

Financial Management Practices Audit Report

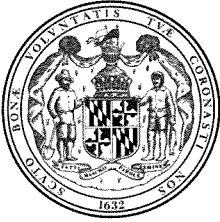
Somerset County Public Schools

September 2014



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Karl S. Aro
Executive Director

September 15, 2014

Thomas J. Barnickel III, CPA
Legislative Auditor

Senator James C. Rosapepe, Co-Chair, Joint Audit Committee
Delegate Guy J. Guzzone, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

We conducted an audit of the financial management practices of the Somerset County Public Schools (SCPS) in accordance with the requirements of the State Government Article, Section 2-1220(e) of the Annotated Code of Maryland. The objectives of this audit were to evaluate whether SCPS procedures and controls were effective in accounting for and safeguarding its assets and whether its policies provided for the efficient use of financial resources.

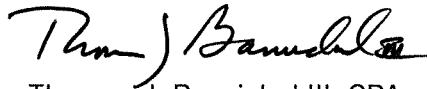
Our audit disclosed that SCPS needs to enhance internal controls and accountability for certain financial operations including procurement and disbursements, payroll processing, information system security, and equipment control. For example, certain critical user functions on the purchasing and payroll systems were not properly restricted, thereby increasing the risk of improper transactions being processed without detection. Also, SCPS needs to improve security and controls over its computer network and information systems.

The audit also identified opportunities to improve cost-effectiveness. For example, certain rates used to pay transportation bus contractors were negotiated without ensuring the amounts were reasonable, considering market conditions or actual costs. We estimated that for the seven buses placed in service between July 2008 and August 2013, SCPS will pay out approximately \$670,000 more over the 15-year life of the buses since the rate established for a particular payment component was not based on market rates.

SCPS also should enhance existing policies for procurements to address all categories of purchases, including service contracts, and expand the types of contracts that should be subject to Board approval. Finally, SCPS needs to ensure that payments to vendors are proper. We identified overpayments totaling approximately \$184,000 for certain transportation related costs.

An executive summary of our findings can be found on page 5 of this report. The SCPS response to this audit is included as an appendix to this report. We wish to acknowledge the cooperation extended to us during our audit by SCPS.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Tom J. Barnickel III".

Thomas J. Barnickel III, CPA
Legislative Auditor

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* Denotes item repeated in full or part from preceding audit report

Executive Summary

Legislative Audit Report on the Somerset County Public Schools (SCPS) September 2014

According to data compiled by the Maryland State Department of Education, SCPS ranks 23rd in student enrollment among the 24 public school systems in Maryland. In fiscal year 2013, SCPS had a total full-time regular and special education pupil population of 2,943 at its 10 schools. SCPS' operating and capital expenditures totaled \$41.5 million during that year.

The Office of Legislative Audits has conducted its second audit of SCPS' financial management practices. The results of the first audit were issued in a report dated March 25, 2010. Our current audit identified a number of opportunities for SCPS to improve internal controls, to adopt more cost effective processes, and to enhance policy direction.

SCPS Needs To Improve Internal Controls and Accountability

SCPS needs to improve internal controls in several financial areas. For example, we noted that SCPS lacked an independent review to ensure that critical personnel and payroll transactions processed were proper. SCPS also needs to restrict user access capabilities to record critical transactions on its automated human resources and payroll system and its procurement and accounts payable system. SCPS also needs to implement adequate security measures and monitoring procedures to protect its network and related critical devices from security risks. Account and password controls to protect critical systems were not sufficient.

SCPS needs to verify the propriety of payments to contractors for health care services and student transportation. SCPS is self-insured for employee medical benefits and uses a third-party administrator to process related claims. The propriety of claims paid on SCPS' behalf by the administrator was not audited to ensure the related services had been provided, nor had SCPS verified that enrolled dependents were eligible to receive health care coverage. Payments to the administrator totaled \$5.8 million in fiscal year 2013. In addition, SCPS did not always ensure the accuracy of payments for student transportation services; consequently, we identified overpayments totaling approximately \$184,000.

SCPS Should Consider Implementing Certain Steps to Improve Cost Effectiveness

SCPS should establish payment rates to bus contractors in a manner that ensures that the amounts are reasonable, considering market conditions and actual costs. For example, we estimated potential cost savings of \$670,000 over the estimated 15-year life of seven buses owned by contractors if a particular payment component was based on market rates. According to SCPS records, fiscal year 2013 transportation costs totaled \$2.8 million with 84 percent paid to contractors.

SCPS Needs to Improve Its Procurement Policies and Practices

SCPS needs to amend existing policies pertaining to the procurement of certain services and the approval of contracts by the Board. For example, SCPS frequently selected vendors without obtaining competitive bids or Board approval. Our test of 12 contracts disclosed that 10 contractors with fiscal year 2013 payments totaling \$1.2 million were selected without competitive procurements. We also noted that contracts (other than construction contracts) were generally not approved by the Board. Furthermore, for one boat contractor, the contract included a provision for SCPS to reimburse the boat's purchase price over a period of years; however, it appears that SCPS' payments toward the purchase price of the boat may have already exceeded the boat's recorded purchase price.

Background Information

Statistical Overview

According to student enrollment records compiled by the Maryland State Department of Education (MSDE), Somerset County Public Schools (SCPS) ranks 23rd in student enrollment among the 24 public school systems in Maryland. Fiscal year 2013 total full-time student population was 2,943 students. SCPS has 10 schools, consisting of 5 elementary schools, 1 intermediate school, 2 high schools, 1 technology and career center, and 1 alternative learning school.

According to SCPS' audited financial statements, expenditures totaled \$41.5 million in fiscal year 2013. The largest expenditure category was salaries and wages, including benefits, which accounted for 74.5 percent of total operating expenditures during fiscal year 2013. According to MSDE records, during the 2012-2013 school year, SCPS had 453 full-time equivalent positions which consisted of 307 instructional and 146 non-instructional employees.

Oversight

SCPS is governed by a local school board, consisting of five elected voting members and two non-voting student members. The State and the Somerset County government provide the majority of SCPS funding. In addition, MSDE exercises considerable oversight through the establishment and monitoring of various financial and academic policies and regulations, in accordance with certain provisions of the Annotated Code of Maryland. MSDE also works with SCPS to comply with the requirements and mandates of federal law. Somerset County government exercises authority over SCPS, primarily through review and approval of SCPS' annual operating and capital budgets.

External Audits

SCPS engages a certified public accounting firm to independently audit its fiscal year-end financial statements. Additionally, the auditor conducts what is referred to as a Single Audit of SCPS federal grant programs (as required by federal regulations). The resulting financial statement and Single Audit reports for fiscal year 2013 were issued in October 2013.

Due to similarities between the work of the independent certified public accounting firm that audited SCPS' financial statements and conducted the Single Audit of federal grants, and the risks and scope of our audit in certain areas, we relied on the results of those fiscal year 2013 audits. This reliance

allowed us to reduce the scope of our audit work related to certain revenues (amounts due from other governments) and federal grant activity.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of 24 of the 35 findings contained in our preceding audit report dated March 25, 2010 (the 35 findings resulted in 23 detailed recommendations in that report). We followed up on these 24 findings based on our current assessment of significance and risk relative to the audit objectives. We determined that SCPS satisfactorily addressed 13 of these findings. The remaining 11 findings are repeated in this report.

