

MIDDLETOWN AREA SCHOOL DISTRICT
DAUPHIN COUNTY, PENNSYLVANIA
PERFORMANCE AUDIT REPORT

JANUARY 2010

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania
Harrisburg, Pennsylvania 17120

Ms. Barbara Layne, Board President
Middletown Area School District
55 West Water Street
Middletown, Pennsylvania 17057

Dear Governor Rendell and Ms. Layne:

We conducted a performance audit of the Middletown Area School District (MASD) to determine its compliance with applicable state laws, regulations, contracts, grant requirements and administrative procedures. Our audit covered the period February 3, 2006 through April 17, 2009, 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, 2007, 2006 and 2005. 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 MASD complied, in all significant respects, with applicable state laws, regulations, contracts, grant requirements, and administrative procedures, except as detailed in the finding noted in this report. In addition, we identified one matter unrelated to compliance that is reported as an observation. A summary of these results is presented in the Executive Summary section of the audit report.

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

Sincerely,

/s/

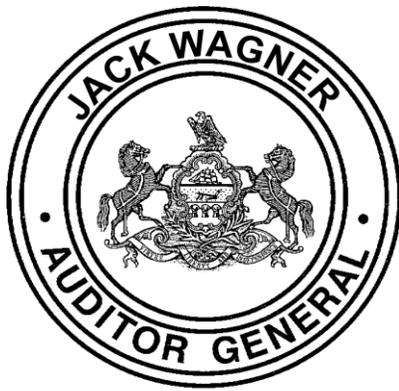
JACK WAGNER
Auditor General

January 15, 2010

cc: **MIDDLETOWN AREA SCHOOL DISTRICT** Board Members

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Executive Summary

Audit Work

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

Our audit scope covered the period February 3, 2006 through April 17, 2009, 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, 2006-07, 2005-06 and 2004-05.

District Background

The MASD encompasses approximately 17 square miles. According to 2000 federal census data, it serves a resident population of 18,355. According to District officials, in school year 2007-08 the MASD provided basic educational services to 2,427 pupils through the employment of 212 teachers, 110 full-time and part-time support personnel, and 18 administrators. Lastly, the MASD received more than \$11.9 million in state funding in school year 2007-08.

Audit Conclusion and Results

Our audit found that the MASD complied, in all significant respects, with applicable state laws, regulations, contracts, grant requirements, and administrative procedures, except for one compliance-related matter reported as a finding. In addition, one matter unrelated to compliance is reported as an observation.

Finding: Pupil Transportation Reporting Errors Resulted in a Net Overpayment of \$11,146.

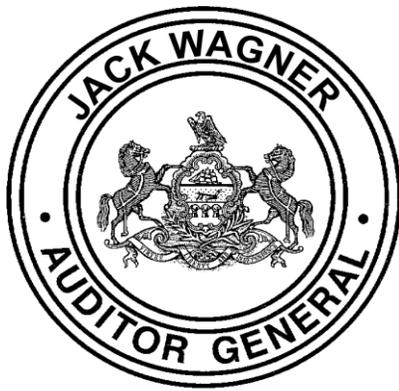
Our audit of the MASD's transportation records for the 2007-08, 2006-07, 2005-06, and 2004-05 school years found errors in reporting daily mileage, the number of pupils, the number of days transportation was provided, nonpublic pupil data, charter pupil data and total pupil data, to the Department of Education for the 2007-08, 2006-07, 2005-06 and 2004-05 school years (see page 6).

Observation: Unmonitored Vendor System Access and Logical Access Control

Weaknesses. We determined that a risk exists that unauthorized changes to MASD's data could occur and not be detected because MASD was unable to provide supporting evidence that it is adequately monitoring all vendor activity in its system (see page 10).

Status of Prior Audit Findings and

Observations. With regard to the status of our prior audit recommendations to the MASD from an audit we conducted of the 2003-04, 2002-03, 2001-02 and 2000-01 school years, we found the MASD had taken appropriate corrective action in implementing our recommendations pertaining to Social Security and Medicare wage reporting errors (see page 13).



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 February 3, 2006 through April 17, 2009, except for the verification of professional employee certification which was performed for the period December 28, 2005 to March 30, 2009.

Regarding state subsidy and reimbursements, our audit covered school years 2007-08, 2006-07, 2005-06 and 2004-05.

