

PENNSYLVANIA DEPARTMENT OF THE AUDITOR GENERAL  
AUDITOR GENERAL, EUGENE A. DEPASQUALE

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*A Performance Audit:*

HAZLETON AREA SCHOOL DISTRICT  
ALTERED SUPERINTENDENT EMPLOYMENT CONTRACT

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JUNE 2013





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EUGENE A. DePASQUALE  
AUDITOR GENERAL

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

Mr. Brian Earley, Board President  
Hazleton Area School District  
1515 West 23<sup>rd</sup> Street  
Hazleton, Pennsylvania 18202

Dear Governor Corbett and Mr. Earley:

The enclosed report contains the results of the Department of the Auditor General's (Department) performance audit of the Hazleton Area School District's (District) altered former Superintendent employment contract. This performance audit covered the period July 1, 2009 through April 2, 2012, and was conducted pursuant to 72 P.S. § 403 and in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. This performance audit is separate and distinct from the District's cyclical performance audits, which the Department conducts approximately every two years. The District's last cyclical performance audit was released on August 4, 2010.

Our audit found that the District complied, in all significant respects, with applicable state laws, contracts, grant requirements, and administrative procedures related to our objectives. However, 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 observations and recommendations have been discussed with the District's management, and its responses are included in this 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 this audit.

Sincerely,

/s/

EUGENE A. DEPASQUALE  
Auditor General

June 5, 2013

cc: **HAZLETON AREA SCHOOL DISTRICT** Board of School Directors

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## **Executive Summary**

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### **Audit Work**

In August 2011, the Department of the Auditor General began immediately auditing instances where local education agencies (LEA) prematurely ended or altered the employment contracts of their chief administrators. These performance audits do not replace the regular cyclical performance audits that the Department conducts of all Commonwealth LEAs. Instead, the Department performs audits involving chief administrators in addition to each LEA's regular review. The Department will still continue to audit the early separations of all other contracted administrators as part of each LEA's regular cyclical performance audit.

The Department made this policy change because LEAs that prematurely end or alter their chief administrators' contracts frequently spend large sums of taxpayer dollars without receiving any services in return. In addition, these arrangements often involve confidentiality clauses that prevent the public from learning why the LEA undertook such an action. Conducting a performance audit of these agreements as soon as the LEAs execute them helps to ensure that taxpayers have more information about these arrangements and that these facts are available as quickly as possible.

### **LEA Background**

The Hazleton Area School District (District) encompasses approximately 250 square miles. According to 2010 federal census data, it serves a resident population of 80,000. According to District officials, the District provided basic educational services to 10,400 pupils through the employment of

717 teachers, 484 full-time and part-time support personnel, and 46 administrators during the 2009-10 school year. Lastly, the District received \$51 million in state funding in the 2009-10 school year.

### **Audit Conclusion and Results**

Our performance audit found that the District complied, in all significant respects, with the applicable state laws, contracts, and administrative procedures related to our objectives (see pages 3-4). However, as noted below, we identified two matters, which we believe deserve further attention:

#### **Observation No. 1: District Entered Into a Separation Agreement with its Former Superintendent Worth at Least \$179,843.**

On July 28, 2011, the Board of School Directors for the District voted to enter into a Separation Agreement (Agreement) to release the former Superintendent from performance of his duties. This Agreement ended the former Superintendent's five-year contract after only two years. The Agreement stated that the former Superintendent shall be paid his annual salary on a leave of absence covering the period July 31, 2011 through August 1, 2012. The former Superintendent would then retire following the paid leave of absence effective August 2, 2012 (see page 6).

#### **Observation No. 2: Possible Improper Reporting of Retirement Wages and Service Years.**

Our audit of the District's former Superintendent's employment contracts, agreements and payroll records found that the District may have improperly

reported ineligible retirement wages to the Public School Employees' Retirement System (PSERS) for the 2011-12 school year (see page 12).

