

MONTROSE AREA SCHOOL DISTRICT
SUSQUEHANNA COUNTY, PENNSYLVANIA
PERFORMANCE AUDIT REPORT

MARCH 2012

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

Mr. Chris Caterson, Board President
Montrose Area School District
273 Meteor Way
Montrose, Pennsylvania 18801

Dear Governor Corbett and Mr. Caterson:

We conducted a performance audit of the Montrose Area School District (MASD) to determine its compliance with applicable state laws, contracts, grant requirements, and administrative procedures. Our audit covered the period August 5, 2009 through July 27, 2011, except as otherwise indicated in the report. Additionally, compliance specific to state subsidy and reimbursements was determined for the school years ended June 30, 2010 and June 30, 2009. 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, contracts, grant requirements, and administrative procedures, except as detailed in two findings noted in this report. A summary of these results is presented in the Executive Summary section of the audit report.

Our audit findings 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.

Sincerely,

/s/

JACK WAGNER
Auditor General

March 9, 2012

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

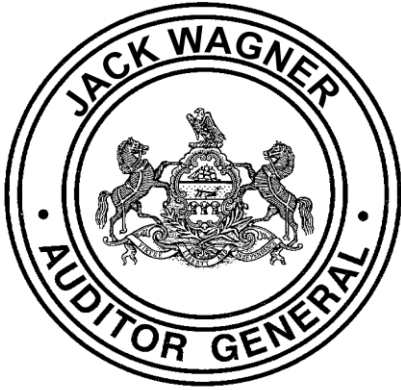
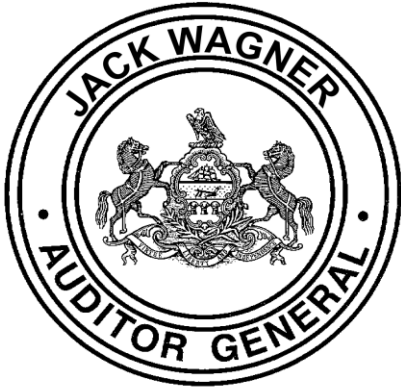


Table of Contents

	Page
Executive Summary	1
Audit Scope, Objectives, and Methodology	3
Findings and Observations	6
Finding No. 1 – Errors in Reporting Social Security and Medicare Wages Resulted in Reimbursement Underpayments of \$18,032	6
Finding No. 2 – Possible Improper Reporting of Retirement Wages and Service Years	9
Status of Prior Audit Findings and Observations	12
Distribution List	13



Executive Summary

Audit Work

The Pennsylvania Department of the Auditor General conducted a performance audit of the Montrose Area School District (MASD). 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 MASD in response to our prior audit recommendations.

Our audit scope covered the period August 5, 2009 through July 27, 2011, 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 2009-10 and 2008-09.

District Background

The MASD encompasses approximately 228 square miles. According to 2000 federal census data, it serves a resident population of 11,708. According to District officials, in school year 2009-10 the MASD provided basic educational services to 1,694 pupils through the employment of 147 teachers, 97 full-time and part-time support personnel, and 10 administrators. Lastly, the MASD received more than \$12.1 million in state funding in school year 2009-10.

Audit Conclusion and Results

Our audit found that the MASD complied, in all significant respects, with applicable state laws, contracts, grant requirements, and administrative procedures; however, as noted below, we identified two compliance-related matters reported as findings.

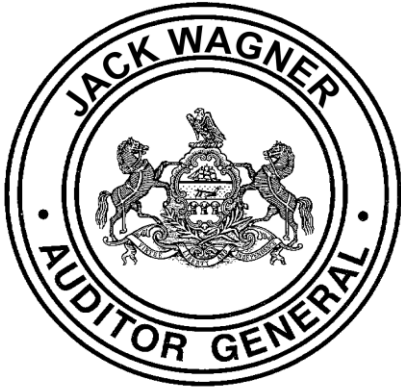
Finding No. 1: Errors in Reporting Social Security and Medicare Wages Resulted in Reimbursement

Underpayments of \$18,032. Our audit of the MASD's Social Security and Medicare wages reimbursement records found that reports submitted to the Department of Education were inaccurate, resulting in reimbursement underpayments of \$13,879 for the 2009-10 school year and \$4,153 for the 2008-09 school year for a total underpayment of \$18,032 (see page 6).

