

Audit Report

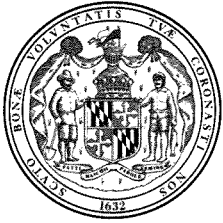
**Board of Public Works
Interagency Committee on School Construction**

April 2013



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

April 22, 2013

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Executive Director

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 have audited the Board of Public Works – Interagency Committee on School Construction (IAC) for the period beginning March 26, 2009 and ending February 5, 2012. IAC supervises and provides funding for public school construction in Maryland, subject to the Board of Public Work's approval.

Our audit disclosed that sufficient controls were not established over IAC's automated accounting system, which is used to track costs and monitor construction project activity, to ensure the accuracy of the data. For example, certain employees could record critical transactions in the automated system without a documented supervisory review.

Our audit also disclosed that IAC was not monitoring to ensure construction project closeout documents needed to identify funds potentially owed to the State by the local jurisdictions were obtained timely. Additionally, IAC had not taken sufficient actions to resolve a matter involving certain debt that was to be assumed by a local jurisdiction for a closed school. Furthermore, although IAC conducted 232 public school maintenance inspections during fiscal year 2011, IAC had issued reports for only 57 of these inspections as of March 21, 2012.

IAC's response to this audit is included as an appendix to this report. We wish to acknowledge the cooperation extended to us during the course of this audit by IAC.

Respectfully submitted,



Thomas J. Barnickel III, CPA
Legislative Auditor

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

Background Information

Agency Responsibilities

In accordance with the provisions of the Education Article, Section 5-301 of the Annotated Code of Maryland, the State established a program to aid the counties and Baltimore City with respect to certain public school construction projects and capital improvements, which are subject to the approval of the Board of Public Works (BPW). BPW has adopted regulations for the administration of the school construction program, which provide for the establishment of an Interagency Committee on School Construction (IAC). IAC consists of the Secretary of the Department of Planning, the Secretary of the Department of General Services, the State Superintendent of Schools, or their respective designees, and two public members appointed by the President of the Senate and the Speaker of the House. According to its records, during fiscal year 2011, IAC disbursed approximately \$249 million in capital funds for public school construction projects, and its operating expenditures totaled approximately \$6.1 million, including \$4.6 million for the Aging Schools Program, which provides funds (without any local match) for capital improvements and repairs to existing schools.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the four findings contained in our preceding audit report dated December 10, 2009. We determined that IAC satisfactorily addressed three of the aforementioned four findings. The remaining finding is repeated in this report.

Findings and Recommendations

Capital Construction Projects

Background

Annually, each local education agency (LEA) submits a capital improvement program detailing its public school construction project needs for the budget year and the next five years to the Board of Public Works (BPW) – Interagency Committee on School Construction (IAC). These projects include the construction of new schools, additions to existing schools, systemic renovations, and capital improvements. Based on the program and the preliminary budget for public school construction projects, IAC creates a State Capital Improvement Plan (CIP) to prioritize the projects on a Statewide basis. Every year between December and May, IAC is responsible for recommending projects that will be funded from the available funds, determining the source of funding for each approved project, submitting these projects to BPW for approval, and recording (allocating) the funds to the approved projects.

Once a project is approved by BPW, LEAs submit LEA-procured contracts for each of the projects for IAC's review for propriety (for example, review for costs that are ineligible for State participation). BPW has delegated approval of these contracts to IAC. Once the LEA incurs expenditures from the approved contracts, it may request payment from IAC if State funds have been allocated to the project. Generally, State funds for these contracts are expended prior to the LEA funds. IAC may make payments directly to the vendors performing construction on the approved contracts or, in other cases, the LEA will pay the vendor and obtain reimbursement from IAC. Upon completion of a project, the LEA is required to submit project closeout documentation which is used by IAC to provide a record of State and local investments in the project, and determine if any amounts are owed to the State (such as expenditures which exceeded the State's agreed upon percentage of the project cost or construction items that were not included in the approved scope of work).

During fiscal year 2011, BPW approved 171 public school construction projects totaling approximately \$257 million and disbursed approximately \$249 million to fund public school construction projects. During fiscal year 2011, IAC approved 355 LEA-procured construction contracts totaling approximately \$566 million, of which the State is to fund \$248 million.

Finding 1

Proper controls were not established over data recorded in IAC's construction project accounting records and certain documentation was not maintained.

