

PERFORMANCE AUDIT

Greater Johnstown School District Cambria County, Pennsylvania

December 2016



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE
AUDITOR GENERAL

Mr. Michael Vuckovich
Acting Superintendent
Greater Johnstown School District
1091 Broad Street
Johnstown, Pennsylvania 15906

Mr. Richard Unger, Board President
Greater Johnstown School District
1091 Broad Street
Johnstown, Pennsylvania 15906

Dear Mr. Vuckovich and Mr. Unger:

Our performance audit of the Greater Johnstown School District (District) evaluated the application of best practices in the areas of finance, hiring practices, conflicts of interest, and school safety. In addition, this audit determined the District's compliance with certain relevant state laws, regulations, contracts, and administrative procedures (relevant requirements). This audit covered the period July 1, 2012 through June 30, 2015, except as otherwise indicated in the audit scope, objective, and methodology section of the report. The audit was conducted pursuant to Sections 402 and 403 of The Fiscal Code (72 P.S. §§ 402 and 403), and 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 objectives.

Our audit found that the District complied, in all significant respects, with relevant requirements and applied best practices, except as detailed in our three findings noted in this audit report. A summary of the results is presented in the Executive Summary section of the audit report.

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 relevant 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

December 9, 2016

cc: **GREATER JOHNSTOWN SCHOOL DISTRICT** Board of School Directors

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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, 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). Compliance specific subsidies and reimbursements were determined for the 2013-14 and 2014-15 school years.

Audit Conclusion and Results

Our audit found that the District applied best practices and complied, in all significant respects, with certain relevant state laws, regulations, contracts, and administrative procedures, except as described in the three findings described below.

Finding No. 1: The District's General Fund Decreased by Over \$10 Million During the Five-Year Period From the 2010-11 Fiscal Year Through the 2014-15 Fiscal Year due to Persistent Operating Deficits. 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 five years - from the fiscal year ended on June 30, 2011 through the fiscal year

ended June 30, 2015. The General Fund balance decreased from \$17 million as of June 30, 2011, to \$6.3 million as of June 30, 2015. The decreasing General Fund balance is the direct result of operational deficits posted for four of the five years reviewed (see page 7).

Finding No. 2: Errors in Reporting the Number of Nonpublic Students Transported by the District Resulted in an Underpayment of \$17,710 to the District. The District was underpaid \$17,710 in transportation reimbursement from the Pennsylvania Department of Education (PDE). This underpayment was due to the District incorrectly reporting the number of nonpublic students who were provided transportation by the District during the 2013-14 and 2014-15 school years (see page 18).

Finding No. 3: Questionable Employment Contracts and Separation Agreement Cost the District Over \$136,000. Our review of the District's employment practices during the audit period found that the District entered into questionable employment contracts with a board member's daughter. The District hired this employee without posting the position or even considering other candidates. Then, six months after approving the second contract, the District executed a Separation Agreement and General Release costing the District more than \$136,000 (see page 22).

Status of Prior Audit Findings and Observations. We conducted procedures to determine the implementation status of our prior audit recommendations to the District

from an audit released on December 11, 2013. We found that the District had taken appropriate corrective action in implementing our recommendations pertaining to errors in reporting nonresident membership (see page 30). We also found that the District had taken appropriate corrective action in implementing our recommendations pertaining to the District's transportation costs exceeding the state reimbursement formula (see page 32). Finally, we found that the District did take some corrective action in response to our prior student transportation finding about internal control weaknesses and lack of documentation (see page 31). However, after reviewing the transportation data reported to PDE, we identified errors in the number of nonpublic students transported by the District. The errors are detailed in Finding No. 2 of this report (see page 18).

Background Information

| School Characteristics 2014-15 School Year ^A | |
|--|-----------------------|
| County | Cambria |
| Total Square Miles | 29 |
| Resident Population ^B | 27,641 |
| Number of School Buildings | 4 |
| Total Teachers | 210 |
| Total Full or Part-Time Support Staff | 87 |
| Total Administrators | 22 |
| Total Enrollment for Most Recent School Year | 3,003 |
| Intermediate Unit Number | 8 |
| District Vo-Tech School | Greater Johnstown CTC |

A - Source: Information provided by the District administration and is unaudited.

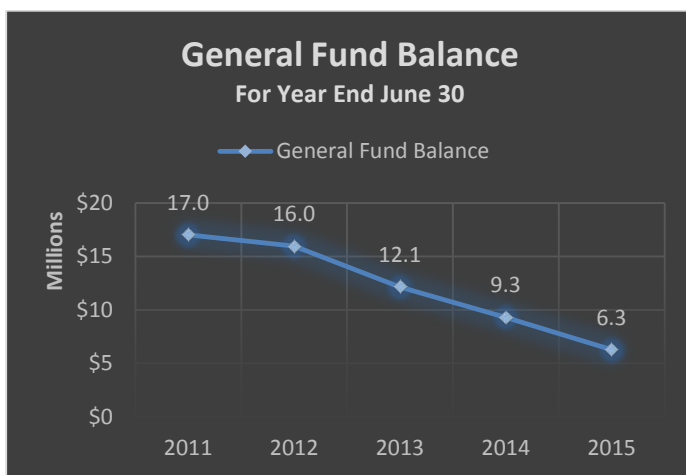
B - Source: United States Census
<http://www.census.gov/2010census>

Mission Statement^A

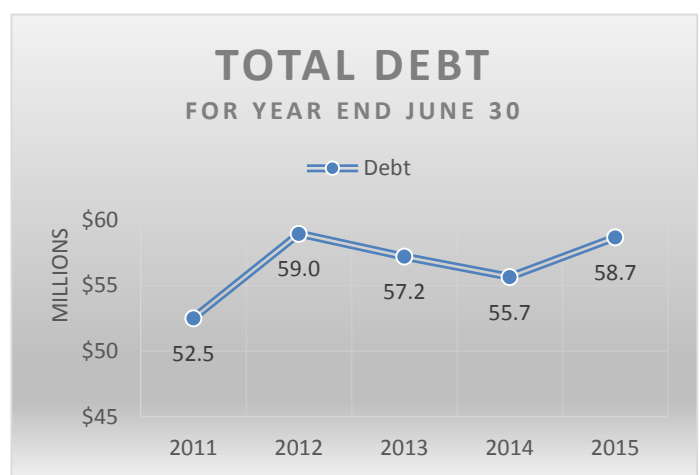
“Through a shared vision, the Greater Johnstown School District, supported by pride and tradition, is committed to creating and sustaining a learning community where all learners will pursue high standards to succeed in a diverse global society.”

Financial Information

The following pages contain financial information about the District obtained from annual financial data reported to PDE and available on PDE’s public website. This information was not audited and is presented for **informational purposes only**.

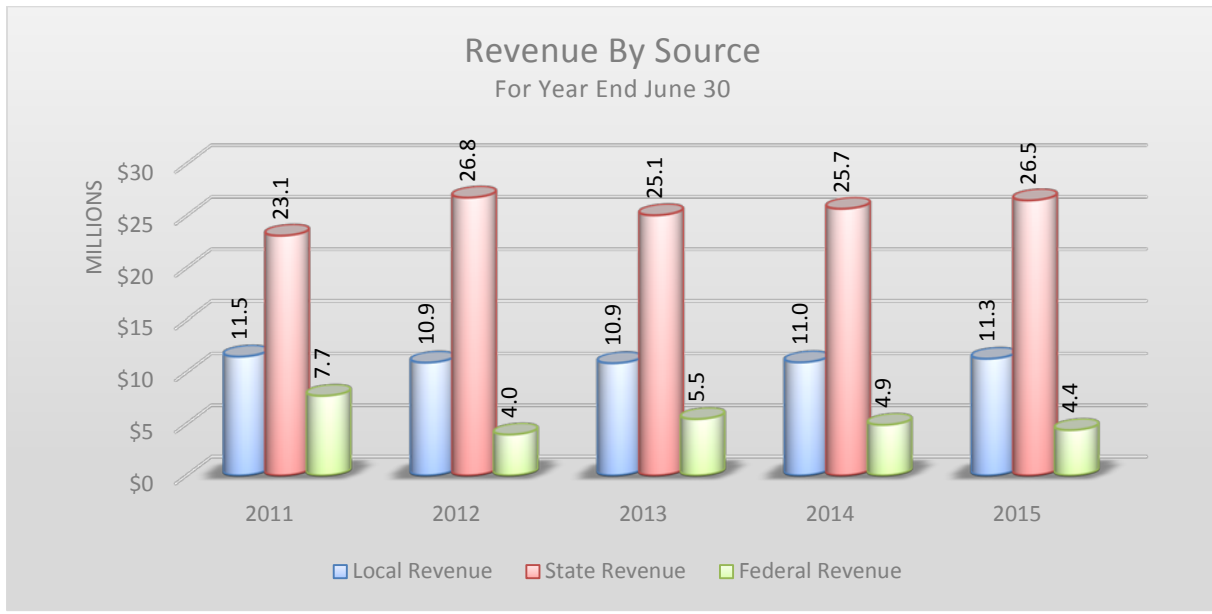
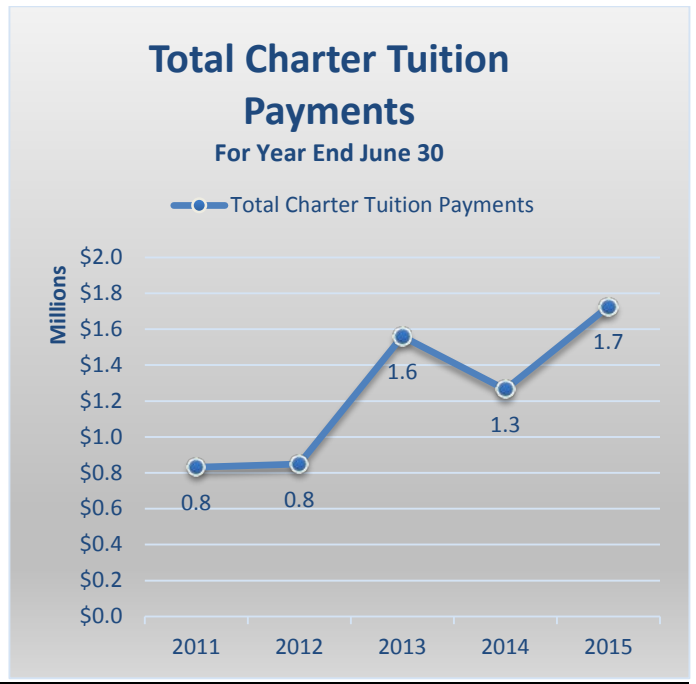
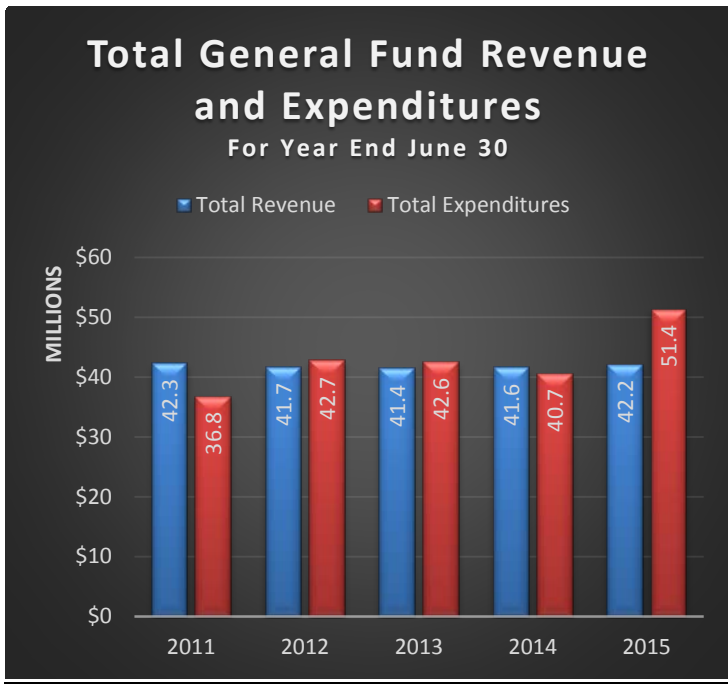


Note: General Fund Balance is comprised of the District’s Committed, Assigned and Unassigned Fund Balances



Note: Total Debt is comprised of Short-Term Borrowing, General Obligation Bonds, Authority Building Obligations, Other Long-Term Debt, Other Post-Employment Benefits, and Compensated Absences.