Findings and Recommendations

Revenue and Billing Cycle

Background

Somerset County Public Schools (SCPS) revenues consist primarily of funds received from Somerset County, the State, and the federal government. According to the SCPS audited financial statements, revenues from all sources totaled \$41.5 million during fiscal year 2013. In addition to these revenue sources, schools also collect funds for various purposes, such as for student activities, clubs, and school publications. Because they are not considered school revenue, these student activity funds are accounted for separately by each school and are reported in summary in the audited financial statements. Although this revenue is raised through student-related activities, SCPS has a fiduciary duty to safeguard these funds. For fiscal year 2013, school activity fund collections totaled \$570,000 and the June 30, 2013 balance was \$254,000.

External Audits

Due to the similarities between the work of the independent certified public accounting firm that audited the SCPS financial statements and our objectives for this area, we placed significant reliance on the results of the firm's audit for certain revenues, including food services revenues, for which the auditor's procedural reviews and testing disclosed no material weaknesses or deficiencies.

Finding 1

Collections were not always deposited timely nor adequately secured prior to deposit.

Analysis

Collections were not always deposited timely and SCPS had not established adequate controls over collections received at the Central Office which, according to SCPS' records, totaled approximately \$10 million during fiscal year 2013, including \$9.1 million in funds received by check from Somerset County. Our test of 10 deposits totaling \$2.7 million, disclosed that collections totaling \$452,000 related to 6 deposits were deposited from 3 to 13 working days after receipt. Untimely deposits increase the possibility of loss or misappropriation. We also noted that prior to deposit those collections were stored in an unattended room readily accessible to headquarters employees.

Recommendation 1

We recommend that SCPS

- a. deposit all funds in a timely manner,
- b. properly safeguard cash receipts prior to deposit, and
- c. investigate with the Somerset County government the possibility of receiving funds by electronic transfer rather than check.

Finding 2

SCPS did not have written policies and procedures for controlling student activity funds.

Analysis

SCPS did not have written policies and procedures for controlling student activity funds. Many other school systems we audited had detailed accounting manuals to provide policy guidance to schools administering such funds. The manuals were designed to enhance the control over these funds and specify requirements for separation of duties, verification that collections are deposited, and ensuring the propriety of disbursements. In addition, some school systems implemented frequent monitoring practices, such as using internal audit units (which SCPS lacks) or hiring independent public accounting firms to evaluate compliance.

We reviewed controls over student activity fund collections at SCPS' two high schools, which collected \$242,324 or 42 percent of the total student activity funds collected by SCPS in fiscal year 2013, and noted control deficiencies at both schools. At one school, independent accountings of athletic tickets were not performed for comparison to the related cash collected. At the other school, there was no independent verification that all recorded collections were deposited. Consequently, for both schools' activity funds, there was a lack of assurance that all collections received were deposited.

Recommendation 2

We recommend that SCPS

- a. develop policies and procedures governing controls and accountability over student activity funds, and
- b. ensure that the developed procedures are followed.

Federal Funds

Background

SCPS receives funds pertaining to federal government programs that are generally restricted for use for a specified program (such as the School Lunch Program or Special Education). According to the audited Schedule of Expenditures of Federal Awards, fiscal year 2013 expenditures of federal award funds totaled \$4.8 million.

Single Audit Report Disclosed Reportable Conditions Regarding Federal Grant Management

Due to work performed by the independent certified public accounting firm that conducted the Single Audit of SCPS federal grants and the objectives of our audit in this area, we relied on the auditor's work and results. Besides expressing an opinion on SCPS compliance with the terms of several grant programs, the auditor also considered the existing internal control structure's impact on compliance and audited the fiscal year 2013 required Schedule of Expenditures of Federal Awards. The related report stated that SCPS complied, in all material respects, with the requirements applicable to its major federal programs. With respect to internal controls over compliance with, and the operation of, major federal programs, the auditors did identify two material weaknesses. These weaknesses related to bank reconciliations that were not prepared timely and various payroll and other liability accounts that were not reconciled throughout the year.

We were advised that the reconciliations were not performed timely due to personnel resources being devoted to implementing new financial software. As of July 2013, bank reconciliations had not been completed since June 2012. Subsequently, SCPS paid its external auditors approximately \$14,000 to complete the bank reconciliations for fiscal year 2013. As of October 2013, SCPS had reconciled all of its accounts for fiscal year 2013.

Medicaid Funds Were Received for Eligible Services

SCPS had established a procedure to identify students eligible for Medicaid-subsidized services. Medicaid is an entitlement program for which certain service costs can be reimbursed to SCPS. Medicaid activity is not covered by the Single Audit of federal grants. Our tests of selected activity disclosed that reimbursement was requested for the Medicaid-subsidized services provided. According to agency records, fiscal year 2013 reimbursement for Medicaid-subsidized services totaled approximately \$703,000.

Procurement and Disbursement Cycle

Background

According to SCPS records, non-payroll disbursements totaled \$8.2 million during fiscal year 2013. Requisitions are computer generated by the requesting department and must be approved by supervisory personnel (such as a respective department head). Approved requisitions are then converted to purchase orders and approved by the Chief Financial Officer. The SCPS procurement policy requires that certain procurements over \$25,000 be competitively bid and approved by the Board. The policy also requires solicitation of quotes (either verbal or written depending on the value of the procurement) for purchases of goods and construction services over \$5,000. Payments are processed by the finance department through an automated system that prints vendor checks and also posts the payment to the financial records.

Finding 3

SCPS did not adequately restrict users' capabilities on its automated procurement and accounts payable system.

Analysis

SCPS did not adequately restrict users' capabilities on its automated procurement and disbursement system to prevent unauthorized purchasing and disbursement transactions. As a result, certain employees could process critical transactions without independent approval.

Five employees could initiate and approve purchase orders and add vendors without independent approvals. Therefore, these employees could make unauthorized purchases without detection. Also, two of these five employees had system administrator access allowing them to add or change employee accesses and capabilities, including their own, in the automated system. A similar condition regarding segregating incompatible functions and restricting system access to critical system functions was commented upon in our preceding audit report.

Invoices are matched to approved purchase orders by the system to ensure that billings from vendors correspond with the specific goods and services acquired by SCPS. However, this process does not provide sufficient controls because as noted above, the purchase approval may not have been independently authorized. Also, a finance office employee examines invoices before they are paid, but this review would not necessarily detect improper disbursements since the employee may not have sufficient knowledge of the purchasing needs of all SCPS schools and departments. Moreover, this

review was being performed by one of the employees that could initiate and approve purchase orders.

Recommendation 3

We recommend that SCPS strengthen its controls over the automated procurement and accounts payable system and processes. Specifically, we recommend that SCPS

- a. restrict users' capabilities to eliminate the ability of users to perform incompatible duties (repeat), and**
- b. establish independent electronic approval requirements for all critical purchasing and accounts payable transactions.**

Finding 4

SCPS' procurement policies generally did not require Board approval for certain purchases and did not address contractual services.

