

Financial Management Practices Performance Audit Report

Allegany County Public Schools

January 2007



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

Bruce A. Myers, CPA
Legislative Auditor

January 5, 2007

Senator Nathaniel J. McFadden, Co-Chair, Joint Audit Committee
Delegate Charles E. Barkley, 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 Allegany County Public Schools (ACPS) in accordance with the requirements of the State Government Article, Section 2-1220(f) of the Annotated Code of Maryland. ACPS is the 16th largest public school system in Maryland based on the number of students enrolled. The educational services are delivered in 23 schools, with an annual budget of \$100 million. The objectives of this audit were to evaluate whether ACPS 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 report contains 17 recommendations. ACPS needs to make certain enhancements to its existing financial management systems and processes, implement adequate safeguards over procurement and improve oversight of transportation and food service operations. For example, we identified certain components of the formula used to establish bus transportation vendor reimbursement rates that should be reevaluated, as they appear to result in unnecessarily high reimbursements, which could cost ACPS approximately \$3.4 million over the life of the new buses put into service during the last 11 years. Furthermore, the Board should establish formal policies addressing certain critical areas such as procurement, human resources and inventory. This report also identifies several instances in which processes and best practices are already in place that help ensure the efficient use of financial resources.

An Executive Summary of our findings can be found on page i, immediately following this cover letter, and our audit scope, objectives, and methodology are explained on page 67. We wish to acknowledge the cooperation extended to us during our audit by ACPS.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

Executive Summary

The Office of Legislative Audits has conducted an audit to evaluate the effectiveness and efficiency of the financial management practices of the Allegany County Public Schools (ACPS) in accordance with the State Government Article, Section 2-1220(f) of the Annotated Code of Maryland. State law requires the Office to conduct such an audit of each of the 24 public school systems in Maryland and provides that the related audit process be approved by the Joint Audit Committee. The Committee approved the audit process in September 2004. The approved process included 11 functional areas to be audited at each system. The following are summaries of the findings in these areas at ACPS.

Revenue and Billing Cycle (see pages 7 through 9)

The procedures in place for the vast majority of revenue, which was received via wire transfer from other government entities, provided sufficient controls to ensure full collection, proper accounting and safeguarding of those funds. Procedures over other sources, such as cash receipts from food service operations and student activities, were also found to be adequate.

Federal Funds (see pages 11 through 13)

ACPS is subject to an annual audit by an independent certified public accounting firm of its federally-funded grant programs. Due to parallels between that work and the scope of our audit, we placed significant reliance on the results of the firm's audit of the fiscal year 2005 grant activity, for which reported expenditures totaled \$11.5 million. The report on the audit of federal grant programs did not disclose any material weaknesses, reportable conditions, or questionable costs. We found that, for Medicaid-subsidized services totaling \$922,000, ACPS had several processes in place to identify and recover eligible costs.

Procurement and Disbursement Cycle (see pages 15 through 20)

ACPS lacked a comprehensive policies and procedures manual for procurement and invoice processing. For example, ACPS needs to develop written procurement policies, including when to use competitive bidding and when to obtain Board approval for purchases. According to ACPS records, during fiscal year 2005, non-payroll disbursements totaled \$25 million. From our review and testing we noted that ACPS' decentralized procurement process led to inconsistencies in procurement, control and contract monitoring deficiencies, and a lack of adequate support documentation for certain transactions.

Human Resources and Payroll (see pages 21 through 25)

ACPS employed 1,400 full and part-time employees during 2005 with associated payroll cost of \$73 million. We noted that ACPS had a highly centralized process to monitor vacancies and control the hiring of new employees, and had developed a leadership program to provide training and mentoring for teachers seeking administrative positions. However, we noted that workforce planning should be expanded to include non-instructional personnel and that a comprehensive human resources and payroll manual should be adopted.

Inventory Control and Accountability (see pages 27 through 29)

ACPS recordkeeping and control need to be improved for equipment which, according to the audited financial statements, had a June 30, 2005 value of \$11.1 million. Necessary actions include the establishment and enforcement of formal policies addressing such issues as recordkeeping, physical inventory procedures, and equipment disposals. Additionally, textbook inventory results should be used to provide accountability and control and to ensure efficient redistribution of textbooks.

Information Technology (see pages 31 through 34)

ACPS shares its information system services with the Allegany County Government. In addition, ACPS shared the development and maintenance of a wireless, high-speed, wide-area network with the Allegany County Government, City of Cumberland, and Allegany County Public Library. Cooperation and sharing of information resources and services is a best practice that enhances cost effectiveness for ACPS and the other participating agencies of government.

Nevertheless, certain aspects of ACPS' information technology operations can be improved. Improvements should be made relative to physical access to ACPS' computer room, software access controls to computers, monitoring of computer security events, program change procedures, and the disaster recovery plan.

Facilities Construction, Renovation, and Maintenance (see pages 35 through 39)

ACPS uses a staff of 130 custodial and maintenance personnel to maintain its 27 facilities, including 23 schools. We identified several best practices that ACPS has put in place to assist in facilities construction, maintenance, and operation. These best practices include the preparation of a six-year Capital Improvement Plan, the following of State guidelines and laws regarding procurement for construction and renovation, the close monitoring of major school construction and renovation projects, and the use of a comprehensive energy management program. However, we did identify two issues that could increase operational efficiency further. One is the need to develop performance standards and measures for maintenance and custodial operations, and the second is the need to document that all maintenance was performed in accordance with the schedules and details of the ACPS comprehensive maintenance plan.

Transportation Services (see pages 41 through 48)

ACPS transports more students more miles than most other similarly-sized public school systems¹ in Maryland, primarily using bus contractors. While transportation costs per rider are highest among its peer group, annual cost per mile is generally consistent with these other systems. ACPS uses a number of best practices, such as staggered school start and stop times so buses can provide multiple trips on the same day, central transfer points to reduce overall mileage, and serving more than one school with a single route. Having noted that, we did identify several issues for additional review by ACPS that could further improve efficiency. ACPS should reevaluate its decision to outsource the majority of its transportation services, since outsourcing may not be the least costly way to provide the needed service. ACPS should also evaluate its relationship with bus contractors to ensure compliance with Internal Revenue Service regulations. Additionally, ACPS needs to reevaluate the formula used to determine payments to bus contractors, which includes a certain rate component intended to provide a return on investment for bus purchases that has remained fixed at 11.67 percent since fiscal year 2003 and 13.17 percent for at least the 8 years prior to that (well above market interest rates). ACPS' rate appears to result in excessive compensation to bus contractors. In this regard, ACPS has paid out \$1.4 million for fiscal years 1996 to 2006 as a result of using higher than market rates, and will pay out an additional \$2 million for fiscal years 2007 to 2017, if they continue to use the same rates. Furthermore, ACPS should formally verify the amount of vendor services received (that is, total time and miles driven on each route) that is used in calculating payments on a timely basis. Finally, since 53 percent of its bus routes are operated below ACPS' desired capacity, and well below the buses' physical capacities, ACPS needs to analyze its bus routes for efficiency on a regular basis and implement its recently purchased computer routing software to assist in designing more efficient routes.