Finding No. 2: Possible Improper Reporting of Retirement Wages and Service Years.

Our audit of the MASD's administrative employment contracts, agreements and payroll records found wages for a prior administrator totaling \$19,103 and \$18,588 for the 2010-11 and 2009-10 school years, respectively, were improperly reported as eligible retirement wages to the Public School Employees' Retirement System. Also, the prior administrator received a net overpayment of \$1,587 (see page 9).

Status of Prior Audit Findings and Observations. There were no findings or observations included in our prior audit report.



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 August 5, 2009 through July 27, 2011.

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

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 MASD'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:

- ✓ Were professional employees certified for the positions they held?
- ✓ 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?
- ✓ 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 use an outside vendor to maintain its membership data and if so, are there internal controls in place related to vendor access?
- ✓ 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 findings 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.

MASD 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 bus driver qualifications, professional employee certification, state ethics compliance, and financial stability.
- Items such as Board meeting minutes and reimbursement applications.

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

Findings and Observations

Finding No. 1

Errors in Reporting Social Security and Medicare Wages Resulted in Reimbursement Underpayments of \$18,032

Criteria relevant to the finding:

Instructions for completing the application state that wages reported in the "Total Taxable Social Security and Medicare Wages" columns must include wages of federally funded employees. Federally funded wages are then reported in a separate column, to be subtracted from the total to determine wages subject to state reimbursement.

Act 29 of 1994 changed the reimbursement calculation for the Commonwealth's share of Social Security and Medicare taxes and created two categories of employees that must be tracked by school entities for reimbursement purposes. The two categories of employees are "existing" employees and "new" employees. The reimbursement calculation is different for each category of employee. These two categories are mutually exclusive and comprehensive, so that an employee will fit into only one category.

Our audit of the Montrose Area School District's Social Security and Medicare wages reimbursement records found that reports submitted to the Department of Education (DE) were inaccurate, resulting in reimbursement underpayments of \$13,879 for the 2009-10 school year and \$4,153 for the 2008-09 school year for a total underpayment of \$18,032.

Certain qualifying wages for both new and existing employees were inadvertently omitted from these reports due to District personnel's misunderstanding of DE's instructions for filing Social Security reimbursement forms.

Furthermore, District personnel failed to reconcile total taxable wages for Social Security and Medicare with wages reported on the Employer's Quarterly Federal Tax Return.

Wages eligible for Social Security and Medicare reimbursement were understated in reports submitted to DE, as follows:

	<u>Wages Subject to State Reimbursement</u>				
<u>Total Wages</u>		<u>Wages</u>			<u>Reimbursement</u>
<u>Audited</u>	<u>Reported</u>	<u>Understated</u>	<u>Rate</u>		<u>Underpayments</u>
2009-10					
SE \$5,281,430	\$5,069,603	\$211,827	.03100		\$ 6,567
ME 5,288,876	5,077,049	211,827	.00725		1,536
SN 6,473,210	6,365,027	108,183	.0432698		4,681
MN 6,473,210	6,365,027	108,183	.0101195		<u>1,095</u>
				Total	<u>\$13,879</u>
2008-09					
SE \$5,262,557	\$5,199,737	\$62,820	.03100		\$ 1,947
ME 5,271,775	5,208,954	62,821	.00725		455
SN 6,186,116	6,153,537	32,579	.0435426		1,419
MN 6,186,116	6,153,537	32,579	.0101833		<u>332</u>
				Total	<u>\$ 4,153</u>
				Grand Total	<u>\$18,032</u>
(SE) Social Security wages for existing employees (ME) Medicare wages for existing employees (SN) Social Security wages for new employees (MN) Medicare wages for new employees					

Recommendations

The *Montrose Area School District* should:

1. Ensure District personnel are aware of the proper procedures for correctly completing state Social Security reimbursement forms.
2. Reconcile total taxable wages for Social Security and Medicare with wages reported on the Employer's Quarterly Federal Tax Return.
3. Review reports filed for years subsequent to the audit period and, if errors are found, submit revised reports to DE.

DE should pay the District \$18,032 to resolve the reimbursement underpayments.