Financial Information Continued



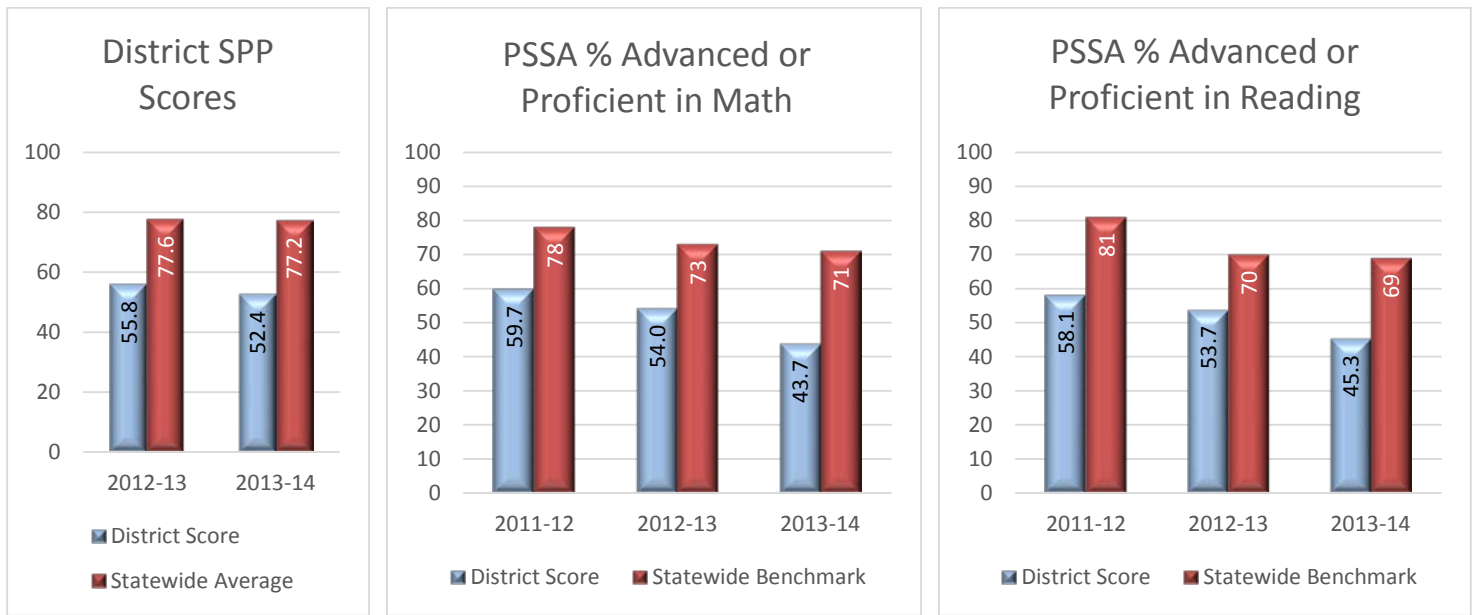
Academic Information

The following table and charts consist of School Performance Profile (SPP) scores and Pennsylvania System of School Assessment (PSSA) results for the entire District obtained from PDE's data files.¹ These scores are presented in the District's audit report for **informational purposes only**, and they were not audited by our Department.

SPP benchmarks represent the statewide average of all district school buildings in the Commonwealth.² PSSA benchmarks and goals are determined by PDE each school year and apply to all public school entities.³ District SPP and PSSA scores were calculated using an average of all of the individual school buildings within the District. Scores below SPP statewide averages and PSSA benchmarks/goals are presented in red.

Districtwide SPP and PSSA Scores

| District | SPP Scores | | PSSA % Advanced or Proficient in Math | | | PSSA % Advanced or Proficient in Reading | | |
|------------------------------|------------|---------|---------------------------------------|---------|---------|--|---------|---------|
| | 2012-13 | 2013-14 | 2011-12 | 2012-13 | 2013-14 | 2011-12 | 2012-13 | 2013-14 |
| <i>Statewide Benchmark</i> | 77.6 | 77.2 | 78 | 73 | 71 | 81 | 70 | 69 |
| <i>Greater Johnstown SD</i> | 55.8 | 52.4 | 59.7 | 54.0 | 43.7 | 58.1 | 53.7 | 45.3 |
| <i>SPP Grade⁴</i> | F | F | | | | | | |



¹ PDE is the sole source of academic data presented in this report. All academic data was obtained from PDE's publicly available website.

² Statewide averages for SPP scores were calculated based on all district school buildings throughout the Commonwealth, excluding charter and cyber charter schools.

³ PSSA benchmarks apply to all district school buildings, charters, and cyber charters. 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 and 2013-14 school years, the state benchmarks reflect the statewide goals based on annual measurable objectives established by PDE.

⁴ The following letter grades are based on a 0-100 point system: A (90-100), B (80-89), C (70-79), D (60-69), F (59 or below).

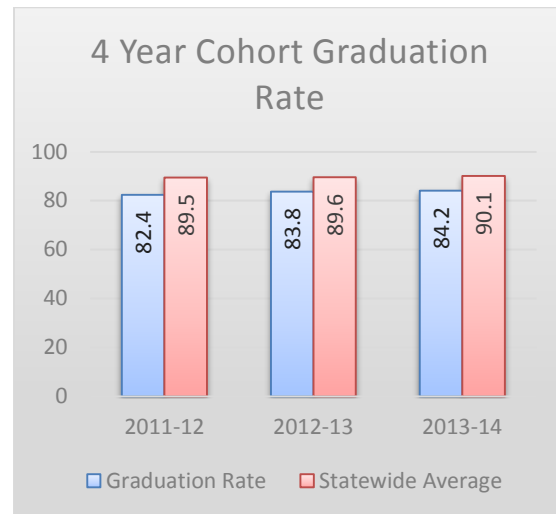
Individual School Building SPP and PSSA Scores

The following table consists of SPP scores and PSSA results for each of the District's school buildings. Any blanks in PSSA data means that PDE did not publish a score for that school for that particular year.⁵

| School Name | SPP Scores | | PSSA % Advanced or Proficient in Math | | | PSSA % Advanced or Proficient in Reading | | |
|---|-------------|-------------|---------------------------------------|-------------|-------------|--|-------------|-------------|
| | 2012-13 | 2013-14 | 2011-12 | 2012-13 | 2013-14 | 2011-12 | 2012-13 | 2013-14 |
| <i>Statewide Benchmark</i> | <i>77.6</i> | <i>77.2</i> | <i>78</i> | <i>73</i> | <i>71</i> | <i>81</i> | <i>70</i> | <i>69</i> |
| <i>East Side Elementary School</i> | 56.6 | 55.2 | 72.9 | 67.5 | 51.1 | 57.0 | 52.7 | 43.4 |
| <i>Greater Johnstown Middle School</i> | 52.1 | 49.1 | 55.3 | 49.9 | 42.8 | 54.8 | 50.8 | 43.4 |
| <i>Greater Johnstown Senior High School</i> | 62.4 | 54.7 | 60.3 | 50.0 | 41.3 | 68.7 | 66.7 | 55.9 |
| <i>West Side Elementary School</i> | 52.0 | 50.6 | 50.3 | 48.6 | 39.8 | 51.9 | 44.7 | 38.5 |

4 Year Cohort Graduation Rates

The cohort graduation rates are a calculation of the percentage of students who have graduated with a regular high school diploma within a designated number of years since the student first entered high school. The rate is determined for a cohort of students who have all entered high school for the first time during the same school year.⁶



⁵ PDE's data does not provide any further information regarding the reason a score was not published.

⁶ <http://www.education.pa.gov/Data-and-Statistics/Pages/Cohort-Graduation-Rate-.aspx>

Findings

Finding No. 1

The District's General Fund Decreased by Over \$10 Million During the Five-Year Period From the 2010-11 Fiscal Year Through the 2014-15 Fiscal Year due to Persistent Operating Deficits

Criteria relevant to the finding:

The benchmarks used as criteria for this objective were based on best business practices established by several entities, including the Pennsylvania Association of School Business Officials (PASBO), the Colorado State Auditor, and the National Forum on Education Statistics. The following are some of the benchmarks used in our evaluation:

1. Operating position is the difference between actual revenues and actual expenditures. Financial industry guidelines recommend that the district operating position always be positive (greater than zero).
2. A school district should maintain a trend of stable fund balances.
3. The district's audit report should contain no instances of significant internal control weaknesses.

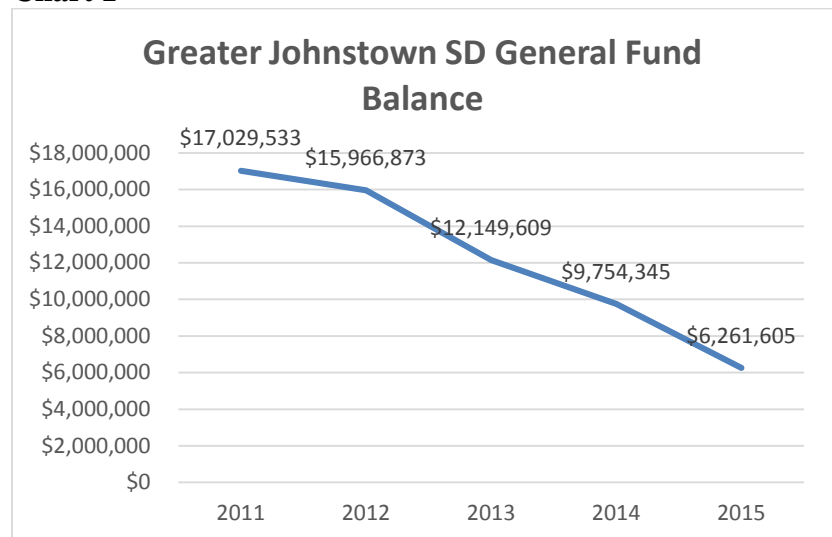
In order to assess the District's financial stability, we reviewed several financial benchmarks to evaluate changes in its financial position over a period of five years from fiscal year ending June 30, 2011 through June 30, 2015. We found that the District is in a declining financial position. Our discussion of the District's declining financial position will cover the following areas:

- General Fund Balance
- Operating Position
- Budgeted vs. Actual Expenditures and Revenues
- Current Ratio
- Charter School Costs

General Fund Balance

Between fiscal years ending June 30, 2011 and June 30, 2015, the District's General Fund balance decreased by \$10.7 million, or 63 percent. The following chart illustrates the District's weakening fund balance:

Chart 1



Note: Information obtained from the District's Independent Auditor's Reports' *Statements of Revenue, Expenditures and Changes in Fund Balance* for the fiscal years ending 2011 through 2015.

