

LEHIGH VALLEY ACADEMY REGIONAL CHARTER SCHOOL
NORTHAMPTON COUNTY, PENNSYLVANIA
PERFORMANCE AUDIT REPORT

FEBRUARY 2012

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

Ms. Diane Lawson, Board President
Lehigh Valley Academy Regional Charter School
1560 Valley Center Parkway, Suite 200
Bethlehem, Pennsylvania 18017

Dear Governor Corbett and Ms. Lawson:

We conducted a performance audit of the Lehigh Valley Academy Regional Charter School (LVARCS) to determine its compliance with applicable state laws, contracts, grant requirements, and administrative procedures. Our audit covered the period July 1, 2006 through August 12, 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 LVARCS 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. A summary of these results is presented in the Executive Summary section of the audit report.

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

Sincerely,

/s/

JACK WAGNER
Auditor General

February 17, 2012

cc: **LEHIGH VALLEY ACADEMY REGIONAL CHARTER SCHOOL** Board of Trustees



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Executive Summary

Audit Work

The Pennsylvania Department of the Auditor General conducted a performance audit of the Lehigh Valley Academy Regional Charter School (LVARCS). Our audit sought to answer certain questions regarding the LVARCS's compliance with applicable state laws, contracts, grant requirements, and administrative procedures.

Our audit scope covered the period July 1, 2006 through August 12, 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.

LVARCS School Background

The LVARCS, located in Northampton County, Pennsylvania opened in August 2002. It was originally chartered on August 21, 2000, for a period of five years by the Bethlehem Area and Saucon Valley school districts. LVARCS's mission states: "It seeks in providing a quality choice in K-12 education, built on a global foundation of academic excellence active parental involvement and applied character development, by integrating technology into innovative teaching strategies and best learning practices." During the 2009-10 school year, the LVARCS provided educational services to 892 pupils from 16 sending school districts through the employment of 66 teachers, 10 full-time and part-time support personnel, and 4 administrators. The LVARCS received approximately \$7.8 million in tuition

payments from school districts required to pay for its students attending the LVARCS in school year 2009-10.

Adequate Yearly Progress

LVARCS made Adequate Yearly Progress (AYP) for the 2009-10 school year by meeting all AYP measures.

AYP is a key measure of school performance established by the federal No Child Left Behind Act of 2001 requiring that all students reach proficiency in Reading and Math by 2014. For a school to meet AYP measures, students in the school must meet goals or targets in three areas: (1) Attendance (for schools that do not have a graduating class) or Graduation (for schools that have a high school graduating class), (2) Academic Performance, which is based on tested students' performance on the Pennsylvania System of School Assessment (PSSA), and (3) Test Participation, which is based on the number of students that participate in the PSSA. Schools are evaluated for test performance and test participation for all students in the tested grades (3-8 and 11) in the school. AYP measures determine whether a school is making sufficient annual progress towards the goal of 100 percent proficiency by 2014.

Audit Conclusion and Results

Our audit found that the LVARCS 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.

Finding: Possible Inaccurate Reporting of Retirement Wages. Our audit of the LVARCS's payroll and retirement records found that retirement wages may have been overstated in reports submitted to the Public School Employees' Retirement System for the 2009-10, 2008-09 and 2007-08 school years (see page 10).

Status of Prior Audit Findings and Observations. This is our first audit of the LVARCS. Therefore, there are no prior audit findings or observations.

Background Information on Pennsylvania Charter Schools

Description of Pennsylvania Charter Schools:

Charter and cyber charter schools are taxpayer-funded public schools, just like traditional public schools. There is no additional cost to the student associated with attending a charter or cyber charter school. Charter and cyber charter schools operate free from many educational mandates, except for those concerning nondiscrimination, health and safety, and accountability.

