

PERFORMANCE AUDIT

Penn Hills School District Allegheny County, Pennsylvania

May 2016



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen
www.PaAuditor.gov

EUGENE A. DePASQUALE
AUDITOR GENERAL

Dr. Nancy Hines, Superintendent
Penn Hills School District
260 Aster Street
Pittsburgh, Pennsylvania 15235

Mrs. Denise Graham-Shealey, Board President
Penn Hills School District
260 Aster Street
Pittsburgh, Pennsylvania 15235

Dear Dr. Hines and Mrs. Graham-Shealey:

Our performance audit of the Penn Hills School District (District) evaluated the application of best practices in the areas of finance, governance, safety, and contracts. In addition, this audit determined the District's compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures (relevant requirements). This audit covered the period July 1, 2012 through June 30, 2015, except as otherwise stated and was conducted pursuant to Section 403 of The Fiscal Code and in accordance with the *Government Auditing Standards* issued by the Comptroller General of the United States. Those 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.

During our audit, we found significant instances of failing to apply best practices and noncompliance with relevant requirements, as detailed in our eight findings. A summary of the results is presented in the Executive Summary section of the audit report. These findings include recommendations for the District.

Our audit findings and recommendations have been discussed with the District's management, and their responses are included in the 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 course of the audit.

Sincerely,

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale".

Eugene A. DePasquale
Auditor General

May 18, 2016

cc: **PENN HILLS SCHOOL DISTRICT** Board of School Directors

Table of Contents

	Page
Executive Summary	1
Background Information	3
Findings and Observations	6
Finding No. 1 – The District’s Deficient Governance Practices, including a Lack of Separation of Duties of Board Officers, Contributed to its Financial Decline Resulting in a Negative \$18.8 Million General Fund Balance as of June 30, 2015	6
Finding No. 2 – Persistent Financial Operating Deficits, Budgeting Errors, and Increased Debt Service Resulted in a Substantial Negative General Fund Balance	14
Finding No. 3 – The District Violated its Policy Governing the Use of Procurement Cards and did not Monitor Purchases	28
Finding No. 4 – The District Failed To Ensure that Approximately \$22,000 in Ticket Sales from 18 Sporting Events Were Deposited	35
Finding No. 5 – The District’s Failure to Monitor its Transportation Contractor Resulted in Misappropriation of District Fuel of Between \$260,000 and \$384,500	40
Finding No. 6 – The District’s Transportation Expenditures Significantly Exceeded PDE’s Final Formula Allowance	47
Finding No. 7 – The District Improperly Sold its Tax-Exempt Fuel to a Municipality at a Markup, But its Deficient Billing Practices Netted Losses in the Thousands of Dollars	53
Finding No. 8 – The District Failed to Ensure that its School Bus Drivers Met All Employment Requirements	57
Status of Prior Audit Findings and Observations	63
Appendix: Audit Scope, Objectives, and Methodology	66
Distribution List	70

Executive Summary

Audit Work

The Pennsylvania Department of the Auditor General conducted a performance audit of the District. Our audit sought to answer certain questions regarding the District's application of best practices and compliance with certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures and to determine the status of corrective action taken by the District in response to our prior audit recommendations.

Our audit scope covered the period July 1, 2012 through June 30, 2015, except as otherwise indicated in the audit scope, objectives, and methodology section of the report. (See Appendix A) Compliance specific to state subsidies and reimbursements was determined for the 2012-13, 2013-14, and 2014-15 school years.

Audit Conclusion and Results

Our audit found significant noncompliance with best practices and certain relevant state laws, regulations, contracts, grant requirements, and administrative procedures, as detailed in the eight audit findings within this report.

Finding No. 1: The District's Deficient Governance Practices, including a Lack of Separation of Duties of Board Officers, Contributed to its Financial Decline Resulting in a Negative \$18.8 Million General Fund Balance as of June 30, 2015. The Board of School Directors (Board) and the District's former Superintendent (former Superintendent) did not adequately fulfill their fiduciary

responsibilities when governing the District. As a result, they not only failed to comply with the PSC and District policies, they also failed to timely intervene at a critical financial juncture for the District (see page 6).

Finding No. 2: Persistent Financial Operating Deficits, Budgeting Errors, and Increased Debt Service Resulted in a Substantial Negative General Fund Balance. The District experienced a significant decrease in its General Fund balance over the past three fiscal years. We reviewed several financial benchmarks to evaluate changes in its financial position over a period of six years. We found that the District had an operating deficit for five of the six years reviewed (see page 14). We also found that the District borrowed \$135 million in 2010 to cover the cost of constructing a new high school and elementary center but did not adequately budget for resulting debt service payments.

Finding No. 3: The District Violated its Policy Governing the Use of Procurement Cards and did not Monitor Purchases. Our review of the District's procurement card practices revealed numerous violations of Board approved policies, including a years-long persistent failure by the District to review, authorize, and account for purchases (see page 28).

Finding No. 4: The District Failed to Ensure that Approximately \$22,000 in Ticket Sales From 18 Sporting Events Were Deposited. Our audit of the District's Athletic Fund from July 1, 2012 through June 30, 2015, revealed that approximately

\$22,000 collected as admission fees to 18 District sporting events were not deposited into the District's General Fund (see page 35).

Finding No. 5: The District's Failure to Monitor its Transportation Contractor Resulted in Misappropriation of District Fuel of Between \$260,000 and \$384,500.

The District failed to monitor the fuel usage of its transportation contractor (Contractor), resulting in a 117 percent spike in the District's fuel costs. It also failed to negotiate and implement an effective lease agreement for the Contractor's use of a District maintenance facility, which is where the District stores its fuel. Finally, it failed to limit the Contractor's access to District fuel supplies, which resulted in the misappropriation of District fuel costing between \$260,000 and \$384,500 (see page 40).

Finding No. 6: The District's Transportation Expenditures Significantly Exceeded PDE's Final Formula Allowance.

The District's transportation expenditures increased more than \$2 million from the 2012 fiscal year through the 2015 fiscal year. We found that the District entered into contracts for transportation services with a payment structure that paid a daily rate per vehicle. However, the District did not adequately monitor bus routes and adjust the number of buses needed to meet District needs. As a result, the District's transportation expenditures were significantly greater than PDE's "final formula allowance" (see page 47).

Finding No. 7: The District Improperly Sold its Tax-Exempt Fuel to a Municipality at a Markup, But its Deficient Billing Practices Netted Losses in the Thousands of Dollars.

We found that the District has been selling its tax-exempt fuel at a 15 cents per gallon markup to a local municipality (Municipality) in violation of the Liquid Fuels and Fuel Tax Act. While the District believed this agreement was a revenue generator, the District actually lost more than \$60,000 due to its deficit billing practices (see page 53).

Finding No. 8: The District Failed to Ensure that its School Bus Drivers Met All Employment Requirements.

The District failed to meet the requirements related to the employment of bus drivers having direct contact with students. Specifically, we found that the District did not obtain, review, and maintain documentation to support that each bus driver was qualified and suitable to transport students (see page 57).

Status of Prior Audit Findings and Observations.

With regard to the status of our prior audit recommendations to the District from an audit released on March 27, 2013, we found that the District had taken appropriate corrective action in implementing our recommendations pertaining to certification deficiencies (see page 63). We also found that the District had taken appropriate corrective action in implementing our recommendations pertaining to unmonitored vendor system access and logical access control weaknesses (see page 64).

Background Informationⁱ

School Characteristics 2013-14 School Year ⁱⁱ	
County	Allegheny
Total Square Miles	19.17
Resident Population ⁱⁱⁱ	42,329
Number of School Buildings	3*
Total Teachers	323
Total Full or Part-Time Support Staff	307
Total Administrators	25
Total Enrollment for Most Recent School Year	3,924
Intermediate Unit Number	03
District Vo-Tech School	Forbes Road CTC

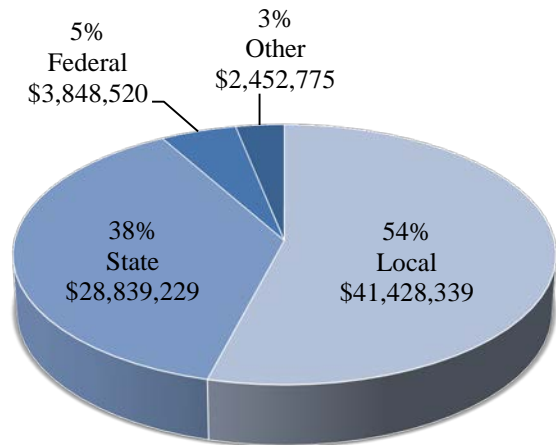
Mission Statement

The visions of the Penn Hills School District is to engage our entire community to inspire individual students to their highest levels of reading and academic achievement while instilling a commitment to service, respect, and life-long learning.

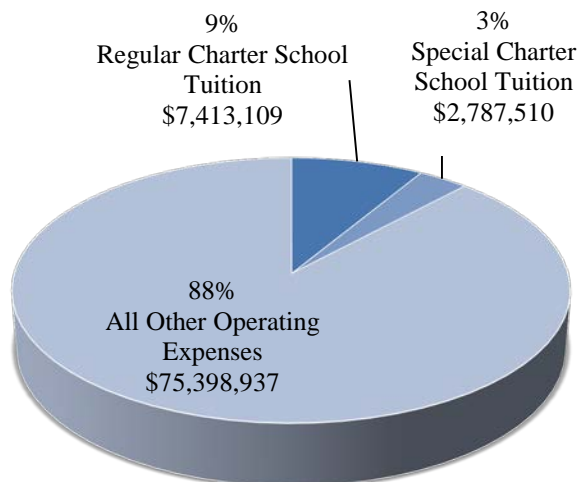
* In the 2014-15 school year, the District consolidated all three elementary buildings with the opening of a new elementary center bringing the total number of school buildings to three.

Financial Information

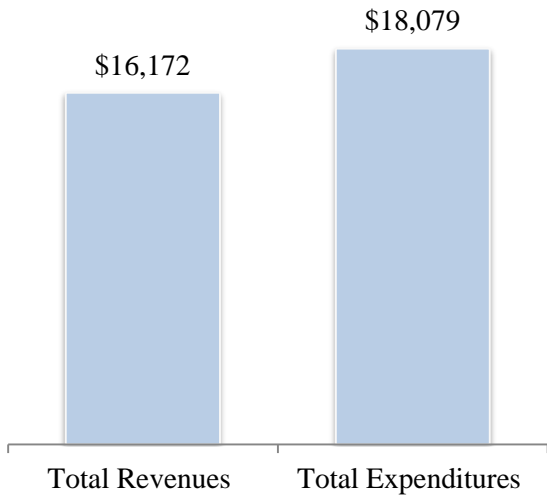
Revenue by Source for 2013-14 School Year



Select Expenditures for 2013-14 School Year

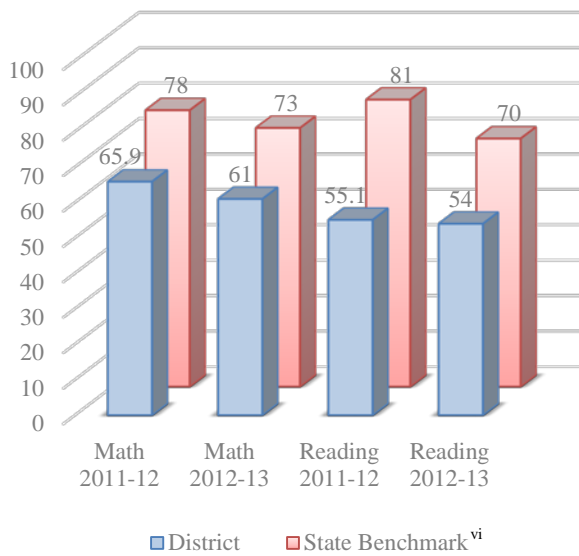


**Dollars Per Student
2013-14 School Year**



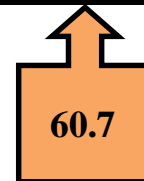
Academic Information

Percentage of District Students Who Scored "Proficient" or "Advanced" on 2011-12 and 2012-13 PSSA^{iv v}



District's 2012-13 SPP Score^{vii}

A	B	C	D	F
90-100	80-89.9	70-79.9	60-69.9	<60
▲	▲	■	▼	▼



**Individual Building SPP and PSSA Scores^{viii}
2012-13 School Year**

School Building	SPP Score	PSSA % School Proficient and Advanced in Math	PSSA % Statewide Benchmark of 73% Above or Below	PSSA % School Proficient and Advanced in Reading	PSSA % Statewide Benchmark of 70% Above or Below	Federal Title I Designation (Reward, Priority, Focus, No Designation)^{ix}
Forbes El Sch	71.4	77	4	62	8	No Designation
Linton MS	55.7	60	13	49	21	No Designation
Penn Hebron El Academy	68.7	70	3	59	11	No Designation
Penn Hills SHS	64.2	48	25	71	1	N/A
Washington El Sch	70.1	61	12	73	3	No Designation

Findings and Observations

Finding No. 1

The District's Deficient Governance Practices, including a Lack of Separation of Duties of Board Officers, Contributed to its Financial Decline Resulting in a Negative \$18.8 Million General Fund Balance as of June 30, 2015

Criteria relevant to the finding:

Article IV of The Public School Code (PSC), 24 P.S. Article IV(d) and (e) address the Board's positions of Secretary and Treasurer, respectively. See 24 P.S. § 4-431 *et seq.* and 24 P.S. § 4-436 *et seq.*

Section 440 of the PSC states, in part: "The treasurer of each school district shall deposit the funds belonging to the school district in the school depository, if any, as directed by the board of school directors, and shall at the end of each month make a report to the school controller, if any, and to the secretary of the board of school directors, of the amount of funds received and disbursed by him during the month." See 24 P.S. § 4-440.

The Pennsylvania School Boards Association's Essentials of School Board Service (2015) states:

"The board fulfills its primary role by adopting and maintaining compliant board policies for the organization and operation of the school district." (p. 1)

The Board and the District's former Superintendent did not adequately fulfill their fiduciary responsibilities¹ when governing the District. As a result, they not only failed to comply with the Public School Code (PSC) and District policies, they failed to timely intervene at a critical financial juncture for the District.

Both the Board and the former Superintendent failed to require routine and timely accountability from the former Director of Business Affairs (former Director), whose unchecked activities negatively affected the District's finances, ultimately resulting in a negative \$18.8 million General Fund balance as of June 30, 2015. The many effects of the failure to govern District operations are highlighted as follows:

- Insufficient budgeting for the cost of debt service as a result of borrowing over \$130 million for a District-wide capital improvement project. (See Finding No. 2, beginning on page 14)
- Under budgeting for student transportation expenses by nearly \$6.5 million from 2012 through 2015. (See Finding No. 2, beginning on page 14)
- Entering into a contract for transportation services with a payment structure that resulted in costs that

¹ Pursuant to Section 321 (relating to Compensation; oath of office) of the PSC, 24 P.S. § 3-321, every director of a school board must before entering upon the duties of their office "take and subscribe to the ...[a] oath or affirmation...[that includes] that I will discharge the duties of my office with **fidelity**." [Emphasis added.] Although the PSC does not provide a definition of "fidelity", the general legal definition of this term is as follows: "*noun* allegiance, conscientiousness, constantia, devotedness, devotion, dutiful adherence, dutifulness, faith, faithfulness, fealty, fides, good faith, homage, loyalty, stanchness, steadfastness, trueness, trustiness, trustworthiness." <http://legal-dictionary.thefreedictionary.com/fidelity>

*Criteria relevant to the finding
(continued):*

“Policies are the means by which a school board governs the school district; they guide its administration, staff, students, parents and the public, and are essential for maintaining compliance, accountability, consistency and fairness.” (p. 25)

The Penn Hill School District Board policy No. 003 states “the Board shall exercise its leadership through its rule making power by adopting Board procedures and policies...” It also states in part: “The Superintendent shall be responsible for implementing Board policies and establishing administrative regulations for the operation of the school district.”