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 (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

Performance audits draw conclusions based on an evaluation of sufficient, appropriate evidence. Evidence is measured against criteria, such as, laws, regulations, and defined business practices. Our audit focused on assessing the MASD's compliance with applicable 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?
- ✓ In areas where the District receives state subsidy and reimbursements based on pupil membership (e.g. basic education, special education, and vocational education), did it follow applicable laws and procedures?

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 law, regulation, 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.

- ✓ In areas where the District receives state subsidy and reimbursements based on payroll (e.g. Social Security and retirement), did it follow applicable laws and procedures?
- ✓ Did the District follow applicable laws and procedures in areas dealing with pupil membership and ensure that adequate provisions were taken to protect the data?
- ✓ Is the District's pupil transportation department, including any contracted vendors, in compliance with applicable state laws and procedures?
- ✓ Does the District ensure that Board members appropriately comply with the Public Official and Employee Ethics Act?
- ✓ 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

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 and conclusions based on our audit objectives.

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, regulations, contracts, grant requirements and administrative procedures.

MASD management is responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the District is in compliance with applicable laws, regulations, 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, professional employee certification, and financial stability.
- Items such as Board meeting minutes, pupil membership records, and reimbursement applications.
- Tuition receipts and deposited state funds.

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

Lastly, to determine the status of our audit recommendations made in a prior audit report released on May 30, 2006, we reviewed the MASD's response to DE dated June 26, 2006. We then performed additional audit procedures targeting the previously reported matters.

Findings and Observations

Finding

Pupil Transportation Reporting Errors Resulted in a Net Overpayment of \$11,146

Criteria relevant to this finding:

DE instructions for completing the end-of-year summary report require any changes in the miles with and miles without pupils, total mileage, number of days the vehicle provided to and from school transportation and pupils transported to and from school be based on actual data using the district's daily records and weighted averaging of mileage and pupils.

Our audit of the District's transportation records for the 2007-08, 2006-07, 2005-06 and 2004-05 school years found errors in data reported to the Department of Education (DE) for all years of audit in the following areas:

- Daily mileage with and without pupils;
- Number of pupils;
- Number of days transportation was provided;
- Nonpublic pupil data;
- Charter pupil data; and
- Total pupil data

DE permitted the District to revise the 2007-08 reported data during our audit. Therefore, we did not determine the monetary effect of those reporting errors. The errors for the other years resulted in a net overpayment of \$11,146, as follows:

	<u>(Over)Underpayments</u>			<u>Totals</u>
	<u>2006-07</u>	<u>2005-06</u>	<u>2004-05</u>	
Nonpublic Subsidy	\$9,240	\$ -	\$(10,780)	\$ (1,540)
Regular Subsidy	<u>(304)</u>	<u>(6,118)</u>	<u>(3,184)</u>	<u>(9,606)</u>
Totals	<u>\$8,936</u>	<u>\$(6,118)</u>	<u>\$(13,964)</u>	<u>\$(11,146)</u>

Daily Mileage

Miles With/Without Pupils

The approved daily miles with/without pupils was incorrectly reported for 9 of 65 contracted vehicles in 2006-07; for 2 of 2 district-owned vehicles in 2004-05; and for 1 of 57 contracted vehicles in 2004-05. The inaccurate

reporting of daily mileage was due to clerical errors when computing the sample average.

Number of Pupils

The number of pupils assigned to each bus was incorrectly reported for 1 of 3 district-owned vehicles and 22 of 65 contracted vehicles in 2006-07; for 1 of 3 district-owned vehicles and 33 of 65 contracted vehicles in 2005-06; for 2 of 2 district-owned vehicles 40 of 57 contracted vehicles in 2004-05. These errors were the result of the District reporting the highest single month pupil count rather than the sample average.

Number of Days

The number of days that buses provided transportation was inaccurately reported for 2 of 65 contracted vehicles in 2006-07. This clerical error was the result of District personnel not accurately computing the actual number of days when these vehicles provided transportation to and from school.

Pupil Data

Nonpublic and Charter Pupil Data

We found that in 2007-08 nonpublic pupils were overstated by 138 pupils and charter school pupils were understated by 1 pupil. Additionally, nonpublic school pupils were understated by 24 pupils in 2006-07, and overstated by 28 pupils in 2004-05. The inaccurate reporting of nonpublic and charter school pupils was due to clerical errors in reporting the number of pupils who rode the buses.

