PERFORMANCE AUDIT

The School District of the City of Erie

Erie County, Pennsylvania

December 2015

EUGENE A. DEPASQUALE • AUDITOR GENERAL •

Commonwealth of Pennsylvania
Department of the Auditor General

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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 January 18, 2011 through November 10, 2015, except as otherwise indicated in the audit scope, objectives, and methodology section of the report. Compliance specific to state subsidies and reimbursements was determined for the 2008-09, 2009-10, 2010-11, 2011-12, and 2012-13 school years.

Audit Conclusion and Results

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

Finding No. 1: The District's Persistent Annual Operating Deficits Have Not Been Cured by Short-Term Financial Maneuvers. Our review of common financial benchmarks used to evaluate school district finances found the District faces a number of fiscal challenges. This finding first addresses the District's deteriorating fund balance, operating deficits, and cash flow problems. It then discusses some of the causes of these problems, such as funding limitations and increasing charter school costs. Finally, it discusses the reporting deficiencies and other accounting issues we identified (see page 7).

Finding No. 2: The District's Poor Internal Controls Over Transportation Data for Services Provided to Nonpublic and Charter School Students Resulted in an Underpayment of Nearly $275,000. The District continued to fail to properly account for transportation operations related to nonpublic and charter school students. In the last five consecutive audit reports, we recommended the implementation of procedures to account for, review, and reconcile transportation services. Failure to do so negatively impacted the already financially strapped District. We found that the District underreported the number of charter school students who received transportation services paid for by the District. This reporting error resulted in potential lost revenue of $272,965 (see page 19).

Finding No. 3: The District Provided More Than 100 Cell Phones to Employees, School Board Members, Consultants, and Others Without Policies and Procedures in Place to Monitor Usage and Increasing Costs. For the four year period, 2011-12 through 2014-15, the District paid for more than 100 cell phones issued to employees, Board of School Directors (Board) members, a consultant, a solicitor, and two retired employees. The

District did not have policies and procedures to govern the assignment and usage of district-paid cell phones or to monitor the corresponding usage and costs. The District also failed to require employees and others to sign user agreements, which typically restrict the use of government property (see page 23).

Finding No. 4: The District Disregarded Regulations Pertaining to the Rehiring of Annuitants and Failed to Document the Exceptions Allowing Them to Work for the District, Several for at Least Eight Consecutive Years. Between 2008 and 2013, we found the District compensated 46 rehired retirees, an average of 29 retirees per year. Many returned to District work for three or more consecutive years, in possible noncompliance with the Public School Employees' Retirement Code (PSERC) and its related guidelines (see page 28).

Status of Prior Audit Findings and Observations. With regard to the status of our prior audit recommendations to the District, we found that the District had taken appropriate corrective action in implementing our recommendations pertaining to findings in the areas of improper tuition agreement and tuition waivers (see page 37), certification deficiencies (see page 38), and charter school tuition (see page 39). Additionally, the District had taken appropriate corrective action in implementing our recommendations pertaining to observations in the areas of information technology (IT) (see page 42) and a Memorandum of Understanding (MOU) (see page 43).

However, the District did not take appropriate corrective action in implementing our recommendations relating to findings in the areas of General Fund deficits see page 35), pupil transportation (see page 38), student activity fund practices (see page 40), and the re-employment of retired employees (see page 41).

Findings and Observations

Finding No. 1	The District's Persistent Annual Operating Deficits Have Not Been Cured by Short-Term Financial Maneuvers

Criteria relevant to the finding:

The annual general fund budget is addressed under Section 687 of the Public School Code (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."

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.
- A current asset ratio or trend of ratios approaching one or less indicates a declining ability to cover obligations with the most liquid assets.

Our review of common financial benchmarks used to evaluate school district finances found the District faces a number of fiscal challenges. This finding first addresses the District's deteriorating fund balance, operating deficits, and cash flow problems. It then discusses some of the causes of these problems, such as funding limitations and increasing charter school costs. Finally, we discuss the reporting deficiencies and other accounting issues we identified.

It was recently brought to our attention that the fiscal year ended June 30, 2014 financial statements audited by an independent auditor are in the process of being restated. As of the date of the issuance of this report, the restated fiscal year end balances were still in draft form and not formally issued by the independent auditor in their fiscal year ended June 30, 2015 audit report. Accordingly, our finding presents the results of our review of the data that was available during the audit

Deteriorating General Fund Balance

For fiscal years 2009 through 2014, we found the District had an overall deteriorating General Fund balance, ending in a $4.7 million deficit for the fiscal year ended June 30, 2014. The following chart indicates the District had General Fund deficits for four of the last six fiscal years.

Criteria relevant to the finding (continued):

- The cost for a school district student attending a charter school is paid out of the sending district's operating funds. This results in a reduction of the funds available for use in providing educational services to the district's students that remained in the traditional public school. This scenario continues until the number of students is so large that the district can reduce costs by closing a school building and reduces the number of staff employed by the district.