Analysis

SCPS' policies in effect during the audit did not require Board approval for the majority of high-value purchases. While SCPS had developed formal procurement policies to address the acquisition and approval of certain procurements over \$25,000, it did not require Board approval for all purchases above this level. Specifically, only facility improvements and equipment procurements required Board approval. Furthermore, SCPS' policies did not address the procurement of contractual services, particularly competitive bidding requirements for those services (see Finding 5). A similar condition regarding inadequate procurement policies was commented upon in our preceding audit report.

Our test of fiscal year 2013 disbursements for items over \$25,000 (such as, special education and therapy services) disclosed that the contracts for 10 of 12 items were not approved by the Board. Disbursements for fiscal year 2013 to these 10 vendors totaled approximately \$1.2 million.

Recommendation 4

We recommend that SCPS amend its existing policies for procurement to address all categories of purchases, including services, and establish a formal dollar threshold requiring Board approval, such as for contracts exceeding \$25,000 (repeat).

Finding 5

Contracts were frequently not awarded through competitive procurements and payment processing was not always adequate.

Analysis

Our test of payments to 12 vendors with fiscal year 2013 disbursements totaling \$1.4 million disclosed that 10 of the vendors, who received payments for good or services totaling \$1.2 million during fiscal year 2013, were not selected through competitive procurement methods. In addition, there were no documented sole-source justifications for these procurements. For four of these vendors, no contract document existed to establish the scope of services or agreed upon rates. These vendors provided goods or services including bulk fuel oil delivery and trash removal services. SCPS did not use eMaryland Marketplace to publish bids or awards for any of the items tested, each of which was in excess of \$25,000. State law requires a local school system to publish a procurement notice or notice of award greater than \$25,000 on eMaryland Marketplace.

We also noted that for three vendors with payments totaling \$250,000 during fiscal year 2013, the review and approval of vendor invoices was insufficient to ensure the propriety of the payment amount. For example, invoices for office supplies were approved without verification of the billed amounts to the original order pricing.

Furthermore, for two vendors providing student boat transportation, SCPS monthly calculates and pays for adjustments in the price of fuel; however, during fiscal years 2010 to 2013 SCPS miscalculated the adjustment amounts resulting in overpayments of \$68,000. The related contracts allowed for monthly adjustments to compensate for changes in fuel prices by multiplying the contractors' monthly fuel usage by the percentage increase in fuel costs. However, SCPS calculated the percentage change in fuel costs each month and multiplied the percentage by the contractors' annual fuel usage to determine the monthly fuel adjustments resulting in inflated adjustments. For example, during a seven-month period during fiscal year 2013, one contractor received seven monthly fuel adjustments of \$1,466 although the payments should have each been only \$147.

The awarding of contracts without competitive bidding was commented upon in our preceding audit report.

Recommendation 5

We recommend SCPS

- a. award contracts through competitive procurement methods or document why competitive procurement methods cannot be used (repeat),
- b. prepare written contracts to document the agreed upon terms,

- c. use eMaryland Marketplace for contract procurements or awards as required by State law, and
- d. ensure that vendor payments are proper and in accordance with the terms of the contracts.

Human Resources and Payroll

Background

Payroll expense represents the largest single cost component in the SCPS budget. According to SCPS records, fiscal year 2013 salary, wage, and benefit costs totaled \$30.9 million. According to Maryland State Department of Education reports, during the 2012 - 2013 school year, SCPS had 453 full-time equivalent positions, which consisted of 307 instructional positions and 146 non-instructional positions.

SCPS uses an automated integrated human resources and payroll system to maintain human resources information, record employee time, track leave usage, and to process and record payroll transactions. The system automatically generates semi-monthly time records and any adjustments are processed by central payroll personnel. The system generates payroll checks and direct deposit advices. Payroll processing involves both automated processes (such as compiling leave and running edit reports) and manual processes (such as data entry of new employee information).

Finding 6

Independent reviews of payroll and personnel transactions were lacking and access to the automated system was not properly restricted.

Analysis

Independent reviews of personnel and payroll changes processed were not performed and certain system users had unneeded capabilities in the automated human resources and payroll systems.

- SCPS lacked an independent review to ensure that processed employee personnel and payroll transactions were correct and appropriate. Transaction reports of new employees added to the system or changes to employee data, including salary changes, were not generated for verification to source documentation by an independent employee. During our test of terminations we noted two overpayments due to errors in SCPS calculations: one employee was paid for four holidays after their termination date and another terminated employee was overpaid \$2,450. We also noted five terminated employees who were underpaid a total of \$13,395.

- SCPS did not adequately restrict employees' capabilities to perform certain critical functions, such as changing employee salary and direct deposit information. Our review of critical functions related to human resources and payroll disclosed that 5 of 18 system users had unnecessary or excessive capabilities that could allow improper entries to go undetected. Specifically, we noted that two employees (IT employees) had complete access to the system allowing them to perform all personnel and payroll functions. Two additional employees had incompatible access to change salary information and process payroll (such as overtime) and one other employee due to a position reassignment no longer required the access. Our test of human resources and payroll changes and adjustments did not disclose any inappropriate transactions. A similar condition regarding inappropriate access to critical system functions was commented upon in our preceding audit report.

Recommendation 6

We recommend that SCPS

- a. perform a documented independent review of personnel and payroll transactions,**
- b. resolve the noted payment errors,**
- c. limit assignments of critical system functions to those employees who require such capabilities to perform their job duties (repeat), and**
- d. eliminate the capability of system users to perform incompatible functions.**

Finding 7

There was no documentation that the Board possessed certain pertinent information prior to approving an employee contract settlement agreement totaling \$168,000.

Analysis

There was no documentation (such as in the minutes of Board meetings) that the Board was aware of the amount SCPS would be required to pay a former school official under an employment settlement agreement.

The former official's employment contract stated that the official shall be entitled to all benefits applicable to administrative employees of SCPS with 11 years of service. We discussed this contract provision with legal counsel to the Maryland General Assembly, who concurred with our assessment that this provision of the contract was ambiguous as it relates to sick leave. Specifically, it could be interpreted to mean that sick leave is earned prospectively at the rate of an 11-year employee, or that sick leave would be

credited as if the official had worked and earned the leave at SCPS for 11 years. Since SCPS used the latter interpretation, the official's sick leave balance was increased by 220 days six months after beginning employment with SCPS to reflect the total amount of sick leave a SCPS employee would earn in 11 years.

In 2013, the Board executed a settlement agreement in which the official agreed to resign after two years of employment. The agreement stated that the official would be paid for unused leave, including sick leave. However, at the time the agreement was executed, there was no documentation to indicate that the Board was formally advised or knew of the amount (number of days) or dollar value of that credited leave. Considering the ambiguous leave provision in this official's contract, we believe the Board should have received all pertinent information, including management's interpretation of the settlement agreement that obligated SCPS to pay the former official \$168,000, \$117,000 of which was due to the aforementioned 220 days of credited sick leave.

Recommendation 7

We recommend that for any future contract settlements, SCPS ensure that all pertinent information is provided to the Board regarding contract interpretations and the related fiscal impact, as part of the decision-making process.

Inventory Control and Accountability

Background

According to SCPS audited financial statements, the undepreciated value of its capital equipment inventory totaled approximately \$3.9 million as of June 30, 2013. SCPS uses automated records to track equipment inventory with a cost of \$1,000 or more (including items capitalized for financial statement purposes).

