

ANNVILLE-CLEONA SCHOOL DISTRICT
LEBANON COUNTY, PENNSYLVANIA
PERFORMANCE AUDIT REPORT

JANUARY 2012

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

Mr. Thomas P. Tshudy, Board President
Annville-Cleona School District
500 South White Oak Street
Annville, Pennsylvania 17003

Dear Governor Corbett and Mr. Tshudy:

We conducted a performance audit of the Annville-Cleona School District (ACSD) to determine its compliance with applicable state laws, contracts, grant requirements, and administrative procedures. Our audit covered the period April 11, 2008 through June 18, 2010, except as otherwise indicated in the report. Additionally, compliance specific to state subsidy and reimbursements was determined for the school years ended June 30, 2008 and June 30, 2007. Our audit was conducted pursuant to 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 ACSD complied, in all significant respects, with applicable state laws, contracts, grant requirements, and administrative procedures, except as detailed in one finding noted in this report. In addition, we identified two matters unrelated to compliance that are reported as observations. A summary of these results is presented in the Executive Summary section of the audit report.

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

Sincerely,

/s/

JACK WAGNER
Auditor General

January 23, 2012

cc: **ANNVILLE-CLEONA SCHOOL DISTRICT** Board Members

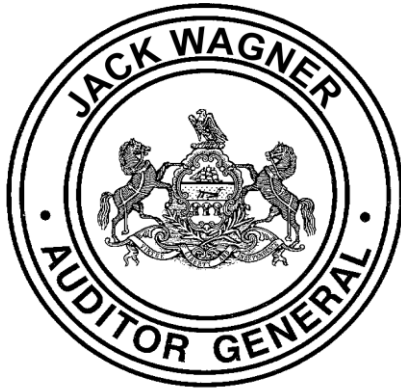


Table of Contents

| | Page |
|---|------|
| Executive Summary | 1 |
| Audit Scope, Objectives, and Methodology | 3 |
| Findings and Observations | 5 |
| Finding – General Fund Deficit of \$89,748 as of June 30, 2009 | 6 |
| Observation No. 1 – Continued Unmonitored Vendor System Access and Logical Access Control Weaknesses | 9 |
| Observation No. 2 – Memorandums of Understanding Not Updated Timely | 12 |
| Status of Prior Audit Findings and Observations | 15 |
| Distribution List | 17 |



Executive Summary

Audit Work

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

Our audit scope covered the period April 11, 2008 through June 18, 2010, except as otherwise indicated in the audit scope, objectives, and methodology section of the report. Compliance specific to state subsidy and reimbursements was determined for school years 2007-08 and 2006-07.

District Background

The ACSD encompasses approximately 40 square miles. According to 2009 local census data, it serves a resident population of 11,319. According to District officials, in school year 2007-08 the ACSD provided basic educational services to 1,750 pupils through the employment of 122 teachers, 55 full-time and part-time support personnel, and 12 administrators. Lastly, the ACSD received more than \$6.9 million in state funding in school year 2007-08.

Audit Conclusion and Results

Our audit found that the ACSD complied, in all significant respects, with applicable state laws, contracts, grant requirements, and administrative procedures; however, as noted below, we identified one compliance-related matter reported as a finding and two matters unrelated to compliance that are reported as observations.

Finding: General Fund Deficit of \$89,748 as of June 30, 2009. Our review of the ACSD's annual financial reports, local auditor's report and general fund budgets for the fiscal years ending, June 30, 2009, 2008 and 2007 found that the ACSD's prior general fund balance surplus of \$2,399,302 as of June 30, 2006, decreased to a deficit fund balance of \$89,748 as of June 30, 2009 (see page 6).

Observation No. 1: Continued Unmonitored Vendor System Access and Logical Access Control Weaknesses. We continued to note that ACSD personnel should improve controls over remote access to its computers. In particular, controls should be strengthened over vendor access to the student accounting applications and the ACSD has certain weaknesses in logical access controls (see page 9).