Section 433 of the PSC, 24 P.S. § 4-433, addresses the duties of the Board Secretary providing, in part:

"The secretary of the boards of school directors shall perform the following duties:

(7) He shall keep correct accounts with each receiver of taxes, school treasurer, or school tax collector of the district, reporting a statement of the same, together with a statement of the finances of the district, at each regular meeting of the board, which statement shall be entered in full upon the minutes . . ."

Erie SD General Fund[1]
Year-End Fund Balance Comparison

June 30	Fund Balance/(Deficit)
2009	($1,987,429)
2010	($7,930,597)
2011	($14,680,022)
2012	$377,897
2013	$2,596,902
2014	($4,734,725)

The primary driver of the District's deteriorating General Fund balance is persistent annual operating deficits, which occur when total expenditures exceed total revenues. The following chart shows that over a six year period, the net operating deficit exceeded $34 million.

Erie SD Comparison of General Fund
Operating Revenues and Expenditures[2]

Fiscal Year	Revenues	Expenditures	Surplus/(Deficit)
2009	$157,390,999	$164,882,293	($7,491,294)
2010	$165,043,382	$172,543,456	($7,500,074)
2011	$168,592,380	$176,458,090	($7,865,710)
2012	$156,726,340	$160,019,477	($3,293,137)
2013	$162,429,323	$163,434,659	($1,005,336)
2014	$168,321,135	$175,207,627	($6,886,492)
Total from Operations	$978,503,559	$1,012,545,602	($34,042,043)

Even with annual operating deficits, the District was able to achieve a positive year-end General Fund balance in fiscal years 2012 and 2013 through its use of other financing sources, which are discussed in more detail later in this finding.

The District's operating revenues are derived from federal, state, and local sources. The local source, which is comprised of tax revenue, accounts for 33 percent of the District's total operating revenue for the 2014 fiscal year. The state and federal revenues make up the remaining 67 percent of the total operating revenues for the 2014

[1] Information obtained from the Independent Auditors Report, Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Funds, fiscal years ending June 30, 2009 through June 30, 2014.
[2] Information obtained from the Independent Auditors Report, Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Funds, fiscal years ending June 30, 2009 through June 30, 2014.

Criteria relevant to the finding (continued):

Additionally, Section 441 of the PSC, 24 P.S. § 4-441, provides:

"The school treasurer shall settle his accounts annually with the board of school directors for each school year."

fiscal year. The state and federal revenue sources are commonly referred to as subsidies. The District relies more heavily on subsidies as a revenue source than most other districts in the Commonwealth.

Because the District relies so heavily on subsidies, its financial condition was greatly affected by a $9 million subsidy cut in 2011-12. While the subsidies increased in the next two fiscal years, subsidy amounts did not return to the 2010-11 level.

According to District officials, in response to the subsidy cuts and the declining fund balance, the District was forced to reduce expenditures. Actions taken by the District included closing three schools and laying off over 200 employees.

Even with the reduced expenditures, the subsidy reductions coupled with annual operating deficits caused the District to pursue other sources of revenue outside of its normal operating revenues. For example, in 2011-12, the District received $10.2 million in proceeds through a sale-leaseback arrangement and it realized another $6 million through a debt restructuring. In 2012-13, the District sold some buildings, which produced a one-time revenue stream of over $2 million.

These actions allowed the District to achieve a positive General Fund balance for the years ended 2012 and 2013, but in the case of the sale-leaseback arrangement, ended up costing the District substantially more in the long term.

Costly Sale-Leaseback Debt

To address the District's anticipated shortfall for fiscal year 2011-12, the Board approved a resolution on March 14, 2012, to enter into a sale-leaseback agreement with the Erie County General Authority for four school district buildings no longer in use. The arrangement provided the District with a one-time cash infusion in exchange for an expensive, 20-year obligation, at the end of which the District has the option to buy back each building for one dollar.

Per the leaseback agreement, the *Guaranteed Lease Revenue Bonds, Series of 2012 A,* issued April 23, 2012, provided the District with $10.2 million in cash after payment of issuance and underwriter costs of more than $300,000. According to the *Bond Debt Service* schedule, the interest rate over the life of the bond increases incrementally from 2.75 percent in 2012, to 5.75 percent in 2026, where it remains for the duration of the 20-year term, which ends in 2031.