### **Audit Recommendations**

#### **Observation No. 1:**

The *Hazleton Area School District* Board should:

1. Enter into employment contracts with prospective superintendents at the three-year minimum term permitted by state law, in order to limit potential financial liability by the District and its taxpayers.
2. Ensure that future employment contracts with prospective administrators contain adequate termination provisions sufficient to protect the interests of the District and its taxpayers in the event that the employment ends prematurely for any reason.
3. Provide as much information as possible to the taxpayers of the District explaining the reasons for entering into the Separation Agreement with the former Superintendent and justifying the District's expenditure of public funds for this purpose.
4. Upon termination of any employee, follow provisions of the contract and pay

only what is due to the employee prorated for the term of services provided.

#### **Observation No. 2:**

The *Hazleton Area School District* Board should:

1. Contingent upon PSERS final determination, report to PSERS only those wages allowable for retirement purposes, as stated in PSERS Employer Reference Manual.
2. Implement procedures for reviewing all salary and contribution reports, to ensure that only eligible wages are being reported to PSERS for retirement contributions.

The *Public School Employees' Retirement System* should:

3. Review the propriety of the wages and service credits for the above mentioned employee and make any necessary adjustments.

## Audit Scope, Objectives, and Methodology

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### Scope

*What is a cyclical performance audit?*

Cyclical performance audits allow the Pennsylvania Department of the Auditor General to determine whether local education agencies (LEA) are spending their state funds, including school subsidies, 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 LEA. The Department shares the results of these audits with LEA management, the Governor, the Pennsylvania Department of Education, and other concerned entities.

According to the Public School Code, LEAs include all school districts, charter and cyber charter schools, intermediate units, and career and technical schools.

This performance 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, or for the Department's regular cyclical performance audit (see text box left). This performance audit focused exclusively on the circumstances surrounding the early separation of the local education agencies (LEA) top administrator. This audit was completed in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States.

Our audit covered the period July 1, 2009 through April 2, 2012.

While all LEAs 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 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 a performance audit?*

Performance audits allow the Pennsylvania Department of the Auditor General to immediately review instances where local education agencies prematurely ended or altered the employment contracts of their chief administrators. These audits do not replace the Department's regular cyclical audit, but are instead, performed in addition to that review.

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 LEA's compliance with applicable state laws, contracts, and administrative procedures related to our objectives. However, as we conducted our audit procedures, we sought to determine answers to the following questions, which serve as our audit objectives:

- ✓ Did employment contracts with the former superintendent or other administration officials contain adequate separation provisions sufficient to protect the interests of the LEA, its students, and its taxpayers in

the event the employment of the administrators ends prematurely for any reason?

- ✓ Did the LEA provide as much information as possible to its taxpayers explaining the reasons for the former Superintendent's separation and justifying the expenditure of funds by or through the LEA in order to terminate the contract early?
- ✓ Did the LEA enter into employment contracts with the former Superintendent at the three-year minimum provided by state law in order to limit potential financial liability by the LEA and its taxpayers in the event financial liability was not adequately limited through contract provisions?
- ✓ To the greatest degree possible, what is the total financial cost of the former Superintendent or other administration officials' early contract termination, including funds received by the LEA from private individuals or other entities to facilitate the buy-out?
- ✓ Was the separation agreement transparent and without confidentiality clauses so taxpayers are aware of why the termination occurred?

## 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 results and conclusions based on our audit objectives. We believe that the evidence we obtained in this audit engagement provides a reasonable foundation for our results and conclusions based on our audit objectives.

The LEA's management is responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the LEA is in compliance with applicable laws, contracts, grant requirements, and administrative procedures related to our objectives. In conducting our audit, we obtained an understanding of the LEA's internal controls, including any information technology controls, as they relate to the LEA's compliance with applicable state laws, regulations, contracts, grant requirements, and administrative procedures 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 control 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.