¹ Similarly-sized public school systems are systems with average daily enrollment under 10,000 students.

Food Services Operations (see pages 49 through 54)

ACPS uses several best practices to help reduce the costs of its food supplies and materials, and to maintain a high student participation rate in the National School Meals Program (a federally-funded program for free and reduce priced meals). However, ACPS' statistical analysis of its food service labor costs showed that it was not meeting either industry guidelines or its own established goals for labor costs and has one of the higher labor costs per meal when compared to other Maryland school systems. The high labor costs have contributed to ACPS food service expenditures exceeding revenues, requiring ACPS to subsidize food service operations with general funds.

School Board Operations and Oversight (see pages 55 through 61)

The five-member Board takes an active role in monitoring financial performance. However, we noted several areas where the Board and ACPS could improve operations and oversight. The Board's policies over financial management generally only assigned responsibilities to key management personnel. The policies did not provide direction and guidance for carrying out responsibilities in areas such as procurement, accounting, and internal financial report distribution. The Board should consider establishing an internal audit function to act as an independent reviewer of ACPS operations for the Board, and augmenting the financial office staff to ensure timely financial reporting.

Other Financial Controls (see pages 63 through 65)

ACPS appropriately managed its investments and covered its risks adequately through commercial insurance policies. However, it needs to adopt a policy on debt management for long-term leases and reconcile bank accounts in a timely manner. Additionally, the risk management process over workers compensation could be more effective

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Background Information

Oversight

Allegany County Public Schools (ACPS) is governed by a five-member elected local school board. The vast majority of ACPS funding is provided by the State and the Allegany County governments. In addition, the Maryland State Department of Education (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 the local school systems to comply with the requirements and mandates of the federal No Child Left Behind Act of 2001. Oversight by the Allegany County government is limited, although the ACPS annual operating and capital budgets require County approval.

Statistical Overview

According to MSDE student enrollment records, ACPS ranks 16th in student enrollment among the 24 school systems in Maryland. From 1996 to 2005 the total full-time regular and special education pupil population has decreased 13 percent from 11,190 to 9,715, with more decreases projected in the coming years to approximately 8,800 by 2014. Presently, ACPS has 23 schools, consisting of 13 elementary, 1 elementary/middle, 3 middle, 1 alternate school, 1 technical education school and 4 high schools. A new high school is currently being built that will consolidate two of ACPS' existing high schools.

Despite a decline in enrollment over the past 10 years, ACPS operating expenditures, excluding capital costs and food service operations², increased from \$59 million in fiscal year 1996 to \$87

² Food service expenditures are generally expected to be paid from food service revenues and are excluded from MSDE statistical data. Chapter 9 on page 49 addresses ACPS food service operations.

million in fiscal year 2005.³ Additionally, ACPS fiscal year 2005 operating expenditures for food services totaled \$4.5 million. In this regard, salaries, wages and benefits accounted for 79 percent (\$72.7 million) of the total fiscal year 2005 operating expenditures of \$91.5 million (\$87 million plus \$4.5 million), and supported 1,392 full-time equivalent positions (997 instructional and 395 non-instructional).

Certain statistical information contained in this report was taken from reports distributed by MSDE and represents the most current comparable information available at the time of our audit.

External Audit of Fiscal Year 2005 Activity

Annually, ACPS engages an independent certified public accounting firm to audit its fiscal year-end financial statements. Additionally, the firm conducts what is referred to as a Single Audit of ACPS federal grant programs (as required by federal regulations). The financial statements audit and the Single Audit for fiscal year 2005 were issued on April 28, 2006 and May 23, 2006, respectively. Neither report included any reportable conditions or material findings on ACPS record keeping, processes or controls.

Furthermore, in the related financial statements audit report, the auditor stated that the financial statements presented fairly, in all material respects, the financial position of ACPS, and the respective changes in financial position for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

³ The primary source for this background data is MSDE statistical data, including the annual Fact Book.