This agreement obligates the District to pay the county authority approximately $900,000 per year for 20 years. The impact on the fund balance from the sale/leaseback transaction appears to be short-term, despite the long-term obligation. The decision to enter into this agreement to meet unanticipated cash needs will end up costing the District over $6 million when it eventually repays all of its principal, interest, and fees as shown below:

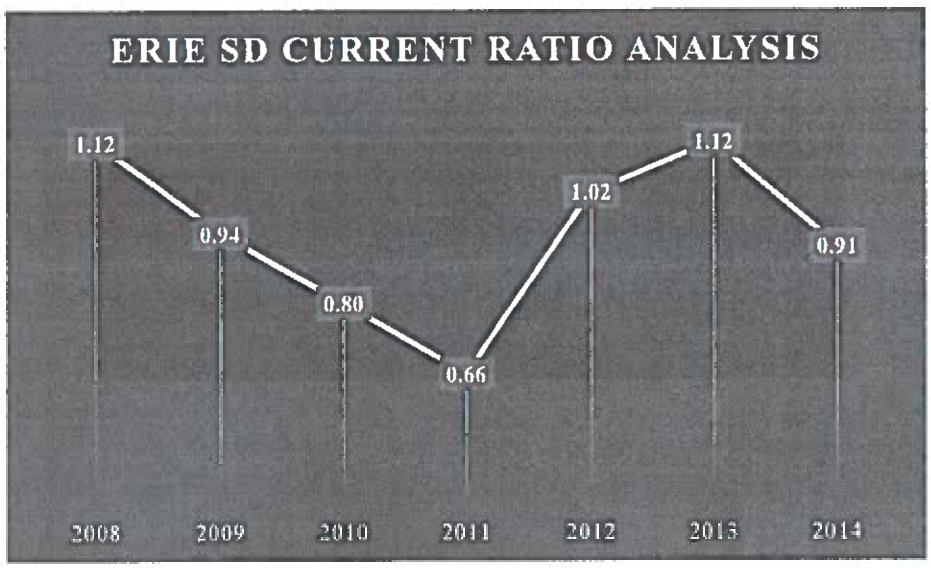
Erie SD Comparison of Sale Proceeds & Leaseback Payments			
Lease Bond Proceeds	$10,475,000	Principal Repayment	$10,475,000
Fees	($314,205)	Total Interest	$6,000,000
Net Proceeds to District	**$10,160,795**	**Total Repayment**	**$16,475,000**

Liquidity & Cash Flow Problems

One of the key measures of a District's financial condition is known as the current ratio, which is used to gauge a school district's ability to meet its current obligations (as opposed to long-term). A current ratio of 1.0 indicates that a school district has current assets equal to its current liabilities and can theoretically pay all of its current bills on time without any cash or other liquid assets leftover. When the current ratio dips below 1.0, then a school district may have trouble paying its current obligations on time due to cash flow shortages.

The table and the graph below highlight two key points: until 2011-12, when the District sought revenues from other financial sources as discussed earlier, its current ratio was deteriorating from year to year. In addition, the effect of those additional revenues appears to be short-term given the District's drop in the current ratio during the 2013-14 fiscal year.

ERIE SD GENERAL FUND ANNUAL CURRENT RATIO[3]			
Fiscal Year	Current Assets	Current Liabilities	Current Ratio
	----- (in millions) -----		
2008	$31.2	$27.9	1.12
2009	$28.9	$30.8	0.94
2010	$31.8	$39.7	0.80
2011	$28.3	$42.9	0.66
2012	$20.8	$20.4	1.02
2013	$24.5	$21.9	1.12
2014	$22.9	$25.1	0.91



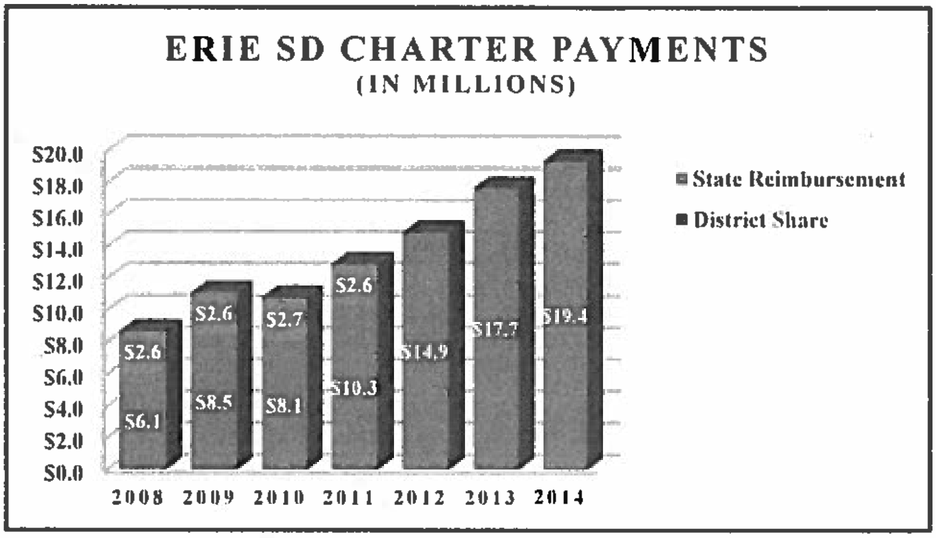
Continually Increasing Charter School Costs