Observation No. 2: Memorandums of Understanding Not Updated Timely. We noted that ACSD personnel should obtain and update its Memorandum of Understanding (MOU) with the Pennsylvania State Police in a timely manner and adopt board policy to require that the MOU be updated every two years (see page 13).

Status of Prior Audit Findings and Observations.

With regard to the status of our prior audit recommendations to the ACSD from an audit we conducted of the 2005-06, 2004-05, 2003-04 and 2002-03 school years, we found that the servers containing the ACSD membership

information changed locations from Lancaster-Lebanon Intermediate Unit #13 to Carbon-Lehigh Intermediate Unit #21. Therefore a complete review was performed and we found the ACSD continued to have access and control weaknesses (see page 15).

Audit Scope, Objectives, and Methodology

Scope

What is a school performance audit?

School performance audits allow the 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 PA Department of Education, and other concerned entities.

Our audit, conducted under authority of 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 11, 2008 through June 18, 2010.

Regarding state subsidy and reimbursements, our audit covered school years 2007-08 and 2006-07.

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 Department of Education 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 ACSD's compliance with applicable state laws, 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:

- ✓ Did the District use an outside vendor to maintain its membership data and if so, are there internal controls in place related to vendor access?
- ✓ Is the District's pupil transportation department, including any contracted vendors, in compliance with applicable state laws and procedures?
- ✓ Are there any declining fund balances which may impose risk to the fiscal viability of the District?

- ✓ Did the District pursue a contract buyout with an administrator and if so, what was the total cost of the buy-out, reasons for the termination/settlement, and do the current employment contract(s) contain adequate termination provisions?
- ✓ Were there any other areas of concern reported by local auditors, citizens, or other interested parties which warrant further attention during our audit?
- ✓ Is the District taking appropriate steps to ensure school safety?
- ✓ Did the District take appropriate corrective action to address recommendations made in our prior audits?

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 applicable laws, contracts, grant requirements and administrative procedures.

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

ACSD management is responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the District is in compliance with applicable laws, contracts, grant requirements, and administrative procedures. Within the context of our audit objectives, we obtained an understanding of internal controls and assessed whether those controls were properly designed and implemented.

Any significant deficiencies found during the audit 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/reimbursement, pupil membership, 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.

Additionally, we interviewed selected administrators and support personnel associated with ACSD operations.

Lastly, to determine the status of our audit recommendations made in a prior audit report released on January 22, 2009, we reviewed the ACSD's corrective actions taken. We then performed additional audit procedures targeting the previously reported matters.

Findings and Observations

Finding

General Fund Deficit of \$89,748 as of June 30, 2009

Public School Code section relevant to the finding:

Section 609 provides, in part:

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

Our audit of the District's annual financial reports, local auditor's report and general fund budgets for fiscal years ended June 30, 2009, 2008 and 2007 found that, although as of June 30, 2006 the District had maintained a \$2,399,302 surplus in its general fund, its deficit spending for the four fiscal years after that date resulted in a deficit fund balance. As of June 30, 2009 the District's general fund had a balance of negative \$89,748.

We found that expenditures exceeded revenues in the 2007-08 and 2008-09 school years, resulting in the depletion of the District's general fund surplus.

| <u>Fiscal Year</u> | <u>Revenues</u> | <u>Expenditures</u> | <u>Expenditures (Over)/ Under Revenue</u> | <u>Refunds/ Transfers In/Out</u> | <u>General Fund Surplus/(Deficit)</u> |
|---------------------------|-----------------|---------------------|---|--|---|
| <u>Ending June 30</u> | | | | | |
| 2006 | - | - | - | - | \$2,399,302 |
| 2007 | \$17,568,050 | \$17,350,903 | \$ 217,147 | (\$379,520) | 2,236,929 |
| 2008 | 18,068,602 | 19,035,974 | (967,372) | (420,198) | 849,359 |
| 2009 | 17,971,045 | 18,756,112 | (785,067) | (154,040) | (89,748) |

According to the District management, they were forced into general fund deficit spending because it failed to fully budget for a 2008 teacher contract settlement, which included a \$650,000 retroactive payment. This payment contributed to the large decrease in the 2007-08 school year. In addition, District management indicated that they failed to properly adjust their budgeting to account for revenue decreases in areas that are sensitive including earned income, real estate, transfer tax and investment earning. The District's failure to make these revisions also contributed to the annual deficits.