Analysis

Proper controls were not established over data recorded in IAC's automated records related to approved construction projects and LEA-procured contracts and certain documentation was not maintained. Specifically, we noted the following conditions:

- IAC had not established sufficient internal controls over its automated accounting system used to track project and contract costs. Specifically, certain critical transactions could be processed without independent supervisory review. For example, four employees could add new construction projects to the system, and process project change orders (increasing the project's value), and three of these employees could also change system access capabilities without independent supervisory review. Although we were advised that a supervisor reviewed project data entered into the system, this review was not documented. Consequently, assurance was lacking regarding the accuracy of the data.
- IAC had not documented its approval of LEA-procured contracts, for which State funding would be provided. Specifically, although the IAC approved the awarding of the contracts during its meetings, IAC staff advised us it had not prepared formal meeting minutes documenting these decisions since December 2007. The Open Meetings Act (Title 10, subtitle 5 of State Government Article, Annotated Code of Maryland) provides that public bodies shall have written minutes of their sessions that reflect each item considered, the action taken and each recorded vote.
- IAC did not ensure that executed copies of LEA-procured contracts were subsequently obtained to ensure that they were consistent with contracts it had previously approved. Our test of 22 contracts totaling approximately \$366 million, for which there were disbursements during fiscal years 2011 and 2012, revealed that signed copies of 6 contracts totaling approximately \$36 million in State funding were not obtained by IAC.

Recommendation 1

We recommend that IAC

- a. establish a documented independent supervisory review of project data entered into the automated project accounting system;**
- b. prepare and maintain written minutes detailing the matters considered and the actions taken by the IAC during its meetings as required by the Opening Meetings Act; and**
- c. obtain copies of the executed contracts for review, including the aforementioned contracts.**

Finding 2

IAC did not monitor the status of construction projects to ensure the timely submission of project closeout documents.

Analysis

IAC did not monitor the status of construction projects to ensure the timely submission of construction project closeout documents by LEAs. These closeout documents include a final cost summary and certificate of completion. As a result, any amounts owed the State (such as for expenditures which exceeded the State's agreed upon percentage of the project cost or construction items that were not part of the approved scope of work) by the LEAs could remain unidentified and uncollected for extended periods. In March 2012, the IAC advised us that the most recent request for closeout information was made in February 2011. As of March 8, 2012, there were 126 projects with State funding totaling \$450 million for which IAC had not determined whether the projects had been completed and the related closeout documents had been received. The last disbursement of State funds for these projects occurred from one to five years earlier.

State regulations require LEAs to submit construction project closeout documentation to the State within 180 days of final payment to the contractor so that IAC can complete its administrative closeout procedures and determine if the LEA owes any amount to the State. Similar conditions have been commented upon in our three preceding audit reports dating back to 2003.

Recommendation 2

We recommend that IAC

- a. determine the status of the aforementioned 126 projects and obtain the related closeout documentation for completed projects;**
- b. establish procedures for the timely monitoring of the status of projects to ensure that, in the future, LEAs submit required project closeout**

- documentation within 180 days of final payment to the contractor for all projects (repeat); and
- c. upon obtaining the required documentation, promptly complete the administrative closeout process and identify and collect any amounts owed to the State (repeat).

Recovery of State Funds

Finding 3

IAC had not taken sufficient actions to resolve a matter involving certain debt that was to be assumed by a local jurisdiction for a closed school.

Analysis

IAC had not taken sufficient actions to resolve a matter involving certain debt that was to be assumed by a local jurisdiction for a school that was no longer being used for school purposes. In February 2007, a local jurisdiction declared a school as being surplus and closed the school, which presently is being used as a training facility for police and firefighters. On February 13, 2008, BPW approved the closure and transfer of the school to the local jurisdiction's government. This approval was given under the condition that the local jurisdiction was to assume the outstanding debt associated with the school, which was calculated as \$837,820 as of June 30, 2007. Subsequently, IAC discovered that the amount of outstanding debt had been incorrectly calculated and had developed a proposal to request BPW approval for the corrected amount of \$890,277. However, this request was withdrawn. Additionally, in a December 2008 letter, a representative of the local jurisdiction requested that the assumption of outstanding debt payments by the jurisdiction be waived. No formal action had been taken on this request and, as of March 12, 2013, this situation had not been resolved. We were advised that the State continued to make the debt payments associated with this debt and ultimately, on July 1, 2011, the State paid off the associated debt in full.

State law requires that the State shall require reimbursement of outstanding debt service for a school that is no longer being used for school purposes. In this particular case, IAC funded the rewiring of the school through the State's Master Lease Purchase Financing Program.

Recommendation 3

We recommend that IAC take the necessary actions to resolve this matter and, in the future, ensure that local jurisdictions assume outstanding debt payments related to schools that are no longer being used for school purposes, as applicable.

Maintenance Inspections

Finding 4

IAC did not finalize the results of the maintenance inspections of public schools conducted during fiscal years 2011 and 2012.

Analysis

Although IAC conducted 232 maintenance inspections for all LEAs during fiscal year 2011, IAC had issued the results of only 57 of these inspections to the LEAs, as of March 21, 2012. Furthermore, we noted that no reports were issued for the 139 inspections of 16 LEAs that were conducted as of March 21, 2012 for fiscal year 2012.