The District's charter school tuition costs tripled during fiscal years 2008 through 2014, and it paid $85 million in that time (net of state reimbursements). This obligation 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 annual increase in the District's required payments to charter schools, offset by the State's partial reimbursements. The financial burden on the District grew from gross tuition payments of

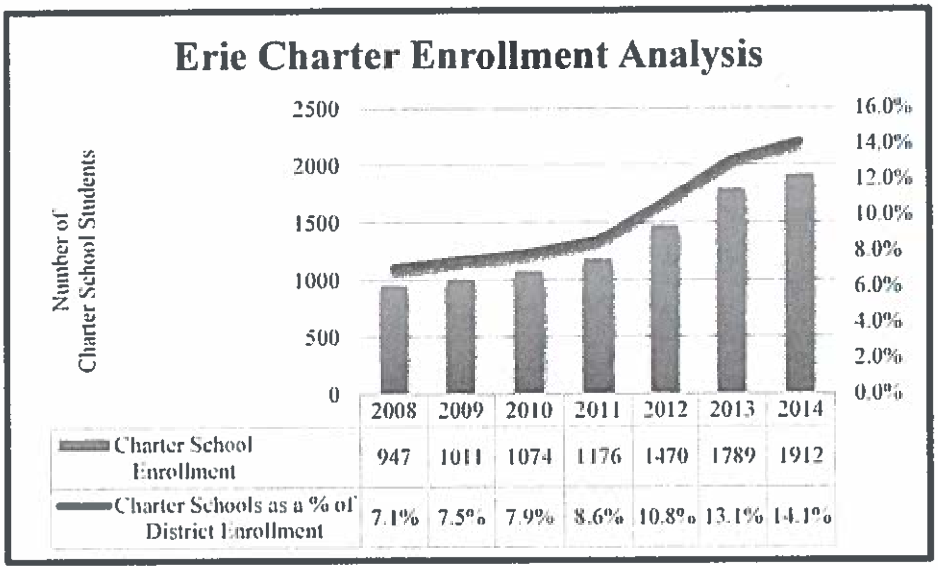
[3] Information obtained from the Independent Auditors Report, Balance Sheet – Governmental Funds, fiscal years ending June 30, 2008 through June 30, 2014.

$8.7 million in 2008, exclusive of the state reimbursement for that year, to over $19 million in 2014. To make matters worse, the State eliminated its partial reimbursements for charter schools after 2011, exacerbating the already growing financial strain on the District.



The charter school funding formula and the State's elimination of school district reimbursements for their charter school costs in 2011, together with the increasing charter school enrollment, produced an increase in the financial obligation each year from 2008 through 2014, except for the 2010 school year. Factoring in the partial reimbursements from the State from 2008 through 2011, the impact on the District's actual expenditures increased from 3.8 percent in 2008 to 11.1 percent in 2014.

Enrollment in charter schools more than doubled during the period to almost 2,000 students, whereas the District's overall enrollment grew by only 1 percent to about 13,600 in the same period. As a result, charter school enrollment as a percentage of District enrollment also doubled from 7 percent in 2008 to 14 percent in 2014. District personnel believe the trend of increasing charter school enrollment will continue. The following chart demonstrates the growth in charter school enrollment and its relationship to the District's enrollment.



Despite the efforts of the District to reduce expenditures by laying off staff and closing buildings, the District's charter school expenses coupled with the lack of state reimbursements are increasing the District's operating expenses and driving their liquidity issues.

Other Fiscal Concerns

Our review of the District's financial operations revealed several other fiscal concerns as detailed in the following sections.

Incomplete and Lack of Timely Reporting

Our audit found the monthly treasurer's report is not being provided to the Board timely, which may impact the Board's ability to make informed financial decisions. We found that these reports were three-to-four months late 39 percent of the time for the 49 regular board meetings held between May 2010 and December 2014. We also found that in several monthly meetings more than one report was presented for approval.

One of the causes noted for late submission of the monthly treasurer's reports was the delayed preparation of bank reconciliations months after the bank statements were received by the District from the bank. Timeliness in performing reconciliations is a key component of its effectiveness as an internal control for discovering and correcting errors. As noted in the criteria, the PSC requires the District to submit a monthly report regarding the District's finances.

Also, while the administration's reporting includes beginning and ending cash availability, revenues received, disbursements made, and cash flow statements, it did not provide reports such as balance sheets and income statements to provide for a more thorough evaluation of the District's financial standing and operations. Without complete monthly treasurer's reports, the Board cannot make sound decisions about how to use the District's public funds. In addition, this lack of information makes it more difficult for the Board to hold the District's administration accountable for its performance and for its implementation of the Board's fiscal policies.

Failure to Reconcile Accounts & Make Adjusting Journal Entries

The issue of unreconciled accounts has been an ongoing problem for the District. Its Independent Audit Report (IAR) for the fiscal years ended June 30, 2013 and June 30, 2014, included findings noting specifically "that the grant program coordinators were not reconciling the expenditures per the general ledger to the program grant reports." Without up-to-date account reconciliations, the District's management and Board cannot make informed financial decisions and errors cannot be detected and corrected in a timely manner.