Finding 8

SCPS equipment policies were not comprehensive and disposals were not approved.

Analysis

Our review disclosed that SCPS procedures and controls over equipment were not adequate in several areas.

- The equipment policies did not address segregation of duties, time requirements for performing physical inventories, and a comparison of

inventory counts to recorded amounts. In addition, SCPS' policy does not contain appropriate procedures to be followed if equipment items are identified as lost or stolen. We did note that in the fall of 2012, SCPS performed an inventory of IT equipment. SCPS has not conducted a complete physical inventory for many years. The lack of adequate equipment policies was commented upon in our preceding audit report.

- SCPS did not obtain approval from supervisory personnel to dispose of equipment although the SCPS equipment policy required the superintendent to approve disposals. Our review disclosed 1,570 items marked as disposed of in the inventory records and 100 of these items had a cost totaling approximately \$91,000 while the remaining 1,470 items had no recorded cost. SCPS had no evidence that the superintendent approved the disposal of any of these 1,570 items.

Recommendation 8

We recommend that SCPS improve its procedures and controls over equipment. Specifically, we recommend that SCPS

- a. update its existing procedures to include requirements for segregating duties, performing physical inventories, comparing inventory counts to recorded amounts, and for following up on lost and missing items (repeat); and**
- b. obtain required approval of all disposals of equipment.**

Information Technology

Background:

The SCPS Department of Technology (DOT) provides information systems services to all SCPS technology users. Specifically, DOT maintains the SCPS academic information application, which includes student grades, demographics, and scheduling, and is responsible for computer operations. DOT uses a vendor maintained system for its finance, human resources, and payroll applications. DOT also operates the SCPS network which links the individual schools' local networks to the computer resources located at the SCPS data center and the Internet.

Finding 9

The SCPS network was not properly secured and user capabilities on workstations were not properly restricted.

Analysis

The SCPS network was not properly secured and user capabilities on workstations were not properly restricted.

- SCPS did not adequately secure its internal network from improper network level access from SCPS high school students using either computer lab workstations or media center workstations. SCPS did not use network access control software or network level traffic filtering to protect its network from activity emanating from these workstations. Student access from these workstations should be limited to devices and ports necessary for these students to perform required tasks.
- Local administrator privileges were not properly restricted. Our test of eight regular users noted that seven of these users were assigned local administrative rights to their workstations. As a result, if these workstations were infected with malware, the malware would run with administrative rights and expose these workstations to a greater risk of compromise than if the workstations' user accounts operated with only user rights. In addition, as a result of this condition, these seven users could disable the antivirus software on their workstations.
- The antivirus software used to protect SCPS workstations was not properly configured to limit users' capabilities. Specifically, users on all eight workstations tested could disable features of the antivirus software that would render it unable to protect against network and file based threats.

Recommendation 9

We recommend that SCPS

- a. implement controls to limit network level student access to only authorized local school and headquarters network resources,**
- b. limit local administrative rights on user workstations to only personnel that require such rights for their job duties, and**
- c. disable the settings which allow users to override and modify default security controls established by management.**

Finding 10

Monitoring, account, and password controls over the SCPS' academic information system were not sufficient.

Analysis

Monitoring, account, and password controls over the SCPS' academic information system were not sufficient.

- The database supporting the academic information application was not configured to log any database security activity and operations executed via several critical accounts were not set to log. These conditions could result in unauthorized or inappropriate activities (affecting the integrity of the production database information) going undetected by management.
- The account and password controls over the application and database were not in accordance with the settings recommended by best practice guidelines from the State of Maryland Department of Information Technology's *Information Security Policy*. For example, application password controls with respect to password age, length, complexity, and history were not in accordance with the aforementioned security policy.

Similar conditions were commented upon in our preceding audit report.

Recommendation 10

We recommend that SCPS

- a. enable logging of all critical database security activities and of all operations executed via critical database accounts (repeat), and**
- b. implement recommended account and password settings over the academic information application and database (repeat).**

Facilities Construction, Renovation, and Maintenance**Background**

SCPS employs a staff of approximately 31 employees to maintain its 10 schools and the administrative office, which is within a school. According to the fiscal year 2013 Capital Improvement Plan, necessary construction, major renovations, and systemic improvements to SCPS facilities over the next six years were estimated to cost \$11.4 million.

Processes are in Place to Minimize Energy Costs

SCPS has processes in place to minimize energy costs. For example, SCPS participates in a consortium with other Eastern Shore entities to purchase energy at the best possible terms for the members of the consortium. In

addition, SCPS utilizes an energy management system that monitors and accounts for energy usage and employs an energy management program manager trained in conservation techniques and monitoring energy practices (such as usage reports and year-to-year comparisons). According to reports prepared by the program manager (which we did not audit), SCPS has avoided over \$1.5 million in energy costs since implementation of the program in 2008.

Finding 11

Construction related goods and services totaling approximately \$321,000 were procured without obtaining competitive bids.

Analysis

Our review of construction related procurements disclosed that competitive bids were not always obtained.

- SCPS executed a \$98,000 change order that materially altered the scope of the project specified in the \$134,800 original contract rather than seek bids for the new work. This change order increased the original contract amount by approximately 73 percent to expand the flooring work to a separate lobby area not covered under the original contract. Change orders should not be used when the new work materially changes the scope of the project as this is contrary to State law.
- Our test of 10 construction contracts totaling \$8.8 million disclosed SCPS did not receive competitive bids for a \$223,000 contract. A similar condition was commented upon in our preceding audit report. Furthermore, SCPS payments to this contractor included \$47,000 of travel expenses. If the contract had been competitively procured, SCPS may have found a company in closer proximity, which could have avoided or reduced travel expenses. State law requires school systems to select construction contractors through a competitive procurement process.

Recommendation 11

We recommend that SCPS

- a. not use change orders for tasks that materially alter the scope of the original project, and**
- b. obtain goods and services through a documented competitive procurement process (repeat).**

Transportation Services

Background

SCPS has approximately 2,850 students eligible to receive student transportation services. These students were transported 825,000 route miles during the 2012-2013 school year using 33 contractor-owned buses and two contractor-owned boats (for students residing on islands). According to SCPS audited financial statements, fiscal year 2013 transportation costs totaled \$2.8 million, with \$2.3 million (82 percent) representing payments for contracted bus services and \$214,000 for boat services. Payments to bus contractors consist of amounts for the purchase of a bus (known as a per vehicle allotment or PVA which consists of a reimbursement for the cost of the bus and a flat rate of return on investment) and for operating costs (such as driver salaries, fuel use, maintenance costs, and certain administrative costs). The contracts for the two boat operators provide for the payment of fuel costs, with adjustments for changes in fuel prices throughout the year.

Finding 12

Certain SCPS payments to transportation contractors did not consider market conditions, actual costs, or available discounts.

Analysis

Certain elements used to determine payment amounts to student transportation contractors did not reflect market conditions, actual costs, or available discounts. SCPS' bus contracts are for one year with annual renewals generally granted over the 15-year useful life of the bus. Boat contracts are also for a one-year period and are generally renewed. Our review of the contract payments disclosed the following conditions:

- SCPS pays bus contractors an annual PVA for each bus. The PVA reimburses the bus contractor for the cost of the bus over the 15 years the bus is in use (depreciation expense is paid each year as 1/15th of the cost of the bus) and also provides an annual return on investment (ROI) for using the bus contractors' funds to buy the bus. The ROI for fiscal year 2013 was 9.93 percent. However, SCPS could not justify the 9.93 percent ROI rate based on market conditions or otherwise.