Until the final reports are issued to the LEAs, the deficiencies identified during the inspections may not be corrected. During its fiscal year 2011 inspections of the 57 schools for which reports had been issued to 9 LEAs, IAC noted that the conditions at certain schools were not adequate. For one LEA, for which a report was issued, the overall condition of 3 of the 35 schools inspected was deemed “not adequate.” Deficiencies affecting the health and safety of its students and staff at these schools, such as unsanitary conditions, were disclosed.

State regulations require IAC to annually rate the maintenance conditions at selected schools in each LEA. To assess the condition of schools, the IAC has a target to perform maintenance inspections at all schools during a six-year cycle. The regulations also require that any LEA that operates a school that receives a “not adequate” rating in any inspection category submit a corrective action plan, stating how and when the deficiencies will be resolved, to IAC within 30 days of receiving the inspection results.

Recommendation 4

We recommend that IAC finalize the maintenance inspections performed and issue the reports of its findings to LEAs timely, and take appropriate follow-up action to obtain corrective action plans from all applicable LEAs as required.

Audit Scope, Objectives, and Methodology

We have audited the Board of Public Works – Interagency Committee on School Construction (IAC) for the period beginning March 26, 2009 and ending February 5, 2012. The audit was conducted 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.

As prescribed by State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine IAC's financial transactions, records and internal controls, and to evaluate its compliance with applicable State laws, rules, and regulations. We also determined the status of the findings included in our preceding audit report.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. The areas addressed by the audit included capital funds used to finance the cost of public school construction and renovation projects, public school maintenance inspections, construction project closeout procedures, cash receipts, and payroll. Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observations of IAC's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

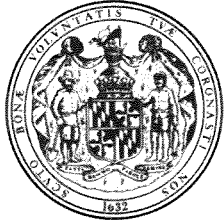
IAC's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of 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.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect IAC's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to IAC that did not warrant inclusion in this report.

IAC's 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 IAC regarding the results of our review of its response.



MARTIN O'MALLEY
GOVERNOR

STATE OF MARYLAND
PUBLIC SCHOOL CONSTRUCTION PROGRAM
200 W. BALTIMORE STREET
BALTIMORE, MARYLAND 21201
410-767-0617

INTERAGENCY COMMITTEE ON SCHOOL CONSTRUCTION

APPENDIX

DAVID G. LEVER
EXECUTIVE DIRECTOR

LILLIAN M. LOWERY, Ed.D
CHAIRPERSON

April 17, 2013

Mr. Thomas J. Barnickel III, CPA
Legislative Auditor
Department of Legislative Services
Office of Legislative Services
Maryland General Assembly
301 West Preston Street, Room 1202
Baltimore MD 21201

Re: Public School Construction Program Legislative Audit Findings 2012 - Response

Dear Mr. Barnickel:

We have received and reviewed the draft audit report dated March 19, 2013 pertaining to the audit of the Public School Construction Program (PSCP) for the period beginning March 26, 2009 and ending February 5, 2012.

The Legislative Auditor's recommendations to improve the operations of this agency are always welcomed and appreciated.

As requested, we are providing you with our responses to the recommendations made. A hard copy will follow. Please note that we have amended certain language within the draft audit report to more accurately reflect the authority and procedures of the agency and the Interagency Committee on School Construction.¹

If you have any questions please contact Bob Crocetti, our Director of Finance, at (410) 767-0612 or myself at (410) 767-0610.

Sincerely,

David G. Lever, R.A., D.A.
Executive Director

cc: Lillian Lowery M. Lowery, Ed.D.
Ms. Joan Schaefer
Mr. Robert C. Crocetti

¹ Certain edits were made to the report to address the agency's concerns.

PUBLIC SCHOOL CONSTRUCTION PROGRAM
LEGISLATIVE AUDIT REPORT
AGENCY RESPONSES
April 17, 2013

Finding 1

Response:

- a. **AGREE** - Changes to the programming of the Capital Financial Accounting System will be made to properly provide for a separation of responsibilities. Specifically, users will be restricted to certain functions within the system and additional reports will be created to provide for documentation of supervisory review of data input. These changes will be finalized and implemented by July 1, 2013.
- b. **AGREE** - A more succinct and efficient process of generating the IAC minutes will be implemented to provide for a timely recordation and submission of IAC actions. As part of this new process, the IAC will record the vote on each item considered and any action taken, and will make these minutes available via the PSCP website. This process will be tested, reviewed, and finalized by July 1, 2013.
- c. **AGREE** - Soon after receipt of the audit discussion notes, the process for reconciling IAC contract approvals with the receipt of signed copies of contract agreements was changed. Rather than being performed periodically, communications with LEAs will take place every two weeks, with follow-up phone calls and/or email reminders for those that are outstanding.