As part of our audit procedures, we obtained copies of employment agreements and other relevant documents associated with the top administrative official's employment. We also interviewed select administrators and support personnel associated with the LEA's operations.



## Findings and Observations

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### Observation No. 1

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*Criteria relevant to the finding:*

Section 1073 of the Public School Code, 24 P.S. § 10-1073(a), requires school districts to enter into three-to-five-year employment contracts with their superintendents.

### **District Entered Into a Separation Agreement with its Former Superintendent Worth at Least \$179,843**

The former Superintendent's original five-year employment contract was effective from July 1, 2009 through June 30, 2014. It included the following provisions regarding the board's termination of the former Superintendent's employment:

- Notwithstanding the five (5) year term of this agreement, the former Superintendent retains the right to retire. However, before doing so the former Superintendent shall give the District not less than one hundred fifty (150) days prior written notice. Absent extraordinary circumstances, such retirement would become effective only on July 1<sup>st</sup> of any year of the term hereof. The former Superintendent further retains the right to resign, absent extraordinary circumstances; such resignation would not become effective sooner than sixty (60) days after it is tendered.
- In accordance with Section 1073 of the Pennsylvania School Code of the Commonwealth of Pennsylvania, the District shall notify former Superintendent no later [than] one hundred fifty (150) days prior to the expiration date of this agreement of the District's intent not to reappoint the former Superintendent. Should the former Superintendent not be so notified, said former Superintendent shall be appointed for a further term of similar length to that which he is serving.

On July 28, 2011, the Board of School Directors (Board) for the Hazleton Area School District (District) voted to enter into a Separation Agreement (Agreement) to release the former Superintendent from performance of his duties. This Agreement ended the former Superintendent's five-year contract after only two years. The Agreement stated that the former Superintendent shall be paid his annual salary on a leave of absence covering the period July 31, 2011 through August 1, 2012. The former Superintendent would then retire following the paid leave of absence effective August 2, 2012.

Under the Agreement, the former Superintendent was entitled to the following salary and benefits worth at least \$179,843:

- Salary of \$130,000.
- Payment of \$6,315 for foregoing medical insurance.
- No change in membership in the Public School Employees' Retirement System (PSERS) and no change in the employer's contributions to PSERS on his behalf.
- No change in disability insurance benefits.
- Payment for 50 unused vacation days at a per diem rate of \$590.91 totaling \$29,545.50.
- Payment for 140.5 unused sick days at \$85 per day totaling \$11,942.50.
- Payment for 8.5 unused personal days and 15.5 unused vacation days converted to sick days at \$85 per day totaling \$2,040.

The former Superintendent was eligible for the payment for unused sick, vacation and personal days per his original contract. Essentially, the Agreement paid the former Superintendent a year's salary to leave his position three years before the expiration of his contract.

The District provided the auditors with a copy of a letter from several Board members dated November 30, 2011, which stated that the Board broke the former Superintendent's original contract for the following reasons:

1. Mediocre evaluation scores.
2. Mishandled paperwork with the state for the alternative education program costing the District nearly \$200,000.
3. Lying to the Board during negotiations to purchase a building.
4. Miscommunication between the Board and the former Superintendent.

Although the Board made the discussion about the separation agreement public, the Board did not provide a public statement in the board meeting minutes explaining why it entered into the separation agreement.

## Recommendations

The *Hazleton Area School District* Board should:

1. Enter into employment contracts with prospective superintendents at the three-year minimum term permitted by state law, in order to limit potential financial liability by the District and its taxpayers.
2. Ensure that future employment contracts with prospective administrators contain adequate termination provisions sufficient to protect the interests of the District and its taxpayers in the event that the employment ends prematurely for any reason.
3. Provide as much information as possible to the taxpayers of the District explaining the reasons for entering into the Separation Agreement with the former Superintendent and justifying the District's expenditure of public funds for this purpose.
4. Upon termination of any employee, follow provisions of the contract and pay only what is due to the employee prorated for the term of services provided.