Board policy No. 004 states: “The Board believes that the preparation of each Board member for the performance of duties is essential to the effectiveness of the Board’s functioning.”

Board Policy No. 011 states that the Board “advocates for a thorough and efficient system of public education by allocating resources in a manner designed to facilitate student achievement consistent with school district goals and plans.” It also states that the Board should “monitor results by using data appropriately to make informed decisions.”

- significantly exceeded the state transportation reimbursement. (See Finding No. 6, beginning on page 47)
- Failure to audit the transportation contractor’s fuel usage records, which allowed fuel with a value of more than \$260,000 to be misappropriated by the contractor. (See Finding No. 5, beginning on page 40)
- Failure to collect agreed upon rental income from the District’s transportation contractor, resulting in receipt of only \$28,698 rather than \$40,000 in the 8 months from September 2014 to April 2015. (See Finding No. 5, beginning on page 40)
- Failure to implement adequate internal controls governing the collection, safeguarding, and depositing of money collected for admission to District sporting events. As a result, more than \$22,000 was never deposited into District accounts. (See Finding No. 4, beginning on page 35)
- Failure to monitor the District’s procurement card usage, which resulted in misuse and unauthorized purchases, ultimately resulting in the District closing all active procurement cards. (See Finding No. 3, beginning on page 28)
- Failure by the District to ensure its contracted bus drivers met all requirements including driver’s licenses and criminal and child abuse clearances. (See Finding No. 8, beginning on page 57)

Board Policy No. 601 places responsibility on the former Director to establish sound accounting procedures, report to the Board, and institute effective business practices. The bulleted list above clearly demonstrates that the former Director neither established sound accounting procedures nor instituted effective business practices.

*Criteria relevant to the finding
(continued):*

Board policy No. 601 states, in part: “The Director of Business Affairs shall review monthly the financial operations, report to the Board on effectiveness and recommend improvements, and prepare administrative procedures for sound district and school fiscal operations.” It also states: “the Board directs the Director of Business Affairs to establish sound accounting procedures based upon recommendations of the District auditor and state and federal government, institute effective business practices, and recommend appropriate equipment and technology when necessary.”

However, it is critical to note that, as the Chief Administrative Officer and governing body of the District, the Superintendent and the Board have the ultimate responsibility for ensuring that effective business practices are consistently met. Therefore, in addition to the PSC and best business practices applicable to school boards, the District’s own Board Policy Nos. 3, 4, and 11 charge the former Superintendent and the Board with overall governance responsibilities. They did not hold the former Director accountable for his job responsibilities, and in so doing, they also failed in their own governance responsibilities.

Simultaneous Treasurer and Secretary

The PSC provides for individual bonding, as well as separate and distinct duties for the Board’s Secretary and Treasurer. Yet, the former Director served simultaneously for years—in noncompliance with the PSC—as the Board’s Secretary and Treasurer. Serving the Board in both these capacities created an immediate lack of separation of duties and an inherently weak internal control environment.

Best practices for maintaining strong internal controls in any organization start with a separation of duties so that no single person is responsible for the movement of funds, as well as the accounting for financial activity. By allowing the former Director to serve as both Treasurer and Secretary, the Board and former Superintendent concentrated too much authority into one person and also reduced transparency since the Treasurer was supposed to provide monthly reports to the Secretary pursuant to the PSC.¹

In addition, the Board was in noncompliance with the PSC by not electing its Treasurer annually as required in Section 404. If it had done so, perhaps it would have earlier recognized it was in noncompliance with the PSC and corrected the internal control weakness it had previously allowed.²

¹ 24 P.S. § 4-440.

² 24 P.S. 4-404.

Lack of Transparency on Financial Affairs

Board Policy No. 601 charges the Director of Business Affairs with the responsibility of reviewing the monthly financial operations of the District, reporting to the Board on effectiveness and recommended improvements, and preparing administrative procedures for sound fiscal operations.

We found that the former Director failed to provide the Board with timely financial reports. Not only was this in noncompliance with the PSC and the former District's own policies, the tardiness in reporting reduced transparency since the Board could not effectively monitor activity. The tardiness was especially significant in the first half of the 2014-15 school year. The Director failed to provide financial reports for the months of July, August, September, October, and November 2014 until six months into the school year, at the January 26, 2015 board meeting. During the intervening months, the District's financial position was deteriorating. The July 2014 report, for instance, disclosed that the General Fund balance had decreased to a negative \$8.9 million. (See Finding No. 2)

If the Board had been provided, and reviewed, the financial reports in a timely fashion, the District's dire financial condition would have been apparent and the Board may have been able to address its fiscal challenges prior to needing an advance in its basic education subsidy.

Our review of the board meeting minutes for the January 2015 meeting, as well as the Finance Committee's meeting minutes for that month, revealed no discussion by either governing body. No one questioned the content of the reports, nor did anyone question their lateness. Instead, the Board accepted all of these reports as follows:

In conformity with provisions under the Public School Code and Series 600 of the Board Policy Manual, the Board approved/ratified of current School District financial reports including the cash balance reports; general fund, food service, capital projects, balance sheets and budget summaries,

secondary school activity fund reports, and budget transfer report as of July 2014 through November 2014 have been provided to the Board in advance of tonight's meeting and will be included in the official minutes of this meeting.³

There were also no comments on these reports or their lateness in the *Board Comments* section of the minutes.

Another example of a lack of transparency relates to the former Director's handling of the independent auditor's report for the school year 2013-14. This report revealed that the District's General Fund balance was a negative \$8.9 million and that the District had committed avoidable budgeting errors. The former Director received the final version of the independent auditors report on January 12, 2015, along with a request by the independent auditor to present this report to the Board. According to emails and other documentation, the former Director cancelled the independent auditing firm's presentation of its report at the January and February Board and Finance Committee meetings.

It is the Board and the Superintendent's ultimate responsibility, however, to govern the District according to its own policies and the PSC. In previous years, the independent auditors report was presented to the Board in January or early February. As such, they should have been aware of the timing of the independent auditor's report and made inquiries of the former Director as to its status.

Possible Conflict of Interest.

Another effect of the Board and its former Superintendent's failure to oversee the activities of the former Director is related to the District's agreement with Boyce Campus Middle College (BCMC), a dual enrollment program, whereby high school students could take college courses for credit. The program was part of an effort by multiple local school districts to send their students to the Community College of Allegheny County

³ Penn Hills School District. Minutes of the Board of School Directors' Meeting. January 26, 2015. <http://www.boarddocs.com/pa/phsd/Board.nsf/Public>. Accessed on April 21, 2016.

(CCAC) at its Monroeville physical and virtual campuses.

The District's former Director authorized payments to BCMC of \$230,000 in excess of the budgeted amount for the fiscal years ended 2012 through 2014. Even with the knowledge that the District's financial condition was worsening, the former Director continued to promote a program that was repeatedly over-budget. At the February 2, 2015 public finance committee meeting, the former Director invited representatives from the college to discuss the program. Meanwhile, other school districts were discontinuing participation in the program, which threatened the long-term viability of the program.

It's important to note that the wife of the District's former Director was an employee and an apparent administrator of the BCMC program during this time period. These transactions may have been in noncompliance with the Pennsylvania Public Official and Employee Ethics Act (Ethics Act), which prohibits public employees from engaging in conflicts of interest.⁴

Again, if the Board and its former Superintendent had required timely accountability from its former Director, it may have been able to inquire about budget variances and the possible noncompliance with the Ethics Act.

New District Leadership

The two key District employees that were at the center of the District's governance and financial issues are no longer employed by the District. The now former Superintendent and the Board entered into a mutual separation agreement at the January 26, 2015 board meeting. The former Superintendent has approximately one year remaining on the original employment contract with the District.

In accordance with the separation agreement, the District placed the former Superintendent on an approved paid leave of absence for three months. In addition to the paid leave, the District paid the former Superintendent for

⁴ Section 1102 of the Ethics Act, 65 Pa.C.S. §1102, defines a conflict of interest as: "Use by a public office or public employee of the authority of his office or employment...for the private pecuniary benefit of himself, a member of his immediate family or a business with which he or a member of his family is associated...."

unused sick, personal, vacation, and emergency days. In total, the District paid the Superintendent more than \$62,000 when he separated employment from the District.

The former Director, who was hired by the District in March 2008, was placed on paid administrative leave on March 24, 2015. Subsequently, the former Director was suspended without pay on June 10, 2015, and was then terminated on November 23, 2015.

The District installed a new leadership team after the above mentioned employees separated from the District. The District's current leadership is in the process of implementing corrective actions to address the deficiencies in the fiscal operations of the District. The Board must provide effective oversight of the District's administration to ensure strong accountability so that the District can accomplish its goal of educating its students through the judicious spending of public funds.

Recommendations

The *Penn Hills School District* should:

1. Require its Director of Business Affairs to comply with board policies by providing monthly financial reports timely and at each board meeting. Board meeting minutes should not be attested as complete unless the required monthly financial reports have been presented.
2. Comply with the PSC and best business practices by disallowing anyone from simultaneously serving as both Board Secretary and Treasurer.
3. Require the independent auditors report to be presented by the independent auditor every year, and if the report is late, the Board should inquire directly of the auditor as to the reasons for the delay.
4. Establish clear reporting and accountability procedures between the Director of Business Affairs, the Superintendent, and the Board.

Management Response

District management provided the following response for each recommendation:

1. The District's new Business Manager has complied with this recommendation since his tenure began in November. The Board receives a Treasurer's Report from the previous month to approve. This report includes a reconciliation of all cash accounts, list of bills, budget, year-to-date and current period reports for all revenues and expenditures. It also includes the District's current cash-flow position, month-end and projected year-end fund balance.
2. The Board has appointed a Board Secretary (Superintendent's Secretary) and a Board Treasurer (Business Manager) as of January 2016 to comply with PSC.
3. The June 30, 2015 audit was presented to the School Board, by the independent auditor, in executive session and in the public Finance Committee meeting the same week of February 2016. The audit was also accepted by the board in the February public voting meeting and is available on the Business Office page on the District web site.
4. The Business Manager, Superintendent, and the Board discuss the Treasurer's Report monthly in the public Finance Committee meetings. In this forum, the Superintendent, Board and public have the opportunity to ask for clarification of the current month's financial position.

Auditor Conclusion

We are encouraged that the District's new leadership team has begun implementing corrective action based upon our recommendations. We believe it is imperative that the Board receives the District's financial reports timely and has the opportunity to review and understand this information. This will allow the Board to make more informed decisions going forward. We are also encouraged that the District is now in compliance with the PSC by having a separate Board Secretary and Board Treasurer.

Finding No. 2

Persistent Financial Operating Deficits, Budgeting Errors, and Increased Debt Service Resulted in a Substantial Negative General Fund Balance

Criteria relevant to the finding:

The Pennsylvania School Boards Association (PASBO) in its Annual Overview of Fiscal Health for the 2009-10 school year provided the following information relevant to the following fiscal benchmarks:

- Operating position is the difference between actual revenue and actual expenditures. Financial industry guidelines recommend that the district operating position always be positive (greater than zero).

Best business practices and/or general financial statement analysis tools require the following:

- A school district should maintain a trend of stable or increasing fund balances.
- Financial industry guidelines recommend that a fund balance should range between 5 and 10 percent of annual expenditures.

The benchmarks used for this objective were also based on best business practices established by several entities/agencies, including PASBO and the National Forum on Education Statistics.

The Manual of Accounting and Related Financial Procedures for Pennsylvania School Systems notes the importance of the operating budget cycle. This process includes budget preparation, budget analysis, board approval, adoption, budget control, and budget to actual reports.

The District experienced a significant decrease in its General Fund balance over the past three fiscal years. In order to assess the District’s financial stability, we reviewed several financial benchmarks to evaluate changes in its financial position over a period of six years from fiscal years ended June 30, 2010 through 2015.

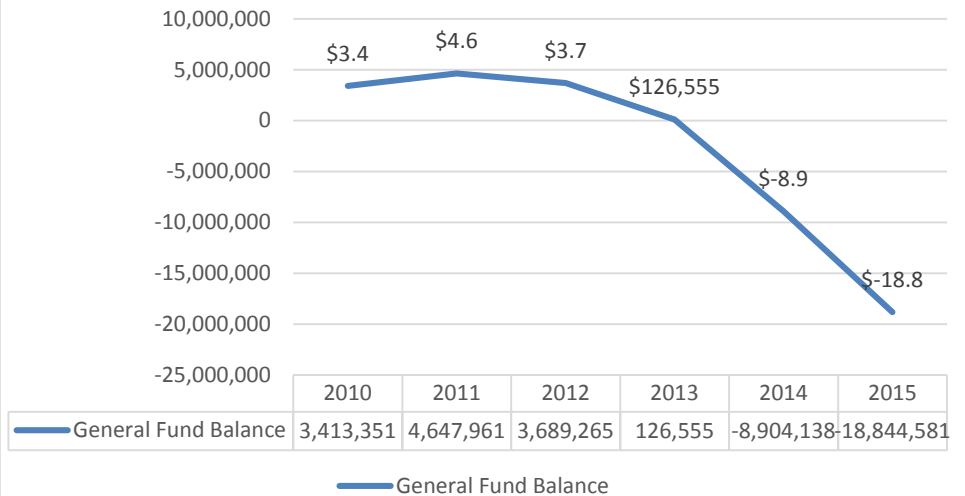
We found that the District had an operating deficit for five of the six years we reviewed. Penn Hills School District, similar to other districts in the Commonwealth, has experienced an increase in fixed expenditures, such as retirement, health care, and special education costs. However, it was primarily the District’s 2010 decision to incur \$130 million in debt for construction projects—without an adequate plan for repayment of that debt—that adversely impacted the District’s financial position.

General Fund

The District’s General Fund has decreased dramatically over the period reviewed as shown in the chart below.

Chart 1

Penn Hills SD General Fund Balance



Criteria relevant to the finding (continued):

The manual addresses each part of budgeting cycle in detail; however, we would like to emphasize the following:

- The accurate estimation of revenue has a critical impact on the budget.
- Analysis of historical trends is a reliable method for the projection of revenue and expenditures for budget preparation and analysis.
- During budget control, revenue collections and expenditures should be monitored on a monthly basis.

The annual General Fund budget is addressed under Section 687 (relating to Annual budget; additional or increased appropriations; transfer of funds) of the PSC, 24 P.S. § 6-687, and specifically subsection (b), which provides, in part:

“The Board of School Directors, after making such revisions and changes therein as appear advisable, shall adopt the budget and the necessary appropriation measures required to put it into effect. The total amount of such budget shall not exceed the amount of funds, including the proposed annual tax levy and State appropriation, available for school purposes in that district.”

As recently as 2012, the District’s General Fund was stable with a balance of close to \$3.7 million. However, rising expenditures have significantly depleted this General Fund balance resulting in a negative \$18.8 million balance as of fiscal year ended 2015.

As detailed in the criteria box, it is considered a best practice for school districts to maintain an unrestricted fund balance of no less than 10% of regular general fund operating revenues. With such a large negative General Fund balance, the District is far from operating in accordance with best practices, and it may be forced to resort to extreme measures just to maintain operations.