To estimate the financial impact to SCPS of using the ROI rates over the life of a bus, we calculated the PVA for each of the 7 new buses placed

into service from July 2008 through August 2013 using the prime interest rate¹ as the ROI and SCPS' 15-year estimated useful life in the PVA formula, and compared our PVA results to the SCPS' PVA payments. This comparison showed that the SCPS annual PVA payments per bus were \$4,635 to \$7,338 higher than the payments would have been had the prevailing prime rate been used in the calculation. The effect is that, over the 15-year life of these 7 new buses, SCPS will pay out approximately \$670,000 more than if the prime rate was used for ROI to determine the PVA payments. This analysis does not include the effects for any new bus purchases that may be made after August 2013 and the lost interest income that could have been earned by SCPS on the excess amounts paid. A similar condition was commented upon in our preceding audit report.

- The SCPS fiscal year 2013 payments also included a \$0.75 per-mile fee to reimburse the contractors for bus maintenance costs. However, SCPS could not show that these payments were supported by documented or specifically estimated maintenance and repair costs.
- SCPS did not exclude federal fuel excise taxes when paying bus contractors for fuel. According to federal law, SCPS contractors are exempt from the \$0.244 per gallon excise tax for diesel fuel and are able to receive a credit for federal fuel taxes paid when they file their income tax returns. As a result, SCPS' total fuel payments to bus contractors were \$116,000 higher than necessary for school years 2010 through 2013.
- SCPS also did not competitively procure its two student boat transportation contracts. Furthermore, we reviewed the contract of one boat owner and SCPS could not substantiate how the annual payments to compensate the owner were determined. The annual contract with this owner includes an amount for amortization and interest, to enable the operator, over a period of time, to recover the boat's purchase price. During fiscal years 2010 to 2013, this payment amount totaled approximately \$35,000 annually. However, SCPS had not determined if the total of the annual payments already made had reimbursed the contractor fully for the cost of the boat. According to Department of Natural Resources' records, the boat currently used was purchased in 1999. Since according to SCPS, the contractor has been continuously providing these transportation services to SCPS since that year at similar annual payment amounts, it appears SCPS payments to date may have

¹The use of the prime interest rate was recommended in a November 1999 study commissioned by another Maryland school system. Also, in 1975 an MSDE study recommended the prime rate as a reasonable ROI interest rate. The prime rate is actually a lending rate that nearly always exceeds the available market investment rate; therefore, it is deemed to be reasonable for the ROI calculation.

already exceeded the recorded purchase price of the boat (based on the titling documents). Furthermore, the boat is not used exclusively for student transportation, but is used by the contractor for other commercial purposes such as cruises.

- SCPS could not provide us with any documentation indicating that the Board had approved the rates used to calculate payments to both bus contractors and the aforementioned boat owner.

Recommendation 12

We recommend that SCPS establish payment amounts to transportation contractors in a manner that ensures all costs are reasonable and necessary. Specifically, we recommend that SCPS

- a. use market investment rates as the basis for establishing contractor rates for the annual PVA (repeat),**
- b. use actual bus operating costs as a basis for establishing contractor rates for per mile maintenance costs,**
- c. exclude federal fuel excise taxes from contractor payments,**
- d. establish an equitable basis for determining the annual contract amounts for boat contractors, such as the use of competitive procurements, and**
- e. obtain Board approval of the rates used to determine transportation contractor payments.**

Finding 13

SCPS did not adequately ensure the accuracy of data used to compute certain payments to the bus contractors.

Analysis

SCPS did not ensure the accuracy of the time and mileage payments to bus contractors. Three times each school year, the contractors completed a manifest, which included the total time and miles driven on each route. SCPS used the data on these manifests without verifying the accuracy of the information to calculate the hourly pay and maintenance and fuel cost components of the semi-monthly payments to the contractors. Similar conditions were commented on in our preceding audit report.

Based on available documentation we estimated that during fiscal year 2013, hourly payments and base mileage payments for maintenance and fuel to contractors totaled approximately \$1 million.

Recommendation 13

We recommend that SCPS

- a. independently verify bus contractor's manifests, at least on a test basis, to ensure that the payments to the contractors accurately reflect the actual bus services provided (repeat);
- b. document the verification process; and
- c. recover any overpayments to the bus contractors identified by that process.

Food Services

Background

SCPS has a cooking cafeteria at 8 of its 10 schools. Food and related supplies are received and stored in each school. In fiscal year 2013, SCPS had 24 cafeteria positions (comprised of 23 cafeteria positions and 1 administrative position). According to the fiscal year 2013 audited financial statements, food service operation expenditures exceeded food service operation revenues by approximately \$71,000.

Finding 14

Food services invoices were not adequately verified prior to payment.

Analysis

Food services invoices were not adequately verified prior to payment. Our test of 10 invoices totaling \$168,324 related to 5 vendors with fiscal year 2013 payments for food expenditures totaling \$800,000 disclosed that for all 10 invoices there was no evidence of a documented review for propriety prior to payment. Specifically, there was no indication that the invoice prices were compared to the contract prices or approved price lists. Furthermore, SCPS procurement policies were not adhered to for food expenditures. Specifically, three vendors included in our test, with SCPS purchases of \$175,000, did not have formal contracts with SCPS and the contracts for the two other vendors, with purchases of \$625,000, were not approved by the Board as required. Total food expenditures for fiscal year 2013 were approximately \$844,000.

Recommendation 14

We recommend that SCPS ensure

- a. that formal contracts are executed with vendors and the contracts are approved by the Board in accordance with SCPS policy, and
- b. invoice prices are compared to the contract prices prior to payment.

School Board Oversight

SCPS Adopted an Ethics Policy that Met the Requirements of State Law

In 2012 the Board of Education adopted a detailed ethics policy that, according to the State Ethics Commission, conforms to State law and includes provisions for conflicts of interest and financial disclosure. Provisions of this policy are applicable to Board members as well as all SCPS employees. SCPS established an Ethics Panel consisting of three members to interpret ethics policies and provide advice on policy implementation. The Panel also reviews and rules on any reported complaints of ethics violations. According to the ethics policy, annual financial disclosure statements are required to be filed by Board members, candidates for the Board, the Superintendent, Assistant Superintendent, and a number of other administrators (such as the Chief Financial Officer and Director of Human Resources) by April 30th of each year. The policy also required that individuals in these positions file within 30 days of appointment or within 60 days of leaving an office.

Finding 15

SCPS financial disclosure statements were not always filed as required.

Analysis

SCPS did not ensure that a financial disclosure statement was filed by all employees required to do so.

- Three of 11 employees required to file a statement for calendar year 2012 did not file the required statement and 1 was filed late (in September).
- None of the 3 employees who were hired during 2013 and were required to file a statement had filed within 30 days of being hired.
- Two employees who left employment during 2013 and were required to file a statement within 60 days for 2013 failed to do so.

Agency personnel indicated that they were unaware that these employees had not filed the required statement. This condition was commented upon in our preceding audit report.