## Management Response

Management stated the following:

“The District entered into a separation/retirement agreement with [the former Superintendent] in July/August 2011. Based upon the prior agreement dated March 26, 2009, entered into with [the former Superintendent], the terms of which were incorporated into the separation agreement of 2011, [the former Superintendent] was to receive a payout for vacation, accrued sick leave at \$85 per day, or the life restructuring plan that provided for health insurance. Again, all items that were previously included within his agreement of March 26, 2009 would be due to him otherwise through the terms of his contract.

Please also note, pursuant to the terms of the separation agreement, [the former Superintendent] would receive his salary for 2011-2012 which was \$130,000 (less regular payroll deductions). At the time of [the former Superintendent's] separation, he had approximately 65.5 vacation days. Per the terms of his original March 26, 2009 contract, he would be paid per diem rate

for up to 50 days. The per diem rate for those days was \$590.91 making the approximate payout \$29,545.50. As noted previously, [the former Superintendent] would also be compensated for 140.5 sick days and 8.5 personal days (plus an additional 15.5 days converted to sick days) at \$85 per day. Once again, it needs to be emphasized that these would be paid at \$85 per day per the terms of his original contract dated March 26, 2009.

These payments would be made whether [the former Superintendent] would have separated from employment with District in 2011 or 2012 or at the end of his then current contract, assuming the days were not all utilized, he would receive the same payout irrespective of his separation from employment with the District.

The District would like to emphasize that as a result of the separation agreement, and not having to compensate [the former Superintendent] his annual salary for two additional years, the District saved approximately \$260,000. In addition, as he separated from employment, [the former Superintendent] would not be able to accrue any additional vacation or sick days into 2013-2014. He also would be foregoing his entitlement to any sabbatical leave of absence he would otherwise be entitled to under the law which represented an additional savings consideration for the District.

Also, by the very nature of the separation agreement, the [former] Superintendent would not be entitled to collect any unemployment compensation thereby further protecting the interests of the District's residents and taxpayers.

The separation agreement is subject to the Right to Know Law and to disclosure to anyone in the Commonwealth of Pennsylvania seeking a copy of same. This issue also was the subject of debate and discussion. The terms of the Agreement were made public to the taxpayers and community. Any requests for copies have been complied with.

Further, the District did not replace or hire an Interim/Acting Superintendent which again saved the District from additional outlay of comparable salary.

Instead, the District named a current employee to assume responsibilities for [the former Superintendent], the Deputy Superintendent. [The Deputy Superintendent] did not receive any additional compensation for assuming these responsibilities for the 2011-2012 school year.

It should also be noted that on January 25, 2011, the District took action to non-renew the position of another Assistant Superintendent. His annual salary was \$125,000.00. The Board did this as part of a cost cutting measure. This position likewise was not filled.

The District believes its efforts in entering into a separation/retirement agreement with the former Superintendent, non-renewing an Assistant Superintendent and having the Deputy Superintendent assume the duties of the Superintendent without additional compensation have saved the District taxpayers in excess of \$505,000 (\$260,000 [the former Superintendent] salary, \$125,000 [the former Assistant Superintendent] salary, \$130,000 replacement superintendent/acting superintendent salary) not to mention the additional costs that may have been incurred if [the former Superintendent] had requested a sabbatical leave or accrued additional vacation and sick days under his prior contract.

The District would like to further emphasize the terms of separation with [the former Superintendent] as outlined in his original of March 26, 2009, as it relates to payouts for any accrued but unused sick/vacation time or any type of retirement benefits comports to the current requirements of 24 PS 1073 and 1073.1 as it relates to transparency and itemization of such benefits at the time the original Superintendent's contract was entered into on March 26, 2009.

The Board of School Directors appreciates the efforts made by the Auditor General's Office in reviewing this matter and will consider the recommendations made as well as current state law as future situations may arise."