*Criteria relevant to the finding
(continued):*

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/uncommitted/unassigned fund balance that should be maintained in the general fund as a reserve to hedge against risk. The GFAO recommends, at a minimum, an unrestricted fund balance in their general fund of no less than 10 percent of regular general fund operating revenues or regular general operating expenditures.

The Pennsylvania School Boards Association (PSBA) in its Annual Overview of Fiscal Health for the 2013-14 school year provided the following information relevant to the following fiscal benchmarks:

- Financial industry guidelines recommend that fund balances be between 5 percent and 10 percent of annual expenditures.
- Operating position is the difference between actual revenues and actual expenditures. Financial industry guidelines recommend that the district operating position always be positive (greater than zero).

The \$17 million General Fund balance as of June 30, 2011, represented 42 percent of the District’s annual expenditures, which is significantly higher than the 10 percent General Fund balance recommended by the GFAO. As of June 30, 2015, the General Fund balance of \$6.3 million represented 14 percent of the District’s expenditures. District officials attributed the steady decline in fund balance to the District utilizing the fund balance to meet rising costs related to employee salaries and benefits.

Of the District’s \$6.3 million General Fund balance, \$4 million has been committed—through formal action of the Board—to pay for future District debt, compensated absences, and retirement payouts. In addition, \$430,282 has been assigned by the District for prepaid expenses.

Deducting the committed⁷ and assigned⁸ amounts from the General Fund balance reduces the District’s available balance to \$1.8 million. This represents less than 4 percent of the District’s expenditures, which is below the recommended 10 percent. Just as individuals should have a “rainy day fund” to deal with emergencies or unforeseen needs, school districts should also have available reserve funds to deal with emergencies, unanticipated expenses, and disruptions to its revenues.

Over the past five fiscal years, the District has depleted more than half of their reserve funds. District officials stated that the District has made financial concessions without eliminating programs. Further, the District has not raised taxes since the 1995-96 school year. This marks a 21 year period of no tax increases as of June 30, 2016.

Operating Position

A school district’s operating position can be determined by reviewing the total expenditures compared to total revenues. An operating deficit occurs when expenditures are greater than revenues. The District’s decreasing fund balance is the direct result of operating deficits in four of the five years reviewed. The District budgeted an operating

⁷ The committed amount is that portion of the fund balance temporarily restricted for specified purposes established by a formal action by the Board. Formal action by the Board is also necessary to modify or rescind a fund balance commitment.

⁸ The assigned amount is that portion of the fund balance intended for a specific purpose that does not meet the criteria to be classified as restricted or committed. The Board has authorized the Business Manager as the official authorized to assign fund balance to a specific purpose.

Criteria relevant to the finding (continued):

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.
- The trend of current ratios should be at least 2 to 1 or increasing. Anything less calls into question the school district's ability to meet its current obligations with existing resources.

deficit for the 2015-16 fiscal year as well. Without an increase in revenue or decrease in expenditures, the District will continue to experience operating deficits and, as a result, the fund balance will continue to decline.

The following table shows a comparison of the District's operational position:

Table 1

| Greater Johnstown SD General Fund Operations | | | |
|---|-----------------------------------|--|------------------------------------|
| Year Ended June 30 | Total Revenues⁹ | Total Expenditures¹⁰ | Surplus/ (Deficit) |
| 2011 | \$ 42,325,450 | \$ 40,703,486 | \$ 1,621,964 |
| 2012 | 41,651,266 | 42,709,928 | (1,058,662) |
| 2013 | 41,397,405 | 46,339,651 | (4,942,246) |
| 2014 | 41,655,204 | 44,495,880 | (2,840,676) |
| 2015 | 42,190,248 | 45,949,307 | (3,759,059) |
| Total: | \$209,219,573 | \$220,198,252 | (\$10,978,679)¹¹ |

District officials attributed the ongoing operating deficits to mandatory increases in expenditures while simultaneously experiencing stagnant revenues. More specifically, District officials stated that the operating deficits were due to the increases in personnel and retirement costs that have outpaced District revenue.

Revenues: The District's total revenue actually decreased during the period reviewed as shown in Table 1. The District's total revenue is comprised of federal, state, and local sources. As shown in Chart 2 below, the District's primary revenue source for the 2014-15 fiscal year was state funding.

As stated above, the District has not raised property taxes since the 1995-96 fiscal year and as a result, local revenue comprises only 27 percent of total revenue in the 2014-15 fiscal year. The District relies heavily on state and federal funding to maintain operations. This reliance on subsidies

⁹ Information obtained from the District's Independent Auditor's Report, *Statement of Revenue, Expenditures and Changes in Fund Balance*, fiscal years ending 2011 through 2015.

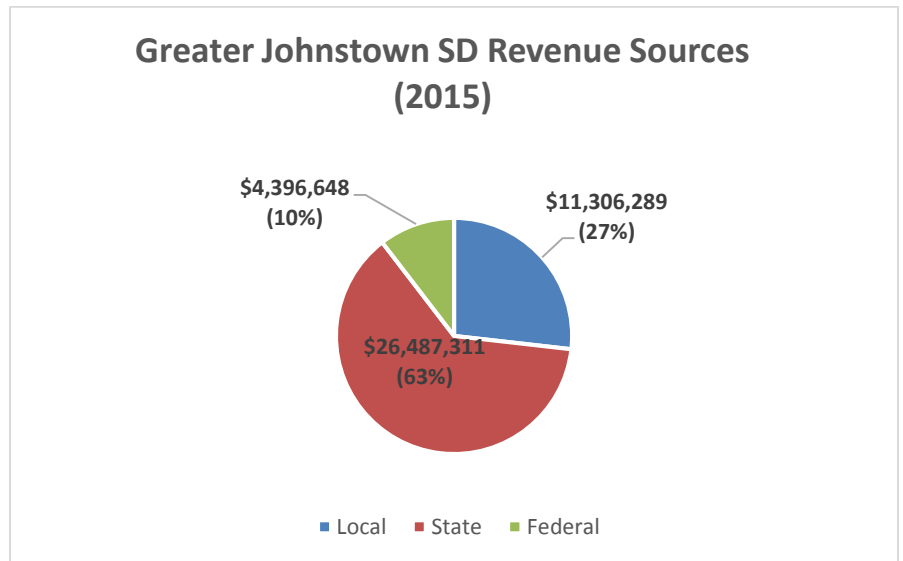
¹⁰ Ibid.

¹¹ The General Fund balance declined by \$10,767,928 over the five fiscal years. The difference between the total operating deficit of \$10,978,679 and the total decrease in the General Fund is due to other financing sources received during the time period.

leaves the District in a position whereby events and decisions made outside of its control can greatly impact operations.

It is important to note that while the District has not raised property taxes in 21 years, the District did experience an increase in local revenue during the 2014-15 fiscal year. In September 2014, a nonprofit health system headquartered within the District with an assessed property value of over \$40 million was sold to a for-profit entity. This transaction resulted in a significant real estate transfer tax which increased the District's local revenue. With a \$40 million addition to its local tax base, the District should realize an increase in its local revenues for several years to come.

Chart 2



Note: Information obtained from the District's Independent Auditor's Report, *Statement of Revenue, Expenditures and Changes in Fund Balance*, fiscal year ending 2015.

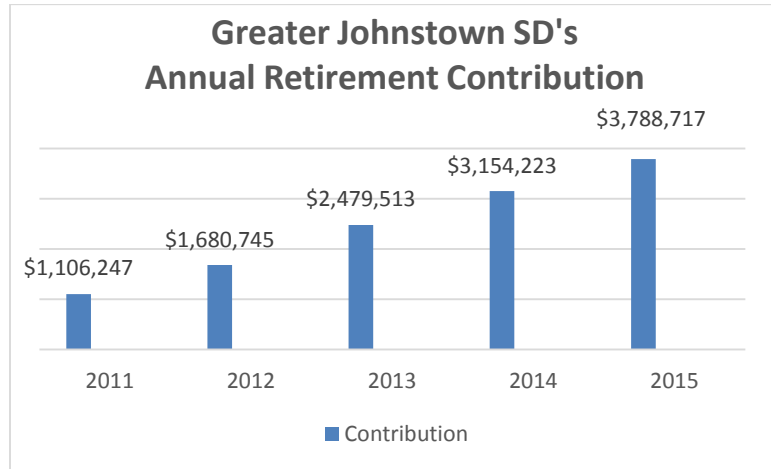
Expenditures: Personnel costs consistently comprised 60 percent to 70 percent of the District expenditures during the period reviewed. We noted that the District reduced its total number of staff from 378 in 2009-10 to 320 in 2014-15. Therefore, total wages have decreased; however, total personnel costs have increased due to rising healthcare and benefits costs.

The District’s support staff contract expired at the end of the 2014-15 school year, and a new contract was ratified in December 2015. According to District officials, provisions in the new contract should result in a reduction in total wages and healthcare costs related to support staff. The District’s instructional staff contract will expire at the end of the 2015-16 school year, and District officials are hopeful that wage and healthcare costs can be reduced in the new contract.

The District also experienced a significant rise its pension costs. The employer contribution rates have risen over the period reviewed and are scheduled to rise at least through fiscal year end June 30, 2020.

The following chart illustrates the significant increase in the District’s annual retirement contribution costs.

Chart 3



Note: Information obtained from the District’s Annual Financial Reports’ *Detail of General Fund Expenditures and Other Financing Uses* for the fiscal years ending 2011 through 2015.

The District’s required contribution rate to the Public School Employees’ Retirement System (PSERS) increased from 16.93 percent in 2013-14 to 21.40 percent in 2014-15. The increased rates were communicated to all school districts well in advance in order to give them the opportunity to prepare for increased costs. When faced with the challenge of increased contribution rates and other expenses, the Board chose to use some of the fund balance to cover these increased costs rather than increase taxes.