Management Response

Management stated the following:

The District payroll clerk inadvertently backed out federally funded wages in preparing the report. Clerk is no longer employed by the District and current business office personnel have placed controls to ensure this will not occur again. Subsequent reports have been corrected with the Department of Education.

Finding No. 2 →

Possible Improper Reporting of Retirement Wages and Service Years

Criteria relevant to the finding:

The PSERS Employer Reference Manual (ERM) Chapter 2 states to be eligible for PSERS membership as a full-time employee, the employee must work 5 hours or more a day, 5 days a 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 a day, 5 days a week or its equivalent and must have his/her salary and retirement deductions reported to PSERS through monthly Work Report Records. Additionally, the PSERS ERM 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 Montrose Area School District's (MASD) administrative employment contracts, agreements and payroll records found wages for a prior administrator totaling \$19,103 and \$18,588 that were improperly reported as eligible retirement wages to the Public School Employees' Retirement System (PSERS) for the 2010-11 and 2009-10 school years, respectively. Also, the prior administrator received a net overpayment of wages of \$1,587.

The prior administrator's employment contract expired June 30, 2009. Effective July 1, 2009, he entered into a three-year agreement with the MASD with the title of "consultant." According to the agreement, he would not be required to appear for work regularly. Instead he will be utilized on an "as needed" basis at the discretion of the District, but will not be required to work more than sixteen hours per month. There is no documentation that the consultant provided any services to the MASD since the inception of the agreement. According to the agreement, the consultant is to be paid \$57,310 for the three-year period, or \$19,103 per year, less usual deductions including PSERS, and paid in accordance with the usual pay cycle.

The consultant received service credits for the years ending June 30, 2011 and 2010 for which he was not eligible for membership with PSERS. Service credits are used to determine the percentage of salary a former employee would receive in retirement payments. According to the criteria included in the PSERS Reference Manual, the consultant was not eligible for PSERS membership since he did not meet the full or part-time requirements and was paid as an independent contractor. The consultant would also not be eligible for PSERS membership for the last year of his contract which is to terminate June 30, 2012.

The consultant received the correct amount of \$19,103 according to the agreement during the 2010-11 school year. During the 2009-10 school year, the consultant received \$18,588, an underpayment of \$515.

Errors in reporting wages and membership for the consultant caused overpayments to PSERS for the 2010-11 and 2009-10 school years by \$1,433 and \$1,394, respectively. Furthermore, the MASD overpaid PSERS \$1,115 and \$889 for the 2010-11 and 2009-10 school years, respectively.

The errors were the result of MASD erroneously reporting the consultant as a full-time employee to PSERS.

Although the board has the authority to craft the terms of a contract, the school board may not supersede the PSERS benefit structure.

Additionally, on July 10, 2009, the prior administrator received \$2,102 in undocumented and unapproved wages for the 2008-09 school year. The prior payroll secretary incorrectly calculated the prior administrator's wages due for the 2008-09 school year. If so, retirement wages to PSERS would be overreported for this employee by an additional \$2,102 for the 2009-10 school year. In that case, the prior administrator would have overpaid PSERS by an additional \$158 and the MASD would have overpaid PSERS by an additional \$100 for the 2009-10 school year.

Recommendations

The *Montrose Area School District* 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, in order to ensure that only eligible wages are being reported to PSERS for retirement contributions.
3. Recover the \$1,587 overpayment in wages from the prior administrator.

PSERS should review the propriety of the wages and service credits for the above mentioned employee and make any necessary adjustments.

Management Response

Management stated the following:

The District entered into a separation agreement with a former business manager that provided for additional service years for contribution services. The District was advised that this was in agreement with current PSERS procedures. The District will move as directed to rectify the situation.

In regards to the payroll of July 10, 2009; the District did not authorize the \$2,102.16 payment to the former business manager by the former payroll clerk. The payment should have been in line with the separation agreement as approved.

Status of Prior Audit Findings and Observations

Our prior audit of the Montrose Area School District resulted in no findings or observations.

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

Ms. Connie Billet
Assistant Internal Auditor
Public School Employees' Retirement
System
5 North Fifth Street
Harrisburg, PA 17101-1905

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.