Recommendation 15

We recommend that SCPS actively enforce its ethics policy and ensure that all required disclosure statements are filed and reviewed by the ethics panel (repeat).

Other Financial Controls

Healthcare Background

SCPS is a member of a consortium for employee and retiree health care. The Consortium members are self-insured for healthcare costs up to the designated stop-loss limit. The Consortium contracts with a vendor to provide administrative services, such as claims processing for participants' medical, dental and vision costs, and for the stop-loss coverage. Stop-loss coverage indemnifies SCPS against health insurance claim amounts that exceed a certain threshold for a member.

Medical providers submit claims to the administrator who pays them on behalf of SCPS. SCPS pays the administrator for claims the administrator reports it paid and pays an administrative fee for these services. Amounts paid for health care during fiscal year 2013 totaled \$5.7 million, including approximately \$250,000 for administrative fees.

Finding 16

SCPS did not ensure the propriety of payments for employee and retiree health care costs.

Analysis

SCPS lacked procedures and controls to ensure that amounts paid to the third-party administrator for medical claims were proper.

- SCPS paid for claim reimbursements invoiced by the administrator without any verification that the amounts invoiced were proper. SCPS did not receive detailed claims data and therefore could not verify that the billed amounts agreed to the amounts of reported claims. Furthermore, SCPS did not audit the propriety of the claims paid on its behalf by the program administrator to ensure that the services were actually provided, were covered by the health plans, and were appropriately priced.
- SCPS did not verify that claims exceeding the stop-loss limit were reimbursed by the administrator under the stop-loss coverage. SCPS relies on the administrator to notify it of any payments above the stop-loss limit. According to the annual settlement, the offset to claims due to individual claims reaching the stop-loss limit are included in the paid claims amount. Since SCPS did not receive documentation of all claims invoiced and stop-loss offsets are not provided for separately, SCPS lacks assurance that it did not pay claims that should have been covered by the stop-loss insurance. For fiscal year 2013, stop-loss insurance paid by SCPS totaled approximately \$271,000.

- SCPS did not verify that enrolled dependents of employees and retirees were eligible to receive health care coverage. As of November 2013, there were approximately 460 dependents who received health coverage from SCPS. Verifications performed by other school systems have identified ineligible dependents, which can result in unnecessary health care expenses. This condition was commented upon in our preceding audit report.

Recommendation 16

We recommend that SCPS establish procedures to verify the amounts paid for health insurance. Specifically, we recommend that SCPS

- a. obtain documentation to support actual claim payments, and verify the propriety of the claims paid by agreeing the invoiced amounts with the related support, and conducting audits of the claims paid by the administrator;**
- b. use detailed claims payment data to ensure that claims paid above the stop-loss limit are reimbursed by the insurer; and**
- c. verify the eligibility of enrolled health care dependents (repeat).**

Audit Scope, Objectives, and Methodology

We conducted a performance audit to evaluate the effectiveness and efficiency of the financial management practices of the Somerset County Public Schools (SCPS). We conducted this audit under the authority of the State Government Article, Section 2-1220(e) of the Annotated Code of Maryland, and performed it in accordance with generally accepted government auditing standards. 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.

We had two broad audit objectives:

1. To evaluate whether the SCPS procedures and controls were effective in accounting for and safeguarding its assets
2. To evaluate whether the SCPS policies provided for the efficient use of financial resources

In planning and conducting our audit of SCPS, we focused on 11 major financial-related areas of operations as approved on September 14, 2004 by the Joint Audit Committee of the Maryland General Assembly in accordance with the enabling legislation. The scope of the work performed in each of these areas was based on our assessments of significance and risk. Therefore, our follow-up on the status of findings included in our preceding audit report on SCPS dated March 25, 2010, was limited to those findings that were applicable to the current audit scope for each of the 11 areas.

The audit objectives excluded reviewing and assessing student achievement, curriculum, teacher performance, and other academic-related areas and functions. Also, we did not evaluate the SCPS Comprehensive Education Master Plan or related updates, and we did not review the activities, financial or other, of any parent teacher association, group, or funds not under the local board of education's direct control or management.

To accomplish our objectives, we reviewed applicable State laws and regulations pertaining to public elementary and secondary education, as well as policies and procedures issued and established by SCPS. We also interviewed personnel at SCPS, the Maryland State Department of Education

(MSDE), and staff at other local school systems in Maryland (as appropriate).² Our audit procedures included inspections of documents and records, and observations of SCPS operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives, generally for the period from July 1, 2010 through June 30, 2013. For certain areas within the scope of the audit, we relied on the work performed by the independent accounting firm that annually audits SCPS' financial statements and conducts the federal Single Audit.

We used certain statistical data—including financial and operational—compiled by MSDE from various informational reports submitted by the Maryland local school systems. This information was used in this audit report for background or informational purposes, and was deemed reasonable.

We also extracted data from SCPS' automated finance management system for the purpose of testing expenditure, inventory, and payroll transactions. We performed various audit procedures on the relevant data and determined the data were sufficiently reliable for the purposes the data were used during the audit.

SCPS' management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate. In addition to the conditions included in this report, other less significant findings were communicated to SCPS that did not warrant inclusion in this report.

We conducted our fieldwork from June 2013 to January 2014. The SCPS response to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise SCPS regarding the results of our review of its response.

²During the course of the audit, it was necessary to contact other systems to identify policies or practices for comparative purposes and analysis.



APPENDIX

Somerset County Public Schools

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Superintendent of Schools

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Robert T. Wells, Vice Chairman

Margo Green-Gale

Dan Kuebler

Warner I. Sumpter

September 8, 2014

Mr. Thomas J. Barnickel III, CPA
Legislative Auditor
Department of Legislative Services
Office of Legislative Audits
301 W. Preston Street, Room 1202
Baltimore, MD 21201

Dear Mr. Barnickel:

Enclosed are the responses to recommendations made in the Financial Management Practices Audit Report for Somerset County Public Schools dated August 2014.

I would like to thank the legislative auditors for providing us feedback in several areas where we can become a more efficient organization.

Please do not hesitate to contact me if you need any additional information regarding this submission.

Sincerely,

John B. Gaddis, Ed.D.
Superintendent of Schools

Somerset County Public Schools

Response to Legislative Audit Final Report

Finding 1

Collections were not always deposited timely nor adequately secured prior to deposit.

Recommendation 1

We recommend that SCPS

- a. deposit all funds in a timely manner,
- b. properly safeguard cash receipts prior to deposit, and
- c. investigate with the Somerset County government the possibility of receiving funds by electronic transfer rather than check.

SCPS Response: Agree.

We agree with the recommendations and have implemented the following updated procedures for Cash Receipts to document that “Cash deposits are hand delivered to the bank within three (3) business days of receipt. Undeposited checks and cash are secured in the vault.” Finance Department staff has been cross-trained to process cash receipts to ensure timely deposits even when the staff member who is primarily responsible is out on leave.

We agree with the recommendation to better safeguard cash receipts. A small safe has been purchased to secure cash until deposit. Access by security code will be limited to staff responsible for collecting and depositing cash receipts.

In April 2014 we contacted Somerset County to discuss the possibility of receiving funds by wire transfer. Their Treasurer’s Office does not yet offer electronic deposits. They are in the process of evaluating electronic transactions but have not scheduled implementation. We will continue discussions with the County for receiving funds electronically when they begin providing the service.