Chapter 1

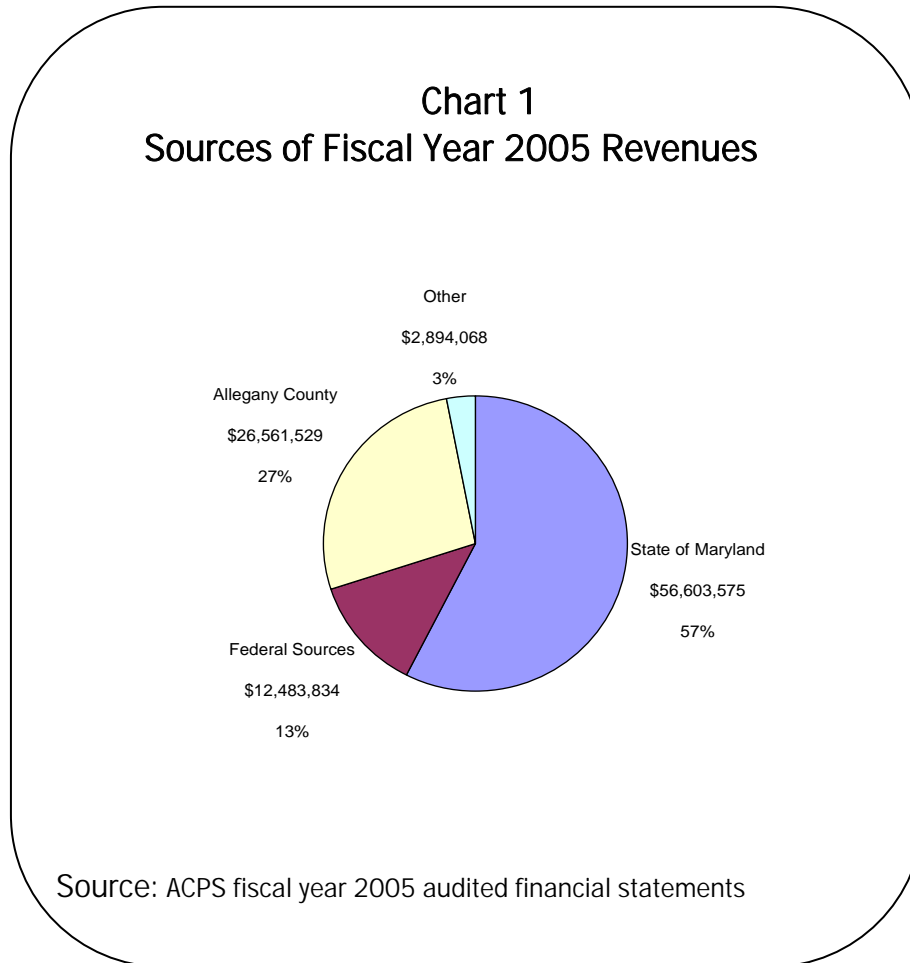
Revenue and Billing Cycle

According to the ACPS audited financial statements for the fiscal year ended June 30, 2005, \$98.5 million of revenue was received by ACPS during that fiscal year. Our review disclosed that the procedures over ACPS' wire transfer transactions, which is the process that ACPS uses to collect the vast majority of its revenues (from the State, Allegany County and federal government), were adequate to safeguard those collections. Due to similarities between the work of the independent certified public accounting firm that audited the ACPS financial statements and the scope of our audit in this area, we placed significant reliance on the results of that audit for certain other sources of revenue (such as student activity fund⁴ cash receipts of \$3 million) and for accounts receivable (for example, amounts due from other governments). The firm's procedural review and testing disclosed that collection activity for these revenue sources and accounts receivable was adequate.

⁴ The Board has a fiduciary responsibility to ensure that the student activity fund is used only for intended purposes by those to whom the assets belong. Receipts for the student activity fund are not included in the \$98.5 million revenue total because the Board cannot use these assets to finance its operations.

Background

ACPS revenues consist primarily of funds received from the State, Allegany County, and the federal government. Other miscellaneous sources include receipts from the sale of food and interest income. Chart 1 (see below) shows the breakdown of the ACPS' fiscal year 2005 revenues of \$98.5 million.



ACPS Revenue and Billing Cycle Activity Was Generally Adequate

Our review disclosed that the procedures over ACPS' electronic fund receipts, which were used for the vast majority of its revenues, were adequate to safeguard those collections. Due to similarities between the work of the accounting firm that audited the ACPS financial statements and the scope of our audit in this area, we

placed significant reliance on the results of the independent audit of the fiscal year 2005 financial statements for certain other sources of revenue and for accounts receivable. That firm's procedural review and testing disclosed that collection activity for these other revenue sources (such as, student activity fund and food service cash receipts) and ACPS' accounts receivable were adequate.

Recommendations

None

Chapter 2

Federal Funds

Annually, ACPS is subject to an audit of its federally-funded grant programs (often referred to as the Single Audit, and required by Circular A-133 issued by the United States Office of Management and Budget). This audit is conducted on a fiscal-year basis. The report on the audit of fiscal year 2005 federal grant activity was issued by a certified public accounting firm on May 23, 2006.

In that report, the firm stated that ACPS complied, in all material respects, with the requirements applicable to its major federal grant programs. In addition, with respect to internal controls over compliance with and the operation of major federal programs, the auditors noted no reportable conditions⁵ and no matters considered to be material weaknesses.⁶

⁵ **Reportable conditions** are issues relating to a significant deficiency in the design or operation of the internal control over compliance that, in the auditor's judgment, could adversely affect the grantee's ability to administer a major federal program.

⁶ **Material weaknesses**, which are more severe problems, are reportable conditions where the existing internal control components might not detect, in a timely manner, a material instance of noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud.

We also noted that ACPS has an adequate process for the identification of children eligible for Medicaid-subsidized⁷ services and recovering the related costs.

Background

ACPS receives funds primarily from the State, Allegany County, and the federal government. Most funds received from the State and Allegany County are unrestricted; however, federal funds are generally restricted for use for a certain specified program (such as School Lunch Program or Special Education). According to the audited Schedule of Federal Awards, fiscal year 2005 expenditures of federal funds totaled \$11.5 million.

ACPS also received an additional \$954,005 of federal fee-for-service payments during fiscal year 2005, of which \$922,438 was reimbursement for Medicaid-subsidized services for qualified students.

ACPS Established Adequate Internal Control over Federal Grants and Complied With Federal Grant Requirements

Because of the accounting firm's work on ACPS federal fund expenditures, we relied on the auditor's results. Besides expressing an opinion on ACPS 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 2005 required Schedule of Federal Awards (which includes claimed and reported grant-related expenditures). In its report, the firm stated that ACPS complied, in all material respects, with the requirements applicable to its major federal grant programs. In addition, with respect to internal controls over compliance with and the operation of major federal programs, the auditors noted no reportable conditions and no matters considered to be material weaknesses.

⁷ The Federal Medical Assistance Program, or Medicaid, is not a grant program under Circular A-133 and is not included in the Single Audit.

Processes Are in Place to Identify Students Eligible for Medicaid-Subsidized Services and to Recover Costs

ACPS determines whether all students participating in Special Education programs within the System are eligible for participation in Medicaid. These determinations are made on an ongoing basis, regardless of the result of the initial assessment. In addition, as permitted by regulation, reimbursement is requested for all assessments performed regardless if the student is eligible to participate in Medicaid.

Processes are in place for timely comparisons of services provided to each Medicaid eligible student (including transportation) to student's individual education plans. Additionally, safeguards are in place to ensure that transportation reimbursements are only requested when the student was actually transported for eligible services.

Recommendations

None

Chapter 3

Procurement and Disbursement Cycle

ACPS did not maintain a comprehensive policies and procedures manual for procurement and contract monitoring. Specifically, ACPS did not have adequate written policies or procedures to govern the procurement of goods, including when and how to use a formal bidding process, when to use cooperative purchasing agreements, or when Board approval was required (see also Chapter 10 – Board Operations). Additionally, ACPS' decentralized procurement practices were not adequate to ensure the use of desirable practices such as bidding, standard contract language, and proper internal controls.

ACPS was not fully using the available functions of its automated procurement and disbursement system to improve the efficiency and control over the purchasing and disbursement process. For the automated processes that were used, certain personnel had excessive capabilities that would allow them to generate disbursements without oversight approval.