On November 19, 2009, the school board approved a transfer of \$500,000 from the Capital Projects Fund to the General Fund to pay interest on the 2005 bonds. Subsequent to our audit completion date, the District ended the 2009-10 school year with a general fund surplus of \$337,504. The surplus was a result of an increase in real estate taxes and lower than projected expenditures.

While we are pleased that the District is now in the black, we continue to have concerns about its overall financial security due to the continued state and nationwide economic downturns that impact a number of the District's revenue streams, such as real estate.

Recommendations

The *Annville-Cleona School District* should:

1. Utilize monthly budget status reports to scrutinize proposed expenditures for current operations and limit expenditures to revenues available and the amounts appropriated to avoid future general fund deficits.
2. Prepare realistic budgets based on historical data and verifiable revenue projections.
3. Budget conservatively due to continued uncertainty surrounding both the Pennsylvania and national economics.

Response of Management

Management stated the following:

Due to lower than anticipated revenues from earned income tax, real estate transfer tax and earnings on investments, the school district's general fund balance for year ended June 30, 2009 was a negative \$89,748. On November 19, 2009, the school board approved a transfer of \$500,000 from the Capital Project Fund to the General Fund to make up for the negative fund balance and address decreases in state revenue that resulted from the late passage of the state's budget. These transferred funds will be used to pay interest on outstanding debt.

In addition, the school board voted [on] April 13, 2010 to close the North Annville Elementary School, due to continued decline in student enrollment. The school district anticipates a yearly savings of approximately \$150,000, with the closure of this building. Also, the school district continually evaluates the need to replace employees as positions become open through either retirement or resignation. For the 2010-11 school year, it is anticipated that three full-time professional positions will be eliminated.

With the one time transfer of funds, the anticipated closure of one of its school buildings and reductions in staff, the Annville-Cleona School District projects that a positive fund balance will be realized at the end of the 2009-10 school year.

Observation No. 1

Continued Unmonitored Vendor System Access and Logical Access Control Weaknesses

What is logical access control?

“Logical access” is the ability to access computers and data via remote outside connections.

“Logical access control” refers to Internal control procedures used for identification, authorization, and authentication to access the computer systems.

The Annville-Cleona School District (ACSD) continues to use software purchased from an outside vendor, through the Carbon-Lehigh Intermediate Unit # 21 (CLIU) for its critical student accounting applications (membership and attendance). The ACSD’s entire computer system, including all its data and the vendor’s software are maintained on the CLIU’s servers physically located at the CLIU. The District changed vendors from Lancaster-Lebanon Intermediate Unit #13 (LLIU) in our prior audit to CLIU. The District has remote access into CLIU’s network servers. CLIU also provides the District with system maintenance and support.

During our prior audit, we found that the ACSD had two weaknesses dealing with the LLIU access into the District’s system. Based on our current year audit procedures, we determined that a risk still exists that the vendor could make unauthorized changes to the ACSD’s data, that might occur and not be detected. However, since the ACSD still has manual compensating controls in place to verify the integrity of the membership and attendance information in its database, that risk is mitigated.

Reliance on manual compensating controls becomes increasingly problematic if the District would ever experience personnel and/or procedure changes that could reduce the effectiveness of the manual controls. Continued unmonitored vendor system access and logical access control weaknesses could lead to unauthorized changes to the District’s membership information and result in the District not receiving the funds to which it was entitled from the state.

During our review, we found the District had the following weaknesses over vendor access to the District’s system:

1. The District’s Acceptable Use Policy does not include provisions for authentication (password security and syntax requirements).