Public School Pupils

Public school pupils were overstated by 238 pupils in 2004-05. Due to clerical errors in reporting the total number of pupils who rode the buses.

Approved daily miles with and without pupils, the number pupils transported, the number of days transportation was provided, and total pupils reported are all integral parts of the transportation reimbursement calculation. These

factors must be reported accurately to DE in order for the District to receive accurate reimbursement for pupil transportation.

We have provided DE with a report detailing the errors for the 2006-07, 2005-06, and 2004-05 school years for use in recalculating the District's transportation reimbursements. As noted previously in this finding, DE accepted the District's 2007-08 revised reports for processing to calculate the District's reimbursement.

Recommendations

The *Middletown Area School District* should:

Establish collection and review procedures to ensure accurate reporting of all data elements, based on DE guidelines, used in the calculation of transportation reimbursement.

The *Department of Education* should:

Adjust the District's allocations to recover the net overpayment of \$11,146.

Management Response

Management stated the following:

Cause of the Problem

For the years ended June 30, 2005, 2006 and 2007, the primary cause of the reporting errors was a failure to require an independent review of transportation reports before submission. During those years, the Coordinator of Educational Services completed the transportation reports and no other District personnel were responsible to review his work because he held an administrative position.

Calculation errors and reporting errors were made that could have been caught had an independent review been conducted.

Corrective Action

A change in personnel responsible for the completion of transportation reports occurred for the 2007-08 school year upon the retirement of the Coordinator of Educational Services. The secretary for the Coordinator of Educational Services transitioned into the role of Transportation Coordinator (a non-administrative position). With this change in personnel, administrative oversight for transportation shifted to the Business Manager. Two errors were noted by the state auditors for the first year (2007-08 school year) of transportation reporting under this change in personnel. However, because the preliminary transportation subsidy report (PDE-2576) for the 2007-08 school year had not yet been received, the District did not have the opportunity to conduct a final review of the reporting and identify the errors before the state audit. The District has been afforded the opportunity to correct the errors with the Department of Education, so that these errors are not reported as a finding for the state audit. The Transportation Coordinator and Business Manager are no longer novices at transportation reporting and are comfortable with the reporting process. Beginning with the reporting for the 2008-09 school year, a second review by the preparer of the transportation reports (Transportation Coordinator) and an independent review by the Business Manager will be required. The District believes that this thorough review will ensure the accuracy of the submitted reports.

Observation



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.

Unmonitored Vendor System Access and Logical Access Control Weaknesses

Middletown Area School District (MASD) uses software purchased from Capital Area Intermediate Unit #15 (CAIU) for its critical student accounting applications (membership and attendance). The CAIU has remote access into MASD’s network servers.

We determined that a risk exists that unauthorized changes to MASD’s data could occur and not be detected because the District was unable to provide supporting evidence that it is adequately monitoring all vendor activity in its system. However, since the District has adequate manual compensating controls in place to verify the integrity of the membership and attendance information in its database, that risk is mitigated. Attendance and membership reconciliations are performed between manual records and reports generated from the Student Accounting System.

Reliance on manual compensating controls becomes increasingly problematic if MASD would ever experience personnel and/or procedure changes that could reduce the effectiveness of the manual controls. 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.

We noted the following weaknesses during our review:

1. The contract with the vendor was not reviewed by the District’s legal counsel.
2. The District’s Acceptable Use Policy does not include provisions for accountability (responsibilities of users, auditing, incident handling) and authentication (password security and syntax requirements).
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; and to maintain a password history (i.e., approximately ten passwords).

4. The District does not have evidence that it is generating or reviewing monitoring reports of user access and activity on the system (including IU and District employees). There is no evidence that the District is performing procedures to determine which data the CAIU may have altered.

Recommendations

The *Middletown Area School District* should:

1. Ensure the contract with the vendor is reviewed by legal counsel.
2. Ensure the District's Acceptable Use Policy includes provisions for accountability (responsibilities of users, auditing, incident handling) and authentication (password security and syntax requirements).
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).
4. Generate monitoring reports (including firewall logs) of CAIU and employee access and activity on their system. Monitoring reports should include the date, time, and reason for access, changes made and who made the changes. The District should review these reports to determine that the access was appropriate and that data was not improperly altered.