ACPS had a travel policy that adequately addressed such areas as advanced approval and documentation requirements, and limited issuance of credit cards to contain costs.

Background

According to ACPS records, non-payroll related disbursements totaled \$25 million during fiscal year 2005. Procurement of goods and services is accomplished using manual processes on a decentralized basis. Purchases anticipated to cost more than \$15,000 generally require bidding, which is handled by the requesting department. Requisitions are not used, and instead purchase orders are manually prepared by the requesting department and generally must be approved by the respective department head. Department heads are also responsible for ensuring purchases do not exceed their Board-approved budgets. Bid results for significant procurements are generally presented to the Board for its approval of the selected vendor. Once approved, the requesting department issues the purchase orders directly to vendors and subsequently receives the goods or services.

Invoices received by the finance office are manually matched to a copy of the original approved purchase order, and a receipt record signed by an employee in the requisitioning/receiving department. The finance office processes related payments through an automated system that prints vendor checks, prepares electronic payment schedules, and records the payments in the financial records.

ACPS Procurement, Disbursement, and Accounting Policies and Procedures Need to be Documented and Could Be Improved

ACPS needs to establish written procurement policies to ensure that goods and services are obtained at the best prices – We were advised that ACPS loosely follows a former State law requirement for obtaining bids for the purchase of goods that cost over \$15,000. Furthermore, ACPS had not established policies delegating responsibility for transactions to certain individuals, describing the Board's involvement in reviewing and approving transactions, and dictating documentation requirements for sole source purchases and provisions to include in contracts (such as expiration dates, retainage requirements, performance bond

requirements, and not-to-exceed limits). Also, there was no policy to encourage best practices, such as participating in cooperative purchasing agreements or piggybacking onto State or other government entity contracts, or requiring evaluation of whether extending contracts with option years would be more beneficial than re-bidding the contracts.

Although there was no specific written policy defining when Board approval for purchases was required, we noted that the Board generally did approve ACPS' largest purchases (for example, 20 laptop computers costing \$28,800). ACPS drafted a procurement policy in April 2005; however, it has not been brought before the Board for review and approval.

ACPS should use more of the automated functions of its procurement and disbursement system to improve the efficiency and enhance control over the purchasing process and budgets – ACPS is not using the available functions of its automated procurement system to help streamline the purchasing process, provide greater control over purchases, and reduce the risk of overspending. Our review disclosed that ACPS' procurement process primarily used manual processes, such as the issuance of paper-based purchase orders and manual signatures for the approval of transactions, instead of generating purchase orders and approvals through the automated system. Increased use of the system capabilities could help standardize and enhance internal control over transactions and help reduce the risk of overspending by encumbering funds immediately upon approval of purchase orders rather than waiting until invoices are processed for payment.

Although ACPS did use some of the automated approval path functions in its finance department for accounts payable processing, the computer controls over disbursements were not adequate. Specifically, three employees had computer capabilities that allowed them to initiate and approve transactions and add vendors to the system, thus allowing them to generate disbursements without oversight approvals. The system does provide for establishment of transaction approval paths to adequately segregate employees' processing capabilities.

ACPS Needs to Improve the Effectiveness of Its Procurement and Contract Monitoring

ACPS should seek competitive bids for needed goods and services – ACPS did not always obtain competitive bids for goods and services. For example, ACPS obtained occupational/physical therapy services and sign language services from two vendors without bidding for these services or justifying them as sole source procurements. Payments to these two vendors for fiscal years 2005 and 2006 (through March 2006) totaled \$1.1 million. Similarly, ACPS purchased diesel fuel for its bus fleet from one vendor without bidding or justifying this sole source procurement. Fiscal year 2005 and 2006 diesel fuel purchases totaled \$76,276 and \$114,154, respectively.

Also, as a general system-wide practice, we noted that contract extensions were exercised without formally determining if re-bidding the service would be more beneficial. This was observed in all procurement areas, such as special education and food services.

Contractual documentation should be improved – ACPS' contracts should clearly express the intentions of ACPS and be retained for reference and enforcement purposes. For example, we noted the following conditions:

- Certain payments to a service contractor (who received \$450,622 in fiscal year 2005) were made at rates that exceeded the rates specified in the executed contract documents (for example \$42.75 per hour paid for occupational therapy versus \$38.50 per hour specified in the contract). In this regard, on 1 of the 10 invoices that we tested, the contractor was paid \$1,770 more than allowed by the contractual rate. We were advised that the contractor was paid at rates reflecting an increase similar to the increases received by teachers even though the contract did not provide for increasing payment rates. Also, this contract did not include important provisions such as a not-to-exceed amount or a contract expiration date.
- Retainage of \$48,000 was released at a contractor's request earlier than specified in the contract, and with ACPS' management's concurrence that the early release was appropriate. However, specific provisions for early release of

retainage were not specified in the contract and the early release was done without Board approval.

- For five food service contracts with related fiscal year 2005 payments totaling \$389,348, ACPS could not provide us with the executed contract documents even though the related requests for bids and vendor bid sheets were on file.

ACPS should compare independent documentation to invoiced charges to ensure that billed special education service expenditures were actually provided – ACPS did not agree invoices from special education service providers (such as physical therapists and occupational therapists) to independent source documents, even on a test basis, to ensure that services being billed by the providers were actually provided. ACPS only compared the providers' invoices to a time record produced by the providers. This provider record was not independently verified to ACPS records, such as ACPS progress notes, time sheets, authorizations for services, or communication logs. Although ACPS informed us that they periodically audited the provider's invoices, ACPS was unable to provide us with documentation of any audit. ACPS' special education contract payments totaled \$850,541 in fiscal year 2005.

ACPS Travel and Credit Card Policies Help to Control Spending

ACPS had established travel policies to control costs – ACPS established a travel policy that was approved by ACPS' Board on October 11, 2005 and became effective on July 1, 2006. The policy adequately addresses such areas as advanced approval and documentation requirements. According to ACPS records, travel expenditures for fiscal year 2005 totaled \$334,414.

ACPS limits the issuance of credit cards – ACPS limits issuance and use of corporate purchasing cards to ACPS Board members and certain top ACPS administrators. The cards are to be used exclusively for travel expenses, including food purchases associated with meetings and conferences attended by the

cardholders. ACPS' total corporate purchasing card expenditures for the period from July 2004 through April 2006 totaled \$10,003.