Budgeted vs. Actual Revenues and Expenditures

The District's budgeted expenditures exceeded its budgeted revenues for each fiscal year we reviewed. As a result, the District's budgets indicated that the District planned to use its fund balance for all five years reviewed in order to balance its budget. The use of the fund balance can only be an effective method of balancing revenues to expenditures for a very limited time.

As Table 2 shows, over the five-year period, the District budgeted for a cumulative operating deficit of over \$23 million. If the District actually incurred that level of deficit, then the General Fund would have been completely depleted. As shown previously in Table 1, the District's actual operating deficit was \$10.9 million—significantly less than the \$23 million budgeted. The District's budgeted expenditures exceeded the actual expenditures (as shown in Table 2) for each year reviewed.

Table 2

| Greater Johnstown SD Budgeted Revenue and Expenditures¹² | | | |
|--|-----------------------------|----------------------------------|---|
| Fiscal Year ending June 30 | Budgeted Revenue | Budgeted Expenditures | Budgeted Operating Deficit |
| 2011 | \$ 42,764,288 | \$ 42,945,131 | \$ 180,843 |
| 2012 | \$ 40,382,945 | \$ 43,299,098 | \$ 2,916,153 |
| 2013 | \$ 39,752,330 | \$ 46,927,580 | \$ 7,175,250 |
| 2014 | \$ 40,853,736 | \$ 48,368,726 | \$ 7,514,990 |
| 2015 | \$ 40,709,058 | \$ 46,478,516 | \$ 5,769,458 |
| Total: | \$204,462,357 | \$228,019,051 | \$23,556,694 |

The Board's practice of repeatedly approving budgets with operating deficits is an unsustainable business model. Not only will this practice likely deplete the General Fund, but if continued, it may lead to the District being forced to borrow money just to fund daily operations.

Current Ratio

One of the key measures of an entity's financial condition is known as the current ratio. The current ratio is calculated by dividing the current assets by the current liabilities. An

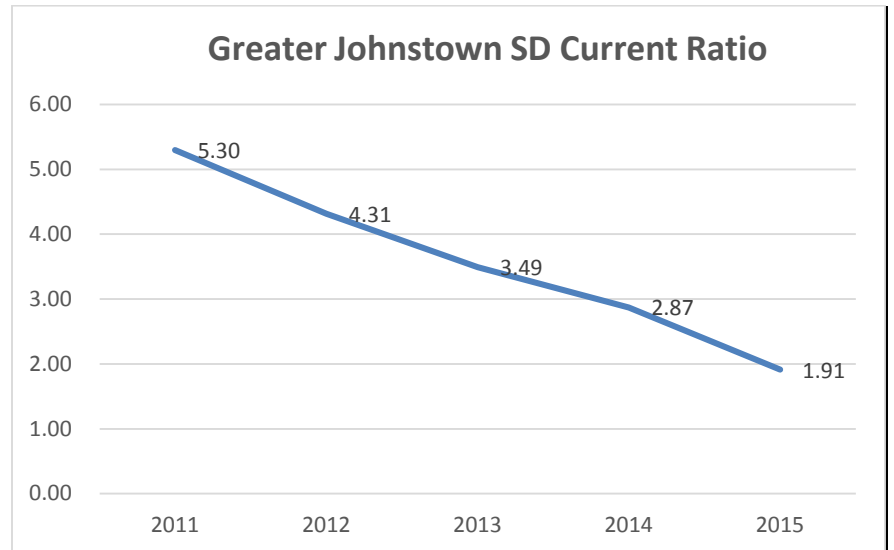
¹² Information obtained from the District's Independent Auditor's Report, *Statement of Revenue, Expenditures and Changes in Fund Balance Budget and Actual-General Fund*, fiscal years ending 2011 through 2015.

entity's current ratio can be used to gauge its ability to meet its current obligations.

A current ratio of "1" 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 having any cash or other liquid assets remaining. When the current ratio dips below a "2", then a school district may have trouble paying its current obligations with the resources it has available. The District's current ratio has steadily declined over the five-year period reviewed and was 1.91 as of June 30, 2015.

The following chart illustrates the District's decreasing current ratio over the period reviewed.

Chart 4

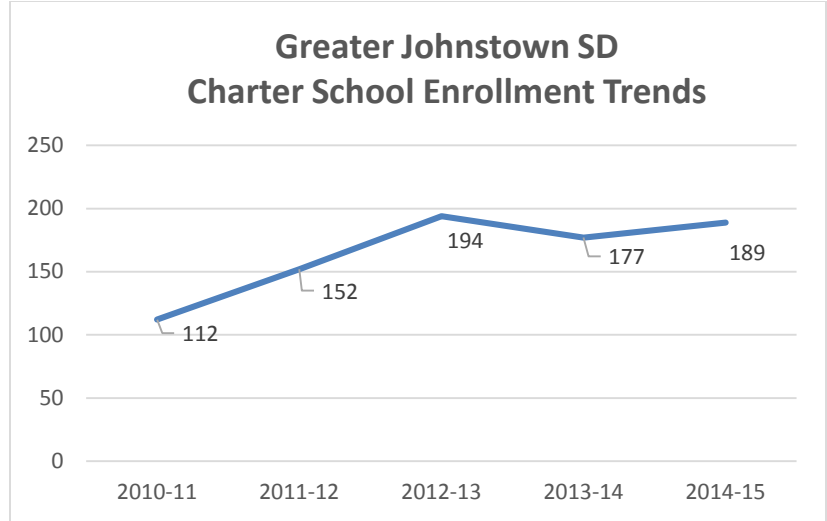


Potential creditors use the current ratio to measure a school district's ability to pay its short-term debts; therefore, a weak current ratio can affect a school district's cost of borrowing.

Charter School Costs

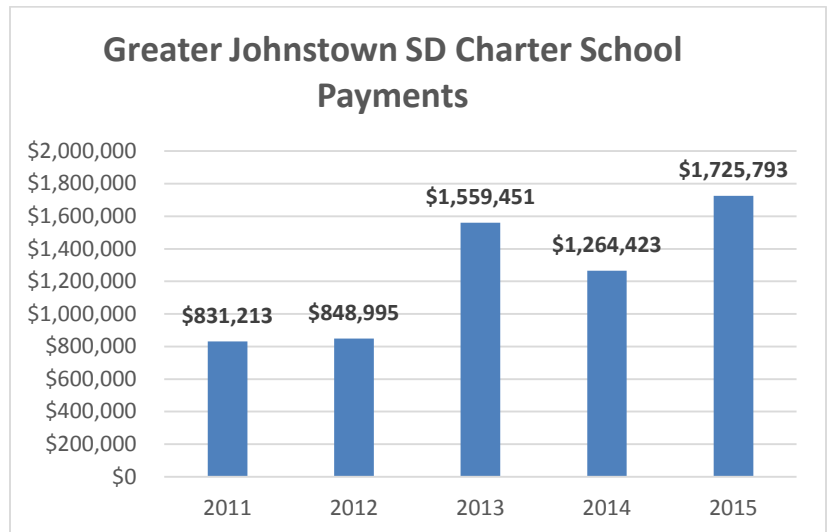
For the five-year period reviewed, the District's charter school enrollment increased 69 percent, and the resulting expenditures for the District more than doubled from \$831,231 in 2010-11 to \$1,725,793 in 2014-15. The charts below show the charter school enrollment and costs to the District.

Chart 5



Note: Information obtained from the District's Charter School Pupil Enrollment Reports for the school years ending June 30, 2011 through 2015.

Chart 6



Note: Information obtained from the District's Annual Financial Reports' Tuition Schedule for the fiscal years ending 2011 through 2015.

During the 2013-14 school year, the District started a cyber education program in an effort to stem the loss of District students to charter schools. The District attributed this program as the cause of the reduction in charter school enrollment for that school year. However, the following year, the principal responsible for recruiting District students to the cyber education program left employment with the District. The subsequent increase in charter school enrollment during the 2014-15 school year was attributed to the loss of this principal.

Charter school costs absorbed a greater percentage of the District's revenues for the same period, increasing from 1.96 percent to 4.09 percent. In addition, the financial burden was compounded by the fact that after 2010 the state stopped providing school districts with partial tuition reimbursement for charter schools students. The increasing financial burden of charter school tuition could cause the District to reduce services and/or eliminate programs in order to balance the budget.

Conclusion

With stagnant revenues and increasing expenditures, the District has reached a point where the fund balance cannot continue to be used much longer to bridge the gap. We encourage the District to develop a business model where expenditures are less than revenues and a balanced budget can be implemented moving forward.

Recommendations

The *Greater Johnstown School District* should:

1. Ensure the District's Business Office continues its process of developing a multi-year (3 to 5 years) financial plan that includes an annual review and revisions, if applicable, after evaluating actual operating revenues and expenditures. This plan should also include developing a written policy setting a minimum General Fund balance.
2. Develop and approve balanced budgets with special consideration given to controlling operating expenses and exploring ways to increase revenues.

3. Explore new ways to encourage District students to stay enrolled in the District to reduce the charter school costs. In addition, the District should develop an effective recruiting process for the District's own cyber-school program to help retain its student who may opt to enroll in other cyber schools.

Management Response

The Greater Johnstown School District's management agreed with our finding and provided a detailed response which can be found in Appendix A. The following is an excerpt of the management response:

“The School Board of Directors passed a 2012-13 preliminary budget in January of 2012 with a deficit of \$7,533,471 and a final budget in June with a deficit of \$7,243,807. At the start of the 2012-13 school year, the existing business manager and the superintendent resigned from their positions within the District, leaving the deficit issue to be resolved by new administrators serving in these positions.

At the local level, the assessed value of real estate taxable properties has decreased from \$200,805,170 in 2008 to \$190,600,750 in 2015. However, with the sale of Conemaugh Hospital to a for-profit hospital the taxable property value increased to over \$230,000,000 over the past two years. During the past 21 years the tax rate for real estate has remained flat at 46.8 mils. At the state level, basic education funding has still not reached the levels it once was in 2010-11.

In addition to the reduction in revenues, expenditures in pension have seriously increased over the past five years. In 2009, the employers' percent of employee salary that went towards retirement was 4.76%. The rate for the 2016-17 school year will be over 30 percent. During this same time period, the District has experienced double digit health care increase percentages, from an overall health care cost of just over \$3,000,000 in 2009 to over an estimated annual \$5,200,000 cost for 2017.

Cyber schooling is another drastically increasing cost amounting to over \$1.9 million in tuition fees for the 2015-16 school year, despite the implementation of a District operated cyber school.

Despite the need for more state revenue, the District built a strategy for 2012-13 to reduce costs and increase revenues that led to an overall reduction deficit gap \$2.3 million better than budgeted. Additionally, the budget gap that was once \$7.2 million in 2012-13 has been reduced by over half for the upcoming 2016-17 school year.”

Auditor Conclusion

We are pleased that management agreed with our finding. We acknowledge the many challenges facing school districts in the Commonwealth, including the increase in charter school costs, and that management is aware of the need for improvement. The financial stability of the District is the responsibility of the Board as part of its governance obligations, and the Board and management should strive to keep the District fiscally stable.