The IARs for the fiscal years ended June 30, 2013 and June 30, 2014, recommended over 100 adjusting journal entries to correct bookkeeping errors or to record accruals and other adjustments that should have been made by the finance department. Without performing year-end closing procedures, including the reconciliation of all balance sheet accounts, the District's true financial standing is unknown. Therefore, the Board lacks the information it needs to make informed decisions.

Incomplete Wage Records

For the 2012-13 fiscal year, the District could not provide quarterly payroll reports to support the social security and retirement wages reported to PDE. In addition, the District did not have the PSERS Act 29 Reconciliation[4] on file to reconcile the District's retirement reimbursement. This report is created by PSERS and includes adjustments that are made to the retirement wages originally reported to them by the District.[5]

The District instead provided the federal quarterly reports.[6] However, there were significant unreconciled differences between the wages reported to PDE and the wages reported to the Internal Revenue Service (IRS), as shown in the following chart:

ERIE SD: Unreconciled Differences in Reported Wages			
Fiscal Year Quarter	**Soc. Sec. & Medicare Reported to PDE**	**Soc. Sec. & Medicare Reported to IRS**	**Unreconciled Difference Over/(Under)**
3rd 2012	$ 29,688,401	$ 34,090,291	($4,401,890)
4th 2012	38,067,859	38,067,859	0
1st 2013	31,337,527	35,671,144	(4,333,617)
2nd 2013	38,804,511	38,403,832	400,679
Total	**$137,898,298**	**$146,233,126**	**($8,334,828)**

The District attributed the unreconciled differences to new financial software that only supported the federal filing of Social Security and Medicare wages and not those reported for reimbursement from PDE. As a result, according to the financial supervisor, the District instead created manual reports to submit to PDE. These reports, however, were not provided to the auditors for verification.

Without adequate supporting documentation, we were unable to determine the accuracy of the reimbursements received for the 2012-13 fiscal year. We found varying levels of incomplete wage records for the other audit years, as well. Inadequate reconciliation procedures allowed this error to go undetected until it was found during our audit.

In conclusion, the District appears to be making efforts to address its cash flow problems through the use of short-term financing maneuvers. The short-term financings have not fixed the real financial problem of annual deficits resulting from operating revenues being consistently lower

[4] 24 Pa.C.S. §§ 8326, 8329, and 8535.
[5] Act 29 of 1994 changed the way Pennsylvania's LEAs are reimbursed for Social Security contributions.
[6] The federal reports filed containing the related data are the IRS 941 forms.

than expenses. Short-term financing sources used by the District during the fiscal years ending 2009 through 2014 provided only short-term financial relief. As discussed earlier in this finding, the cumulative effect of its operations resulted in a $34 million operating deficit for the period from fiscal years ending 2009 through 2014. The structural operating issues must be corrected if the District is to stop the ongoing annual deficits and rebuild a fund surplus. To help the District improve management of its fiscal environment it should, at a minimum, implement the following recommendations.

Recommendations

The *School District of the City of Erie* should:

1. Develop a short-term (one-to-three years) operating plan to identify and address the structural elements that are leading to annual operating deficits. This plan must, at a minimum, annually balance operating expenditures with operating revenues.

2. Establish procedures to make appropriate periodic journal entries, as well as year-end adjustments, in order to properly and timely account for all transactions and provide the Board with complete, accurate financial information. If necessary, it should seek assistance from outside professional accountants.

3. Obtain in a timely manner, and maintain as part of wage documentation records, the PSERS Act 29 reports and any other wage documentation required to verify the District received the correct amount of social security and retirement reimbursements.

Management Response

District management provided the following response:

"The district agrees with the Auditor General's finding regarding financial reporting and is in the process of restructuring its accounting system to provide complete, timely, and accurate financial information to the School Board, Administration, and others. Once the accounting system has been restructured, a five-year financial projection model will be developed to assist with long-term planning.

The Auditor General's recommendation to develop an operating plan that annually balances operating expenditures with operating revenues is just not possible in the current fiscal environment. As detailed in this finding, the district has been in a situation where it has had to cut its way to a balanced budget for the last five years. Early on, there was room to trim programs, staff and other expenditures. But, as the years have gone on, it has been an increasing painful process. The refinancing options of the district's various debt instruments have been maxed out, three elementary schools have been closed, more than 200 staff have been furloughed, and central administration staff has been cut in half. Many employee groups have had salaries frozen or have received 1% increases, and the teachers have worked without a contract for nearly two years. Despite these local efforts, each budget year begins in a multi-million dollar deficit.

The district has done its part. On a per pupil basis, Erie's Public Schools spends less than 80% of the districts across the commonwealth. There is nothing left to cut without causing serious damage to educational programs. The district's buildings are crumbling, and though there is a detailed and will researched ten-year facilities plan, it would require an investment of about $300 million to build or renovate schools that are equitable locally and on par with schools throughout the state. The simple fact is the district needs additional funding.

