cost savings. Several professional and support staff were furloughed beginning in the 2011-12 school year. Also, Business Office costs are currently being shared with another school district. Management will continue to examine all ways to curtail costs.”

Auditor Conclusion

We commend the District for making an effort to identify potential savings and for using innovative approaches to reduce its costs, such as sharing its business office function with another school district. The severity of the District’s financial condition will require it to work collaboratively with PDE to find substantial opportunities to reduce its expenditures. In doing so, the District should develop more realistic budgets and then adhere to them so that its actual expenditures do not exceed its budgeted expenditures. Moreover, the District’s administration and its Board

should continue to monitor the negative financial benchmarks outlined in PDE's financial watch list designation. Without significant improvement, it is possible that the District will face further state intervention through financial recovery status designation.

Status of Prior Audit Findings and Observations

Our prior audit of the Aliquippa School District (District) released on December 13, 2010, resulted in one reported finding. The finding pertained to certification deficiency. As part of our current audit, we determined the status of corrective action taken by the District to implement our prior recommendations. We performed audit procedures and interviewed District personnel regarding the prior finding. As shown below, we found that the District did implement recommendations related to certification deficiency.

Auditor General Performance Audit Report Released on December 13, 2010

Finding: **Certification Deficiency**

Finding Summary: Our prior audit found one teacher was assigned to a position without proper certification. As a result, the District was subject to a subsidy forfeiture of \$1,840.

Recommendations: Our audit finding recommended that the District:

1. Review the assignments of all employees and reassign positions, if necessary, to comply with certification requirements established by the Pennsylvania Department of Education (PDE).
2. Hire only individuals holding valid certificates for the subjects or positions to which they are assigned.

We also recommended that PDE:

3. Adjust the District's allocations to recover the subsidy forfeitures of \$1,840.

Current Status: During our current audit, we found that the District did implement the recommendations. The teacher cited during our prior audit obtained their proper certification.

On June 1, 2011, PDE withheld \$1,840 from the District's allocations.

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
Commonwealth of Pennsylvania
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The Honorable Carolyn Dumaesq
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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.