Finding No. 2

Errors in Reporting the Number of Nonpublic Students Transported by the District Resulted in an Underpayment of \$17,710 to the District

Criteria relevant to the finding:

Section 2509.3 of the Public School Code (PSC) provides, in part, that each school district shall be paid the sum of \$385 for each nonpublic school pupil transported. *See* 24 P.S. § 25-2509.3.

Nonpublic school pupils are children whose parents are paying tuition for them to attend a nonprofit or parochial school.

Additionally, instructions provided by PDE to complete the Summary of Pupils Transported Form (PDE-2089) specify that districts are to report the total number of nonpublic pupils transported to and from school.

Board Policy #810 states in part:

“The District shall transport eligible resident students who are enrolled in nonpublic schools within the distance prescribed by law.”

The District was underpaid \$17,710 in transportation reimbursement from PDE. This underpayment was due to the District incorrectly reporting the number of nonpublic students who were provided transportation by the District during the 2013-14 and 2014-15 school years. We were unable to review the 2012-13 school year for the number of nonpublic students reported to PDE because the District was unable to produce the source documents for this school year.

According to the PSC, a nonpublic school is defined, in part, as a nonprofit school other than a public school within the Commonwealth of Pennsylvania.¹³ The PSC requires school districts to provide transportation services to students who reside in its district and who attend nonpublic schools. Further, the PSC requires that the Commonwealth provide school districts with a reimbursement of \$385 for each nonpublic school student transported by the district.¹⁴

Our review of the District’s transportation data reported to PDE for the 2013-14 and 2014-15 school years, found that the District used the nonpublic student count as of the month of October. By using the nonpublic student count in October of each school year, the District under reported the nonpublic student count to PDE. In both school years, the District transported nonpublic students who were not part of the October count. Failing to report these students transported by the District resulted in the District being underpaid in transportation reimbursement from PDE.

The nonpublic student count was under reported due to District officials being unaware that the reimbursement subsidy is based on the total number of all nonpublic students transported throughout the school year.

¹³ 24 P.S. 9-992.1-A(b). This definition relates to auxiliary services provided to pupils by the state’s various intermediate units.

¹⁴ 24 P.S. § 25-2509.3.

The following chart summarizes the District’s reported total versus our audited total of nonpublic students, the difference by school year, and the resulting cumulative underpayment:

| GREATER JOHNSTOWN SD REPORTING OF NONPUBLIC STUDENTS BY YEAR | | | | |
|---|---------------------------|----------------------|--|--------------------------------------|
| School Year | Report by District | Audited Total | Amount of Students Incorrectly Reported | Subsidies Due to the District |
| 2013-14 | 428 | 444 | 16 | \$ 6,160 |
| 2014-15 | <u>394</u> | <u>424</u> | <u>30</u> | <u>\$ 11,550</u> |
| Total | 822 | 868 | 46 | \$ 17,710 |

As a result of our audit, District officials informed us that it is in the process of developing new procedures to help ensure that all nonpublic students who are provided transportation by the District are properly accounted for and accurately reported to PDE.

Finally, we provided PDE with reports detailing the discrepancies we identified for the 2013-14 and 2014-15 school years. PDE can use these reports to adjust the District’s future transportation reimbursement allocations.

Recommendations

The *Greater Johnstown School District* should:

1. Maintain accurate lists of total nonpublic students who were provided transportation, by building, for each school year.
2. Conduct a multi-year trend analysis of student data and transportation reimbursements to help ensure the accuracy of nonpublic students reported to PDE.
3. Implement a monitoring process to ensure that its newly developed procedures, including the student roster reconciliations, are consistently followed.

The *Pennsylvania Department of Education* should:

4. Adjust the District’s transportation allocations to reimburse the District for the underpayment of \$17,710.

Management Response

District management provided the following response:

“Management agrees with the finding and has updated the District’s Transportation Reporting procedure to reflect the method provided by PDE in the instructions for the Summary of Pupils Transported, form PDE-2089. It was approved by the School Board on September 20, 2016.

As reported in the finding, District staff calculated the nonpublic count based on the data reported for October of each year. The District collected the proper documentation to support the number reported during the 2013-14 and 2014-15 school years on file. However, the number did not reflect any new students provided transportation to the nonpublic schools after October.

The revision to the Transportation Reporting procedure incorporates the recommendations made by the Auditor General’s Office in the finding. The revised procedure was implemented for the 2015-16 PDE-2089 report. The District’s procedure is as follows:

‘The nonpublic pupil count is calculated by entering the total number of nonpublic pupils transported to and from school. A nonpublic student is included in the count on the PDE-2089 if transported at least one day. A list of nonpublic resident students transported by the District throughout the year is compiled annually. The list is updated monthly by adding any new nonpublic students provided transportation. The total count at the end of the school year is used on the PDE-2089 from for the number of nonpublic school students transported. Documentation is maintained by the District, identifying the names of these pupils and is provided to the Auditor General’s staff during a state audit.’

On August 2, 2016, a full-time Transportation Coordinator was hired by the District. The multi-year trend analysis of student data and transportation reimbursements recommended by the Pennsylvania Department of Education shall be conducted by this employee. In addition, the Transportation Reporting procedure shall be monitored by the Business Manager and the Coordinator of Internal Controls to ensure it is consistently followed.”

Auditor Conclusion

We are pleased that the District has implemented corrective actions to address our finding and recognizes the significance and importance of the errors noted for the 2013-14 and 2014-15 school years. During our next audit, we will determine the effectiveness of the District's corrective actions.

Finding No. 3

Questionable Employment Contracts and a Separation Agreement Cost the District Over \$136,000

Criteria relevant to the finding:

According to the PSBA governance standards called, *Principles for Governance and Leadership*, to **govern effectively**, school directors collectively and individually should:

- Adhere to an established set of rules and procedures for board operations.
- Develop, adopt, revise, and review policy.
- Align decisions to policy.
- Differentiate between governance and management, delegating management tasks to administration.
- Allocate finances and resources.
- Ensure compliance with local, state, and federal laws.

Additionally, PSBA's governance principles specific to **acting ethically** state, in part:

- Never use the position for improper benefit to self or others.
- Act to avoid actual or perceived conflicts of interest.

Our review of the District's employment practices during the audit period found that the District entered into two questionable employment contracts and a separation agreement for the equivalent of two years' salary with a board member's daughter for a clerical position.

In addition, we found that, as of July 2016, the District incurred costs totaling \$136,615 through the Separation Agreement, including payments made directly to the employee totaling \$120,990; payments to the employee for unused vacation days totaling \$4,109; and payments for the employee's single medical coverage totaling \$11,516.

A summary of the steps taken and timeline in hiring this clerical employee are as follows:

In June 2012, the District hired the employee without posting the position or even considering other candidates before approving a five-year employment contract (Contract I) from July 1, 2012 through June 30, 2017.

In May 2014, just two years later, the Board voted to approve a new employment contract (Contract II) with this same employee from July 1, 2014 through June 30, 2019.

In December 2014, just six months after approving Contract II, the District executed a Separation Agreement and General Release (the Separation Agreement) costing the District more than \$136,000.

We question the hiring of the board member's daughter for several key reasons:

- The position was newly created and not posted as it should have been, and the District did not consider other candidates.
- The position was clerical in nature, yet the District executed an employment contract, which is not customary for support personnel positions.
- The employee was placed on paid administrative leave for approximately one month before the Separation Agreement was executed.

Criteria relevant to the finding (continued):

The employee's employment contract effective July 1, 2014, Article V – Reappointment and Termination, contains general termination provisions that state, in part:

“ . . . (a) This Agreement may only be changed or terminated by mutual consent of both parties, except for the purpose of official retirement of the ‘Project Director, Alternative Education.’ (b) The ‘Project Director, Alternative Education’ shall, throughout the term of this Agreement, be subject to termination of contract for valid and just cause.”

The employee's Separation Agreement and General Release states, in part:

“ . . . Payment to Employee

Within fourteen (14) days after the approval of the Agreement by the ‘District,’ payment will be made to the Employee in the sum of \$60,495 less all applicable deductions and withholding taxes by law. The second payment will be made July 8, 2015 in the amount of \$60,495, less all applicable deductions and withholding taxes as required by law. Employee will also receive per diem pay for any unused vacation days.

Medical Coverage

The District will provide Employee upon last day of employment single medical coverage that is provided in the Non-Professional Employees Contract for a term of four (4) years. . . .”

- The Separation Agreement resulted in the employee receiving payments totaling \$120,990, essentially the equivalent of two years' salary.
- The Separation Agreement also required that the District provide full medical coverage to the employee for four years. The medical coverage cost the District \$11,516 through July 2016.
- The position was not filled after this employee separated from the District, which makes us question the necessity of the position to begin with.

More important, just 19 months after executing the Separation Agreement and buying out the employee's contract for a total cost of \$136,615, the District later rehired this same employee for a different position. Again, the District did not post the position or consider other candidates for this position. In addition, the District did not require the employee to return any portion of the monies she received as part of the prior Separation Agreement.

By approving the employment contracts and a costly Separation Agreement with a board member's daughter, the Board failed to follow best practices essential for selecting the most qualified candidate without any possible preferential treatment and maintaining accountability, consistency, and fairness in the hiring process. While it is in the best interest of a school district to have comprehensive hiring policies and procedures in place and to document a fair and competitive hiring process, it is especially important when hiring a family member to avoid even the appearance of a conflict or bias.

The following sections of this finding outline the details of Contract I, Contract II, and the Separation Agreement, as well as describes the resulting effect on the District.

Hiring of Board Member's Daughter Without an Open and Competitive Process

At the June 28, 2012 board meeting, the Board approved the hiring of a board member's daughter for a newly created position of Project Manager.¹⁵ The Board also approved Contract I, which was a five-year employment contract with this employee. The contract term was

¹⁵ The contract agreement for the position of Project Manager states, “The compensation shall be a salary of \$54,870.00 pro-rated for the school fiscal year 2012-13 of the agreement.”

*Criteria relevant to the finding
(continued):*

The District's Board Policy No. 304, Employment of District Staff, adopted January 19, 2016, states, in part:

“ . . . The district will interview the top seven (7) candidates for each position. If there are less than seven qualified candidates, all shall be interviewed. The interview shall be conducted by a minimum of two (2) district administrators and may include the Board President and/or Board Member. The Superintendent or designee will recommend the top three (3) scoring candidates to the Board for each position. . . . ”

Additionally, the District's written procedures called, *Hiring Practices – Application Procedure*, were approved by the Board on June 7, 2016 to supplement the aforementioned Board Policy No. 304. These procedures require an open, systematic, and competitive hiring process.

effective July 1, 2012 through June 30, 2017. This position was classified as support personnel, and its purpose was to serve as the Principal's office support for supervisory staff at the District's Alternative School.