The District’s negative General Fund balance has adversely affected its credit rating, which was significantly downgraded on April 2, 2015.⁵ Borrowing costs will increase as a result of the District’s credit rating downgrade. This is especially detrimental for the District, since borrowing costs are one of the primary reasons for the District’s overall financial struggles.

General Fund Operating Deficits

A school district’s operating position (revenues minus expenditures) is one important indicator of a district’s financial health. The result of total expenditures exceeding total revenues is an operating deficit. The District’s cumulative operating deficit of more than \$27.5 million was a primary factor of the significant decrease in the General Fund balance.⁶ The District’s annual operating position is shown in the table on the next page.

⁵ The downgrade to B3 negative from Baa1 negative took place over two rating actions. The first was a downgrade to Ba3 review for downgrade, and the second to B3 negative.

⁶ The General Fund balance did not decrease at the same rate as the operating position solely due to inter-fund transfers from other district funds to the General Fund throughout the period reviewed.

Criteria relevant to the finding (continued):

Section 609 (related to Budgeted funds not to be used for other purposes or exceeded) of the PSC, 24 P.S. § 6-609, provides, in part:

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

The Government Finance Officers Association (GFOA) has developed Budgeting Best Practices for School Districts.

Among the best practices are:

General Fund Reserve. School districts should establish a formal process on the level of unrestricted fund balance that should be maintained in the general fund as a reserve to hedge against risk. The GFAO recommends, at a minimum, that school districts maintain an unrestricted fund balance in their general fund of no less than 10% of regular general fund operating revenues or regular general operating expenditures and operating transfers out.

Table 1

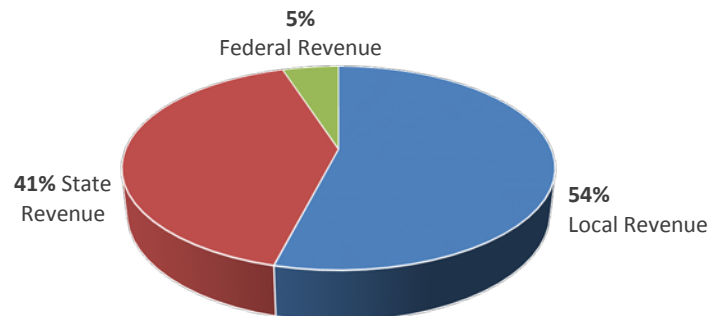
Penn Hills SD General Fund Operating Position⁷			
Fiscal Year ended June 30	Total Revenues	Total Expenditures	Operating Surplus/(Deficit)
2010	\$70,900,970	\$71,945,228	(\$1,044,258)
2011	\$75,618,790	\$74,649,042	\$969,748
2012	\$70,523,646	\$72,716,525	(\$2,192,879)
2013	\$74,070,086	\$77,699,752	(\$3,629,666)
2014	\$74,116,087	\$86,000,620	(\$11,884,533)
2015	\$79,647,327	\$89,451,873	(\$9,804,546)
Total:	\$444,876,906	\$472,463,040	(\$27,586,134)

The majority of the District’s \$27.5 million cumulative operating deficit was incurred in the fiscal years ended 2014 and 2015. The operating deficits in these two years were the result of significant increases in the District’s student transportation and debt service expenditures. Actual student transportation expenditures increased by more than \$2.5 million while actual debt service expenditures increased by \$6.5 million.

Revenues: Local, state, and federal revenues are the three components of the District’s “Total Revenues.” The following chart shows the composition of “Total Revenues” for the fiscal year ended 2015.

Chart 2⁸

**Penn Hills SD Revenue Composition
FY 2014-15**



⁷ Information obtained from the District’s Independent Auditor’s Report, *Statement of Revenue, Expenditures and Changes in Fund Balance*, fiscal years ending 2010 through 2015.

⁸ Information obtained from the District’s fiscal year ending 2015 Independent Auditor’s Report.

Total revenues increased 12 percent over the period reviewed primarily due to an increase in state revenue. Local revenue, mainly comprised of property taxes, has been stagnant largely due to the District's decision to not raise local property taxes from 2010 through 2013, and then reducing the property tax in 2014. The reduction in property taxes was implemented even though the District was experiencing an increase in fixed expenditures and was saddled with significant debt service payments related to the bond issuance to fund the District-wide construction projects. The District's decision to reduce property taxes was a significant factor in the District's operating deficits. A reduction in property taxes decreased the District's local revenue, which as shown in Chart 2, is the largest component of the District's total revenue.

Expenditures. The District's total expenditures increased by 24 percent - double the rate that total revenues increased over the same time period. The majority of the increase in expenditures occurred during the fiscal years 2014 and 2015.

As previously stated, school districts across the Commonwealth experienced increases in their retirement costs, and the Penn Hills School District was no exception.

The District's employer contribution rate more than tripled over the review period. The contribution rate for fiscal year 2010 was 4.78 percent of total payroll costs and increased to 21.4 percent in fiscal year 2015. We also found that special education costs have increased from \$9.4 million in 2010 to over \$12 million for the fiscal year 2015. However, it was the substantial increase in the District's debt service expenses that put the District on a perilous financial path.

Increase in Debt Service Expenditures

The District was relatively debt free prior to the fiscal year 2010. As of the fiscal year 2009, the District's total outstanding debt was less than \$11 million. But during fiscal year 2010, the District borrowed nearly \$135 million to cover the cost of constructing a new high school, a new elementary center and renovating the middle school.

The District hired an architectural firm to conduct a feasibility study of the projects. The architectural firm stated in its feasibility study report that the construction of the new high school would require a 2.275 millage rate⁹ increase (real estate taxes) and the new elementary center would require an additional 1.167 millage rate increase. The architect's report, related to the new elementary center, indicated that the tax increase could be avoided if the District reduced staffing levels when it consolidated three existing elementary schools into the new elementary center. These actions would allow the District to achieve cost savings that would be sufficient to cover the debt service requirements.

Despite the architectural firms' recommendation to raise taxes, the District's former Director publicly stated that the District was not anticipating tax increases to cover the debt service requirements. Instead, the District was relying on \$5 million in annual cost savings from the consolidation of the elementary schools. However, the District did not reduce staffing levels as suggested by the architect, and the former Director never disclosed the specifics of how the estimated \$5 million in costs savings would be achieved.

Because the District did not reduce staff when it consolidated the elementary schools, it did not realize any cost savings. Without the estimated cost savings, coupled with the decision to not raise local property taxes, the District was faced with debt service expenditures that have crippled the District's finances.

The District's total outstanding debt as of June 30, 2015, was \$167,370,959. This debt amount is greater than the District's total combined revenue of \$153,763,414 for the fiscal years 2014 and 2015 (see annual revenues on Table 1). Because the District engaged in multiple refinancing efforts, the total outstanding debt has increased significantly from the original amount of \$134,755,000 that was incurred for the District wide construction projects.

⁹ The millage rate is the amount per \$1,000 that is used to calculate taxes on property. The millage rate is multiplied by total taxable value of the property to arrive at the property taxes due.

Total Expenditures Exceeded Budgeted Amounts

The District’s total expenditures exceeded budgeted amounts for four fiscal years in a row (fiscal years 2012 through 2015). While over expending the budget is a direct violation of the PSC, it is also a red flag to the District that its financial position could be in jeopardy.

The following table presents the District’s total actual expenditures compared to budgeted amounts.

Table 2

Penn Hills SD Budget Vs. Actual Expenditures Fiscal Years 2010 to 2015			
Fiscal Year ending June 30	Budgeted Amount ¹⁰	Actual Expenditures ¹¹	(Under)/ Over Budget
2010	\$76,444,068	\$71,945,228	(\$4,498,840)
2011	\$77,020,343	\$74,649,042	(\$2,371,301)
2012	\$72,281,422	\$72,716,525	\$435,103
2013	\$74,477,616	\$77,651,434	\$3,173,818
2014	\$75,518,635	\$85,599,557	\$10,080,922
2015	\$79,105,297	\$89,451,873	\$10,346,576
Total:	\$454,847,381	\$472,013,659	\$17,166,278

We reviewed the budgeted expenses for several line items and compared them to actual expenses and found that transportation and debt service expenditures were significantly under budgeted which was the primary reason that the District overspent its total budget. We discuss the details of these budgeting errors later in this finding.

Consequently, as the District began to overspend budgetary amounts, the District began to incur annual operating deficits, which ultimately reduced the District’s General Fund balance.

Failure to Properly Budget for Debt Service

Requirements. We reviewed the District’s annual budget documents and found that the District did not accurately budget for its debt service requirements in 2014 and 2015 (see table below). Specifically, the District’s actual debt

¹⁰ Information obtained from the District’s final budget (PDE-2028) for the fiscal years ending 2010 through 2015.

¹¹ Information obtained from the District’s Independent Auditor’s Report, Statement of Revenue, Expenditures and Changes in Fund Balance, fiscal years ending 2010 through 2015.

service expense for these two years combined was over \$10 million more than the budgeted amount.

The errors in budgeting for debt service requirement was avoidable because debt service requirements were known at the time budgets were prepared. Effective budgeting practices suggest that expenditures with fixed costs should be identified accurately at the start of the budgeting process. The failure to appropriately budget for debt service payments was one of the major causes of the District’s significant operating deficit and negative General Fund balance in fiscal years ending 2014 and 2015.

Also, by not accurately budgeting for debt service requirements, the true financial position of the District was not known until the end of the fiscal year. If the District had accurately budgeted its debt service requirements, the District’s financial challenges would have become apparent at the beginning of the budgeting process and the Board would have had more reliable data to make informed decisions.

Table 3

Penn Hills SD Debt Service Payments Comparison of Budget to Actual			
Fiscal Year ending June 30	Budgeted Amount ¹²	Actual Expenditures ¹³	(Under)/ Over Budget
2010	\$3,513,098	\$2,655,570	(\$857,528)
2011	\$2,721,400	\$2,648,881	(\$72,519)
2012	\$2,642,196	\$2,642,196	-----
2013	\$4,578,480	\$4,451,980	(\$126,500)
2014	\$4,515,279	\$11,056,766	\$6,541,487
2015	\$7,460,953	\$10,960,071	\$3,499,118
Total:	\$25,431,406	\$34,415,464	\$8,984,058

Basic Education Subsidy Advance. As previously stated and shown in the table above, the District’s debt service increased dramatically in fiscal years 2014 and 2015. Because the District did not accurately budget for these expenditures, the District had difficulty making the required payments. On January 13, 2015, the District’s former Superintendent, acting on the advice of the former

¹² Information obtained from the District’s final budget (PDE-2028) for the fiscal years ending 2010 through 2015.

¹³ Information obtained from the District’s Independent Auditor’s Report, Statement of Revenue, Expenditures and Changes in Fund Balance, fiscal years ending 2010 through 2015

Director, submitted a request to PDE for a \$3.1 million advance in the District’s basic education subsidy to make a debt service payment that was due on April 1, 2015.

PDE granted the request and advanced the District \$3.1 million on March 31, 2015. This advance came too late for the District to meet its April 1 debt service requirements. As a result, the \$3.1 million debt service payment was made by the Pennsylvania School District Enhanced Intercept Program.¹⁴ Without the intervention of this Commonwealth intercept program, the District would have missed the debt service payment and defaulted on this obligation.

Failure to Appropriately Budget Student Transportation Expenditures. The District also experienced a 42 percent increase in actual student transportation expenditures over the period reviewed. We found that transportation expenditures were also not accurately budgeted by the District’s former Director (see table below). Similar to the District’s debt service expenditures, the actual transportation expenditures greatly exceeded budgeted amounts. As shown on the following table, actual student transportation expenditures exceeded the budgeted amount for five of the six fiscal years reviewed.

Table 4

Penn Hills SD Transportation Expenditures Comparison of Budgeted to Actual			
Fiscal Year ending June 30	Budgeted Amount¹⁵	Actual Expenditures¹⁶	(Under)/ Over Budget
2010	\$5,508,334	\$5,636,062	\$127,728
2011	\$6,287,971	\$6,166,070	(\$121,901)
2012	\$4,832,065	\$5,836,667	\$1,004,602
2013	\$4,401,936	\$5,506,736	\$1,104,800
2014	\$5,075,301	\$6,030,808	\$955,507
2015	\$4,588,525	\$8,015,895	\$3,427,370
Total:	\$30,694,132	\$37,192,238	\$6,498,106

Based on the information presented above, it appears that historical trends and actual expenses were not considered

¹⁴ Section 633 (relating to Reports to Secretary of Education; withholding state appropriations) of the PSC, 24 P.S. § 6-633, as amended by Act 150 of 1975 (as last amended by Act 70 of 2004).

¹⁵ Information obtained from the District’s final budget (PDE-2028) for the fiscal years ending 2010 through 2015.

¹⁶ Information obtained from the District’s Independent Auditor’s Report, Statement of Revenue, Expenditures and Changes in Fund Balance, fiscal years ending 2010 through 2015.

when the former Director developed the budgeted expenses for student transportation.

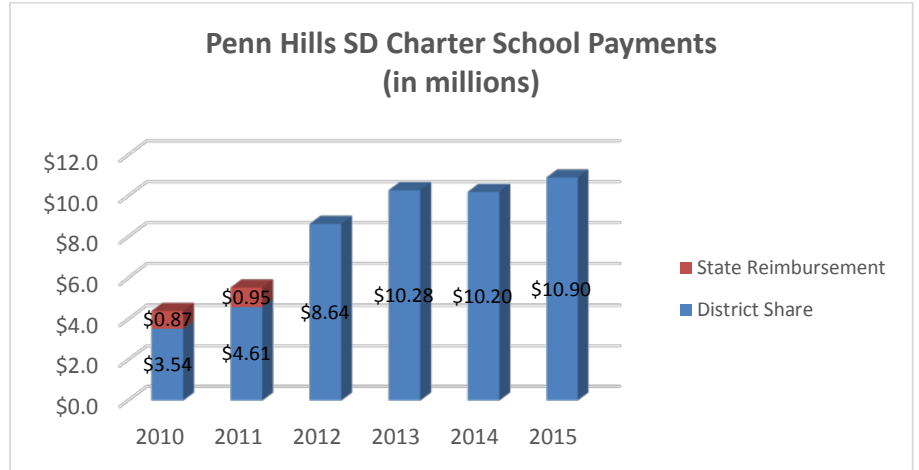
This conclusion is demonstrated by the transportation budgets for fiscal years 2013 and 2015. In both years, the District budgeted less than the previous year, even though actual amounts significantly exceeded budgeted amounts for the previous year. It is difficult to understand why the District would reduce the 2015 budget to \$4.5 million when the actual expenditures for 2014 were more than \$6 million. The significant increase in transportation expenses was caused by the District's poor internal controls and inadequate record keeping. These deficiencies are discussed in further detail in Finding No. 5 and Finding No. 6 of this report.

Increase in Charter School Expenditures

The District's charter school tuition costs more than doubled from 2010 through 2015, with payments totaling nearly \$50 million over the six year period. These increasing charter school costs not only adversely affected the District's already strained financial status but also reduced the funds available to support academic programs for District students.

The chart below illustrates the increase in the District's required payments to charter schools. The financial burden on the District grew from \$4.41 million in fiscal year ending 2010 to \$10.9 million in fiscal year ending 2015. The Commonwealth eliminated its partial reimbursements for charter schools after the 2011 budget, exacerbating the already growing financial strain on the District.