Management Response

Management stated the following:

Cause of the Problem

1. The District has been very pro-active in having its solicitor review all contracts and agreements. However, the District failed – this one time – to have its solicitor review the vendor contract.

2. The District believed that all essential items were included in its Acceptable Use Policy and was not aware of any omitted items prior to the state audit.
3. The District's student information software does not have the capabilities to require the suggested access controls.
4. The District is unable to identify a process that can be used to generate and review reports on user access and activity that would not be a burden with the available staff resources.

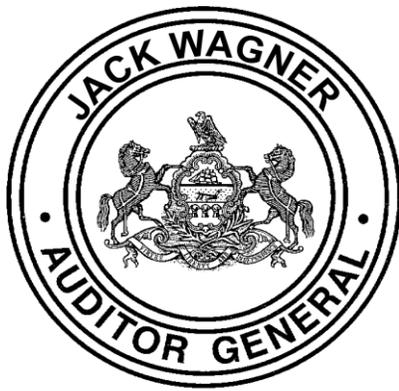
Corrective Action

1. The District will continue to ask the solicitor to review all contracts and agreements prior to board action. When a request to approve contracts and agreements are placed on the board agenda for adoption, the Board Secretary will verify that solicitor review has occurred.
2. The District will update its Acceptable Use Policy to include all essential items.
3. The District will use a Lightweight Directory Access Protocol (LDAP) to authenticate users of the student information system against its current Active Directory. This will enable the District to force password changes every 30 days, enforce strict password syntax criteria, and maintain a password history. LDAP will result in controlled access that the system alone cannot provide.
4. The District will continue to research how to accomplish the review of user access and activity reports with limited staffing. At this time, the District is unable to ascertain whether it can accomplish this recommendation.

Status of Prior Audit Findings and Observations

Our prior audit of the Middletown Area School District (MASD) for the school years 2003-04, 2002-03, 2001-02 and 2000-01 resulted in one reported finding. The finding pertained to error in Social Security and Medicare wages. As part of our current audit, we determined the status of corrective action taken by the District to implement our prior recommendations. We analyzed the MASD Board’s written response provided to the Department of Education (DE), performed audit procedures, and questioned District personnel regarding the prior findings. As shown below, we found that the MASD did implement recommendations related to errors in Social Security and Medicare wages.

<i>School Years 2003-04, 2002-03, 2001-02 and 2000-01 Auditor General Performance Audit Report</i>		
<i>Prior Recommendations</i>	<i>Implementation Status</i>	
<p><u><i>I. Finding: Errors in Reporting Social Security and Medicare Wages Resulted in Reimbursement Underpayments of \$21,117</i></u></p> <ol style="list-style-type: none"> 1. Become familiar with DE’s instructions for completing the PDE-2105 and reconcile federal wages reported on the PDE-2105 with wages reported on the Internal Revenue Service Federal Form 941. 2. Review reports submitted for years subsequent to our audit and, if similar errors occurred, submit revised reports to DE. 3. DE should adjust the District’s allocations to resolve the \$21,117 Social Security and Medicare reimbursement underpayments. 	<p>Background:</p> <p>Our audit of the District’s 2003-04, 2002-03, 2001-02 and 2000-01 school years’ Reconciliation of Social Security and Medicare Tax Contributions (PDE-2105) found errors in total taxable Social Security and Medicare wages reported for the 2003-04, 2002-03 and 2001-02 school years.</p>	<p>Current Status:</p> <p>Our current audit found that the District had taken corrective action beginning with the 2004-05 school year to address both recommendations.</p> <p>The current audit also found that DE had not yet adjusted the District’s allocations. We again recommend that DE adjust the District’s allocations to resolve the \$21,117 Social Security and Medicare reimbursement underpayments.</p>



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:

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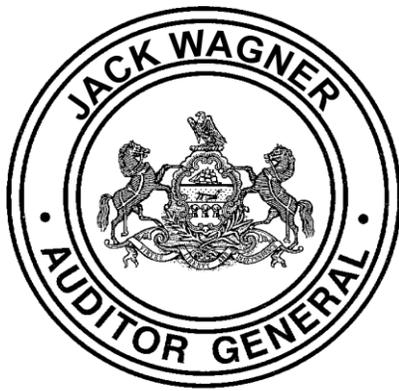
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