2. The District does not maintain proper documentation to evidence that terminated employees were removed from the system in a timely manner.
3. The District has certain weaknesses in logical access controls. We noted that the District's system parameter settings do not require all users, including the vendor, to change their passwords every 30 days; to use passwords that are a minimum length of eight characters and include alpha, numeric and special characters; to maintain a password history (i.e., approximately ten passwords); log users off the system after a period of inactivity (i.e., 60 minutes maximum).
4. The CLIU has unlimited access (24 hours a day/7 days a week) into the District's system.

Recommendations

The *Annville-Cleona School District* should:

1. Ensure that the Acceptable Use Policy includes provisions for authentication (password security and syntax requirements).
2. Maintain documentation to evidence that terminated employees are properly removed from the system in a timely manner. The information technology (IT) department should verify to administration when all changes have been completed.
3. Implement a security policy and system parameter settings to require all users, including the vendor, to change their passwords on a regular basis (i.e., every 30 days). Passwords should be a minimum length of eight characters and include alpha, numeric and special characters. Also, the District should maintain a password history that will prevent the use of a repetitive password (i.e., last ten passwords). The District should also log users off the system after a shorter period of inactivity (i.e., 60 minutes maximum) than the current 120 minute period.
4. Only allow access to their system when the CLIU needs access to make pre-approved changes/updates or requested assistance. This access should be removed when the CLIU has completed its work. This

procedure would also enable the monitoring of CLIU changes.

Management Response

Management stated the following:

- 1. Response:** Student access to the school's network is governed by a username and password on all district owned electronic devices. A time and date stamped log of that access is kept. Likewise a student cannot access network resources without a username, password, and 13 digit WPA-2 authentication key. Teachers and other staff are not required to use a username and password challenge to use network resources; however, they are still required to have the 13 digit WPA-2 encryption key embedded in their network settings by the IT staff or its designates.
- 2. Response:** When an employee is terminated for any reason their status in [software] is immediately set to inactive. At that moment they can no longer access student information or maintain classroom grades. This is performed after school board action which officially terminates employment.
- 3. Response:** **In a district our size the cost to implement such a rigorous system would be in excess of any benefit derived. We do instruct students and staff every fall in the creation of strong passwords. We describe in detail the process to change their [software] password and encourage them to do so periodically.**

We will reset the automatic log out to 60 minutes of inactivity.

We do not have the ability to store old passwords and prevent their reuse. Once again the software and staffing costs associated with such solutions would be beyond our means to implement.

- 4. Response:** [CLIU] have signed an AUP and we have a valid 5 year contract with them to be our student information system provider. The contract spells out their rights and responsibilities. Many maintenance activities take place after school hours, over holiday breaks, and during the weekends. The vendor has the

need to have access 24/7/365 in order to keep our system operating efficiently.

All changes made by the vendor are time and date stamped in logs and an E-mail is sent from the vendor documenting the changes.

Auditor Conclusion

While we can appreciate their concerns regarding the cost of certain changes, best practices indicate that these procedures are important to maintaining the security of the District's data. Therefore, we continue to recommend that the District take action to modify its current practices, whenever it is financially feasible. We reevaluate the District's progress during our next audit.

Observation No. 2

Public School Code section and Criteria relevant to the observation:

Section 13-1303-A(c) requires:

All school entities shall develop a memorandum of understanding with local law enforcement that sets forth procedures to be followed when an incident involving an act of violence or possession of a weapon by any person occurs on school property. Law enforcement protocols shall be developed in cooperation with local law enforcement and the Pennsylvania State Police.

Additionally, the Basic Education Circular, issued by the Department of Education entitled Safe Schools and Possession of Weapons, contains a sample MOU to be used by school entities.

Section VI, General Provisions, item (B) of this sample states:

This Memorandum may be amended, expanded or modified at any time upon the written consent of the parties, but in any event must be reviewed and re-executed within two years of the date of its original execution and every two years thereafter. (Emphasis added).