Chart 3

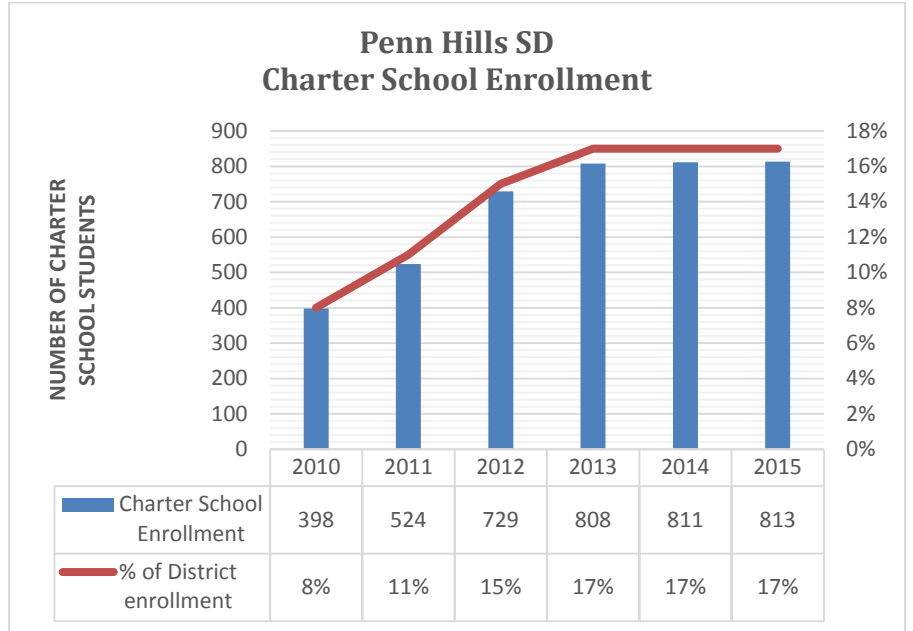


The charter school funding formula, together with the increasing charter school enrollment, produced an increase in the District's financial obligation each fiscal year from 2010 through 2015, except for 2014. Factoring in the partial reimbursement from the Commonwealth in 2010 and 2011, the impact on the District's total expenditures increased from 5 percent in fiscal year ending 2010 to 12 percent in fiscal year ending 2015.

District enrollment in charter schools more than doubled from 2010 to 2013 to over 800 students; whereas the District's overall enrollment decreased by 4 percent to about 4,700 in the same period. As a result, charter school enrollment, as a percentage of District enrollment, more than doubled from 8 percent in fiscal year ending 2010 to 17 percent in fiscal year ending 2015.

The following chart demonstrates the growth in charter school enrollment and its relationship to the District's enrollment.

Chart 4



Possible Financial Recovery Status

Act 141 of 2012 permits PDE and the Secretary of Education to place up to nine school districts at a time in Financial Recovery Status.¹⁷ The Act provides several reasons to declare a school district in financial recovery status. One of the reasons is a school district receiving an advance of its basic education subsidy.¹⁸ As stated previously, Penn Hills School District received such an advance on March 31, 2015; therefore, the District is a prime candidate to be declared in financial recovery status.

School districts in financial recovery status have a PDE appointed chief recovery officer whose responsibilities include oversight of the district and the development of a district-wide financial recovery plan. If placed in financial recovery status, the district will lose local oversight of district operations and will be forced to make operational changes that result in lower expenditures and/or increased revenue.

¹⁷ 24 P.S. § 6-601-A *et seq.*

¹⁸ Under Act 141 of 2012, a school district that receives an advance of its basic education subsidy is deemed a *Moderate Financial Recovery School District*. See Subsection on “Process for Moderate Financial Recovery School Districts” (24 P.S. § 6-651-A *et seq.*).

Conclusion

Over the course of the audit period, the District's financial position significantly deteriorated. Similar to other school districts, the Penn Hills School District incurred increased fixed costs related to retirement contributions, employee health care, and charter schools. Yet, the District exacerbated its financial problems by failing to manage those financial activities it could control.

Most notably, the District did not ensure that it had a long-term plan to cover the cost of the district-wide capital project that resulted in a \$130 million increase in long-term debt. It did not increase local revenues and did not achieve the cost savings that were anticipated with the consolidation of the elementary schools. The lack of a plan, coupled with the District's failure to appropriately budget for the increase in annual debt service, are the primary factors that led to the negative \$18.8 million General Fund balance as of June 30, 2015.

As discussed in Finding No. 1, ineffective governance, including weak oversight of the former Director, also contributed to financial decline and led to a request to PDE for an advance of the District's basic education subsidy. Consequently, the District is now a prime candidate for designation in financial recovery status by PDE.

It is important to note that during our fieldwork, the District's new leadership team, including the current Superintendent and Business Manager, began to implement corrective action as weaknesses were identified. In addition, the District continues its efforts to conduct thorough analyses of all District operations, as well as reviews of expenditures and revenue sources. This effort will hopefully allow the District to develop a business model that can stabilize the District's financial position.

Recommendations

The *Penn Hills School District* should:

1. Prepare a multi-year budget that adequately reflects annual commitments to help ensure that the District is prepared to meet future obligations.

2. Evaluate all revenue streams and discuss the possibility of increasing local revenue through an increase in property taxes to help with the debt service payments.
3. Evaluate the District's total outstanding debt and debt service obligations for future years to devise a realistic yearly budgetary amount. All future budgets should be developed after factoring the debt service obligation for that year.
4. Review all variable costs to ensure that revenues are being spent in the most needed and cost effective areas. Specifically, review the District's transportation operations and charter school expenditures to ensure District funds are being spent wisely and are protected from abuse.
5. Ensure that the District's Board is provided with sufficient, reliable, and accurate information in order to make informed decisions.

Management Response

District management provided the following response for each recommendation:

1. The Business Office has already started the process of preparing a five-year budget to help assist the Board and Public in understanding the future financial obligations. In addition, the Board is presented with the cumulative effect of the budget in its current draft state.
2. The Board acted in the 2015-16 budget by raising taxes to the index. They have also requested the 2016-2017 budget be prepared with a 1.5 mil increase using the Act 1 index, special education and retirement exceptions. This will net the District almost \$2.6 M dollar in new tax revenue.
3. The 2016-2017 budget includes the actual debt service payments required. The five-year budgets also include future obligations that include increased principal payments.

4. The District has watched the transportation department and charter school enrollments very carefully. We are on target to spend just over \$6M in Transportation costs this school year, a \$2M reduction for the 2014-2015 school year. We have also created our own Cyber program and brought back over 40 students from Charter Schools. The Charter enrollments are down and staying at that level.

NOTE: Page 17 paragraph 1. The District complied with the recommended “Revenue Neutral” calculation in the 2014 year where the Auditor General suggests a property tax reduction. The real estate tax revenue received that year was in-line with the prior years and demonstrates that tax rates were not increased or decreased.

Auditor Conclusion

We feel strongly that the development of a five year budget/financial plan will be vital in the District’s fiscal recovery. We are encouraged that the District has proactively budgeted for future debt service requirements and believe this will help the District more accurately determine the District’s financial position.

In 2014, an ongoing county wide property tax re-assessment was underway in Allegheny County. The Penn Hills School District expected property values in the District to increase as a result of the re-assessment. In preparation of the expected increase in property values, the District took a “Revenue Neutral” approach and lowered the millage rate. This approach was referred to as “Revenue Neutral” due to the fact that higher property values coupled with a lower millage rate would generate the same expected local tax revenue for the District. Due to the District’s financial condition in 2014, during this re-assessment, it would have been financially beneficial for the District to not lower millage rates.

We will evaluate the District’s corrective actions during our next audit of the District.

Finding No. 3

The District Violated its Policy Governing the Use of Procurement Cards and did not Monitor Purchases

Criteria relevant to the finding:

Board Policy No. 625, approved on March 3, 2009, states in relevant part;

“the Board approves the use of procurement cards for permissible purchases and/or services to be purchased for the official use of the Penn Hills School District by designated employees to improve the efficiency of purchasing activities, reduce processing expenses, improve controls for small-dollar purchases, and streamline purchases and payment procedures. The board directs the administration to establish safeguards to prevent misuse of such cards.

Specifically, the policy states:

1. A list of authorized users of procurement cards shall be maintained in the business office and shall include employees in designated positions.
2. All use of procurement cards shall be supervised and monitored on a regular basis by the Director of Business Affairs, who shall ensure the use of such cards is in accordance with funds budgeted for this purpose.
3. An employee authorized to use a procurement card shall maintain adequate security of the card while it is in his/her possession.

Our review of the District’s procurement card practices revealed numerous violations of board-approved policies, including a years-long persistent failure by the District to review, authorize, and account for purchases. As a result, misuse of the procurement cards went unnoticed for several years, and the following occurred:

- Numerous employees had unmonitored access to 21 total cards in circulation.
- Numerous purchases lacked supporting receipts.
- Unnecessary, non-emergency purchases were made without regard to budgets.
- Some purchases were made by employees for items not delivered to the District and appear to have been for personal use.

The District issued two types of cards, 18 general procurement cards and 3 retailer-specific cards. As shown in the table below, the District purchased more than \$424,000 using these cards in the three-year audit period ending June 30, 2015.

Table 1

Penn Hills SD Procurement Card Expenses			
Fiscal Year	General Cards (18)	Retailer Specific (3)	Annual Total
2013	\$164,772	\$7,724	\$172,496
2014	\$112,634	\$12,214	\$124,848
2015	\$115,708	\$11,093	\$126,801
Total	\$393,114	\$31,031	\$424,145

In addition to procurement card misuse, the District also maintained an open account at a local hardware store with lax authorization and procurement procedures. Purchases

Criteria relevant to the finding (continued):

4. Only daytime and nighttime supervisors of maintenance, transportation director, and the district accountant shall have access to procurement cards. Each of these employees may allow an employee to use the card for district purchases but not without justification. It is the responsibility of the card holder to reconcile with the employee once receipts have been submitted.
5. After receipts have been justified to the immediate supervisor, the Director of Business Affairs or designee must reconcile receipts to original invoices.
6. Each employee using a district procurement card shall sign a card usage agreement and receive training on applicable policies and procedures.
7. Procurement cards shall be used only for authorized district purchases and shall not be used for personal purchases or other use that is contrary to laws, regulations, or internal policies.
8. Any use of procurement cards for personal use or unauthorized purchase will result in termination of the employee.
9. Business office receives the consolidated invoice for payment and must match to original receipts.
10. Business office verifies all reconciliations and investigates discrepancies and Director of Business Affairs signs as correct.
11. Business office will conduct random audits of cardholder statements to justify purchases.
12. Procurement cards are only to be used for emergency purposes and not lack of preparation.

at this store exceeded \$21,500 for the audit period. Our findings on this account are discussed later.

Plenty of Cards and Plenty of Access

The District’s board-approved Policy No. 625 (#4) restricted access to procurement cards to four positions:

- Daytime maintenance supervisor
- Nighttime maintenance supervisor
- Transportation director
- District accountant

While the policy allowed the above-listed employees to let other employees use their cards—a caveat that we would not recommend—they were responsible for justifying other employees’ usage, and they were also responsible for accounting for purchases and receipts.

We found the District expressly violated the policy of limiting access to the four positions listed above when it issued 21 procurement cards to a number of other District employees, including:

- School principals
- The athletic director
- Non-supervisory maintenance employees
- The secretary to the superintendent
- Other employees

In addition, one of the three retailer-specific procurement cards was assigned to “anyone in uniform.” This authorization criteria inherently weakened the internal control over access to that particular card because anyone wearing a District uniform could potentially use the card regardless of whether he or she was an actual employee with authorization to use it.

Former Director’s Failure to Monitor Expenses

We found the District’s former Director did not perform many of the responsibilities assigned to him related to procurement cards, such as reviewing all receipts prior to authorizing payment for procurement card purchases.

We reviewed all general procurement card purchases, as well as retailer-specific purchases for all three years in our audit period. We found that procurement card invoices were paid without the required matching receipts to support specific purchases. District business office employees stated that the former Director, on a regular basis, authorized payment without receipts. They also stated that the former Director did not review purchases to verify that items purchased were within budgetary allowances and were emergency in nature.

The District's current Superintendent closed all of the District's active procurement cards on June 10, 2015. The District then initiated an investigation into procurement card usage. The former Director told the administration that even though it was his responsibility to verify receipts before payment, it was realistically impossible due to the number of purchases being made with procurement cards. The District's failure to limit the number of procurement cards in circulation appears to have been a factor in weakening the ability of the District to monitor procurement card activity.

Daily and Non-Emergency Usage

Board Policy 625 No. 12 restricts the use of procurement cards to emergency purposes. This type of restriction helps to minimize the risk of incurring expenses in excess of budgets or for items not essential to District operations.

Our review of the procurement cards' transaction history showed they were used on a daily basis to purchase non-emergency items. For example, in August 2012, District procurement cards were used multiple times to purchase the following:

- School supplies
- Doughnuts for meetings
- Lunch at local restaurants
- Sports equipment
- Hotel rooms for consultants providing district training

None of these expenses were emergency in nature, and by charging such items to the procurement cards, the District would not have been able to perform an important internal

control procedure – ensuring sufficient unexpended budgeted funds are available *prior* to the expenditure of funds to ensure the expenditure does not exceed budgetary limits. Charging such items to the procurement cards also prevented the evaluation of the propriety of the expenditure prior to the transaction being made.

Examples of Procurement Card Abuse

The District’s internal investigation revealed multiple examples of abuse that occurred with the District’s retailer-specific procurement cards. Examples include the following:

- On September 22, 2014, a non-supervisory maintenance employee purchased a residential water heater for \$358.98. The invoice authorizing payment for this item was approved by the former Director, despite the lack of a receipt. Current District officials verified this purchase through the retailer’s security camera footage. The water heater was not found at any District facilities.
- A second non-supervisory maintenance employee purchased asphalt sealant in August 2014, even though the District did not have a need for asphalt sealant. This purchase was not made during the employee’s work hours. The invoice authorizing payment for this item was also approved by the former Director, despite the lack of a receipt.

An Unmonitored Account at Local Hardware Store

Similar to the procurement card assigned to “anyone in uniform,” the District also has operated an open account with a local hardware store. During the audit period, this arrangement enabled anyone wearing a District uniform to make purchases from that store. No procurement cards were used; instead, the purchaser was merely required to sign a physical log maintained by the store to track District purchases. Again, the internal control over this store account was inherently weak due to easy access.

The table below shows the amounts paid by the District to the local hardware store during the audit period.

Table 2

Penn Hills SD Local Hardware Store Expenditures	
Fiscal Year	Expenditures
2013	\$5,710
2014	\$8,081
2015	\$7,718
Total	\$21,509

We found the following problems as part of our review of transactions related to this account:

1. The signature of the purchaser on the account logs was illegible for a significant number of transactions, and we, therefore, could not verify the purchaser was a District employee.
2. Even when we could verify the name of an employee of the District, we had no way of knowing whether that employee actually signed for the purchase or if someone else signed.

We asked current business office employees how this account was monitored, and we were told that the accounts payable clerk was supposed to reconcile the invoices from the store to the receipts turned in by employees. In circumstances where receipts were not produced, the former Director authorized payment of the invoices without investigating whether the purchases with missing receipts were valid and appropriate.

The District still maintains this open account with the local hardware store; however, according to District officials, stricter controls have been implemented. For example, purchases now require a purchase order and prior approval from the Superintendent. Also, the District now limits purchases from the store to just two employees and the Superintendent.

Recommendations

The Penn Hills School District should:

1. Since the District currently has no procurement cards in active use, we do not have specific recommendations. However, if the Board authorizes the use of procurement cards in the future, it should review and update its policies, and then it should timely ensure that those policies are being followed by regularly reviewing procurement card spending and reconciliation reports.
2. Require someone who is independent of both the facilities department and the business office to routinely review the purchases made on the open account with the local hardware store to ensure that all purchases are pre-approved, accompanied by a purchase order, and for appropriate District purposes. All discrepancies should be investigated and resolved in a timely manner.
3. The Board should timely review and approve all reconciliation reports on the open account at the local hardware store.