Finding 2

SCPS did not have written policies and procedures for controlling student activity funds.

Recommendation 2

We recommend that SCPS

- a. develop policies and procedures governing controls and accountability over student activity funds, and
- b. ensure that the developed procedures are followed.

SCPS Response: Agree

We agree with the recommendation to develop policies and procedures. The Finance Department has created an accounting manual regarding School Activity Funds and provided it to school bookkeepers and principals. The School Activity Funds manual outlines the responsibility of the Principal (or their assignee) to review and verify Deposit Records for School events as an independent review. The independent review includes reconciliation to receipts and consecutive ticket numbering.

Written procedures have been created for Finance Staff to use in the periodic review process of School Activity Funds. Documentation of the reviews will be kept in the Finance Office.

Finding 3

SCPS did not adequately restrict users' capabilities on its automated procurement and accounts payable system.

Recommendation 3

We recommend that SCPS strengthen its controls over the automated procurement and accounts payable system and processes. Specifically, we recommend that SCPS

- a. restrict users' capabilities to eliminate the ability of users to perform incompatible duties (repeat), and
- b. establish independent electronic approval requirements for all critical purchasing and accounts payable transactions.

SCPS Response: Agree

We agree with the recommendation to implement effective internal controls over the accounts payable and procurement systems. A review of staff having access to enter requisitions, approve purchase orders, create new vendors and issue AP checks will be done on an annual basis. This review will be conducted by the CFO and verified by the Assistant Superintendent for Administration. Documentation of the review will be kept on file by the CFO.

We agree with the recommendation to perform an independent review of purchase orders approved by the system administrator. An automated report has been created and will generate on a monthly basis showing all purchase orders approved by anyone other than the CFO. This report will be emailed directly to the CFO who will verify that approvals listed are appropriate. The report will be kept on file by the CFO.

Finding 4

SCPS' procurement policies generally did not require Board approval for certain purchases and did not address contractual services.

Recommendation 4

We recommend that SCPS amend its existing policies for procurement to address all categories of purchases, including services, and establish a formal dollar threshold requiring Board approval, such as for contracts exceeding \$25,000 (repeat).

SCPS Response: Disagree

We disagree that the Bidding & Purchasing Policy (200-14), which was revised in 2013 to address sole-source procurements and in 2014 to address services purchased with Federal funds needs to be revised again to address all categories of purchases. We believe we are in compliance with state law regarding purchasing. The policy already has an established threshold of \$25,000.¹

Finding 5

Contracts were frequently not awarded through competitive procurements and payment processing was not always adequate.

Recommendation 5

We recommend SCPS

- a. award contracts through competitive procurement methods or document why competitive procurement methods cannot be used (repeat),
- b. prepare written contracts to document the agreed upon terms,
- c. use eMaryland Marketplace for contract procurements or awards as required by State law, and
- d. ensure that vendor payments are proper and in accordance with the terms of the contracts.

SCPS Response: Agree

We agree with the recommendation and will implement a process to ensure that procurements are competitively bid whenever practical and are consistent with Board policies. All purchases and contracts will be reviewed by the Assistant Superintendent for Administration before being approved or signed in order to ensure they comply with Board policy. Documentation of sole source purchasing will be kept on file with contracts when necessary.

¹ **Auditor's Comment:** The SCPS response indicates that Board procurement policy does not need to be revised to address competitive procurements and Board approval for services. In addition, the response indicates that the current procurement policy complies with State law. While State law does not require school system procurement policies to address services, comprehensive procurement policies that require competitive procurements for all types of purchases as well as board approval for all purchases above a specific limit is a recognized best practice. Moreover, other Maryland school systems have established comprehensive procurement policies, including requirements to conduct competitive procurements for service contracts and to obtain board approval for all contracts over a designated value.

We agree that written contracts should be acquired to document the agreed upon terms. A review of services in the maintenance and operations department will be completed by the newly hired supervisors. Written contracts will be requested from any vendor currently providing services. A review of services needing to be put out to bid will also be conducted.

We agree with the recommendation to ensure the use of eMaryland Marketplace for procurements or contract awards. SCPS has registered with eMaryland Marketplace and posted all procurement documents for qualifying projects this year. The newly hired Supervisor of Facilities and Capital Planning will develop and implement a procedure to ensure this practice is continued.

We agree with the recommendation to monitor services received and reconcile these records with invoices. A test on services provided by each vendor will be preformed quarterly by the appropriate supervisor and verified by the Assistant Superintendent of Administration. Results of the test will be documented and kept on file by the Operations & Facilities Associate.

Finding 6

Independent reviews of payroll and personnel transactions were lacking and access to the automated system was not properly restricted.

Recommendation 6

We recommend that SCPS

- a. perform a documented independent review of personnel and payroll transactions,**
- b. resolve the noted payment errors,**
- c. limit assignments of critical system functions to those employees who require such capabilities to perform their job duties (repeat), and**
- d. eliminate the capability of system users to perform incompatible functions.**

SCPS Response: Agree

We agree that a documented review of personnel and payroll transactions should be performed by an independent employee. We disagree that SCPS lacked such a process. A process was in place but was not being followed consistently by the appropriate staff. We will establish a written procedure for the independent review which will include printing a report on a monthly basis of changes made and having it verified by the Human Resources Supervisor.

The CFO is looking into the status of the noted payment errors and will report to the Assistant Superintendent for Administration on the appropriate resolution.

We agree that access to critical functions should be limited to those employees who require such capabilities to perform their assigned job duties. Employees with inappropriate access had those rights taken away immediately upon notification by the auditors. The two IT

employees mentioned in the findings are the System Administrators and as such require total access to perform their job duties.

Finding 7

There was no documentation that the Board possessed certain pertinent information prior to approving an employee contract settlement agreement totaling \$168,000.

Recommendation 7

We recommend that for any future contract settlements, SCPS ensure that all pertinent information is provided to the Board regarding contract interpretations and the related fiscal impact, as part of the decision-making process.

SCPS Response: Agree

We agree that the Board should gather all pertinent information regarding the fiscal impact of any settlement agreement prior to approving it. A written procedure will be established to ensure this happens.

Finding 8

SCPS equipment policies were not comprehensive and disposals were not approved.

Recommendation 8

We recommend that SCPS improve its procedures and controls over equipment.

Specifically, we recommend that SCPS

- a. update its existing procedures to include requirements for segregating duties, performing physical inventories, comparing inventory counts to recorded amounts, and for following up on lost and missing items (repeat); and
- b. obtain required approval of all disposals of equipment.

SCPS Response: Agree

We agree with the recommendation to update procedures for inventorying equipment. Procedures and policies for both Fixed Assets and Sensitive equipment inventories will be reviewed and updated as necessary. The updated procedures will include a process that provides for approval of all disposals of equipment. Although we recognize the need for these controls it will be difficult to fully implement this recommendation with existing staff.

Finding 9

The SCPS network was not properly secured and user capabilities on workstations were not properly restricted.

Recommendation 9

We recommend that SCPS

- a. implement controls to limit network level student access to only authorized local school and headquarters network resources,
- b. limit local administrative rights on user workstations to only personnel that require such rights for their job duties, and
- c. disable the settings which allow users to override and modify default security controls established by management.