Unfortunately, property tax payers in the City of Erie – already stretched thin due to the City's own financial challenges – have been forced to bite off an even larger piece of the educational funding pie. And, considering the fact that 30% of all property in the City is deemed tax exempt (representing $1.2 billion in assessed real estate value), the burden is even greater on the individual homeowner in urban areas like Erie. Continuing to raise taxes is not an option.

The absence of a fair funding formula ensures that Erie's Public Schools will continue to exemplify the embarrassing disparity between the wealthiest and poorest districts in Pennsylvania. The fact that our state ranks 50th in that regard should be motivation enough to implement the recommendations of the Basic Education Funding Commission."

Auditor Conclusion

We are encouraged that the District realizes the seriousness of its financial challenges and is in the process of restructuring its accounting system in order to provide complete, timely, and accurate financial information to the Board, administration, and others. We believe the development of a short-term operating plan will assist the administration in identifying the structural element deficiencies which have led to the historical annual operating deficits. Furthermore, the development of a five-year financial plan will allow the District's administration and Board to make better long range financial decisions. Since the District is in the process of restructuring the accounting system and developing a five-year financial projection, we will evaluate the effectiveness of those actions and any other corrective actions during our next audit of the District.

Finding No. 2	**The District's Poor Internal Controls Over Transportation Data for Services Provided to Nonpublic and Charter School Students Resulted in an Underpayment of Nearly $275,000**

Criteria relevant to the finding:

Section 2509.3 of the PSC, 24 P.S. § 25-2509.3, provides for payments on account of transportation of nonpublic school students.* This provision provides that each school district, regardless of classification, shall be paid by the Commonwealth for the 2001-02 school year, and every school year thereafter, the sum of $385 for each nonpublic school student transported.

*PDE also reimburses school districts $385 for each charter student transported, which is the same as for nonpublic school students. *See* Section 1726-A(a) of the Charter School Law (CSL), 24 P.S. § 17-1726-A(a).

Section 23.4 of the State Board of Education regulations, *22 Pa. Code § 23.4*, states, in part:

The board of directors of a school district shall be responsible for all aspects of student transportation programs, including the following:

***

(6) The maintenance of a record of students transported to and from school, including determination of students' distances from home to pertinent school bus loading zones.

PDE's instructions for completing End-of-Year Student Transportation reports provide that procedures, information, and data used by the LEA should be retained for audit purposes.

The District continued to fail to properly account for transportation operations related to nonpublic and charter school students. We found significant errors in the District's transportation reporting to PDE that resulted in a potential underpayment of $272,965.

In the last five consecutive audit reports, we recommended the implementation of procedures to account for, review, and reconcile transportation services. Failure to do so continued to negatively impact the already financially-strapped District either by having its funding reduced for over-reporting errors,[7] as identified in previous audits, or by not receiving all that it was entitled to due to underreporting its numbers, as identified in this current audit.

According to the PSC, a nonpublic school is defined, in part, as a nonprofit school other than a public school within the Commonwealth.[8] The PSC requires school districts to provide transportation services to students who reside in its district and who attend nonpublic schools, providing for a reimbursement from the Commonwealth of $385 for each nonpublic school student transported by the District. PDE also reimburses school districts this same amount for the transportation of charter school students pursuant to an equivalent provision in the CSL that refers to Section 2509.3 of the PSC.

Our current audit again found errors in the District's reporting of transportation rosters for nonpublic and charter school students for all five school years from 2008-09 through 2012-13. We noted clerical errors, double-reporting of students, and the erroneous inclusion of students who attended schools that didn't fall into the classification of nonpublic or charter schools. However, the most significant error we noted was that the District

[7] In October 2014, the District's funding was reduced by $145,000 for reporting errors related to transportation services.

[8] *See* Section 922.1-A(b) (pertaining to "Definitions") of the PSC, 24 P.S. § 9-922.1-A(b).

failed to account for charter school students who were provided public transportation tokens which are paid for by the District.

(Over)/Under-reporting of students by year			
School Year	Nonpublic	Charter	Under/(Excess) Subsidies
2008-09	(115)	162	$18,095
2009-10	(123)	115	($3,080)
2010-11	(34)	228	$74,690
2011-12	(53)	317	$101,640
2012-13	(31)	243	$81,620
Total	(356)	1,065	$272,965

The numerous reporting errors were caused by a failure to implement internal control procedures as recommended in previous audits. We found the following problems with the District's accounting and reporting procedures related to the transportation of nonpublic and charter school students:

- Failure to obtain independent transportation rosters from the educating nonpublic schools and charter schools, which could be used to reconcile with the District's source documents before submitting data to PDE.

- Absence of a secondary review of transportation data before submission to PDE, or at least the absence of any evidence thereof.

- No evidence of reconciliations between source documents and District records with the preliminary reports from PDE.