Management Response

District management provided the following response for each recommendation:

1. As stated, the District has destroyed and stopped the use of all procurement cards.
2. All requisitions are reviewed and approved by the Business Manager and the Superintendent before becoming a purchase order. The purchases are reconciled monthly by the facilities department and accounts payable before payment is made.
3. As recommended, the District will now include the reconciliation reports in the monthly list-of-bills to the Board.

Auditor Conclusion

We believe that the District's abolishment of procurement cards represents a positive step in controlling expenses. We are encouraged by the new procedures adopted to control the remaining open vendor account. We will review this and other corrective actions during our next audit of the District.

Finding No. 4

The District Failed To Ensure that Approximately \$22,000 in Ticket Sales from 18 Sporting Events Were Deposited

Criteria relevant to the finding:

Section 511 (relating to School athletics, publications, and organizations) of the PSC, subsection (d) states: “The treasurer or custodial of such funds shall furnish to the school district a proper bond, in such amount and with such surety or sureties as the board shall approve, conditioned upon the faithful performance of his duties as treasurer or custodian.” Furthermore, “The treasurer or custodian shall be required to maintain an accounting system approved by the board, shall deposit the funds in a depository approved by the board, shall submit a financial statement to the board quarterly or oftener, at the direction of the board, and shall submit the accounts to be audited in like manner as the accounts of the school district.”

The September 2014 revision of *Standards for Internal Control in the Federal Government*, issued by the Comptroller General of the United States and commonly referred to as *The Green Book*, under Design of Appropriate Types of Control Activities, Section 10.03 relating to Physical control over vulnerable assets states: “Management designs appropriate types of control activities for the entity’s internal control system. Control activities help management fulfill responsibilities and address identified risk responses in the internal control system.”

Our audit of the District’s Athletic Fund from July 1, 2012 through June 30, 2015, revealed that approximately \$22,000 collected as admission fees to 18 District sporting events were not deposited into the District’s General Fund. The District’s lack of written procedures outlining the duties of District personnel involved in collecting, safeguarding, and depositing admission fees from sporting events, coupled with poor oversight and monitoring of this process, resulted in the loss of much needed revenue for the District.

Background

The District has numerous athletic teams where admission fees are collected at its sporting events.¹⁹ All money collected at a sporting event is supposed to be deposited in the District’s General Fund. According to District officials, the District’s Athletic Director is responsible for assigning individuals the responsibility to collect admission fees at sporting events held at the District.

The District uses an event sheet to track the number of tickets sold at each sporting event and the corresponding cash collected for tickets sold. After each sporting event, the Athletic Director was to reconcile the cash collected to the number of tickets sold as documented on the event sheet. Since most sporting events are held outside of normal school hours, the Athletic Director was responsible for safeguarding the cash until it could be physically given to the business office. The business office was responsible for recording the receipt of cash and for depositing the funds into the District’s General Fund.

The Athletic Director received a receipt when the money from a sporting event was physically given to the business office. The receipt detailed the amount of cash turned over

¹⁹ District sporting events that charge admission are football, boys’ and girls’ basketball, wrestling, boys’ volleyball, and swimming. There is no admission charge for girls’ volleyball.

Criteria relevant to finding (continued):

Green Book (continued)

Also, under Section 10.03, states: “Management establishes physical control to secure and safeguard vulnerable assets. Examples include security for and limited access to assets such as cash, securities, inventories, and equipment that might be vulnerable to risk of loss or unauthorized use. Management periodically counts and compares such assets to control records.”

Board Policy:

Penn Hills School District Board Policy No.000 specifically states, “The policies and procedures adopted by the Board establish the general parameters within which the daily operations for the school district are to be governed. Administrative regulations for carrying out and implementing Board policies are developed and implemented by the administration under the direction of the Superintendent.”

The District is responsible for creating job descriptions which fully explain the roles and responsibilities for each position in the District.

to the business office and the date and type of the applicable sporting event.

Missing Deposits

We reviewed all sporting events held by the District for the 2012-13, 2013-14, and 2014-15 school years and found 18 sporting events, including two football games, where admission fees were collected, but we could not find evidence that the funds were deposited into the District’s account. The following chart details the sporting events and amount of missing funds.

Penn Hills SD Athletic Fund Schedule of Missing Deposits			
Event Date	Sporting Event	Admission Fees	
12/10/12	Boys Basketball	\$789	Actual
12/19/12	Wrestling	\$219	Estimated
8/30/13	Football	\$6,383	Estimated
10/4/13	Football	\$2,920	Actual*
12/11/13	Girls Basketball	\$340	Estimated
12/17/13	Boys Basketball	\$583	Estimated
12/18/13	Wrestling	\$79	Estimated
12/18/13	Swimming	\$250	Estimated
1/2/14	Swimming	\$250	Estimated
4/22/14	Boys Volleyball	\$222	Estimated
8/29/14	Football	\$7,497	Actual
1/9/15	Boys Basketball	\$385	Estimated
1/9/15	Girls Basketball	\$385	Estimated
1/20/15	Swimming	\$244	Actual
2/3/15	Swimming	\$207	Estimated
2/5/15	Swimming	\$98	Actual
2/6/15	Boys Basketball	\$760	Actual
2/6/15	Girls Basketball	\$760	Actual
Total		\$22,371	

* The total amount collected was \$6,655 but only \$3,735 was deposited; therefore, it appears that \$2,920 was not deposited.

In 6 of those 18 sporting events, the Athletic Director provided us with a receipt signed by the former Director of Business Affairs’ secretary confirming the actual amount of money that was physically turned over to the business office for recording and deposit.

For the remaining 11 sporting events, the District could not provide an event sheet receipt from the business office or a verification of deposit. While the District is confident that admission fees were collected at each of these sporting

events, there was no documentation to verify that the money was turned into the business office or ever deposited.

Without event sheets receipts documenting the actual amount collected at each event, we had to estimate the admission fees collected but never deposited. We determined the estimated admission fees for each event by calculating the average attendance for the sporting team's other events during the same season. We reviewed our estimated admission fees with District officials. The District agreed with our estimates of admission fees collected.

According to the Athletic Director, all money collected from sporting events was turned over to the business office, but the receipts for these 11 events could not be located. District officials could not provide an explanation of why the money from these events was not deposited. Both the former Director of Business Affairs (former Director) and the former Director's secretary, who signed the receipts, are no longer employed by the District.

Weak Internal Controls and Poor Management Oversight

We found that the District did not develop and implement Board approved policies and administrative procedures governing athletic event admission fees. For example, the District did not have basic internal control procedures such as a reconciliation of the event sheet receipts to the bank deposits. In addition, we found that the District did not conduct adequate monitoring and oversight procedures of such a high risk asset like cash. This lack of oversight was evident by the District's failure to identify missing deposits over a three year period.

As previously stated, much of the responsibility for athletic event admission fees fell to the Athletic Director, who did not have the benefit of documented procedures to use as guidance for collecting, safeguarding, and depositing admission fees.

We reviewed the Athletic Director's job description and found that it did not contain provisions related to duties and responsibilities regarding the Athletic Fund. Furthermore,

the PSC requires custodians of district funds to be bonded. We found that the Athletic Director was not bonded separately for his role as custodian of the money collected at sporting events.

Summary

The District's failure to implement adequate internal controls over the Athletic Fund is troubling because it created an environment without accountability and resulted in numerous instances of money not being properly accounted for or deposited. Further, due to the poor monitoring and oversight, the missing deposits went unnoticed by District officials for multiple school years.

The Athletic Fund is a highly vulnerable program area for which staff have a duty to ensure the safeguarding, recording, and depositing of cash receipts. A district of this size has numerous athletic teams and venues and, therefore, cash receipts can be substantial. Without adequate internal controls and oversight, there is an increased risk for fraud and abuse which can potentially lead to lost revenue.

Recommendations

The *Penn Hills School District* should:

1. Develop a Board approved policy and administrative procedures to ensure all money collected at sporting events is timely and accurately deposited in the General Fund. These policies and procedures should include, at a minimum, provisions related to how money is collected, safeguarded, recorded, and deposited.
2. Develop and implement monitoring and oversight procedures to ensure that District staff comply with the Board approved policies.
3. Update the Athletics Director job description to include his role and responsibilities in regard to the Athletic Fund.
4. Purchase a separate bond for the Athletics Director for his role as custodian of the Athletic Fund.

Management Response

District management provided the following response to each recommendation:

1. The Business Manager and Athletic Director have created internal control manual specific to cash collection at athletic events. This guide includes a clarification on how monies should be collected, safeguarded, recorded and deposited. It also includes the proper documentation required to be kept at the Athletic Office and the Business Office.
2. The Business Manager is in the process of developing an internal control guide that documents the procedures for oversight and internal auditing.
3. The Athletic Director's job description is in the process of being revised to comply with the aforementioned policies and procedures.
4. The 2016-2017 Budget will include monies for the separate bonding of the Athletic Director.

Auditor Conclusion

We are encouraged that the District has begun to implement our recommendations. We believe that developing and implementing proper internal control procedures to safeguard and document all gate receipts received at sporting events is vital due to the amount of money collected at these events. We will determine the effectiveness of these and any other corrective actions during our next audit.

Finding No. 5

The District’s Failure to Monitor its Transportation Contractor Resulted in Misappropriation of District Fuel of Between \$260,000 and \$384,500

Criteria relevant to the finding:

Penn Hills Board Policy 601 places the following responsibilities on the Director of Business Affairs:

“The Director of Business Affairs shall review monthly the financial operations, report to the Board on effectiveness and recommended improvements, and prepare the administrative procedures for sound district and school fiscal operations.”

“The Board directs the Director of Business Affairs to establish sound accounting procedures based upon recommendations of the district auditor and state and federal government, institute effective business practices, and recommend appropriate equipment and technology when necessary.”

The Green Book Section 10.03 states in part:

“Management designs appropriate types of control activities for the entity’s internal control system. Control activities help management fulfill responsibilities and address identified risk responses in the internal control system.”

“Management establishes physical control to secure and safeguard vulnerable assets. Examples include security for a limited access to assets such as cash, securities, inventories, and equipment that might be vulnerable to risk of loss or unauthorized use.” *See US Government Accountability Office’s The Green Book.*

The District failed to monitor the fuel usage of its transportation contractor (Contractor), resulting in a 117 percent spike in the District’s fuel costs. It also failed to negotiate and implement an effective lease agreement for the Contractor’s use of a District maintenance facility, which is where the District stores its fuel. Finally, it failed to limit the Contractor’s access to District fuel supplies, which resulted in the misappropriation of District fuel costing between \$260,000 and \$384,500. This added to the stress on the District’s already burdened financial position.

We believe the actions by the Contractor warrant termination of the contract at the end of the 2015-16 school year and a resolution to prohibit this vendor from bidding on a new contract with the District.

Terms of the Transportation Contract

At the District’s April 28, 2014 board meeting, the Board approved an agreement between the District and the Contractor. The agreement stated that the Contractor would provide transportation services to District students beginning on July 1, 2014 through June 30, 2019. The agreement was approved by the Board on the recommendation of the District’s former Superintendent and former Director of Business Affairs (former Director).

The District agreed to pay the Contractor a daily rate per vehicle as opposed to paying the contractor based on miles traveled and students transported. (As discussed in Finding No. 6, this is an inefficient payment method that has led to increasing transportation expenditures to the District.) The agreement also stipulated that the District would be responsible for 100 percent of the cost of all fuel used by the Contractor to provide transportation for the District. The Contractor would be responsible for maintaining transportation records to substantiate all fuel purchases.

In addition to the transportation agreement between the parties, the former Director stated, at the April 28, 2014 board meeting, that the Contractor also wanted to lease the

District's maintenance facility for approximately \$5,000 per month. The District previously used the maintenance facility as a bus garage when the District provided transportation to students. It also used the maintenance facility to store and disburse its purchased fuel. The Board agreed to the proposed lease agreement primarily to receive the lease revenue that would be generated through this agreement.

Unauthorized Fuel Usage by the Contractor

The District failed to limit the Contractor's access to the fuel stored at the maintenance facility and to monitor the Contractor's fuel usage. The District did not ensure that a District employee was present at the maintenance facility to observe the Contractor fueling its vehicles. District officials admitted to neglecting to ensure that the key card system used to fuel individual vehicles was being properly used by the Contractor. We also could not find any evidence that the District required the Contractor to submit transportation records to substantiate fuel purchases as stated in the contract. Detailed usage reports provided by the Contractor would have allowed the District to compare those reports to its internal usage reports to monitor fuel usage by the Contractor. If the District had requested and timely reviewed these reports, it might have caught or prevented the misappropriation of fuel by the Contractor.

When the District agreed to lease the maintenance facility to the Contractor and at the same time allowed the Contractor to purchase its fuel from the District without adequate oversight at the maintenance facility, the District lost control of the fuel disbursement process, which should have limited the Contractor to purchasing fuel for its transportation of District students. As a result, the Contractor misused the District's fuel supplies and used District-purchased fuel in other Contractor vehicles, misappropriating between \$260,000 and \$384,500 of District fuel. The following sections detail the calculation of the misappropriated fuel.

Cameras Capture Misuse of District Fuel by Contractor

Near the end of the 2014-15 school year, current District officials became concerned about the Contractor's fuel usage, particularly after they observed fuel deliveries occurring every other week, as opposed to once a month, which was the previous standard. The District installed security cameras at the maintenance facility. As of May 2, 2015, one camera focused on the diesel pump, and one camera captured the entry and exit gate.

These cameras documented the misappropriation of District fuel by showing the Contractor filling up vehicles that were not used to transport District students. The cameras confirmed what current District officials suspected - the Contractor was using District-purchased fuel for other transportation uses.

The District recorded unauthorized usage of District-purchased fuel for twelve consecutive days from the date of installation. The District extrapolated the unauthorized usage of fuel over the life of the contract and estimated the amount of unauthorized fuel to be \$260,461. It then presented this amount to the Contractor for repayment. The Contractor immediately agreed to this estimate and began making restitution. However, after additional negotiations with the Contractor, the District ultimately collected restitution in the amount of \$234,254.

District's Internal Fuel Usage Reports Show 117 Percent Increase in First Contract Year.

While the District estimated that the Contractor misappropriated approximately \$260,000 in fuel, our calculation show that the amount could be much higher. We analyzed the District's internal usage reports to determine the amount of fuel used by the transportation contractors for the 2013-14 and 2014-15 school years.¹ The following table illustrates the spike in total fuel costs and total gallons used by the contractors during these years.

¹ Fuel used by the municipality and by the District itself was not included in these numbers so that the year to year comparison was contractor fuel use only.

Penn Hills SD Analysis of Contractor Fuel Expense and Usage				
	2013-14	2014-15	Increase	%
Total fuel expense	\$366,883	\$795,163	\$428,280	117%
Total gallons used	121,795	264,040	142,245	117%

As shown above, there was a 117 percent increase in fuel costs and usage. We then analyzed the total miles traveled as reported to PDE for each year and calculated the average price per gallon for both diesel and unleaded fuel. The table below shows modest increases in annual miles and price per gallon. These increases would suggest a modest increase in fuel expense.

However, if we conservatively estimate the average Contractor vehicle operates at ten miles per gallon, we would expect an increase in total expense of approximately \$43,500.² Instead, the District's fuel expense increased by over \$428,000 or over eight times what would be expected with the increase in miles and price per gallon between the two school years.