Recommendation⁸

1. ACPS should establish appropriate procedures and controls to ensure the propriety of procurements and related disbursements, including competitive bidding whenever practical, documenting the required independent review and approval of transactions, and ensuring that adequate support exists for each procurement. ACPS should consider using more fully the features of its automated procurements and disbursements system to enhance controls and improve efficiency.

⁸ Recommendations are numbered consecutively through the entire report.

Chapter 4

Human Resources and Payroll

ACPS exercised position control and filled vacant positions by the use of centralized hiring and approval of all new employees. Furthermore, duties over human resources and payroll processing were appropriately segregated among ACPS staff to establish strong internal control. Although the human resources and payroll processes in use were appropriate, a formal comprehensive procedures manual, including current job descriptions for all positions, did not exist for these areas.

While ACPS has implemented workforce planning⁹ for its academic work force, its planning efforts should be extended to address ACPS' needs and processes for employees other than teachers and related instructional positions. We did note that ACPS has developed a leadership training program to provide teachers interested in a professional administrative position, such as vice principal, with training and mentoring opportunities.

⁹ Workforce planning represents the strategic alignment of an organization's human capital with its business direction. It includes processes such as analyzing the current workforce, determining workforce needs, identifying gaps in the workforce, and implementing necessary solutions.

Background

According to ACPS records, salary, wage and benefit costs for fiscal year 2005 totaled \$72.7 million, and ACPS had approximately 1,400 employees in calendar year 2005, giving it a 7 to 1 student to employee ratio (see Table 1 below). ACPS uses an automated system to maintain human resources information, process payroll and track employee leave balances. Time records are prepared manually by all employees and are approved by the employees' supervisors. Time records are entered onto the automated system every two weeks by one of two payroll clerks. After various system edit checks, the system generates payroll checks (which are mailed to the employees' homes) and direct deposit advices,¹⁰ which are returned to the originating location and distributed to the applicable employees. Leave accumulation is automatically calculated, whereas leave taken is recorded in the system by the payroll clerks.

Table 1
Comparison of Employee to Student Ratios – Fall 2004
(Unaudited)

School System	Number of Students (as of September 30, 2004)	Number of Full-Time Equivalent Employees	Student to Employee Ratio
Allegany Co.	9,840	1,392	7.1 to 1
Queen Anne's Co.	7,713	894	8.6 to 1
Dorchester Co.	4,788	580	8.3 to 1
Caroline Co.	5,412	689	7.9 to 1
Kent Co.	2,514	331	7.6 to 1
Talbot Co.	4,505	601	7.5 to 1
Garrett Co.	4,737	667	7.1 to 1
Somerset Co.	2,952	418	7.1 to 1
Worcester Co.	6,676	1,084	6.2 to 1

Source: MSDE 2004-2005 Factbook

¹⁰ Direct deposit became mandatory in 2003 for all full-time employees.

Appropriate Hiring and Payroll Controls Were Established

ACPS exercises position control and the filling of vacant positions by use of centralized hiring and approval of all new employees. Furthermore, duties over human resources and payroll processing were appropriately segregated among ACPS staff to establish strong internal control. Such processes helped ACPS control payroll costs, which is the largest category of expenditures for the school system.

Also, ACPS has developed a formal leadership training program to assist teachers interested in transitioning into administrative positions, such as vice principal. The program consists of classes to introduce candidates to the administrative aspects of ACPS and a month-long internship at a school (other than the one where they teach) working with that school's principal. After the internship, each candidate's competence and fitness to become an administrator is evaluated by the principal and used to assist in selecting individuals for administrative positions.

Existing Workforce Planning Should Be Expanded to Non-Instructional Areas

ACPS should enhance its existing workforce planning efforts to include positions other than instructional personnel. The ACPS Master Plan sets the strategic direction of the school system and provides coordination and focus for initiatives to address challenges faced by ACPS. The Plan includes a number of objectives and strategies to address human resource needs (which is evidence of workforce planning). However, it addresses only the recruitment and retention of highly qualified instructional staff (that is, teachers and certain other instructional aides). The Plan does not address other personnel employed by ACPS, such as central office and critical support staff. About 28 percent (395, total of 85 and 310 from Table 2 on the following page, divided by 1,392, from Table 1) of ACPS employees fill non-instructional positions. These other support functions also play a key role in the ultimate success of ACPS in providing quality education and, therefore, ACPS' workforce planning should include them.

**Table 2
Comparison of Non-instructional Staff Per 1,000 Pupils for Select Categories
Fiscal Year 2005 (Unaudited)**

School System	Number of Non-instructional Positions ^①		Number of Non-instructional Positions Per 1,000 Pupils ^②		
	Professional ^③	Support Staff ^④	Professional	Support Staff	Combined
Allegany Co.	85	310	8.64	31.50	40.14
Talbot Co.	70	158	15.54	35.07	50.61
Worcester Co.	92	200	13.78	29.96	43.74
Somerset Co.	38	91	12.87	30.83	43.70
Garrett Co.	48	147	10.13	31.03	41.17
Kent Co.	26	75	10.34	29.83	40.18
Caroline Co.	63	151	11.64	27.90	39.54
Dorchester Co.	47	134	9.82	27.99	37.80
Queen Anne's Co.	94	176	12.19	22.82	35.01
Statewide	8,713	26,218	10.07	30.29	40.36

Source: MSDE 2004-2005 Fact Book

- ① - Excludes contractual and consulting positions.
- ② - Based on September 30, 2004 student enrollment.
- ③ - Includes principals, vice principals, social workers, and other administrators.
- ④ - Includes technicians, secretaries, clerks, trades personnel, etc.

Comprehensive Human Resource and Payroll Procedures Should Be Documented

ACPS should develop a formal comprehensive human resources and payroll operations and procedures manual. We noted that ACPS relies on contracts with four unions (which include approximately 1,350 employees) to address many personnel and pay issues for ACPS employees. However, these rules are not sufficiently comprehensive; for example, they do not address the salaries and benefits of 41 non-union employees, with total salaries of approximately \$1 million. A comprehensive procedure manual for its human resources and payroll processes would provide management approved guidance to staff and would be particularly helpful for educating new employees and evaluating compliance with those procedures. Also, although the procedures actually in use appear adequate and duties are currently appropriately segregated among ACPS staff, none of the procedures currently performed have been directly approved by the Board.