Pennsylvania Charter School Law

Pennsylvania's charter schools were established by the Charter School Law (Law), enacted through Act 22 of 1997, as amended. In the preamble of the Law, the General Assembly stated its intent to provide teachers, parents, students, and community members with the opportunity to establish schools that were independent of the existing school district structure.¹ In addition, the preamble provides that charter schools are intended to, among other things, improve student learning, encourage the use of different and innovative teaching methods, and offer parents and students expanded educational choices.²

The Law permits the establishment of charter schools by a variety of persons and entities, including, among others, an individual; a parent or guardian of a student who will attend the school; any nonsectarian corporation not-for-profit; and any nonsectarian college, university or museum.³ Applications must be submitted to the local school board where the charter school will be located by November 15 of the school year preceding the school year in which the charter school will be established,⁴ and that the board must hold at least one public hearing before approving or rejecting the application.⁵ If the local school board denies the application, the applicant can appeal the decision to the State Charter School Appeal Board,⁶ which is comprised of the Secretary of Education and six members appointed by the Governor with the consent of a majority of all of the members of the Senate.⁷

¹ 24 P.S. § 17-1702-A.

² Ibid.

³ 24 P.S. § 17-1717-A (a).

⁴ 24 P.S. § 17-1717-A (c).

⁵ 24 P.S. § 17-1717-A (d).

⁶ 24 P.S. § 17-1717-A (f).

⁷ 24 P.S. § 17-1721-A (a).

Pennsylvania ranks high compared to other states in the number of charter schools:

According to the Center for Education Reform, Pennsylvania has the 7th highest charter school student enrollment, and the 10th largest number of operating charter schools, in the United States.

Source: "National Charter School and Enrollment Statistics 2010." October, 2010.

Funding of Pennsylvania Charter Schools:

Brick-and mortar charter schools and cyber charter schools are funded in the same manner, which is primarily through tuition payments made by school districts for students who have transferred to a charter or cyber charter school.

The Charter School Law requires a school district to pay a per-pupil tuition rate for its students attending a charter or cyber charter school.

With certain exceptions for charter schools within the School District of Philadelphia, initial charters are valid for a period of no less than three years and no more than five years.⁸ After that, the local school board can choose to renew a school's charter every five years, based on a variety of information, such as the charter school's most recent annual report, financial audits, and standardized test scores. The board can immediately revoke a charter if the school has endangered the health and welfare of its students and/or faculty. However, under those circumstances, the board must hold a public hearing on the issue before it makes its final decision.⁹

Act 88 of 2002 amended the Law to distinguish cyber charter schools, which conduct a significant portion of their curriculum and instruction through the Internet or other electronic means, from brick-and-mortar charter schools that operate in buildings similar to school districts.¹⁰ Unlike brick-and-mortar charter schools, cyber charter schools must submit their application to the Department of Education (DE), which determines whether the application for a charter should be granted or denied.¹¹ However, if DE denies the application, the applicant can still appeal the decision to the State Charter School Appeal Board.¹² In addition, DE is responsible for renewing and revoking the charters of cyber charter schools.¹³ Cyber charter schools that had their charter initially approved by a local school district prior to August 15, 2002 must seek renewal of their charter from DE.¹⁴

Pennsylvania Charter School Funding

The Commonwealth bases the funding for charter schools on the principle that the state's subsidies should follow the students, regardless of whether they choose to attend traditional public schools or charter schools. According to the Charter School Law, the sending school district must pay the charter/cyber charter school a per-pupil tuition rate

⁸ 24 P.S. § 17-1720-A.

⁹ Pennsylvania Department of Education, Basic Education Circular, "Charter Schools," Issued 10/1/2004.

¹⁰ 24 P.S. §§ 17-1703-A, 17-1741-A *et seq.*

¹¹ 24 P.S. § 17-1745-A(d).

¹² 24 P.S. § 17-1745-A(f)(4).

¹³ 24 P.S. § 17-1741-A(a)(3).

¹⁴ 24 P.S. § 17-1750-A(e).

based on its own budgeted costs, minus specified expenditures, for the prior school year.¹⁵ For special education students, the same funding formula applies, plus an additional per-pupil amount based upon the sending district's special education expenditures divided by a state-determined percentage specific to the 1996-97 school year.¹⁶ The Charter School Law also requires that charter schools bill each sending school district on a monthly basis for students attending the charter school.¹⁷

Typically, charter schools provide educational services to students from multiple school districts throughout the Commonwealth. For example, a charter school may receive students from ten neighboring, but different, sending school districts. Moreover, students from numerous districts across Pennsylvania attend cyber charter schools.