Two years into the original contract, at the May 28, 2014 board meeting, the Board voted to approve a new employment contract – Contract II, with this same employee. Contract II contained the same job responsibilities, duties, and salary, but the title was changed to be more specific to the Alternative School. The new title for this position was Project Director, Alternative Education.¹⁶ In addition to the title change, the term of the contract changed to July 1, 2014 through June 30, 2019. By entering into a second five-year contract without any substantial position or contract changes, the District essentially extended the original employment contract by two more years.

It is important to note that the District did not have an anti-nepotism and conflict of interest policy in place at the time, so there weren't any policies or procedures that prohibited family members from being hired. Additionally, the board member appropriately abstained from both votes and noted the family relationship as the reason for abstention, as required by law.

However, from a good governance, ethical, and best practices standpoint, we question the hiring of an immediate family member of a board member for a newly created position without an open, competitive, and documented hiring process. Specifically, we found that the District did not publically post the position or consider other candidates for the position. Additionally, a review of the personnel file for this employee revealed that the District did not have the standard hiring documentation on file, such as an employment application, resume, or standard District interview forms documenting that an interview occurred and an evaluation was conducted. Only background clearances were in the file.¹⁷ After questioning this lack of documentation, the District was able to produce

¹⁶ The contract agreement for the position of Project Director, Alternative Education states, “The compensation of the ‘Project Director, Alternative Education’ shall be a salary of \$59,348.00 pro-rated for the school fiscal year 2014-15 of this agreement.” The increase in the salary from footnote 19 above is the result of pay increases the employee received between the time of the first contract and the second contract.

¹⁷ We reviewed a test group of other newly hired employees for the most recently completed 2015-16 school year and found all of the aforementioned employment documents in the personnel files.

a resume that District officials stated was on file with the District's solicitor.

Further, we question why the District entered into an employment contract for a support personnel position performing mainly clerical duties, which again, is not customary practice at most school districts. Typically, employment contracts are entered into for key leadership and management positions, such as a Superintendent,¹⁸ Principal, and Business Manager.

Good governance and best practices suggest that all hiring processes be formalized, systematic, competitive, and documented to maintain accountability, consistency, and fairness and to ensure the most qualified candidates are hired. By not having an open and competitive hiring process for this position, the District created the appearance of favoritism to a family member of one of the board members, did not follow best practices, and cannot be assured that it hired the best candidate for the job.

Separation Agreement Resulted in Additional Costs to the District

In December 2014, just six months after approving the second employment contract, the Board voted to place the employee on paid administrative leave for unknown reasons. At the same meeting, the Board voted to approve a Separation Agreement for this employee to prematurely terminate her employment contract. The Separation Agreement became effective on January 5, 2015, when it was signed by both parties.

As a result of terminating the employment contract and agreeing to separation terms, we found that as of July 2016 the District incurred costs totaling \$136,615. The Separation Agreement required the District to make the following payments:

- Payments of \$120,990, made in two equal payments, paid directly to the employee.
- Payments to the employee for unused vacation days totaling \$4,109.

¹⁸ Section 1073(e)(1) of the PSC prohibits a Superintendent and Assistant Superintendent from being hired "except pursuant to a written contract of employment expressly stating the terms and conditions of employment." See 24 P.S. § 10-1073(e)(1) (Act 141 of 2012, effective September 10, 2012).

- Payments for the employee's single medical coverage totaling \$11,516.¹⁹

Our review of the employment contract effective July 1, 2014, found that it lacked provisions specific to an early termination of the contract. A general termination provision stated that the contract could only be changed or terminated by mutual consent of both parties and that the employee was subject to termination of the contract for valid and just cause. Since the contract lacked specific separation terms and the reason for early termination is unknown, we cannot determine if the District had cause for termination or any obligation to negotiate and offer separation terms. However, we believe that the District put itself in a compromising position by unnecessarily entering into two long-term contracts for a support personnel position that normally would not be a contracted position.

District Rehired the Employee Without Following District's Employment Policy and Hiring Practices

In August 2016, approximately 18 months after buying out her previous employment contract, the Board voted to rehire the board member's daughter as the District's Transportation Coordinator. Once again, the District did not consider or interview other candidates and did not publically post or advertise the position.²⁰ Subsequently, the District failed to comply with its own employment policy and written hiring practices adopted in 2016.²¹ Moreover, the continued failure to post and consider other candidates when hiring the board member's daughter for positions within the District gives the appearance of favoritism, possible preferential treatment, and family influence.

This contract for the Transportation Coordinator position had a one-year term beginning August 2, 2016, and ending July 31, 2017, with an annual salary of \$50,000. This new contract ended the District's obligation to pay the remaining medical benefits under the Separation Agreement; however, the employee continued to receive medical benefits under her new employment contract. It is

¹⁹ The employee's Separation Agreement required the District to pay for single medical coverage for a total of four years through January 4, 2019.

²⁰ Our review of the board meeting minutes did disclose that the board member properly abstained from the vote approving her as the Transportation Coordinator and the reason for abstention was also noted.

²¹ Board Policy No. 304, dated January 19, 2016, and the District's written hiring practices dated June 7, 2016.

important to note that the Separation Agreement did not contain any provisions related to the possibility of rehiring this employee or provisions requiring the employee to return any portion of the buy-out payments.

In addition to not complying with established policies and procedures, we found that the District may not have hired the most qualified person for the job. For example, we learned that since the employee had no prior work experience with student transportation services, the District is continuing its contract with an outside vendor to provide transportation services and training to the employee for the 2016-17 school year at an additional cost not to exceed \$40,000. While this outside vendor had been providing services to the District for the prior two years, the decision to essentially pay the employee and the vendor to perform the same transportation services duties during the 2016-17 school year occurred because the District hired someone lacking the necessary experience to fulfill the job duties. If a competitive hiring process had occurred, it is possible that these additional costs could have been avoided.

Conclusion

By hiring and entering into three employment contracts with a board member's daughter without a systematic, competitive, and documented hiring process, we concluded that the District's actions lacked accountability, consistency, and fairness. With the approval of each contract, routine and/or required employment practices appear to have been circumvented. Additionally, we question the appropriateness of entering into long-term employment contracts for a support personnel position, especially when we found that the position was never refilled after this employee separated from the District.

In addition, it is our position that the costly Separation Agreement was not in the best interest of taxpayers, especially when we considered that the District rehired this employee and did not require her to return any portion of the buy-out payments. Finally, we concluded that the Board did not follow good governance and best practices when making employment decisions concerning a board member's immediate family.

Recommendations

The *Greater Johnstown School District* should:

1. Ensure that both District personnel and the Board are adhering to the District's employment policies and procedures to ensure accountability, consistency, and fairness when considering and selecting potential candidates for employment.
2. Document each step in the hiring process to show that the selection process proceeded systematically and without bias. This will also help to ensure that the strongest candidates are hired.
3. Consult with its solicitor to ensure that future employment contracts contain adequate termination provisions sufficient to protect the interests of the District and its taxpayers in the event that the employment ends prematurely for any reason. These provisions will help to avoid costly Separation Agreements.
4. Revisit its practice of entering into long-term employment contracts for support personnel positions and consider the financial impact of an early termination of a contract term.

Management Response

The District was provided with two opportunities to respond directly to this finding and the recommendations; however, District management opted instead to provide the following response that is not relevant to the finding or recommendations:

“We are pleased that the audit resulted in no findings in a variety of areas including: academics, Right to Know Law processes and procedures as well as school safety and bullying. However, work still remains to be done in the area of transportation. We will continue to work with commonwealth leadership to improve our internal processes to maximize our transportation reimbursements and practices. Based on the recommendations of Pennsylvania Auditor General Eugene DePasquale's audit report, Greater Johnstown School District took steps to

enhance our transportation processes and will continue to grow, learn, and develop.

One of the recommendations related to bringing additional transportation expertise to the district. We followed this recommendation initially through a transportation consultant who brought clarity to the transportation processes. The Auditor General's report also recommended a full time internal director of transportation to provide ongoing oversight and management of the district's transportation program. Since the first month of school is the busiest from a transportation perspective, we set and achieved our goal of hiring a transportation director in early August.

We look forward to improving as a result of this audit and the findings contained within.”

Auditor Conclusion

Since District management chose to not respond directly to the issues identified in this finding, we are concerned that it will not take action to implement the recommendations. This finding details a serious issue with the hiring practices of the District, and we made solid recommendations to address these deficiencies. We are hopeful that the District will reevaluate its hiring practices and consider implementing our recommendations.

Also, as a matter of clarity, we should note that the District's response references recommendations made in our prior audit report finding related to transportation documentation issues. These references are not relevant to this finding.

Status of Prior Audit Findings and Observations

Our prior audit of the District released on December 11, 2013, resulted in two findings 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 reviewed the District's written response provided to PDE, interviewed District personnel, and performed audit procedures as detailed in each status section below.

Auditor General Performance Audit Report Released on December 11, 2013

Prior Finding No. 1: Errors in Reporting Nonresident Membership Resulted in a \$16,061 Total Underpayment in Tuition for Foster Children

Prior Finding Summary: Our prior audit found errors in the reporting of nonresident pupil membership. For the 2009-10 school year, District personnel understated nonresident pupil membership by 189 days resulting in a \$9,355 underpayment to the District. For the 2008-09 school year, District personnel understated nonresident pupil membership by 139 days resulting in a \$6,706 underpayment to the District. The total underpayment was \$16,061.

Prior Recommendations: We recommended that the District should:

1. Ensure that someone, other than the person preparing the membership reports, reviews the data thoroughly to ensure students are properly classified prior to submitting reports to PDE.
2. Review reports submitted to PDE for the years subsequent to the audit period and submit revised reports if errors are found.
3. Contact PDE to determine if additional training can be obtained for those individuals responsible for classifying students and nonresidents in order to ensure that this process is being performed correctly.

We also recommended that PDE should:

4. Adjust the District's allocations to correct the total underpayment of \$16,061.

Current Status: The District did implement our prior recommendations. The District now has the Administrative Assistant to the Business Manager/Child Accounting review the membership reports prior to submission to PDE. In addition, the PIMS Coordinator has attended several training sessions put on by the Attendance/Child Accounting Professional

Association. The staff also reviewed and revised the 2010-11 through 2014-15 school year reports. Revised reports were submitted to PDE, and the District is waiting for PDE's final approval and adjustment of its transportation subsidy. Finally, we noted that as of October 7, 2016, PDE has not made the adjustment to the District's allocation for the \$16,061 underpayment.

Prior Finding No. 2: Continued Weaknesses in Controls and a Lack of Documentation Supporting Reimbursements for Pupil Transportation

Prior Finding Summary: Our prior audit found weaknesses in internal controls and a lack of documentation supporting reimbursements totaling \$1,151,764 for the 2009-10 school year and \$1,114,808 for the 2008-09 school year.

Prior Recommendations: We recommended that the District should:

1. Contact PDE and/or PASBO to arrange training on how to properly report transportation data for District transportation personnel.
2. Ensure that the District personnel obtain and maintain the supporting documentation necessary to prepare the annual PDE transportation reports, as required by PDE.
3. Ensure that the District's transportation director, or a member of his staff, verifies the accuracy of all the data provided to the District, including the number of miles per day the buses traveled, prior to reporting the information to PDE for subsidy reimbursement.