ACPS has begun to update its job descriptions for current positions which would also be appropriate to include in the manual; however, this process has not been completed. We were advised that ACPS staff do not have sufficient time available to dedicate to this task and, consequently, many position descriptions are only updated once they become vacant and need to be advertised.

Recommendations

2. ACPS should expand its workforce planning to include all critical operational units and non-instructional positions.
3. ACPS should develop formal written human resource and payroll policies and procedures, including updated job descriptions that address current criteria and job requirements. These policies and procedures should also be presented to the Board for its approval.

Chapter 5

Inventory Control and Accountability

Accountability was lacking over ACPS property, including textbook and equipment inventories. The policies and procedures governing the accounting and safeguarding of these assets were insufficient or non-existent. Furthermore, physical inventories of equipment were not documented to substantiate that they had been performed and appropriate record keeping adjustments made. Also, the textbook inventories were not used for accountability and control purposes nor analyzed to ensure efficient redistribution or purchases of textbooks.

Background

According to ACPS' audited financial statements, as of June 30, 2005, the value of ACPS equipment was \$11.1 million, and its fiscal year 2005 capital equipment expenditures totaled \$816,899. ACPS inventories its textbooks annually and tracks the inventory on a separate database. According to ACPS records, textbook purchases totaled \$990,777 during fiscal year 2005.¹¹

¹¹ Textbook purchases are not capitalized, so no inventory value exists.

Record Keeping and Physical Inventory Processes Need to Be Enhanced to Safeguard Property Items

Policies over equipment need to be established and

controls over equipment need to be enhanced – ACPS did not have written policies or procedures to govern accountability and control for its equipment. As a result, our testing disclosed that certain equipment items purchased and received had not been recorded in the ACPS equipment records, and other equipment was removed from the records without any supporting documentation justifying the need to remove the items. For example, our test of 27 capital equipment items costing \$158,630 that were purchased in fiscal year 2006 disclosed that none of the items (such as snow plows and kitchen and computer equipment) had been recorded in the ACPS equipment records. In addition, we noted that 43 equipment items, with a depreciated cost of \$28,403, were removed from the equipment records without any supporting documentation. Finally, although ACPS personnel informed us that a physical inventory of equipment was performed during fiscal year 2005, no documentation could be provided to support this assertion. Certain similar equipment accountability and control issues were also noted by the ACPS independent certified public accounting firm in its management letter pertaining to the fiscal year 2005 financial statement audit.

Policies over textbooks should be enhanced and physical inventory results should be used more effectively –

Annually, ACPS performed a physical inventory of its textbooks. However, the results of physical inventories were not used to actually provide control. Specifically, none of the adjustments made to the textbook inventory records as a result of the physical inventories were reviewed and approved by supervisory personnel. In addition, there was no investigation of any significant differences between the inventory records and the results of the physical inventories to determine the causes of the differences. Furthermore, ACPS personnel informed us that the inventory records are rarely used when making purchasing decisions (that is, whether used textbooks could reduce new purchases) or to maximize redistribution of excess books to other schools within ACPS. Finally, policies or procedures did not exist to govern other

aspects of textbook management, such as the resale or disposal of textbooks.

Recommendation

4. ACPS should better account for its equipment and textbooks by developing and enforcing written policies and procedures to govern the accounting and safeguarding of these items, recording all acquisitions, transfers and disposals, and documenting all physical inventories and supervisory approval for any subsequent adjustments needed to the records. ACPS also should use the results of its textbook physical inventories to enhance redistribution in lieu of purchasing new textbooks. Finally, ACPS should develop a policy regarding the resale and disposal of textbooks.

Chapter 6

Information Technology

ACPS shares its information system services with the Allegany County Government. In addition, ACPS shared the development and maintenance of a wireless, high-speed, wide-area network (WAN) with the Allegany County Government, City of Cumberland, and Allegany County Public Library. Cooperation and sharing of information resources and services is a best practice that enhances cost effectiveness for ACPS and the other participating agencies of government.

However, we noted that certain aspects of the operation of ACPS' Information Technology Department (ITD) could be improved. Improvements should be made over access controls for the minicomputer, monitoring of security events on the minicomputer, program change procedures on the minicomputer and physical access to ACPS' computer room. In addition, a formal, comprehensive disaster recovery plan should be developed.

Background

ACPS' ITD provides information system services to the Allegany County Commissioners (County Government) and ACPS.

Specifically, ITD maintains and administers the ACPS computer network, computer operations and instructional information systems applications. ACPS operates a WAN, with internet connectivity, which connects the individual schools' local networks to the computer resources located at the ACPS headquarters (Board of Education building). This WAN is also used by the County Government, City of Cumberland, and the Allegany County Public Library.

ITD maintains a computer room at the headquarters location in which assorted computer servers and a minicomputer operate to support ACPS information system needs. Several significant administrative and academic information system applications exist on the minicomputer, such as the budget and accounting applications, payroll and human resource applications, and the grade reporting and the daily student attendance applications.

ITD has 7 employees whose salaries and benefits are funded 50 percent by ACPS and 50 percent by County Government; other information service costs are also shared equally. ACPS maintains proprietary funds for its information technology services due to the support activities provided to entities outside of ACPS. Fiscal year 2005 operating expenditures for the information technology proprietary funds totaled \$1.1 million, including \$364,000 of depreciation expense. As of June 30, 2005, the proprietary funds' net assets totaled \$3.2 million.

Sharing Information Technology Resources with Other Local Government Units Promotes Efficiencies

ACPS shares computing resources with several local governmental units. This includes ACPS sharing a computer data center, which includes a minicomputer and the related information technology personnel, with the Allegany County government. Both entities maintain computer applications such as accounting and budgeting and other operational applications on the minicomputer. The costs of the computer data center (including hardware, maintenance, and personnel) are shared equally between ACPS and the County Government. ACPS also shared in the development and maintenance of a wireless, high-speed, WAN with the County

Government, the City of Cumberland and the Allegany County Public Library.

Steps Should Be Taken to Ensure Access to IT Software Applications is Appropriate and Controlled

Changes should be made to existing procedures to ensure all access is appropriate – User access to computer resources is commonly controlled through the use of individual passwords and user logon ids. ACPS' use of these tools could be more effective for both the financial and student information applications. For example, automatic password expirations (requiring periodic use and password changes) and idle terminal logouts were not enforced. Also, while security events such as violations and changes to security settings were logged by the existing system audit software, we were advised that the recorded events were not regularly reviewed.