Penn Hills SD Analysis of Miles and Price per Gallon				
	2013-14	2014-15	Increase	%
Miles³	872,418	1,018,640	146,222	16.8%
Price/gallon⁴	\$2.92	\$2.97	.05	1.7%

Our calculation shows that the Contractor may have misappropriated as much as \$384,500, while the District estimated \$260,000. Insufficient documentation, coupled with the lack of adequate controls and oversight, during this time makes it difficult to accurately determine the total amount of fuel that was misappropriated.

Another Surveillance Issue

In November 2015, the District installed three additional cameras at the maintenance facility. Two of these cameras were mounted on the Contractor's bus garage; however, these two cameras malfunctioned within days of installation. Upon inspection, the two cameras were

² Increase in miles (146,222) divided by 10 miles per gallon = 14,622.20 X \$2.97 = \$43,427.93.

³ Total annual miles reported to PDE by the District for transportation reimbursement subsidy.

⁴ Price per gallon was computed by using the average of both diesel and unleaded fuel prices during the fiscal year.

discovered to have been disconnected from inside the Contractor's bus garage. When District officials questioned the Contractor about the disconnected cameras, the Contractor stated that this may have been the act of a rogue employee. The District took further corrective action which is discussed later; however, we believe this information, coupled with the misappropriation of hundreds of thousands of dollars in fuel, warrants termination of the contract at the end of the school year.

Maintenance Facility Lease Problems

As stated earlier, the District agreed to lease the District-owned maintenance facility to the Contractor for \$5,000 per month at the April 28, 2014 board meeting. However, no formal lease agreement was signed between the parties, and yet the Contractor began to occupy one of the District's garages in August 2014.

The Contractor sent the former Director a proposed lease in early September stipulating a monthly lease payment of \$2,500 rather than the \$5,000 announced at the April 2014 board meeting. The Contractor asked the former Director to have the District sign the lease or reply with proposed modifications. There is no evidence that a lease was signed or modifications were proposed by the District. Even without a signed lease between the parties, the District failed to invoice and/or collect lease revenue from the Contractor. The only lease revenue received by the District was a check in the amount of \$7,500 to cover the \$2,500 lease payment for September, October, and November 2014. No lease revenue was collected by the District from the Contractor for the months of December 2014 or January, February, and March 2015.

After the new leadership team took over operations in March 2015, they invoiced the Contractor for the back payments. As of June 24, 2015, the District recovered back payments for the lease totaling \$21,198 from the Contractor. This amount of back payments represents a compromise between the \$5,000 per month that was stated to the Board on April 28, 2014, and the \$2,500 amount proposed by the Contractor. In total, the District collected \$28,698 in lease payments when the District could have collected \$40,000 resulting in a loss of more than \$11,000. However, on April 27, 2015, the District did sign a formal

lease agreement with the Contractor for \$5,000 per month for the remainder of the school year.

Corrective Action Implemented by District

The District's current Superintendent and Business Manager have been proactive in implementing safeguards to ensure District-purchased fuel is not misappropriated. In addition to installing cameras at the maintenance facility, receiving restitution for an estimated amount of misappropriated fuel by the Contractor, and recovering back lease payments from the contractor, current District officials have implemented the following.

- Notification to the Contractor that its contract with the District may be terminated at the conclusion of the 2015-16 school year.
- Plans to solicit bids or proposals for District transportation services for the 2016-17 school year.
- A requirement of the Contractor to submit detailed and accurate fuel usage reports *prior* to payment (while the contract is still in place).
- District review and reconciliation of all fuel usage reports submitted by the Contractor *prior* to payment.

Recommendations

The *Penn Hills School District* should:

1. Terminate its contract with the District's current transportation provider at the end of the 2015-16 school year and prohibit that vendor from bidding on a new contract.
2. Develop and formally solicit a request for bids or proposals for District transportation services beginning with the 2016-17 school year.
3. Review and revise, as necessary, all of its security and internal accounting control procedures governing any Contractor's access to the maintenance facility and the District's fuel supplies.

4. Require all prospective lease agreements to be formalized, signed in writing, and approved by the Board *prior* to any vendor's use of District property.

Management Response

District management provided the following response for each recommendation:

1. The Board has taken the necessary steps to approve a resolution for the advertisement of request for bids for the 2016-2017 school year.
2. With approval of the resolution, the Business Office will prepare to solicit for requests for proposals for transportation services. These documents will require the new transportation company to comply with the necessary standards to maximize our transportation subsidies.
3. The Business Office has started to develop the necessary internal control manual to formalize our process and procedures. We have also taken the necessary steps to internally monitor fuel use by a key system. And, we require the contractor to provide fuel logs to compare to our internal records before we release any payments to the contractor.
4. The Board has approved all the necessary leasing documentation in conjunction with the use of our bus garage facility.

Auditor Conclusion

We are encouraged that the District is in the process of soliciting proposals for transportation services. We continue to believe that the transportation vendor for the 2015-16 school year should be prohibited from bidding on this contract. We are also encouraged that the District has started to develop safeguards and internal controls over fuel purchased by the District. We will evaluate these and any other corrective actions during our next audit of the District.

Finding No. 6

The District’s Transportation Expenditures Significantly Exceeded PDE’s Final Formula Allowance

Criteria relevant to the finding:

Section 2541 of the PSC states that school districts shall be paid by the Commonwealth for every school year for costs related to pupil transportation.

Daily miles traveled, the greatest number of pupils transported, days of service, and contractor cost are an integral part of the transportation reimbursement calculation. These factors must be reported accurately to PDE in order to receive the correct reimbursement.

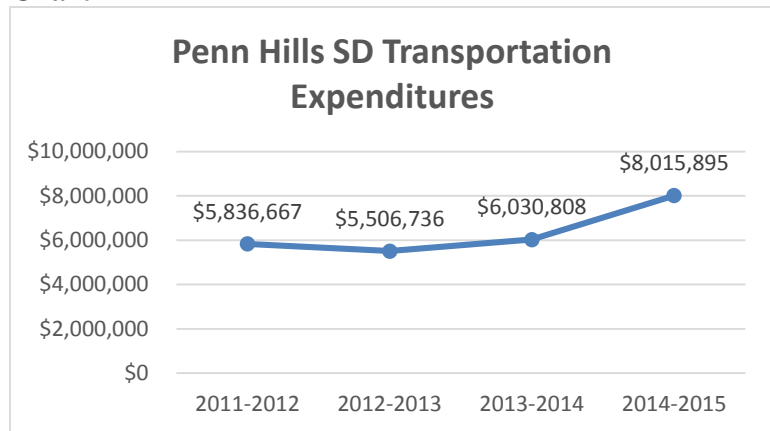
Chapter 23 of the State Board of Education Regulations indicates a school district’s board of directors is responsible for the negotiation and execution of contracts or agreements with contractors, drivers of district vehicles and common carriers.

PDE’s “final formula allowance” provides for a per-vehicle allowance based on the year of manufacture of the vehicle chassis, the approved seating capacity, number of trips the vehicle operates, the number of days pupils were transported, the approved daily miles driven, any excess hours, and the greatest number of pupils transported. The final formula allowance is adjusted annually by an inflationary cost index.

The District receives the lesser of the final formula allowance for the vehicles or the actual amount paid to the contractor, multiplied by the District’s aid ratio.

The District’s transportation expenditures increased more than \$2 million, or 37 percent, from Fiscal Year 2012 through Fiscal Year 2015 (see Chart 1). We found that the payment structure outlined in the transportation contracts was based on a per-vehicle daily rate, which did not align with the mileage calculations that PDE uses to reimburse districts for transportation expenditures. Furthermore, the District did not adequately monitor bus routes and adjust the number of buses needed to meet District needs. As a result, the District’s transportation expenditures were significantly greater than PDE’s “final formula allowance;” therefore, the District had to use significant amounts of local tax revenue to pay for transportation expenditures.

Chart 1



Prior to Fiscal Year 2012, the District owned and operated its own buses/vans to provide transportation services to its students. During a special board meeting on May 12, 2011, the Board approved a resolution to outsource transportation services, based on recommendation from the District’s former Superintendent and former Director of Business Affairs. After issuing a Request for Proposal, the District entered into a four year contract with a vendor (Contractor A) to provide transportation services beginning with the 2011-12 school year.

District Transportation Contract (Contractor A)

The District's agreement with Contractor A specified that the District would pay the contractor based on the number of vehicles in service. There was a payment schedule that outlined the cost per type of vehicle used. In addition, the contract provided for an annual 3 percent increase in the per-vehicle cost.

Agreeing to pay a transportation contractor based on the number of vehicles in service, as opposed to actual mileage traveled or number of students transported, requires a strategic plan to develop routes to ensure that vehicles are filled as close to capacity as possible, while trying to ensure students are not in vehicles for an unreasonable amount of time. The contract stated that the District was primarily responsible for planning all routes, stops and schedules. A provision in the contract also required the District and the contractor to consult on a regular basis to review usage and to adjust the number of vehicles accordingly.

PDE's Transportation Reimbursement

As stated in the criteria box, PDE reimburses districts for transportation expenditures. PDE calculates a "final formula allowance" using, among other items, the number of days students were transported and the approved daily miles driven. The "final formula allowance" is then multiplied by the District's aid ratio⁵ to determine the reimbursement amount. School districts are reimbursed at the lesser of the actual amount paid to the contractor or the "final formula allowance," multiplied by the District's aid ratio.

To maximize the use of state subsidies, school districts should try to align their transportation expenditures as close to the "final formula allowance" as possible to reduce the amount of other district funds used to pay this expense. To that end, school districts that outsource transportation services will commonly use a payment structure that is

⁵ *Aid ratio* is the general term for three numerical values -- market value aid ratio (MV AR), personal income aid ratio (PI AR), and market value/personal income aid ratio (MV/PI AR) -- calculated in accordance with Section 2501(14) and (14.1) of the [School Code](#). Various state subsidies use aid ratios in their calculations. The MV/PI AR represents the relative wealth (market value and income), in relation to the state average, for each pupil in a school district.

based on the actual mileage traveled and the number of students transported, as opposed to a per vehicle rate.

Reported Contractor Costs Significantly Greater than Reimbursement Amount

As the following table demonstrates, the District’s costs exceeded PDE’s allowance each year. Furthermore, the percentage in which the costs exceeded the allowance increased to 90% by Fiscal Year 2014.

Table 1

Penn Hills SD Contracted Transportation Costs Comparison to PDE Allowance				
Fiscal Year	Contractor Cost Reported to PDE	Final Formula Allowance	Amount Contractor Costs exceeds Formula	Percentage that Contractor Costs exceeded Formula
2011-12	\$3,631,566	\$2,534,210	\$1,097,356	43%
2012-13	\$4,244,724	\$2,697,561	\$1,547,163	57%
2013-14	\$4,781,126	\$2,519,341	\$2,261,785	90%
Total:	\$12,657,416	\$7,751,112	\$4,906,304	

During our review, we found buses that were filled to less than one-third of capacity, a clear indication that the District was not effectively planning bus routes and consulting with the contractor concerning the number of buses needed in service. When we asked the District how it was monitoring the contract, we found that the District did not obtain and review reports from the contractor detailing students transported, routes, stops, and mileage.

The per-vehicle payment structure with annual increases, coupled with the District’s failure to adequately plan and monitor bus routes to ensure that contracted vehicles were operating close to capacity, were primary factors in the District’s contracted costs significantly exceeding the “final formula allowance.”

As previously stated, as the District’s contractor costs increased, the percentage over “final formula allowance” increased, resulting in the District having to use a greater

share of other revenue to cover transportation expenditures. As more revenue is needed to fund District transportation expenditures less revenue is available to be used for academic and facility needs. The following table depicts the increasing amount of other District revenue used for transportation costs.

Table 2

Penn Hills SD Contracted Transportation Costs Comparison of PDE Reimbursement vs. District Share			
Fiscal Year	Contractor Cost Reported to PDE	Transportation Reimbursement Received⁶	District Share from Other Revenue
2011-12	\$3,631,566	\$1,945,784	\$1,685,782
2012-13	\$4,244,724	\$2,114,501	\$2,130,223
2013-14	\$4,781,126	\$1,927,840	\$2,853,286
Total:	\$12,657,416	\$5,988,125	\$6,669,291

More than half of the District’s total revenues come from local property taxes. District officials stated that one mill⁷ of property taxes is needed to generate \$1.5 million in local tax revenue. Therefore, nearly two mills of property taxes were needed to pay for the District’s share of transportation expenditures in Fiscal Year 2014.

Second Transportation Contractor

After the 2013-14 fiscal year, the District terminated their contract with Contractor A, citing poor overall service. The District then executed a five-year agreement with another vendor (Contractor B) to provide transportation services beginning on July 1, 2014.

When it was procuring the services of the second vendor, the District had the opportunity to redefine their transportation payment structure and base payment on actual miles traveled and students transported. However, we found that the new contract contained a similar payment structure as the previous contract. (See Finding No. 5 for more information on Contractor B.)

⁶ Transportation Reimbursement Received is PDE’s final formula allowance from Table 1 multiplied by the District’s aid ratio.

⁷ One mill is equivalent to \$1 in taxes per \$1,000 in taxable value.

We could not include the 2014-15 fiscal year in Tables 1 and 2 because those figures had not been released by PDE as of April 1, 2016. However, due to the similar payment structure included in the agreement with Contractor B and the overall increase in transportation expenditures, we expect that a significant amount of local tax revenue was needed to pay for District transportation expenditures.

Recommendations

The Penn Hills School District should:

1. Ensure all future District transportation contracts contain a payment structure that is based on actual mileage traveled and number of student transported as opposed to a flat daily rate.
2. Monitor and evaluate transportation routes to ensure that they are planned to maximize efficiency and are adjusted accordingly to balance vehicle capacity with time spent in transit.
3. Review transportation contracts for other similarly sized districts whose transportation costs are closer to PDEs “final formula allowance.”

Management Response

District management provided the following response for each recommendation:

1. With the Board taking the necessary steps to approve a resolution for the advertisement of request for bids for the 2016-2017 school year, the Business Office will insure the payment structure of the new contract require mileage traveled and student counts.
2. The Business Manager, Technology Director and Transportation Manager have recently attended a webinar that assisted us in planning and maximizing our efficiencies in transportation. With the help of PASBO we have a new found understanding of our inefficiencies and are adjusting accordingly.
3. The District has gathered multiple contracts from neighboring Districts and from the PASBO electronic

resource center to assist us in developing a request for bid and contract that maximizes our final formula allowance.

Auditor Conclusion

We are encouraged to learn that the administration and the Board have taken steps to begin the competitive bid process for transportation services in the 2016-17 school year. We are also pleased to see that all District staff involved in transportation are receiving appropriate training. Finally, it's our position that the District is taking the proper approach by basing future transportation contracts on actual miles traveled, number of pupils transported, as opposed to a flat daily rate per vehicle. We will evaluate the District's corrective actions during our next audit.

Finding No. 7

The District Improperly Sold its Tax-Exempt Fuel to a Municipality at a Markup, But its Deficient Billing Practices Netted Losses in the Thousands of Dollars

Criteria relevant to the finding:

The Pennsylvania Liquid Fuels and Fuels Tax Act, 75 Pa.C.S. § 9001 *et seq.*, does not include political subdivisions or exempt entities such as school districts in its definition of those who qualify to be “distributors” of liquid fuels or fuels. *See* 75 Pa.C.S. § 9002.