Current Status: The District did implement our recommendations. The District received a transportation review from PASBO in March 2014. This review resulted in a written report that contained nine recommendations. PASBO then conducted a transportation follow-up study in January 2016 to determine a status of its recommendations. The District's staff, including the Business Manager, Coordinator of Internal Controls, and Transportation Director now verifies the accuracy of all the data provided to the District to prepare the PDE transportation reports. Finally, while we noted that the District took steps to improve its process for maintaining and reporting transportation data, we found discrepancies when we reviewed the supporting documentation for the reported number of nonpublic pupils transported by the District. The errors we identified resulted in an underpayment with the District's transportation subsidies in 2013-14 and 2014-15. Details of the errors we identified can be found in Finding No. 2 of this report, beginning on page 18.

Prior Observation: District's Transportation Costs Exceeded the State Formula

Prior Observation Summary: Our prior audit found that the District's operational expenses for transportation were substantially higher than PDE's inflation-adjusted final formula allowance. The District's percentage of cost over formula grew from 24.4 percent for the 2005-06 school year to 86 percent for the 2009-10 school year.

Prior Recommendations: We recommended that the District should:

1. Consider bidding transportation contracts to determine if taxpayers would benefit from a more favorable contract for the District.
2. Consider renegotiating the District's current transportation contract next year, instead of allowing it to automatically renew.
3. Consider the State's final formula allowance when renewing or renegotiating the District's transportation contract.

Current Status: The District did implement our prior recommendations. The Business Manager issued a Request for Proposals for Transportation Operations for the 2013-14 through 2017-18 school years. Based on the proposals received, the Business Manager was able to renegotiate the terms of the current transportation contract. For the 2014-15 school year, the District's percent of transportation costs over the final formula allowance is 37 percent. That is a significant decrease from the 86 percent we identified in the 2009-10 school year.

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 Sections 402 and 403 of The Fiscal Code,²² 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 controls²³ 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 information technology controls, which 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.

²² 72 P.S. §§ 402 and 403.

²³ 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, new or amended policies and procedures, and the independent audit report of the District's basic financial statements for the fiscal years ending 2010 through 2015. 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:

- ✓ Financial Stability
- ✓ Hiring Practices/Conflict of Interest
- ✓ Transportation Operations
- ✓ Right to Know Law
- ✓ Bus Driver Requirements
- ✓ School Safety

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

- ✓ 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, budget, independent auditor's reports, summary of child accounting, and general ledger for fiscal years 2011 through 2015. 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 PASBO, the Colorado Office of the State Auditor, and the National Forum on Education Statistics. Finding No. 1 describes the results of our review of this objective.
- ✓ Did the District follow the PSC and best practices when hiring new staff, and did the District pursue a contract buy-out with an administrator or employee and if so, what was the total cost of the buy-out, what were the reasons for the termination/settlement, did the current employment contract(s) contain adequate termination provisions and were the termination provisions followed?

- To address this objective, we obtained and reviewed the District’s hiring policies and procedures. We selected the three of the employees most recently hired by the District during the period July 1, 2012 through June 30, 2015, and reviewed documentation to determine if the District complied with the PSC, District policies and procedures, and best practices identified by state school board organizations when hiring new employees. We reviewed applications and resumes as well as documentation evidencing the reason for selecting the candidate for interview, why the candidate was offered the position over other candidates, and the Superintendent’s recommendation to the Board.
 - We reviewed the District’s board meeting minutes from August 6, 2013 through August 2, 2016, to determine if board members properly abstained from voting on actions related to the hiring of their family members. We also reviewed the employment contracts and other hiring documentation for two employees who were related to a board member to determine if the employees were given preferential treatment because of their relationship with board member(s). Finally, we reviewed the employment contracts, settlement agreement, and payroll records for an employee who separated from employment with the District. Finding No. 3 describes the results of our review of this objective.
- ✓ Did the District establish internal controls to ensure compliance with applicable laws and regulations governing transportation operations, and did the District receive correct transportation reimbursements from the state?²⁴
- To address this objective, we randomly selected for review 15 of the 60 contracted buses used to transport students during the 2014-15 school year. We examined the certificate of insurance as proof that current coverage is being carried on all vehicles used in transporting pupils. In addition, we reviewed bus odometer readings, board approved route descriptions, student rosters, total mileage verification, year-to-date expenditure ledgers, contractor invoices, school calendars, and District work papers for weighting of students and mileage.
 - We also conducted testing to verify the accuracy of the number of nonpublic students reported to PDE as being provided transportation by the District for the 2013-14 and 2014-15 school years. We reviewed supporting documentation for all students classified as nonpublic students for these school years to determine if they were correctly identified. For students not properly classified, we calculated the amount of the potential adjustment to the transportation reimbursement from PDE. Finding No. 2 describes the results of our review of this objective.
- ✓ Did the District establish board policies and administrative procedures related to the Commonwealth’s Right-to-Know Law²⁵ (RTK), were those policies and procedures adequate to ensure compliance with the law, and have they been properly implemented and followed by the District?

²⁴ See 24 P.S. §§ 3-1301, 13-1302, 13-1305, 13-1306; 22 Pa. Code Chapter 11.

²⁵ 65 P.S. § 67.101 *et seq.*

- To address this objective, we reviewed the District’s board policies and procedures and examined the District’s publicly accessible website. In addition, we examined documentation from the four most recent RTK requests as of May 19, 2016, including the request form, the District’s response to the request, and any appeal information to determine whether the District complied with the RTK law and with its own policies and procedures. Our review of this area did not disclose any reportable issues.
- ✓ 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?²⁶ Also, did the District have adequate written policies and procedures governing the hiring of new bus drivers?
 - To address this objective, we randomly selected 5 of the 8 bus drivers hired by the District’s bus contractor(s) during the 2015-16 school year 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. Our review of this area did not disclose any reportable issues.
- ✓ Did the District take appropriate actions to ensure it provided a safe school environment?²⁷
 - To address this objective, we reviewed a variety of documentation including safety plans, training schedules, anti-bullying policies, the District’s suicide prevention program, and after action reports. 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, PDE.

²⁶ 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.

²⁷ 24 P.S. § 13-1301-A *et seq.*

Appendix A: Management Response

The following is the Greater Johnstown School District's management response in its entirety:

Financially Declining LEA:

The objective is to balance the budget while continuing to provide a full range of services to our students while increasing student outcomes making our human resource pipeline competitive with the world. The School Board of Directors passed a 2012-13 preliminary budget in January of 2012 with a deficit of \$7,533,471 and a final budget in June with a deficit of \$7,243,807. At the start of the 2012-13 school year, the existing business manager and the superintendent resigned from their positions within the district, leaving the budget deficit issue to be resolved by new administrators serving in these positions. Numerous problems exist in closing the financial gap as discussed by the audit report and will be highlighted below.

The first 5 year model presented (Chart 1) in 2012-13 shows a complete depletion of the fund balance by the 2014-15 school year:

Chart 1:
General Fund
Fiscal Gap

| BASELINE | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|--|--------------|--------------|---------------|---------------|---------------|---------------|----------------|----------------|----------------|
| TOTAL REVENUES | \$43,859,914 | \$42,325,450 | \$41,651,266 | \$38,165,942 | \$39,099,171 | \$40,258,981 | \$41,512,627 | \$42,629,004 | \$43,426,221 |
| TOTAL EXPENDITURES | \$40,395,344 | \$40,936,365 | \$42,713,926 | \$45,409,750 | \$47,132,468 | \$49,157,762 | \$51,268,814 | \$53,159,541 | \$54,794,787 |
| BASELINE OPERATING BALANCE (Pre Initiatives) | \$3,464,570 | \$1,389,085 | (\$1,062,660) | (\$7,243,808) | (\$8,033,297) | (\$8,898,781) | (\$9,756,187) | (\$10,530,537) | (\$11,368,566) |
| TOTAL INITIATIVES | | | | - | - | - | - | - | - |
| BASELINE OPERATING BALANCE (Post Initiatives) | \$3,464,570 | \$1,389,085 | (\$1,062,660) | (\$7,243,808) | (\$8,033,297) | (\$8,898,781) | (\$9,756,187) | (\$10,530,537) | (\$11,368,566) |
| FUND BALANCE AND CAPITAL RESERVE (Beginning of Year) | | | \$22,651,114 | \$21,677,370 | \$14,433,562 | \$6,400,265 | (\$2,498,515) | (\$12,254,702) | (\$22,785,239) |
| FUND BALANCE AND CAPITAL RESERVE (End of Year) | | | \$21,677,370 | \$14,433,562 | \$6,400,265 | (\$2,498,515) | (\$12,254,702) | (\$22,785,239) | (\$34,153,805) |

Decreasing Revenues

At the local level, the assessed value of real estate taxable properties has decreased from \$200,805,170 in 2008 to \$190,600,750 in 2015. However, with the sale of Conemaugh Hospital to a for profit hospital the taxable property value increased to over \$230,000,000 over the past two years. The District along with the city and the county has ordered an assessment of the current hospital properties to ensure we retain its market value. During the past 21 years the tax rate for real estate has remained flat at 46.8 mils.

At the state level, basic education funding has still not reached the levels it once was in 2010-11. The state promised that during the Federal ARRA and ED Jobs funding years that they would make up the difference once these federal programs ended. The state level year to year funding is illustrated in Chart 2 below:

Chart 2

| Greater Johnstown School District | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 |
|---|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| | Budget | Actual | Actual | Actual | Actual | Actual | Actual | Actual |
| Basic Ed | 18,765,329 | 17,801,338 | 16,766,578 | 16,726,968 | 16,464,680 | 16,464,680 | 14,938,282 | 15,050,771 |
| ARRA | | | | - | - | - | 2,061,733 | \$2,022,944 |
| Ed Jobs | | | | - | - | - | 1,223,865 | - |
| Ready to Learn | | 529,656 | 529,656 | - | - | - | - | - |
| ABG (Block Grant) | | | | 263,303 | 263,303 | 307,248 | 735,944 | 778,005 |
| EAP (Tutoring) | | | | - | - | 83,322 | 210,128 | 248,940 |
| Dual Enrollment | | | | - | - | - | - | 739 |
| Science/Improvement Grants | | | | - | - | - | 5,000 | 5,000 |
| Alternative Education | | | | - | - | - | - | 62,856 |
| Charter Reimburse (promise of 30% annually) | | | | - | - | - | 158,351 | 143,361 |
| CFF (technology) | | | | - | - | - | - | - |
| TOTAL | 18,765,329 | 18,330,994 | 17,296,234 | 16,969,034 | 16,727,983 | 16,855,250 | 19,333,303 | 18,312,616 |

The funds listed in the Chart 1 represent educational funds; not special education, transportation, vocational, retirement funds, etc. Transportation and special education funds have remained relatively flat across the same years. Retirement has increased significantly this year due to the increase prescribed by the Act 120. Retirement reimbursement funds are prescribed by law.