Program change procedures need to be improved – ACPS' program change procedures over the minicomputer applications need improvement. Specifically, we noted that:

- technical reviews were not made of the detailed differences to source code between the modified and prior version of programs being changed;
- the programmer who made the program changes was also the person who moved the new program into production; and,
- supporting documentation to establish the propriety of modified programs was unavailable.

As a result, unauthorized changes to production programs could go undetected by management.

Data Processing Functions Should Be Better Safeguarded from Disruption

Physical access to the instructional and financial computer system was not adequately controlled. Specifically, the key lock in use did not provide for accountability of individuals who entered the room

after hours, when the room was unsupervised. Furthermore, the IT Director was unaware of how many keys to the computer room existed and the identity of all individuals who had keys to the room.

Also affecting ACPS operations was the lack of a formal, comprehensive and consolidated disaster recovery plan (DRP). Such a plan should include:

- the identification and prioritization of all mission critical applications, with the related software and hardware required to accomplish recovery;
- the description of network restoration plans if the headquarters building was unavailable;
- a listing of current emergency contact information and responsibilities for staff; and,
- offsite storage of the ACPS DRP.

Without a complete and comprehensive DRP, a disaster could cause significant and unacceptable delays in restoring information systems operations above and beyond the expected delays that would exist in a planned recovery scenario.

Recommendations

5. ACPS should implement appropriate measures, including the use of the system's audit functions and program change controls to ensure that only authorized users have access to applications and data systems and that all changes to production programs are approved.
6. ACPS should establish physical controls and safeguards over its computer rooms and also develop a comprehensive disaster recovery plan.

Chapter 7

Facilities Construction, Renovation, and Maintenance

ACPS maintains 23 schools and 4 other facilities (such as administrative and support offices) with a staff of approximately 130 custodial and maintenance personnel. ACPS uses a comprehensive and public process to plan for construction and renovation of school facilities. Plans are long-term and updated annually and reflect input from the Board. We also noted that ACPS has adopted a number of State required guidelines and practices for the procurement and monitoring of construction and renovation projects.

ACPS has developed an energy conservation program to control energy costs and has instituted certain best practices, such as training its maintenance personnel to reduce the need for work to be performed by outside vendors and the use of a full-time inspector on large construction projects to ensure that the projects are being completed properly and cost effectively.

However, ACPS did not always document the performance of routine preventive maintenance. Also, ACPS had not established formal

performance measures and related benchmarks and goals to assess program efficiency for both operations and maintenance

Background

ACPS uses a six-year Capital Improvement Plan (CIP) to identify ongoing and projected needs for new buildings and major renovations. In the fiscal year 2006 CIP, necessary major renovations, repairs, and systemic improvements to existing schools over the next six years were estimated to cost \$113 million, including \$43.6 million for construction of a new high school.

Table 3 (see below) compares ACPS fiscal year 2005 plant costs (that is, maintenance and operational costs) with other similar-sized systems in Maryland. It also compares two measurement techniques used to assess plant costs: plant costs per student and plant costs per square foot. When these two costs are considered, along with square footage per student, these statistics generally show that ACPS facilities are less fully utilized than most similar systems based on square footage per student, while the plant costs are generally in line with its peer group.

Table 3					
Plant Cost Comparison Per Student and Per Square Foot					
Fiscal Year 2005 (Unaudited)					
School System	Plant Costs			Square Footage Per Student	Total Gross Square Footage
	Total	Per Student ●	Per Square Foot		
Allegany Co.	\$7,912,555	\$808.06	\$4.23	191.10	1,871,207
Caroline Co.	3,366,021	622.19	3.82	162.87	881,103
Dorchester Co.	3,924,398	831.44	4.49	185.36	874,885
Garrett Co.	3,906,885	826.50	4.90	168.84	798,123
Kent Co.	2,514,655	1,009.09	4.43	228.00	568,172
Queen Anne's Co.	5,943,085	722.03	4.98	155.00	1,193,161
Somerset Co.	2,996,528	1,030.80	4.98	207.03	601,848
Talbot Co.	3,684,746	820.66	5.25	156.28	701,684
Worcester Co.	6,391,834	947.92	5.59	169.49	1,142,847
Average of Comparable Schools	\$4,091,019	\$851.27	\$4.81	179.11	845,228

Sources: MSDE Selected Financial Data, LEA Capital Improvement and Maintenance Plans, LEA Staff

● - Based on average daily enrollment 2004-2005 (most recent data available)

A Number of Best Practices Were in Place Regarding Project Inspections, Maintenance Staff Training and Energy Cost Control

Project inspections and maintenance staff training were being conducted – ACPS had instituted certain best practices that should enhance project results and cost effectiveness in its facilities and maintenance department. These best practices include the following:

- ACPS used a full-time inspector for large construction projects to ensure that projects were being constructed to specifications and being performed within budget and on-time.
- Training of ACPS maintenance staff had resulted in virtually all maintenance work being performed in-house.

A comprehensive energy management program is in place to control energy costs - ACPS has contracted for energy management consulting services, including computer software that monitors and accounts for energy usage at all facilities. ACPS has also hired an energy management program coordinator who is trained in conservation techniques and monitors energy practices at all facilities, including making unannounced visits. Based on reports from ACPS energy management software, which we did not verify, the school system has saved approximately \$1.4 million in energy costs from 2003 through 2005.

Certain Processes Should Be Implemented to Increase the Effectiveness of Maintenance and Custodial Operations

ACPS should develop performance standards and measures for operational efficiency – ACPS had not implemented a performance measurement system to measure and assess the efficiency of its maintenance and custodial operations, both for internal self-evaluation purposes and for comparisons with

other systems (which could identify other best practices). Comparability with other systems in Maryland could not necessarily be done unilaterally since there would need to be a consensus on the measures and methodology; however, other states (for example, Michigan and Florida) have mandated the establishment and use of measures and benchmarks (such as maintenance expenditures per square foot) to assist schools in the evaluation of costs and practices.

Furthermore, ACPS should fully use its automated work order system when assigning maintenance work and tracking the completion of assigned tasks to help it control costs and assess performance. We noted that although all work orders are logged, along with information related to the actual resources used to perform the task (including labor hours and equipment expenditures), no information is entered indicating the resources expected to be used to perform the task, based on either past history or industry guidebooks. As a result, completed work orders are not evaluated for efficiency and are not used to assess the performance of both individual employees and the entire department. An effective work order system can be used to generate a variety of statistical data including employee productivity, cost reports and facility assessments, all of which are key pieces of a performance measurement system.