Under the Public School Code of 1949, as amended, the Commonwealth also pays a reimbursement to each sending school district with students attending a charter school that amounts to a mandatory percentage rate of total charter school costs.¹⁸ Commonwealth reimbursements for charter school costs are funded through an education appropriation in the state's annual budget. However, the enacted state budget for the 2011-12 fiscal year eliminated funding of the charter school reimbursement previously paid to sending school districts.¹⁹

¹⁵ See 24 P.S. § 17-1725-A(a)(2).

¹⁶ See 24 P.S. §§ 17-1725-A(a)(3); 25-2509.5(k).

¹⁷ See 24 P.S. § 17-1725-A(a)(5).

¹⁸ See 24 P.S. § 25-2591.1. Please note that this provision is contained in the general funding provisions of the Public School Code and not in the Charter School Law.

¹⁹ Please note that the general funding provision referenced above (24 P.S. § 25-2591.1) has not been repealed from the Public School Code and states the following: "For the fiscal year 2003-2004 and each fiscal year thereafter, if insufficient funds are appropriated to make Commonwealth payments pursuant to this section, such payments shall be made on a pro rata basis." Therefore, it appears that state funding could be restored in future years.

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 Pennsylvania Department of Education, and other concerned entities.

Our audit, conducted under the 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 July 1, 2006 through August 12, 2010.

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

For the purposes of our audit work and to be consistent with Department of Education (DE) 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 PMCS’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:

- ✓ Was the charter school in overall compliance with the Public School Code of 1949²⁰ (PSC) and the Charter School Law²¹ (Law)?
- ✓ Did the charter school have policies and procedures regarding the requirements to maintain student health records and perform required health services, and keep accurate documentation supporting its annual health services report filed with the Department of Health to receive state reimbursement?

²⁰ 24 P.S. § 1-101 *et seq.*

²¹ 24 P.S. § 17-1701-A *et seq.*

- ✓ Did the charter school receive state reimbursement for its building lease under the Charter School Lease Reimbursement Program, was its lease agreement approved by its board of trustees, and did its lease process comply with the provisions of the Public Official and Employee Ethics Act?²²
- ✓ Did the charter school comply with the open enrollment and lottery provisions of the Law?
- ✓ Does the charter school provide the services required for its special education students through outside agencies and/or through properly certified professional staff with the required instructional hours and/or training?
- ✓ Did the charter school board of trustees and administrators, and the chartering school board members comply with the Public School Code, the Public Official and Employee Ethics Act, and the Sunshine Act?
- ✓ Were at least 75 percent of the charter school's teachers properly certified and did all of its noncertified teachers meet the "highly qualified teacher" requirements?
- ✓ Did the charter school require its noncertified professional employees to provide evidence that they are at least 18 years of age, a U.S. citizen, and certified by a licensed Pennsylvania physician to be neither mentally nor physically disqualified from successful performance of the duties of a professional employee of the charter school?
- ✓ Did the charter school accurately report its membership numbers to DE and were its average daily membership and tuition billings accurate?
- ✓ Did the charter school comply with the Law's compulsory attendance provisions and, if not, did the charter school remove days in excess of ten consecutive unexcused absences from the school's

²² 65 Pa.C.S. § 1101 *et seq.*

reported membership totals pursuant to the regulations?²³

- ✓ Did the charter school take appropriate steps to ensure school safety?
- ✓ Did the charter school require that all of its employees enroll in the Public School Employees' Retirement System at the time of filing its charter school application as required by the Law, unless the board of trustees had a retirement plan that covered the employees or the employees were already enrolled in another retirement program?
- ✓ Did the charter school use an outside vendor to maintain its membership data and, if so, are internal controls in place related to vendor access?
- ✓ Were there any other areas of concern reported by local auditors, citizens, or other interested parties which warrant further attention during our audit?

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 findings, observations, and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings, observations, and conclusions based on our audit objectives.

LVARCS management is responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the charter school 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.

²³ 22 Pa. Code § 11.24.

Our audit examined the following:

- Records pertaining to professional employee certification, student health services, special education, lease agreements, open enrollment, vendor contracts, and student enrollment.
- Items such as board of trustees' meeting minutes, pupil membership records, IRS 990 forms, and reimbursement applications.
- Tuition receipts and deposited state funds.