Increasing Mandated Expenses

In addition to the reduction in revenues, expenditures in pension have seriously increased over the past five years. In 2009, the employers' percent of employee salary that went towards retirement was 4.76%. The rate for the 2016-17 school year will be over 30 percent. The cost for funding the district pension increased over \$4,500,000 million annually from 2010 to the current anticipated cost, despite decreasing annual payroll costs. See chart 3:

Chart 3:

| <i>Recent History of PSERS Costs Against Salary Costs</i> | | | | | | | | |
|---|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| | (Actual) | (Actual) | (Actual) | (Actual) | (Actual) | (Actual) | (Budget) | (Budget) |
| EXPENDITURES | 2009-10 | 2010-11 | 2011-12 | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 |
| 100 Personnel Services - Salaries | \$18,019,630 | \$18,711,289 | \$18,912,348 | \$19,475,671 | \$18,678,103 | \$18,183,260 | \$18,482,970 | \$17,865,684 |
| PSERS Contribution Rates * | 0.0478 | 0.0564 | 0.0865 | 0.1236 | 0.1693 | 0.214 | 0.2584 | 0.3003 |
| 230 Actual Contributions (from AFR) | \$818,398 | \$1,106,247 | \$1,680,745 | \$2,479,513 | \$3,154,225 | \$3,788,717 | \$4,433,265 | \$5,365,065 |

During this same time period, the district has experienced double digit health care increase percentages, from an overall healthcare cost of just over \$3,000,000 in 2009 to over an estimated annual \$5,200,000 cost for 2017.

Cyber schooling is another drastically increasing cost amounting to over \$1.9 million in tuition fees for the 2015-16 school-year, despite the implementation of a District operated cyber school.

The Auditor General has spoken publically about the need to address the mandated pension costs placed on schools and potential reform of the Public School Employees' Retirement System (PSERS) and we applaud his plan for auditing the system. The District also is grateful that the Auditor General has been aware of the issues public schools are facing with the tuition costs of cyber school education and has brought this issue to the public.

Costing Out Study

In 2007, a PDE driven costing out study was developed by Augenblick, Palaich and Associates, Inc. to determine whether financial resources were adequate to meet state performance expectations. With increased accountability for student, school and district performance there is ever-increasing pressure on education systems to ensure that all students leave school with the tools and skills they need to succeed in life. The costing out approach was designed to help address this issue in Pennsylvania and to develop a supportable means for policymakers and other education leaders to understand what it will cost for each district in the state to achieve the performance that is expected of them. In Pennsylvania's case, this estimated the resources needed so that 100 percent of students can achieve proficiency in reading and math by the year 2014.

For GJSD, the costing out study determined that the district spent \$9,253 on each of its 3,264 students for instruction and support services in 2007. The costing out study found that to adequately fund to meet student needs the district should spend \$12,240 per student. The adequacy total called for almost \$10 million (\$40,000,320 compared to \$30,023,804) more per year than the district spent on these services. Pennsylvania was to help financially support schools in meeting these adequacy targets.

Fair Funding and Adequacy

Early this year, Pennsylvania joined 47 other states in the nation when the legislature passed a formula for funding public education. It adopted the formula created for fair funding based a number of factors including acute poverty to equitably distribute state education dollars. The formula provides guidance for how to distribute state funds but it did not address what schools need from the state to be adequately funded.

Public Interest Law Center of Philadelphia has revived the costing out study to determine adequacy. The reports states, "In order for districts to have adequate funding to enable their students to meet state standards, the state must provide school districts with between \$3.188 and \$4.280 billion in additional funding. Given the struggle of students in a majority of the districts within the state to score proficient with current funding, it seems that the \$3.2 billion increase should be the minimum target for state funding increases." **Under this formula at \$4.3 billion in additional funds needed for adequacy, the Greater Johnstown School District would receive an additional \$16 million dollars in state funding over the next 8 years.**

We ask for the Auditor General to support our cause to obtain adequate state funding to meet the needs of our students.

Fund Balance

According to PASBO, 83% of PA schools will use fund balance to balance their budgets for the 2016-17 school year.

Despite the need for more state revenue, the district built a strategy for 2012-13 to reduce costs and increase revenues that led to an overall reduction deficit gap \$2.3 million better than budgeted. Additionally, the budget gap that was once \$7.2 million in 2012-13 has been reduced by over half for the upcoming 2016-17 school year. Despite the better position, the district still is operating in a yearly deficit and is projecting eventual fund balance depletion. The School Board of Directors will need to continue to implement a budget strategy to reduce the budget gap. Chart 4 shows the District's financial position since 2009-10 and chart 5 shows the most current 5 year model.

Chart 4:

| | (Actual) 6/30/2010 | (Actual) 6/30/2011 | (Actual) 6/30/2012 | (Actual) 6/30/2013 | (Actual) 6/30/2014 | (Actual) 6/30/2015 | (Budget) 6/30/2016 | (Budget) 6/30/2017 |
|--------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| Total Revenue | \$43,859,914 | \$42,325,450 | \$41,651,266 | \$42,550,473 | \$42,003,520 | \$42,341,555 | \$43,546,227 | \$45,199,191 |
| Total Expenditures | \$40,395,844 | \$40,936,365 | \$42,713,926 | \$46,367,737 | \$44,398,786 | \$45,834,294 | \$46,502,500 | \$48,642,890 |
| Operating Balance | \$3,464,070 | \$1,389,085 | -\$1,062,660 | -\$3,817,264 | -\$2,395,266 | -\$3,492,739 | -\$2,956,272 | -\$3,443,699 |

Chart 5:

| | (Actual) 2013 | (Actual) 2014 | (Actual) 2015 | (Budget) 2016 | (Projected) 2017 | (Projected) 2018 | (Projected) 2019 | (Projected) 2020 | (Projected) 2021 |
|-------------------------------------|------------------|------------------|------------------|------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| REVENUES VS. EXPENDITURES | | | | | | | | | |
| <i>Total Revenues</i> | 42,550,473 | 42,003,520 | 42,341,555 | 43,546,227 | 45,199,191 | 45,828,457 | 46,542,672 | 47,237,223 | 47,770,761 |
| <i>Total Expenditures</i> | 46,367,737 | 44,398,786 | 45,834,294 | 46,502,500 | 48,642,890 | 49,328,033 | 49,931,621 | 50,561,968 | 50,901,774 |
| <i>Operating Balance</i> | (3,817,264) | (2,395,266) | (3,492,739) | (2,956,272) | (3,443,699) | (3,499,575) | (3,388,949) | (3,324,745) | (3,131,013) |
| <i>Total Initiatives</i> | | | | | | | | | |
| <i>Op. Balance Post Initiatives</i> | (3,817,264) | (2,395,266) | (3,492,739) | (2,956,272) | (3,443,699) | (3,499,575) | (3,388,949) | (3,324,745) | (3,131,013) |
| <i>Adequacy Target</i> | 48,527,443 | 49,352,409 | 50,388,810 | | | | | | |
| GENERAL FUND BALANCE | | | | | | | | | |
| <i>Beginning of the Year</i> | 15,966,873 | 12,149,609 | 9,754,343 | 6,261,604 | 5,705,331 | 2,261,632 | (1,237,943) | (4,626,892) | (7,951,637) |
| <i>End of the Year</i> | 12,149,609 | 9,754,343 | 6,261,604 | 3,305,331 | 2,261,632 | (1,237,943) | (4,626,892) | (7,951,637) | (11,082,649) |
| <i>As a % of Expenditures</i> | 26.20% | 21.97% | 13.66% | 7.11% | 4.65% | (2.51%) | (9.27%) | (15.73%) | (21.77%) |
| <i>Capital Project Funds</i> | 4,590,896 | 4,213,805 | 4,037,385 | 4,037,385 | 1,637,385 | 1,637,385 | 1,637,385 | 1,637,385 | 1,637,385 |
| <i>Total Fund Balance</i> | 16,740,505 | 13,968,148 | 10,298,989 | 7,342,716 | 3,899,017 | 399,442 | (2,989,507) | (6,314,252) | (9,445,264) |
| <i>As a % of Expenditures</i> | 36.10% | 31.46% | 22.47% | 15.79% | 8.02% | 0.81% | (5.99%) | (12.49%) | (18.56%) |

IV. Strategic Options:

During the time period, the District has implemented the following:

Cost reduction strategies:

- Implementation of staffing task force to ensure the security of incumbent employees and to analyze whether any vacated position could be eliminated or redesigned through more efficient use of staff, result was sharing of staff between buildings and combing of educational programs that led to over 50 less staff members than in 2010.
- Implementation of a grant matrix team that led to securing over \$3 million in competitive grant funds including school improvement grant.
- Removal of a bid for janitorial and educational supplies to move towards a Just-In-Time system where inventories are better managed.
- Outsourced substitute teachers and avoided the large potential cost of provided healthcare.
- Renegotiation with teachers union, results led to teachers taking a half-year pay freeze and a freeze on salary step for one year.
- Renegotiation with support union, used savings from healthcare plan adjustments to ensure employees were adequately compensated, resulting in an employee cost that will be lower in 3 years than current costs.
- Renegotiations with vendors to ensure that the District is maximizing service for a reasonable price. Including transportation, garbage disposal, security services and banking services.
- Development of a District cyber school designed to recruit resident students back who attend other tuition based cyber schools, currently 65 students are enrolled and approximately half returned from other cyber schools, reducing cyber costs by \$295,000 in 2014-15.
- Subcontract Pre-K program resulting in a \$350,000 annual savings.
- Closed the gap in transportation from \$1 million gap between revenue and expenditure as of the last state audit to close to \$600,000 in 2014-15 school year.
- Took advantage of low interest programs such as the QZAB to revitalize Johnstown Middle School.
- Eliminate building-level budgets and create a committee for materials and resources.
- Move administrators into HQHD healthcare plan, an annual savings of over \$50,000.
- Refinance bonds that become callable at a lower interest rate a savings of \$400,000 over the life of the loan.

Revenue increasing strategies:

- Driving state revenue through the understanding of state funding formulas that include Child Accounting, transportation, SHARRS and Access, this will become much more important as the fair funding formula is implemented at the state level.
- One of a few school districts that filed a lawsuit against the state to get a fair and equitable state funding formula.
- Maximizing the free and reduced lunch rates to increase dollars through Federal funds and E-Rate.
- Driving E-Rate dollars securing priority 2 funding allowing all schools to have the wireless capabilities needed to operate, District received 85% reimbursement for these costs.
- Rental use of educational facility through partnerships with local colleges and universities.

- Execution of a Chinese exchange program, where students from China pay tuition to attend the District.
- Hospital in taxation- attend County assessment hearings.
- Potential sale of administration building- \$400,000 offer.

Additional Options:

- Renegotiating expiring teacher contract to reduce overall employee cost.
- Examine the option to subcontract Kindergarten program.
- Replace retirees with lower cost part time employees.
- Reduce transportation fleet, a potential savings to the District and State of over \$500,000 by adding a third bus tier.
- Increase real estate taxes to Act 1 index.

Distribution List

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

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