Finding 2

Response:

- a. **AGREE** – The IAC has determined the status of the aforementioned 126 projects and, where appropriate, has obtained the related closing documentation.
- b. **DISAGREE** – IAC staff did monitor the status of construction projects to ensure the timely submission of project close-out documents, based upon the best information available to the finance office in order to determine an estimated date of completion or occupancy. The list of the aforementioned 126 projects (for which required closeout documentation was not available at the time of the audit) was derived by using the State’s final expenditure as a flag for further investigation. The LEA’s final expenditure, i.e. for final payment, completed punch list items, or last minute credit change orders, could, for large projects, occur several years or more after the State’s final expenditure. The IAC has no way of knowing if the LEA’s final payment has

been made except through the periodic contacts it makes based on the list of final State payments.

The new procedure for monitoring the status of projects to ensure timely submission of LEA closeout documentation uses IAC/PSCP Form 102.5-Status of Previously Approved Projects, which is submitted during the CIP process showing the status of all active projects and the percentage of completion. Form 102.5 is compared to the records in the PSCP financial and facility inventory databases. From this Form, letters are generated requesting outstanding documentation, with follow-up occurring every three months. In October every year, the PSCP meets with almost every LEA to discuss their Capital Improvement Program (CIP) requests for the next fiscal year, and it is at these meetings that IAC/PSCP Form 102.5 is presented and discussed. These meetings are frequently attended by the Superintendent or other high ranking officials of the school systems, and they provide an opportunity to raise issues not directly related to the CIP such as delinquent close-out documentation. To date, this process has resulted in a number of close-out submissions as well as discussions with our finance department to resolve outstanding issues.¹

- c. **AGREE** – However, it should be noted that the primary purpose for which closeout documents were created was to audit ineligible expenditures and reconcile project advances. Prior to the late 1980s, the LEAs were advanced cash on a monthly basis upon receipt of a phone call to PSCP estimating their cash needs for the upcoming 30 days. There were no invoices submitted with this request, and no reviews were conducted by PSCP finance staff of the cash transaction until after the work was completed. Clearly, this arrangement created more reliance on closeout documentation as an audit tool to identify and collect any amounts owed to the State. This process of payment is, however, no longer used. All payments made to contractors or LEAs are supported by invoices, cancelled checks, and notarized signatures for review (as well as DGS reviews and PSCP Program Manager reviews) *prior* to any payment transaction. The secondary purposes for which closeout documents were created was to have an archive of all local costs for the project and to confirm that no further adjustments in the State funding participation would be needed. This has now become the primary purpose for which closeout documentation is still needed; however, the documentation clearly does not serve the same level of importance nor does it carry the same time sensitivity as it did when it supported the former primary purpose.

¹ **Auditor's Comment:** In its response, IAC indicated disagreement and stated it did monitor the status of construction projects to ensure timely submission of closeout documents. However, at the time of our audit there was no documentation of such monitoring for over one year. IAC's response indicates that a new monitoring procedure has been established which requires quarterly follow-up on the status of projects. The implementation of this procedure addresses the audit recommendation.

Finding 3

Response:

Disagree. To clarify, the representative of the local jurisdiction appealed in December 2008 for waiver of the outstanding debt to the State Treasurer's Office (STO), not to the IAC. We understand that the Board of Public Works (BPW) is currently seeking advice from the Office of the Attorney General (OAG) whether the BPW can waive the obligation of Baltimore City to repay the cost of the capital investment now that the capital lease has been paid off. Once advice of counsel from the OAG is received, we will work with the BPW and with the STO to determine next steps.²

Finding 4

Response:

Agree. We agree that the fiscal year 2011 and 2012 maintenance inspection reports must be finalized and issued to the LEAs, and we are currently dedicating staff resources to achieve that outcome. Since the auditors' findings of March 2012, we have issued 153 additional reports and have established a schedule to complete and issue all survey reports ahead of the September 8, 2013 deadline that is required in the 2012 budget.

While the field inspections have been completed on schedule in every year of the Inspection Program, we acknowledge that the paperwork dimension of the Program has lagged. This is due to the expansion of the scope of the program since it was relocated to the PSCP in 2006 as well as to increasing staff constraints. The problem has been addressed by re-defining and filling an administrative support position that is now entirely dedicated to assisting the Deputy Director with the Maintenance Inspection Program. We will follow our standard procedure for timely follow-up action to obtain appropriate corrective action plans from all applicable LEAs.

² **Auditor's Comment:** IAC indicated disagreement with this finding. However, its response acknowledges that this matter has not been resolved and that additional action will be taken.

AUDIT TEAM

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