Furthermore, Section 9003 (relating to Liquid fuels and fuels permits; bond or deposit of securities) of the act, 75 Pa.C.S. § 9003, stipulates that any distributor of liquid fuels and/or fuels within the Commonwealth must first obtain a license to distribute liquid fuels or fuels. Section 9003(b) states, in part: (b) A person desiring to operate as a distributor shall file an application for a liquid fuels permit or a fuels permit, or both, with the department [of Revenue]....” The definition of “Person” in the act, includes: “Every natural person, association or corporation....” *See* 75 Pa.C.S. §§ 9002, 9003(b).

Finally, Section 9004 (relating to Imposition of tax, exemptions and deductions) of the act, 75 Pa.C.S. § 9004, addresses the distributor’s duty to collect and remit taxes to the Commonwealth, and it does not provide for any distribution by an exempt entity to another exempt entity.

We found that the District has been selling its tax-exempt fuel at a 15 cents per gallon markup to a local municipality (Municipality) in violation of the Liquid Fuels and Fuel Tax Act.⁸ Furthermore, this arrangement, which has been in place for at least 22 years, was neither supported by a written contract, nor approved by the Board, which also resulted in apparent noncompliance with the PSC.⁹ The arrangement created a scenario whereby one political subdivision, the District, attempted to profit from the sale of tax-exempt commodities to another political subdivision, the Municipality.

Ironically, the District’s billing practices were so deficient that it actually failed to collect enough revenue from the Municipality to cover the cost of the fuel it sold in at least the 2013-14 and 2014-15 years, and it is possible that this also occurred in other years.

Background

The District experienced a 37 percent increase in transportation expenditures over the four school years ending June 30, 2015. As part of our review of transportation expenses, we found significant increases in fuel expenditures, which warranted closer review of these expenses by our Department. We reviewed fuel usage and related expenses for three distinct users: the primary transportation contractor, the District itself, and the Municipality. This finding focuses on the fuel sales arrangement with the Municipality and its financial impact on the District. (Also see Finding No. 5 and Finding No. 6)

No Board-Approved Agreement

We found that the arrangement between the District and the Municipality was never formalized in a written agreement

⁸ 75 P.S. Chapter 30.

⁹ 24 P.S. § 508.

Criteria relevant to the finding (continued):

Public School Code:

Section 508 (relating to *Majority Vote Required; Recording*) of the Public School Code (PSC), 24 P.S. § 508, states, in part: “The affirmative vote of a majority of all the members of the board of school directors in every school district, duly recorded, showing how each member voted, shall be required in order to take action on the following subjects:--

Entering into contracts of any kind, including contracts for the purchase of fuel or any supplies, where the amount involved exceeds one hundred dollars (\$100).”

nor was it publicly approved by the Board. According to the District’s current administration, there was only a verbal agreement, dating back to 1994, calling for the District to supply all of the Municipality’s fuel needs and providing for a fifteen cents per gallon markup to be paid by the Municipality to the District. The arrangement created transactions in which a political subdivision may have profited for years from the sale of tax-exempt commodities.

Erroneous Invoices and District Losses

Our review of the District’s invoices and fuel usage reports for the 2013-14 and 2014-15 school years found the District failed to properly charge the Municipality for the fuel it sold, resulting in erroneous invoicing and insufficient revenues. Not only did the District fail to collect the total amount of the markup in each of the two years reviewed, it also failed to recoup nearly \$66,000 in fuel costs, as shown in the chart below. Based on our testing of these two school years, we believe the District may have significantly deprived itself of revenues in other years that would have at least recouped the cost of the fuel it sold to the Municipality.

PENN HILLS SD TWO-YEAR ANALYSIS OF UNDER-BILLING OF FUEL SALES TO MUNICIPALITY				
School Year	Municipality Fuel (Gallons)	Agreed-Upon Fuel (Costs + Markup)	Invoiced & Received	Total Under-Billed
2013-14	108,152	\$328,936	\$289,188	\$39,748
2014-15	98,038	\$303,677	\$246,604	\$57,073
Total	206,190	\$632,613	\$535,792	\$96,821
Less 15¢ per gallon markup				-\$30,928
Net loss in cost of fuel sold to Municipality				\$65,893

When we presented the District’s current administration with the impropriety of this arrangement, it promptly contacted the Pennsylvania Department of Revenue (Revenue) and received confirmation of our position. The

District discontinued fuel sales to the Municipality on December 18, 2015.

Given that the District's longstanding fuel sales arrangement with the Municipality is clearly in noncompliance with the Liquid Fuels and Fuel Tax Act, as confirmed by the Pennsylvania Department of Revenue, the District must never engage in this practice again. Furthermore, it is evident that the Board failed in its fiduciary responsibility to oversee this long-standing verbal arrangement by not undertaking public discussion, research into legalities, and a formal vote to approve a written agreement. This failure in transparency and accountability cost the District nearly \$66,000 for two school years and possibly more money in the preceding years it participated in this arrangement with the Municipality.

Recommendations

The *Penn Hills School District and the Board* should:

1. With the collaboration of the District's Business Manager and solicitor, review its billing for fuel sold to the Municipality and determine whether it should attempt to recoup some of the costs of the fuel it sold in past years.
2. In close coordination with the District's Solicitor, require that all future District contracts exceeding \$100 be reviewed and approved by the Board at a public meeting *before* any transactions occur.

Management Response

District management provided the following response for each recommendation:

1. The District is in the process of reviewing fuel usage by the Municipality in an effort to recover lost monies.
2. The District will Board approve all contracts in the future.

Auditor Conclusion

We are pleased to note that, after bringing this issue to the attention of District officials during the audit, the District has discontinued the practice of selling fuel to other Municipal entities and are in the process of attempting to recover lost monies due to billing discrepancies. District officials stated that the District is currently involved in ongoing discussions with the Department of Revenue concerning the legal implications of this past practice. We sent this audit report to the Department of Revenue to be used in determining if the District is subject to financial penalties for engaging in the practice of selling fuel to other Municipal entities.

Finding No. 8

The District Failed to Ensure that its School Bus Drivers Met All Employment Requirements

Criteria relevant to the finding:

The Pennsylvania Vehicle Code and Pennsylvania Department of Transportation's (DOT) regulations require bus drivers to possess a valid driver's license, obtain certification of safety training, and pass a physical examination. (*See* 75 Pa.C.S. §§ 1508.1, 1509 and 67 Pa. Code §§ 71.1- 71.6)

Section 111 of the PSC, 24 P.S. § 1-111, as amended, requires state and federal criminal background checks, and Section 6344 of the Child Protective Services Law (CPSL), 23 Pa.C.S. § 6344, as amended, requires a child abuse clearance.

Specifically, Section 111(b) of the PSC requires prospective school employees who have direct contact with children, including independent contractors and their employees, to submit a report of criminal history record information obtained from the Pennsylvania State Police. *See* 24 P.S. § 1-111(b).

The District failed to meet the requirements related to the employment of bus drivers having direct contact with students. Specifically, we found that the District did not obtain, review, and maintain documentation to support that each bus driver was qualified and suitable to transport students. Furthermore, after our detailed testing of employment records for 25 contracted drivers, we found that all 25 records were missing documentation for at least one of the employment requirements. The most significant effect of this deficiency is that we determined that the District used two bus drivers who were ineligible for employment based on prior criminal convictions, therefore potentially jeopardizing the welfare and safety of its students.

Several state statutes and regulations establish the minimum required qualifications for school bus drivers. The ultimate purpose of these requirements is to ensure the safety and welfare of the students transported. The District uses three independent transportation contractors to transport students. The primary transportation contractor provides transportation to approximately 90 percent of all students. We obtained a list of all contracted bus drivers currently driving in the District. We randomly selected (using a random number generator) 25 drivers, or 24 percent,¹⁰ and requested to review those bus drivers' personnel records and clearances to determine if those drivers met the minimum qualifications to transport students and are free of criminal convictions impacting employment eligibility.

Employment Qualifications and Clearances

We requested documentation to verify that the bus drivers we tested complied with the following pre-employment qualification requirements in compliance with the

¹⁰ There was a total of 106 bus drivers during this time period.

*Criteria relevant to the finding
(continued):*

Additionally, Section 111(c.1) of the PSC requires public and private schools to review federal criminal history record information (CHRI) records for all prospective employees and independent contractors who will have direct contact with children, and make a determination regarding the fitness of the individual to have contact with children. The law requires the report to be reviewed in a manner prescribed by PDE. The review of CHRI reports is required prior to employment, and includes school bus drivers and other employees hired by independent contractors who have direct contact with children. *See* 24 P.S. § 1-111(c.1).

Section 111(b) of the PSC also requires that both state and federal criminal history records are not more than one (1) year old at the time of employment. It also requires school administrators to obtain the required records prior to employment and to maintain a copy on file with the employment application, including documentation for individuals hired by a contractor. *See* 24 P.S. § 1-111(b).

Section 111(e) of the PSC lists convictions for certain criminal offenses that require an absolute ban to employment. *See* 24 P.S. § 1-111(e).

In addition, effective September 28, 2011, Act 24 added Section 111(f.1) to the PSC which provides that a 10, 5, or 3 year *look-back period* for certain convictions be met before an individual is eligible for employment. *See* 24 P.S. § 1-111(f.1).

Pennsylvania Vehicle Code and Pennsylvania DOT's regulations:

- Possession of a valid driver's license.
- Completion of school bus driver skills and safety training.
- Completing a physical examination.

We also requested documentation (i.e., background clearance documents) to confirm that the District obtained the following background checks prior to employment.

- State Criminal History Record
- Federal Criminal History Record
- Official Child Abuse Clearance Statement

Finally, we requested the *Arrest/Conviction Report and Certification Form* for each driver as required by Act 24 of 2011. The purpose and intent of the forms was to ensure that all currently employed drivers complete and submit the form to their employer indicating whether or not the driver was arrested or convicted of a Section 111 criminal offense, some of which require an absolute ban to employment.¹¹

Failure to comply with the PSC by obtaining, reviewing, and maintaining employment qualifications and clearances for all bus drivers.

When we requested employment qualification and clearance documentation from the District, the District was not able to produce any of the required documentation. District officials stated that this information was not kept on file at the District. Furthermore, officials confirmed that the qualification and clearance information was not reviewed by anyone at the District prior to the bus drivers having contact with students.

We further inquired as to why the District did not comply with Section 111 of the PSC (see criteria box to the left). District officials stated that its former transportation manager, who was employed from August 2013 through September 2014, did not believe it was the District's responsibility to review and maintain employment

¹¹ 24 P.S. § 1-111(e).

*Criteria relevant to the finding
(continued):*

Section 111(g)(1) of the PSC provides that an administrator, or other person responsible for employment decisions in a school or other institution under this section who willfully fails to comply with the provisions of this section commits a violation of this act, subject to a hearing conducted by PDE, and shall be subject to civil penalty up to \$2,500. *See* 24 P.S. § 1-111(g)(1).

Effective September 28, 2011, amendments to Section 111 of the PSC brought about through Act 24 required all current school employees to submit an “Arrest/Conviction Report and Certification” form to their employing school entity indicating whether or not they have ever been arrested or convicted of any Section 111(e) or (f.1) offense by December 27, 2011. Furthermore, all employees subsequently arrested or convicted of a Section 111(e) or (f.1) offense must complete the form within 72 hours of the arrest or conviction and file it with the school. *See* 24 P.S. § 1-111(e), (f.1).

Additionally, Chapter 23 (relating to Pupil Transportation) of the State Board of Education Regulations, among other provisions, provides that the board of directors of a school district is responsible for the selection and approval of eligible operators who qualify under the law and regulations. *See* in particular 22 Pa. Code § 23.4.

Section 6344(a.1)(1) and (b) of the CPSL, require a child abuse clearance for all school employees. *See* 23 Pa.C.S. § 6344(a.1)(1) and (b).

qualifications since the bus drivers were contracted employees. The former manager relied entirely on the contractor to ensure that drivers were qualified and eligible for employment as a bus driver.

While the transportation contract explicitly states that the contractor will ensure that all drivers will comply with all state laws and regulations regarding employment eligibility, the District still has the statutory obligation to perform the function of the oversight responsibility to ensure compliance. In fact, under the PSC, an administrator, or other person responsible for employment decisions in a school, who willfully fails to comply with the code’s criminal check background requirements may, after hearing, be subject to a civil penalty up of to \$2,500 imposed by PDE.

After we informed current District officials about the District’s responsibility of ensuring all bus drivers meet employment qualifications, the current District transportation secretary requested pre-employment qualification and clearance documentation for all drivers from the transportation contractors.

We then reviewed the employment qualification and clearance documentation provided by District contractors for the 25 drivers selected for testing to determine if the drivers possessed the necessary qualifications and were free of any convictions for particular criminal offenses that require an absolute ban or temporary ban to employment. We found the following deficiencies:

- 2 drivers did not have the state criminal record check
- 1 driver did not have the child abuse clearance
- 23 drivers did not have the arrest/conviction report
- 25 drivers did not have the federal criminal history check

Upon examination of the records that were provided for our review, we determined that two current bus drivers had prior criminal convictions that permanently barred them from employment. When we presented our results to the District, the District consulted with its solicitor who agreed with our determination. District officials then required the contractor to remove these drivers from having contact with

*Criteria relevant to the finding
(continued):*

Section 6303 of the CPSL, defines “School employee” as, in part: “[a]n individual who is employed by a school or who provides a program, activity or service sponsored by a school...” See 23 Pa.C.S. § 6303.

Section 6444.4(1)(ii) of the CPSL now requires recertification as follows: “(1) Effective December 31, 2014:*** (ii) School employees identified in section 6344(a.1)(1) (ii) School employees identified in shall be required to obtain reports under section 111 of the [PSC]..., and under section 6344(b)(2) **every 60 months.**” [Emphasis added.] 23 Pa.C.S. § 6344.4(1)(ii)

students. It was not until we brought these prior criminal convictions to the District official’s attention, during the 2015-16 school year, that the District officials removed these bus drivers from having direct contact with students. We noted that the drivers in question were hired on August 1, 2014, by the transportation contractor, and were transporting District students since the 2014-15 school year.

Since none of the 25 drivers we selected for testing had the federal criminal history check, the District cannot ensure that its drivers are eligible for employment as a bus driver.

Effect of District’s failure to meet employment responsibilities

It is the responsibility of District management to have adequate policies and procedures in place to ensure that all employees or contracted employees who have direct contact with children have the proper qualifications prior to employment. By not having the required bus driver qualification documents on file at the District, District personnel were not able to verify whether all drivers were properly qualified to transport students. Having unqualified or unsuitable drivers to transport students results in noncompliance with the PSC, the CPSL, the Vehicle Code, and the applicable regulations. In addition, the unqualified or unsuitable drivers create an increased risk to the safety and welfare of students.

Any delay in collecting or failure to collect required employment documentation may impede the identification of individuals who are not to have direct contact with children under the law. Similarly, the failure to review and document continued employment eligibility based on revisions to the law and new absolute bans for prior criminal convictions resulted in two individuals having direct contact with children when they may not be suitable to do so. Therefore, it is imperative that the District implement effective procedures to ensure that the bus contractors review and verify the employment documentation of its bus drivers. Also, District’s personnel must review and maintain the contractor’s documentation to ensure that all of the District’s contracted bus drivers have met the statutorily mandated requirements. In

addition, the procedures must include the requirement that the Board approve the annual list of district bus drivers.