In addition to the errors, we found instances where the source documentation provided by the District did not agree with the records provided for the District's transportation services, which were used to report data to PDE.

When we summarized the total errors we identified, we determined that the net effect was the District underreported the number of non-public and charter school students. PDE reimburses the District for transportation services provided to each of those students; therefore, if the District underreported the total number of students then, based on our calculation, the District may been entitled to receive an additional $272,965.[9]

Again, it appears the District is negatively affected by its continued failure to properly and timely account for transportation services provided to its nonpublic and charter school students.

Recommendations

The *School District of the City of Erie* should:

1. Establish detailed, written procedures to ensure the number of nonpublic and charter school students is accurately recorded, reconciled, reviewed, and reported to PDE.

2. Review reports already submitted for the 2013-14 and 2014-15 school years for accuracy and, if errors are found, submit revisions to PDE.

Management Response

District management provided the following response:

"The district agrees with the Auditor General's finding and has already begun to implement the recommendations."

Auditor Conclusion

We are encouraged that the District's current administration has realized the seriousness of the District's inadequate procedures to obtain, verify, and report transportation data to PDE. We are further encouraged that the current administration noted they have begun to implement corrective actions to address the deficiencies outlined in this finding. Since these actions were

[9] The PDE reimbursement is $385 per student, and we identified errors with 709 students. Therefore, the potential underpayment is $272,965.

implemented subsequent to our audit, we will evaluate the effectiveness of the corrective actions during our next audit of the District.

Finding No. 3	The District Provided More Than 100 Cell Phones to Employees, School Board Members, Consultants, and Others Without Policies and Procedures in Place to Monitor Usage and Increasing Costs

Criteria relevant to the finding:

The *E-policy Handbook: Rules and Best Practices to Safely Manage Your Company's Email, Blogs, Social Networking, and Other Electronic Communication Tools* (2009) states, in part:

http://www.lbm-engine.com/messagelabs/MessageLabs_ePolicy_Guidebook.pdf

"As an organization, it's crucial to develop guidelines that curb the boundless problems that excessive or inappropriate cell phone use can create for your organization."

"A well-crafted cell phone usage policy will not only set expectations for incoming employees but will also address serious issues concerning the safety, security, responsibility, and privacy of cell phone use."

"Having a policy is only the first step. The policy must be enforced and your employees must understand the consequences of failing to abide by its terms."

"Any workplace policy is useless if not properly enforced. After you've solidified your guidelines, here's how you can make sure they're abided by.

- Keep it updated.
- Have training sessions.
- Explicitly explain disciplinary action.
- Have every employee review and sign it."

For the four year period, 2011-12 through 2014-15, the District paid for more than 100 cell phones issued to employees, school board members, a consultant, a solicitor, and two retired employees. The District did not have policies and procedures to govern the assignment and usage of district-paid cell phones or to monitor the corresponding usage and costs. The District also failed to require employees and others to sign user agreements, which typically restrict the use of government property.

Furthermore, we found that many cell phones were provided with authorization for unlimited personal use. According to District officials, employees who were given permission to use their district-issued cell phones for personal use were required to reimburse the District monthly. The reimbursement rate was $25 per month for individuals who had a phone with a data plan and $15 per month for phones without a data plan.

However, unlike the employees, the school board members, a consultant, the solicitor, and two retired employees were not required to reimburse the District even though there were no restrictions on personal usage.

Cell phone expenses for board members cost nearly $25,000.

We found the District paid nearly $25,000 over four years for cell phones for the Board, yet the Board did not reimburse the District for costs related to personal usage.

The following chart shows the annual costs for the review period.

Board Members with District-Paid Cell Phones		
School Year	# Members with Cell Phones	Expense
2011-12	10	$ 7,734
2012-13	7	5,501
2013-14	8	5,713
2014-15	7	5,846
Total		$24,794

According to the Board Secretary, the Board came to an "informal agreement" several years ago to allow its members to have cell phones in exchange for not claiming personal mileage for attending board meetings. Not only did the Board fail to agree to this arrangement at a public meeting, but the arrangement also resulted in a costly tradeoff for a city district such as Erie where reimbursable mileage for board members is significantly less than other area school districts. Mileage is significantly less due to the requirement for board members to reside in the District and the square mileage of the District is less than most districts in the county.

<u>The District paid more than $4,000 for a consultant's cell phone and $1,400 for a solicitor's cell phone.</u>

The District also provided a cell phone to the former Athletic Director, a rehired annuitant who worked as an independent consultant. Total costs for the four years, between 2011-12 and 2014-15, were nearly $4,200. The cell phone was not disclosed as a fringe benefit in any of his consulting agreements for each of the four years.

The District also paid more than $1,400 over the three years, between 2011-12 and 2013-14, for a cell phone used by its former contracted solicitor. Again, the District did not require the consultant or the solicitor to reimburse the District for the personal usage benefit.