Recommendations

Memorandums of Understanding Not Updated Timely

Our audit of the ACSD's records found that the current Memorandums of Understanding (MOU) with the Annville Township, North Annville Township, South Annville Township and Cleona Borough police departments had not been updated since the 2007-08 school year.

The failure to update MOUs with all local law enforcement agencies could result in a lack of cooperation, direction, and guidance between District employees and law enforcement agencies if an incident occurs on school property, at any school-sponsored activity, or any public conveyance providing transportation to or from a school-sponsored activity. This internal control weakness could have an impact in law enforcement notification and response, and ultimately the resolution of a problem situation.

District administrative personnel stated that they had submitted MOUs to the local law enforcement agencies in May 2010. As of our fieldwork completion date of June 18, 2010, the District has not received the MOUs from the police departments.

The *Annville-Cleona School District* should:

1. In consultation with the solicitor, continue to review, update and re-execute the current MOUs between the District and local law enforcement.
2. Adopt a policy requiring the administration to review, update and re-execute the MOUs every two years.

3. Contact the respective law enforcement agencies to persuade them that it is imperative that an MOU is signed and provided to the District immediately.

Management Response

Management stated the following:

Current Memorandums of Understanding were in place during the 2007-08 school year. Before the end of the 2009-10 audit, the Memorandums of Understanding were updated, as required.

Auditor Conclusion

We are pleased that the District obtained these updated agreements, and continue to encourage the District to make certain that these documents remain current in the future.

Status of Prior Audit Findings and Observations

Our prior audit of the Annville-Cleona School District (ACSD) for the school years 2005-06, 2004-05, 2003-04 and 2002-03 resulted in one reported observation. The observation pertained to their student accounting applications. 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 questioned District personnel regarding the prior observation. As shown below, we found that the servers holding the District's child accounting data changed from Lancaster-Lebanon IU#13 (LLIU) to Carbon-Lehigh IU#21 (CLIU). The outside vendor remained the same. We determined the District continued to have access and control weaknesses at the new location resulting in a continuation observation in the current audit report.

School Years 2004-05, 2003-04 and 2002-03 Auditor General Performance Audit Report

Observation: Unmonitored IU System Access and Logical Access Control Weaknesses

Observation

Summary:

Our prior audit found that the ACSD uses software purchased from an outside vendor for its critical student accounting applications (membership and attendance). Additionally, the District's entire computer system, including all its data and the vendor's software are maintained on Lancaster-Lebanon Intermediate Unit # 13's (LLIU) servers which are physically located at LLIU. The District has remote access into LLIU's network servers. LLIU also provides the District with system maintenance and support.

Recommendations: Our audit observation recommended that the ACSD:

1. Implement a security policy and system parameter settings to require all users, including the vendor, to change their passwords on a regular basis (i.e., every 30 days).
2. Implement a security policy and system parameter settings to maintain password history, that will prevent the use of repetitive passwords (i.e., last ten passwords).

Current Status:

We followed up on the ACSD student accounting applications and found that the servers containing the District's membership information changed locations from LLIU to CLIU. Therefore, a complete review was performed and we found that the District continued to have access and control weaknesses (see Observation No. 1, page 9).



Distribution List

This report was initially distributed to the superintendent of the school district, the board members, our website address at www.auditorgen.state.pa.us, and the following:

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

The Honorable Ronald J. Tomalis
Secretary of Education
1010 Harristown Building #2
333 Market Street
Harrisburg, PA 17126

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

Ms. Nichole Duffy
Director, Bureau of Budget and
Fiscal Management
Department of Education
4th Floor, 333 Market Street
Harrisburg, PA 17126

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

Dr. David Davare
Director of Research Services
Pennsylvania School Boards Association
P.O. Box 2042
Mechanicsburg, PA 17055

This report is a matter of public record. Copies of this report may be obtained from the Pennsylvania Department of the Auditor General, Office of Communications, 318 Finance Building, Harrisburg, PA 17120. If you have any questions regarding this report or any other matter, you may contact the Department of the Auditor General by accessing our website at www.auditorgen.state.pa.us.