Failure to implement prior recommendations. At the conclusion of our prior audit in February 2012, we notified the District that its oversight of bus driver qualifications and approval was inadequate. We issued a “verbal comment” and recommended that the District implement a more formal and inclusive monitoring system to document and retain all mandated bus driver qualifications. We also recommended that the Board comply with the State Board of Education’s regulatory requirement to annually approve a list of all bus drivers prior to the beginning of the school year. Our current audit testing revealed that the District did not implement our prior recommendations as evidenced by the lack of employment records for contracted bus drivers and the Board’s failure to approve the list of bus drivers for the 2013-14 and 2014-15 school years.¹²

Recommendations

The *Penn Hills School District* should:

1. Immediately obtain and review all employment qualification documentation for all current bus drivers. Document the results of this review and remove bus drivers if they don’t meet employment requirements.
2. Develop and implement procedures to ensure all bus driver’s employment qualifications and clearances are reviewed and approved prior to the driver transporting District students. In addition, the District should ensure that appropriate documentation to evidence the review and approval is maintained by the District.
3. Annually present to the Board of Directors a list of bus drivers to be approved prior to the start of the school year.

¹² After we brought this discrepancy to the attention of the current administration in October 2015, the Board ultimately approved the list of bus drivers for the 2015-16 school year at the January 2016 board meeting.

Management Response

District management provided the following response for each recommendation:

1. Clearances and eligibility have been reviewed by PHSD and records are being maintained on District property for all current drivers. Drivers were Board-approved October 26, 2015.
2. All contracted employees are being reviewed on a monthly basis. Any questionable qualifications and clearances are reviewed by the HR Director, the Superintendent and the Solicitor.
3. For new drivers and substitutes, credentials are being reviewed and Board-approved monthly, effective January 25, 2016, February 22, 2016, and April 25, 2016. The list of drivers for the 2016-2017 year will be approved before the start of school in August.

Auditor Conclusion

We are encouraged that the District has newly established policies and procedures to ensure that all drivers meet all necessary employment qualifications prior to board approval. We are also pleased that the District realizes the importance of the Board approving bus drivers prior to the start of the school year. Since these procedures were developed after our audit work, we will evaluate their implementation and effectiveness during our next audit of the District.

Status of Prior Audit Findings and Observations

Our prior audit of the District released on March 27, 2013, resulted in one finding and one observation, as shown below. As part of our current audit, we determined the status of corrective action taken by the District to implement our prior audit recommendations. We interviewed District personnel and performed audit procedures as detailed in each status section below.

Auditor General Performance Audit Report Released on March 2013

Prior Finding No. 1: Certification Deficiencies (Resolved)

Finding Summary:

Our prior audit of professional employees' certificates and assignments found that one individual was assigned a teaching position without being certified, and one individual was assigned to a teaching position with a lapsed certificate. PDE's Bureau of School Leadership and Teacher Quality (BSLTQ) confirmed the deficiencies, and the District was subject to subsidy forfeitures of \$2,910, \$4,447 and \$2,121 for the 2011-12, 2010-11, and 2009-10 school years, respectively.

Recommendations:

We recommended that the District should:

1. Implement appropriate controls so that only properly certified teachers are assigned to applicable teaching assignments. The controls should prevent uncertified teachers from teaching any course which requires certification and prevent teachers with lapsed certificates from teaching any course until a valid certificate is obtained.

We also recommended that PDE should:

2. Recover the appropriate subsidy forfeiture.

Current Status:

The District did implement our prior recommendations. The employee with the lapsed certificate was permanently certified in December 2011, prior to the end of our prior audit. The employee working out of classification received the appropriate certification for the position in July 2012. In addition, the Board passed Policy Number 304 "Employment of District Staff" and has put in place standard operating procedures to control the tracking and assignment of professional employees. However, as of April 28, 2016, PDE still has not adjusted the District's subsidy recover the forfeiture. We again recommend that PDE recover the subsidy forfeiture.

Prior Observation: Unmonitored Vendor System Access and Logical Access Control Weaknesses (Resolved)

Observation Summary: The District uses software purchased from an outside vendor for its critical student accounting applications (membership and attendance). The software vendor has remote access into the District's servers. Based on our prior audit procedures, we determined that a risk exists that unauthorized changes to the District's data could occur and not be detected because the District was unable to provide supporting evidence that it was adequately monitoring all vendor activity in its system. Further, the District does not perform formal, documented reconciliations between manual records and computerized records for membership and attendance.

Recommendations: We recommended that the District should:

1. Develop and maintain a written information technology (IT) security policy and ensure that all employees are aware of this policy.
2. Establish separate IT policies and procedures for controlling the activities of vendors/consultants and have the vendor sign this policy, or require the vendor to sign the District's Acceptable Use Policy.
3. Allow access to the system only when the vendor needs access to make pre-approved changes/updates or requested assistance. This access should be removed when the vendor has completed its work. This procedure would also enable the monitoring of vendor changes.
4. Generate monitoring reports (including firewall logs) of vendor and employee access and activity on the system. Monitoring reports should include the date, time, and reason for access, changes(s) made and who made the change(s). The District should review these reports to determine that the access was appropriate and that data was not improperly altered. The District should also ensure it is maintaining evidence to support this monitoring and review.
5. The upgrades/updates to the District's system should be made only after receipt of written authorization from appropriate District officials.
6. Reduce the number of staff with access to the hardware (servers) that contains the membership/attendance data to only those

members of staff with direct responsibility for system operation and maintenance.

Current Status:

The District did implement our prior recommendations. On November 23, 2015, the District updated the Board Policy Number 815 - Acceptable Use of the Internet, which governs passwords and user IDs. In addition, we found that the student information system vendor no longer has 24-hour access into the District's student information software. Finally, we noted that all vendors now must sign a Technology Code of Conduct.

Appendix: Audit Scope, Objectives, and Methodology

School performance audits allow the Pennsylvania 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, PDE, and other concerned entities.

Our audit, conducted under authority of Section 403 of The Fiscal Code,¹ is not a substitute for the local annual financial audit required by the PSC of 1949, as amended. We conducted our audit in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. Those 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.

Scope

Overall, our audit covered the period July 1, 2012 through June 30, 2015. In addition, the scope of each individual audit objective is detailed on the next page.

The District's management is responsible for establishing and maintaining effective internal controls² to provide reasonable assurance that the District is in compliance with certain relevant state laws, regulations, contracts, and administrative procedures (relevant requirements). In conducting our audit, we obtained an understanding of the District's internal controls, including any IT controls, 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 controls 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.

¹ 72 P.S. § 403

² 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; and compliance with certain relevant state laws, regulations, contracts, and administrative procedures.

Objectives/Methodology

In order to properly plan our audit and to guide us in selecting objectives, we reviewed pertinent laws and regulations, board meeting minutes, academic performance data, financial reports, annual budgets, and new or amended policies and procedures. We also determined if the District had key personnel or software vendor changes since the prior audit.

Performance audits draw conclusions based on an evaluation of sufficient, appropriate evidence. Evidence is measured against criteria, such as laws, regulations, third-party studies, and best business practices. Our audit focused on the District's efficiency and effectiveness in the following areas:

- ✓ Governance
- ✓ Financial Stability
- ✓ School Safety
- ✓ Athletic Funds
- ✓ Bus Driver Requirements
- ✓ Transportation
- ✓ State Subsidy Reimbursements
- ✓ Procurement Cards

As we conducted our audit procedures, we sought to determine answers to the following questions, which served as our audit objectives:

- ✓ Did the LEA's Board and administration maintain best practices in overall organizational governance?
 - To address this objective, we conducted in-depth interviews with the current Superintendent and his or her staff, reviewed board meeting books, policies and procedures, and reports used to inform the Board about student performance, progress in meeting student achievement goals, budgeting and financial position, and school violence data to determine if the Board was provided sufficient information for making informed decisions. Finding No. 1 describes the exceptions noted during our review.
- ✓ Based on an assessment of fiscal benchmarks, was the District in a declining financial position, and did it comply with all statutes prohibiting deficit fund balances and the over expending of the District's budget?
 - To address this objective, we reviewed the District's annual financial reports, budgets, independent auditor's reports, summary of child accounting, and general ledger for fiscal years 2009-10 through 2014-15. The financial and statistical data was used to calculate ratios and trends for 22 benchmarks which were deemed appropriate for assessing the District's financial stability. The benchmarks are based on best business practices established by several agencies, including the Pennsylvania Association of School Business Officials, the Colorado Office of

the State Auditor, and the National Forum on Education Statistics. Finding No. 2 contains the results of our review.

- ✓ Did the District take appropriate actions to ensure it provided a safe school environment?
 - To address this objective, we reviewed a variety of documentation including, safety plans, training schedules, anti-bullying policies, and after action reports. In addition, we conducted on-site reviews at the District's two newly built school buildings to assess whether the District had implemented basic safety practices. Due to the sensitive nature of school safety, the results of our review of this objective area are not described in our audit report. The results of our review of school safety are shared with District officials and, if deemed necessary, with PDE.

- ✓ Did the District ensure that its athletic fund monies were properly collected, verified, documented, safeguarded and deposited?
 - To address this objective, we reviewed whether the District developed and implemented adequate policies and procedures governing athletic fund. We reviewed the job description for the Athletic Director to obtain an understanding of his role and responsibilities for maintenance of the fund; and determined whether the Athletic Director is separately bonded as custodian of the fund. We reviewed gate receipts, supporting documentation, and deposit information for all 129 athletic events held at the District from July 1, 2012 through June 30, 2015. Finding No. 4 contains the results of our review.

- ✓ Did the District ensure that bus drivers transporting District students had the required driver's license, physical exam, training, background checks, and clearances as outlined in applicable laws?³ Also, did the District have adequate written policies and procedures governing the hiring of new bus drivers?
 - To address this objective, we selected 25 of the 106 bus drivers employed by the District's bus contractor, during the period July 1, 2015 to April 20, 2016, and reviewed documentation to ensure the District complied with bus driver's requirements. We also determined if the District had written policies and procedures governing the hiring of bus drivers and if those procedures were sufficient to ensure compliance with bus driver hiring requirements. Finding No. 8 contains the results of our review.

³ 24 P.S. § 1-111, 23 Pa.C.S. § 6344(a.1), 24 P.S. § 2070.1a *et seq.*, 75 Pa.C.S. §§ 1508.1 and 1509, and 22 *Pa. Code Chapter 8.*

- ✓ Did the District have basic internal controls established to ensure the District's compliance with laws and regulations governing transportation operations? Did the District ensure that its transportation contract was properly approved, executed, and monitored?
 - To address this objective, we haphazardly selected and reviewed 25 percent of the transportation data submitted by the District to PDE for the 2013-14 school year. We obtained the invoices, odometer readings and student rosters and calculated the amount paid by the District to their transportation contractors. We then compared our calculations to the data the District submitted to PDE to determine if the proper amount of transportation subsidy was received. We also obtained the Board minutes to determine if all current transportation contracts were approved by the Board and if the Board minutes contained evidence of District monitoring of this contract. For the 2013-14 school year, we reviewed all 44 fuel invoices (21 diesel and 13 unleaded) paid by the District. For the 2014-15 school year, we reviewed all 51 fuel invoices (31 diesel and 20 unleaded) paid by the District. Subsequently, we obtained the District's fuel usage reports for those school years and compared the amount of fuel used by the District, contractor, and municipality to the amount of fuel purchased by the District. Finally, we reviewed the fuel usage reports compared to what was invoiced to the municipality to determine if the amount billed to the municipality was accurate and proper. Finding Nos. 5, 6, and 7 contain the results of our review.

- ✓ Did the District receive the funding to which they were entitled from PDE for the various General Obligation Bonds for their construction projects?
 - To address this objective, we reviewed all 19 of the subsidy applications construction projects from July 1, 2009 to June 30, 2015, and reviewed documentation to support that these applications submitted to PDE were properly computed, received, and reported. Our review found that the District properly computed, received, and reported subsidy amounts from District construction projects.

- ✓ Did the District ensure that procurement card and vendor account purchases were made and approved in accordance with District policies?
 - To address this objective, we obtained a list of Board approved policies for procurement cards. We interviewed District personnel to determine the process for approving purchases made with District issued procurement cards. For two local vendor accounts, we performed a review of all 1,447 purchases made between July 1, 2012 and June 30, 2015. This review included a comparison of monthly statements received from the local vendors and comparing each statement to the corresponding receipt turned into the District by the employees with access to the procurement cards in question. We determined the total expenditures and reviewed the vendor account log for the open account at a local hardware store for the period July 1, 2012 through June 30, 2015.

Distribution List

This report was initially distributed to the Superintendent of the District, the Board of School Directors, and the following stakeholders:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania
Harrisburg, PA 17120

The Honorable Pedro A. Rivera
Secretary of Education
1010 Harristown Building #2
333 Market Street
Harrisburg, PA 17126

The Honorable Timothy Reese
State Treasurer
Room 129 - Finance Building
Harrisburg, PA 17120

Mrs. Danielle Mariano
Director
Bureau of Budget and Fiscal Management
Pennsylvania 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

Mr. Lin Carpenter
Assistant Executive Director for Member
Services
School Board and Management Services
Pennsylvania School Boards Association
P.O. Box 2042
Mechanicsburg, PA 17055

Mr. Robert Caruso
Executive Director
State Ethics Commission
309 Finance Building
P.O. Box 11470
Harrisburg, PA 17108

Ms. Eileen McNulty
Secretary of Revenue
11th Floor, Strawberry Square
Harrisburg, PA 17128

This report is a matter of public record and is available online at www.PaAuditor.gov. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 229 Finance Building, Harrisburg, PA 17120; via email to: news@PaAuditor.gov.

ⁱ Source: School district, PDE, and U.S. Census data.

ⁱⁱ Source: Information provided by the District administration.

ⁱⁱⁱ Source: United States Census <http://www.census.gov/2010census>

^{iv} PSSA stands for the Pennsylvania System of School Assessment (PSSA), which is composed of statewide, standardized tests administered by PDE to all public schools and the reporting associated with the results of those assessments. PSSA scores in the tables in this report reflect Reading and Math results for the “All Students” group for the 2011-12 and 2012-13 school years.

^v PSSA scores, which are Pennsylvania’s mandatory, statewide academic test scores, are issued by PDE. However, the PSSA scores issued by PDE are collected by an outside vendor, Data Recognition Corporation (DRC). The Pennsylvania Department of the Auditor General and KPMG issued a significant weakness in internal controls over PDE’s compilation of this academic data in the Single Audit of the Commonwealth of Pennsylvania for the fiscal year ended June 30, 2014, citing insufficient review procedures at PDE to ensure the accuracy of test score data received from DRC.

^{vi} In the 2011-12 school year, the state benchmarks reflect the Adequate Yearly Progress targets established under No Child Left Behind. In the 2012-13 school year, the state benchmarks reflect the statewide goals based on annual measurable objectives established by PDE.

^{vii} SPP stands for School Performance Profile, which is Pennsylvania’s new method for reporting academic performance scores for all public schools based on a scale from 0% to 100% implemented in the 2012-13 school year by PDE.

^{viii} *Id.* Additionally, federal Title I designations of Priority, Focus, Reward, and No Designation are new federal accountability designations issued by PDE to Title I schools only beginning in the 2012-13 school year. Priority schools are the lowest 5%, focus schools are the lowest 10%, and reward schools are the highest 5% of Title I schools. All Title I schools not falling into one of the aforementioned percentage groups are considered “No Designation” schools. The criteria used to calculate the percentage rates is determined on an annual basis by PDE.

^{ix} Title I Federal accountability designations for Title I schools originate from PDE and are determined based on the number of students at the school who receive free and/or reduced price lunches. School lunch data is accumulated in PDE’s CN-PEARS system, which is customized software developed jointly with an outside vendor, Colyar, Inc. The Pennsylvania Department of the Auditor General and KPMG issued a significant deficiency in internal controls over the CN-PEARS system in the Single Audit of the Commonwealth of Pennsylvania for the fiscal year ended June 30, 2014.