<u>The District continued to pay for cell phone service for two employees after they retired.</u>

A former Assistant to the Superintendent, who retired in August 2008, retained possession of his district-provided cell phone with the District paying for the service through April 2012. This former employee entered into a consulting agreement with the District for the 2008-09 and 2009-10 school years. We noted that this former employee did start reimbursing the District $25 per month beginning in August 2011. However, the District continued to incur costs and provide this benefit to a former employee.

We also found that an Assistant Superintendent, who retired in January 2009, also retained possession of his district-provided cell phone, with the District paying for the service through December 2011, three years after his retirement. The District did not provide any documentation of reimbursements from this former employee. The District explained that it allowed the former employee to keep his cell phone so the employee could maintain his phone number, and the actual phone itself had little to no value to the District.

A lack of policies and procedures contributed to the district's failure to adequately monitor cell phone costs.

During our review of cell phone invoices, we noted that the total "usage and purchase" charges were more than $18,000 for the four-year audit period. These charges are related to roaming charges, global texting, long distance charges, data overages, and 411 phone number search charges.

A more detailed analysis of the invoices disclosed instances of significant roaming and other usage charges. For example, we found one employee who incurred more than $1,800 in roaming charges over a four-month billing period. When we asked the District about these charges, officials explained that the employee incurred the charges when she was studying abroad on a Fulbright scholarship. The District further indicated that "the employee will be invoiced for the roaming charges."

We found other numerous examples of employees incurring significant "usage" charges. In response to our inquiries, District officials stated that "other employee(s) who utilized the phone for global texting and long distance charges will be invoiced to reimburse the District and reminded that they are not permitted to use the phone for personal and/or international use." Without user agreements, however, the District may not be able to recoup these charges.

When we reviewed cell phone usage and costs with the District in June 2015, we found that the District still had not developed a written policy even though we first discussed the lack of policies with the District as early as August 2013.

We found that for each succeeding year in the four-year review period, cell phone costs increased, bringing the total cost in just four years to over $370,000. Considering the increasing costs along with the numerous issues we found as part of our audit, it is imperative that the District develops and implements policies and procedures to govern the assignment of cell phones, personal use restrictions and reimbursements, as well as the timely monitoring of usage and costs. These policies and procedures are also necessary to help ensure prudent use of taxpayer dollars.

Recommendations

The *School District of the City of Erie* should:

1. Immediately develop and implement board-approved cell phone policies to address the following, at a minimum:

    a. The use of District cell phones by the Board, current employees, retired employees, terminated employees, and consultants.

    b. Roaming, data, long-distance, and other charges.

    c. Personal use restrictions.

    d. A requirement of every recipient of a District cell phone to sign a user agreement so that the District has remedies it can enforce in the event of misuse of the cell phones.

2. Implement oversight procedures so that cell phone costs and usage are monitored on a monthly basis. It should also review cell phone plan features on all of its currently issued cell phones to ensure that those features are necessary.

Management Response

District management provided the following response:

"The district agrees with the Auditor General's recommendations to implement Board approved cellular phone policies and implement stricter oversight procedures.

As indicated in the finding, the district's total cellular charges over the four year audit period were just over $370,000. However, 37% of that cost was offset by reimbursements from employees and the federal e-Rate program. The district's net annual cost ranged from $34,342 to $56,575 during the audit period. Although the district's cellular costs did increase over the four year period, the increase can be attributed to the increase in the number of students participating in the district's cyber program during the same period. Students participating in this program receive a laptop with a wireless internet card provided by the district's cellular provider. This program was developed to compete with cyber charter schools and saves the district between $5,000 and $14,000 per student annually. Participation in this program has increased from 4 students in 2011-12 to 52 students in 2014-15."

	Cellular Charges			Reimbursements		
Year	**Regular**	**Cyber Program**	**Total**	**e-Rate**	**Employee**	**Net Cost**
2011-12	$ 64,179.81	$ 2,940.00	$ 67,119.81	$ (29,009.28)	$ (3,767.75)	$ 34,342.78
2012-13	$ 74,925.77	$ 16,080.00	$ 91,005.77	$ (33,196.00)	$ (12,654.75)	$ 45,155.02
2013-14	$ 72,027.27	$ 24,480.00	$ 96,507.27	$ (25,689.63)	$ (18,780.34)	$ 52,037.30
2014-15	$ 88,494.28	$ 27,420.00	$ 115,914.28	$ (37,332.88)	$ (22,006.33)	$ 56,575.07
Total	$ 299,627.13	$ 70,920.00	$ 370,547.13	$ (125,227.79)	$ (57,209.17)	$ 188,110.17

Auditor Conclusion

We are encouraged that the District agrees with our recommendations for policies and greater oversight procedures. Full implementation of policies and procedures would be a positive step to help ensure the proper use of District cellular phones and prudent use of taxpayer dollars. We will evaluate the corrective actions taken by the Board and administration during our next audit.