**Auditor Conclusion**

Although the District contends that the result of the Agreement was a savings to the District, our observation stands as written. The Agreement resulted in the former Superintendent being paid a year's salary to leave his position three years before the expiration of his contract.

## Observation No. 2

## Possible Improper Reporting of Retirement Wages and Service Years

### *Criteria relevant to the finding:*

The Pennsylvania Retirement Code, 24 Pa. C.S. § 8102, provides, that a “school employee” is defined as “any person engaged in work relating to a public school for any governmental entity and for which work he is receiving regular remuneration. . . .” (emphasis added).

The Public School Employees’ Retirement System (PSERS) Employer Reference Manual, Chapter 2, states to be eligible for PSERS membership as a full-time employee, the employee must work 5 hours or more per day, 5 days per week or its equivalent. It further states to be eligible as a part-time employee, the employee must be contracted to work less than 5 hours per day, 5 days per week or its equivalent and must have their salaries and retirement deductions reported to PSERS through monthly Work Report Records. Additionally, the PSERS Employee Reference Manual states that independent contractors are not eligible for PSERS membership.

PSERS allows only qualified salary and wages to be included for retirement purposes. According to Pennsylvania School Employees’ Retirement Board Regulations, Section 211.2, reported compensation should: “exclude . . . payments or similar emoluments which may be negotiated in a collective bargaining agreement for the express purpose of enhancing the compensation factor for retirement benefits.”

Our audit of the Hazleton Area School District’s (District) former Superintendent’s employment contracts, agreements and payroll records found that the District may have improperly reported ineligible retirement wages to the Public School Employees’ Retirement System (PSERS) for the 2011-12 school year.

The former Superintendent’s tenure prematurely ended through a separation agreement (Agreement) effective July 28, 2011. Under the Agreement, the former Superintendent shall be on a paid leave of absence and be paid his annual salary covering the period July 31, 2011 through August 1, 2012. The former Superintendent then retired effective August 2, 2012, following a paid leave of absence.

Our audit found that the former Superintendent has not provided any services to the District since the Agreement went into effect. The District is continuing to report the former Superintendent’s wages to PSERS as though he were still a full-time employee. He will, therefore, receive service credits for the year ending June 30, 2012. Service credits are used to determine the percentage of salary a former employee would receive in retirement payments.

According to the PSERS Employer Reference Manual, only employees who work 5 hours or more a day, 5 days a week or its equivalent, can be considered full-time. It further states that to be eligible for participation in PSERS as a part-time employee, an individual must be contracted to work less than 5 hours a day, 5 days a week, or its equivalent and must have their salaries and retirement deductions reported to PSERS monthly.

Based on the Agreement’s description, it appears that the former Superintendent’s current \$130,000 salary may not be eligible for inclusion in PSERS as either a full-time or a part-time employee.

Although the Board has the authority to craft the terms of a contract, it may not supersede PSERS' benefit structure. If PSERS determines the administrator's wages are not eligible retirement wages, their inclusion in PSERS will result in reporting errors and retirement overpayments to the former Superintendent for the 2011-12 school year.

## **Recommendations**

The *Hazleton Area School District* Board should:

1. Contingent upon PSERS final determination, report to PSERS only those wages allowable for retirement purposes, as stated in PSERS Employer Reference Manual.
2. Implement procedures for reviewing all salary and contribution reports, to ensure that only eligible wages are being reported to PSERS for retirement contributions.

The *Public School Employees' Retirement System* should:

3. Review the propriety of the wages and service credits for the above mentioned employee and make any necessary adjustments.

## **Management Response**

Management waived the opportunity to reply.



## **Distribution List**

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This report was initially distributed to the Superintendent of the District, the Board of School Directors, our website at [www.auditor.gen.state.pa.us](http://www.auditor.gen.state.pa.us), and the following stakeholders:

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