SCPS Response: Agree with exception

We agree with the recommendation to strengthen controls to limit access to our networks. We are going to work with a network consultant to redesign our local and wide networks using VLANs and access control lists. This will be a multi year project and will be finished as funding permits.

We have such a small IT staff, we count on our regular staff members to help themselves, their students and their colleagues with technical issues. That requires all staff members to have local administrator privileges for doing things like installing software, installing updates to software and renewing computer certificates. We have also moved to a better antivirus product which is password protected. It cannot be automatically disabled or uninstalled by non IT staff.

We agree with the recommendation to not allow users to override and modify security controls. We have already moved to a different antivirus product which is password protected.

Finding 10

Monitoring, account, and password controls over the SCPS' academic information system were not sufficient.

Recommendation 10

We recommend that SCPS

- a. enable logging of all critical database security activities and of all operations executed via critical database accounts (repeat), and
- b. implement recommended account and password settings over the academic information application and database (repeat).

SCPS Response: Agree with exception

SCPS will work with the application vendor to determine the best possible way to implement the recommendation that we enable logging of all critical database security activities in a way that doesn't compromise the licensing agreement between the application vendor and the database vendor. As this requires third-party involvement, it will be difficult to establish a reasonable timeline for the completion of this item.

We agree with the recommendation to strengthen the password security over the academic information application and database and are working within the abilities of the application to comply. We have already changed the password again rule to 360 days for students and 60 days for staff. We now require the password length of 8 characters as a minimum and are enforcing the complexity rules. In addition we have changed the Password Reuse Rule to 10 for all users and the lockout rate to be disabled after not more than four consecutive failed login attempts.

Finding 11

Construction related goods and services totaling approximately \$321,000 were procured without obtaining competitive bids.

Recommendation 11

We recommend that SCPS

- a. not use change orders for tasks that materially alter the scope of the original project, and**
- b. obtain goods and services through a documented competitive procurement process (repeat).**

SCPS Response: Agree

We agree with the recommendation to not use change orders for tasks that materially alter the scope of a project. The Change Order Procedures Policy has been revised to include a process of having the Construction Manager and the project Architect confirm the proposed change order is warranted and is consistent with the original scope of work. Material additions to the original project scope must be bid separately.

We agree with the recommendation that all goods and services should be competitively bid in accordance with SCPS policy 200-14. See response to Finding #4.

Finding 12

Certain SCPS payments to transportation contractors did not consider market conditions, actual costs, or available discounts.

Recommendation 12

We recommend that SCPS establish payment amounts to transportation contractors in a manner that ensures all costs are reasonable and necessary. Specifically, we recommend that SCPS

- a. use market investment rates as the basis for establishing contractor rates for the annual PVA (repeat),**

- b. use actual bus operating costs as a basis for establishing contractor rates for per mile maintenance costs,
- c. exclude federal fuel excise taxes from contractor payments,
- d. establish an equitable basis for determining the annual contract amounts for boat contractors, such as the use of competitive procurements, and
- e. obtain Board approval of the rates used to determine transportation contractor payments.

SCPS Response: Agree

We agree with the recommendation that SCPS should establish payment amounts to transportation contractors in a manner that ensures all costs are reasonable and necessary. We will continue to work with our Board to investigate our method for establishing contractor rates for the annual PVA as well as per mile and maintenance costs. In this process the Board will consider excluding federal excise taxes from contractor payments. These methods will be establish for both boat and bus contractors.

We agree with the recommendation to seek Board approval of the rates used to determine transportation contractor payments each year as part of the formal budget process.

Finding 13

SCPS did not adequately ensure the accuracy of data used to compute certain payments to the bus contractors.

Recommendation 13

We recommend that SCPS

- a. independently verify bus contractor's manifests, at least on a test basis, to ensure that the payments to the contractors accurately reflect the actual bus services provided (repeat);
- b. document the verification process; and
- c. recover any overpayments to the bus contractors identified by that process.

SCPS Response: Agree

We agree with the recommendation that bus contractor's manifests need to be independently verified. The newly hired Supervisor of Transportation will be responsible for developing and implementing a process to verify manifests. The process will include documentation and a process for attempting to recover any adjustments.

Finding 14

Food services invoices were not adequately verified prior to payment.

Recommendation 14

We recommend that SCPS ensure

- a. that formal contracts are executed with vendors and the contracts are approved by the Board in accordance with SCPS policy, and**
- b. invoice prices are compared to the contract prices prior to payment.**

SCPS Response: Agree

We agree with the recommendation that formal contracts are executed with vendors and contracts are approved by the Board in accordance with SCPS policy. SCPS participates in the Shore Four Group which competitively bids services for many products and services. A process will be put in place to ensure the Board is notified of all contracts being used to purchase food and food related products.

We agree with the recommendation to compare invoice prices with contract or agreed-upon prices. A test on food prices for each vendor invoice will be performed to match the price list and documented on a monthly basis, along with the monthly food cost comparison chart. It should be noted that due to USDA regulations, food purchases are at an extremely high cost which is primarily on fresh fruits and vegetables. Our produce company provides us with a new price sheet each month. Product choices are determined by price. We must continue to offer our students fresh fruits and vegetables in order to be compliant.

Finding 15

SCPS financial disclosure statements were not always filed as required.

Recommendation 15

We recommend that SCPS actively enforce its ethics policy and ensure that all required disclosure statements are filed and reviewed by the ethics panel (repeat).

SCPS Response: Agree

We agree with the recommendation that SCPS actively enforce its ethics policy and ensure that all disclosure statements are filed and reviewed by the ethics panel. The Assistant Superintendent for Administration will submit a list to the Board Associate of employees required to fill out a financial disclosure statement form in October each year. Forms will be sent out to employees by the Board secretary in January to be completed and returned no later than April 30th. The Board secretary will submit names of anyone who has not turned in a form to the Assistant Superintendent for Administration by May 15th.

Finding 16

SCPS did not ensure the propriety of payments for employee and retiree health care costs.

Recommendation 16

We recommend that SCPS establish procedures to verify the amounts paid for health insurance. Specifically, we recommend that SCPS

- a. obtain documentation to support actual claim payments, and verify the propriety of the claims paid by agreeing the invoiced amounts with the related support, and conducting audits of the claims paid by the administrator;
- b. use detailed claims payment data to ensure that claims paid above the stop-loss limit are reimbursed by the insurer; and
- c. verify the eligibility of enrolled health care dependents (repeat).

SCPS Response: Agree

We agree with the recommendation and recognize that better controls need to be in place to verify amounts paid for health insurance. This is a challenge due to the nature of the ESMEC Trust. However, SCPS will be presenting the findings to the ESMEC trust to help ensure that controls are put in place. SCPS would accept and be appreciative for any advice on how this can be accomplished with the health care trust structure that is now in place for the purpose of reducing costs. SCPS ESMEC Trustee started a conversation at the recent meeting on this topic. ESMEC has agreed to work with the legislative auditors to resolve this issue.

AUDIT TEAM

Stephen C. Pease, CPA
Audit Manager

Richard L. Carter, CISA
Stephen P. Jersey, CPA, CISA
Information Systems Audit Managers

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Information Systems Senior Auditors

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Staff Auditors