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

Findings and Observations

Finding

Criteria relevant to the finding:

For retirement purposes, all employee earnings are either qualified or unqualified. Only qualified earnings may contribute to retirement benefits.

Section 8102 of the Public School Employees' Retirement Code, 24 Pa.C.S. § 8102, provides that only compensation based on the standard salary schedule may be reported as qualified earnings to PSERS for retirement purposes.

According to Chapter 5 of the PSERS Employer's Reference Manual for Reporting, unqualified earnings not eligible for retirement contributions include:

"Payment to an employee in lieu of a benefit the employee is eligible to receive, or any reimbursement received by the employee. (These payments do not become part of your standard pay schedule.)"

Possible Inaccurate Reporting of Retirement Wages

Our audit of the Lehigh Valley Academy Regional Charter School (LVARCS) payroll and retirement records found that retirement wages may have been overstated for 61 employees for a total of \$113,900 in reports submitted to the Public School Employees' Retirement System (PSERS) for the 2009-10, 2008-09 and 2007-08 school years. These possible inaccuracies occurred because the LVARCS included health care opt-out payments to employees as part of qualified wages reported to PSERS.

The LVARCS adopted a policy that employees may waive the health care coverage to which they are entitled, and instead receive an opt-out payment of \$2,000 or less per year. The total amount of the payment depended on the length of time they were employed during the year. Over a three year period, a total of 61 employees elected to receive opt-out payments in lieu of health care coverage, for a total of \$113,900, which consisted of the following:

- 21 employees in the 2009-10 school year, for a total of \$41,000;
- 19 employees in the 2008-09 school year, for a total of \$36,100; and
- 21 employees in the 2007-08 school year, for a total of \$36,800.

There were no significant wage reporting errors found for the 2006-07 school year.

Retirement regulations specify that certain types of payments made to employees other than their standard salary do not qualify for retirement calculations. Consequently, a cash payment to an employee in lieu of a benefit he/she is eligible to receive, such as a payment for opting out of health care benefits, is defined as unqualified earnings and should not be included in the employee's salary reported to PSERS for retirement purposes.

Although the board has the authority to allow for a cash payment in lieu of entitled health benefits, the LVARCS

must follow PSERS's guidelines and may not include these payments as qualified earnings reported to PSERS.

Moreover, the Commonwealth reimburses public schools, including charter schools, for a portion of the employers' share of contributions paid to PSERS. Since the basis of the state's reimbursement is the school's PSERS earnings reports, any inaccuracies in the reported amounts will impact the state's reimbursement paid to the school. As such, the LVARCS's inclusion of opt-out payments in reports filed with PSERS may have resulted in overpayments in the state's reimbursements for retirement contributions paid to the LVARCS for the 2009-10, 2008-09 and 2007-08 school years. Consequently, adjustments to the state's reimbursements may be necessary.

Information pertaining to these opt-out payments was sent to PSERS for its determination regarding the eligibility of wages reported by the LVARCS and any necessary adjustments to retirement benefits and contributions based on these results.

Recommendations

The *Lehigh Valley Academy Regional Charter School* 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 compensation reported for employees who received opt-out payments for the 2009-10, 2008-09 and 2007-08 school years and render an opinion on the propriety of the wages reported by the LVARCS for these individual employees.

4. If any part of the reported wages are determined to be ineligible for retirement, make the necessary corrections to retirement benefits for these individual employees and adjust the LVARCS's required share of retirement contributions paid to PSERS based on these corrected amounts.
5. If any inaccuracies occurred, in coordination with the Department of Education, make any necessary adjustments to the state's reimbursements for retirement contributions paid to the LVARCS for the 2009-10, 2008-09 and 2007-08 school years based on the corrected reports.

Management Response

Management stated the following:

Payments to employees for waiving health insurance coverage were erroneously set up to have PSERS contributions withheld in the payroll system. Lehigh Valley Academy will work with the PSERS representative to make corrections to the PSERS work reports that were filed incorrectly.

Status of Prior Audit Findings and Observations

This is our first audit of the Lehigh Valley Academy Regional Charter School. Therefore, there are no prior audit findings or observations.



Distribution List

This report was initially distributed to the chief executive officer of the charter school, the board of trustees, our website address at www.auditor.gen.state.pa.us, and the following:

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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.