ACPS should maintain documentation that all required preventive maintenance work was performed – ACPS could not provide us with documentation that all required preventive maintenance to be performed by custodial and maintenance staff had been completed. ACPS had developed a comprehensive maintenance plan with schedules and details for preventive maintenance tasks, such as checking the operation of air conditioning units and lubricating motors and pumps on other mechanical equipment. Although periodic inspections and evaluations of the work are conducted by supervisors, neither the staff's nor the supervisors' documentation provided a record that all preventive maintenance required by the comprehensive maintenance plan had been performed.

Recommendation

7. ACPS should develop a performance system with standards and measures, coupled with a detailed work order system and documentation that all preventive maintenance was performed, to ensure appropriate and timely maintenance is provided to all facilities.

Chapter 8

Transportation Services

ACPS transports its students more miles than most of the other similarly-sized public school systems in Maryland. Transportation costs per rider are highest among its peer group but annual cost per mile is generally consistent with others (see Table 4 on the following page). Transportation is primarily provided by vendors under contract with ACPS, while ACPS operates a small fleet of its own buses to transport disabled students. ACPS faces several obstacles in providing efficient transportation services to its students, such as declining student enrollment with associated school consolidations, traveling in mountainous terrain, and serving sparsely populated areas.

ACPS uses several practices that increased the efficiency of transporting students, such as staggering school start and stop times so buses can provide multiple trips on the same day, using central transfer points to reduce overall mileage, and serving more than one school with a single route.

**Table 4
Comparison of Transportation Costs per Rider and per Mile
Fiscal Year 2005 (Unaudited)**

School System	Number of Eligible Riders		Miles (in thousands)		Expenditures (in thousands)	Annual Cost per	
	Non-Disabled	Disabled	Non-Disabled	Disabled		Rider	Mile
Allegany Co.	6,124	228	1,365	364	\$4,753	\$748	\$2.75
Queen Anne's Co.	7,597	67	1,686	433	4,424	577	2.09
Somerset Co.	2,774	58	645	100	1,955	690	2.63
Garrett Co.	4,580	39	1,050	71	3,184	689	2.84
Kent Co.	2,178	55	518	92	1,487	666	2.43
Talbot Co. ✓	3,032	14	486	31	1,877	616	3.63
Worcester Co.	6,363	58	1,266	121	3,793	588	2.73
Caroline Co.	4,722	110	897	168	2,788	577	2.62
Dorchester Co.	4,463	86	853	153	2,345	516	2.33
Statewide	589,231	26,608	90,324	40,996	\$427,759	\$695	\$3.26

Source: MSDE 2004-2005 Fact Book

✓ - System owns and operates its own fleet of buses for transportation services.

Nevertheless, we did note that ACPS had not performed any cost benefit analysis of continuing to outsource the majority of its transportations services. Furthermore, ACPS had not analyzed its relationship with bus contractors to ensure compliance with Internal Revenue Service regulations. Also, ACPS had not adequately adjusted certain rates used to reimburse the bus contractors, did not analyze all bus routes for efficiency on a regular basis, had not begun using its computer routing software to design efficient routes, and did not independently verify the receipt of vendor services in a timely manner when calculating related payments.

Background

Over 6,300 students are eligible to ride the bus each day to ACPS' 23 schools. The majority of ACPS students are transported on one of the 100 buses owned by 38 bus contractors. Disabled students are transported by ACPS using its own fleet of 21 buses. Fiscal year 2005 transportation costs totaled \$4.8 million, with 75 percent representing payments to bus contractors. Of the 1.7 million reported route miles for the 2004-2005 school year, 21 percent were for transporting disabled students.

Several Best Practices Were in Place To Enhance Bus Route Efficiency

The ACPS Transportation Department has several practices in place to help control student transportation costs, including the use of

- staggered school arrival and dismissal times;
- central transfer points to enable consolidation of students into fewer buses for portions of their ride;
- a single route for several schools due to their relative proximity; and
- four-wheel drive vehicles to transport students located in remote areas not easily accessible by a conventional school bus.

Outsourcing of Transportation Services Has Not Been Established As Cost Beneficial

The cost benefits of outsourcing transportation services

have not been determined - ACPS personnel advised us that a cost benefit study has never been conducted to determine the cost efficiency of contracting out these transportation services versus ACPS directly owning and operating the buses. Furthermore, no recent analysis has been performed to determine the amount of the bus contractors' profits and what rates are most appropriate for each of the bus contractor pay elements.

ACPS should undertake a study to determine whether its current method of transporting students via private contractors is the most cost beneficial alternative. Under current arrangements with bus contractors, ACPS assumes nearly all of the risks for bus operations while essentially guaranteeing a profit to the contractors for the expected 12-year¹² life of a bus. Specifically, contractors are paid a "per vehicle allowance" (PVA) that covers full depreciation of the bus over 12 years with the assumption that there is no residual value. The PVA also provided an additional annual payment to the

¹² Conventional school buses in Maryland have a useful life of 12 years as established by Maryland law. Under prescribed maintenance and inspection conditions, the State Superintendent of Schools can grant approval to operate a conventional school bus beyond 12 years.

contractors, which is established when a bus is purchased and remains fixed over the expected life, as a return on investment. The return on investment component of these annual payments was 11.67 percent or 13.17 percent of the bus' cost.¹³ Furthermore, the bus contractors are paid a per mile rate for operating and maintenance costs, a driver per hour allotment to cover the contractor's labor costs¹⁴, an annual administrative cost allotment, and reimbursement for fuel at market rates. Additionally, ACPS pays for the liability insurance, including personal injury, property damage, and medical coverage for all buses operated for ACPS, including contractor buses. ACPS also purchases and maintains most of the "loaner buses" used by contractors when the contractors' buses are out-of-service due to mechanical breakdown, maintenance or any other reason. When the contractors use a loaner bus, ACPS charges them only for the same per mile operating and maintenance rate normally paid to the contractors, but nothing toward the depreciable cost of the loaner bus.

ACPS has contracts with 38 bus operators who provide service using 100 buses. Individual contractors own between 1 and 13 buses. Available routes are advertised and awarded to interested operators based principally on past performance. Bidding per se is not used since the ACPS Transportation Department annually prepares a Table of Rates to be paid to bus operators for each of the pay elements described in the preceding paragraph. The Table of Rates is approved annually by the ACPS Board. Once a route is awarded, the contract renews automatically and typically lasts for the 12-year life of the bus.¹⁵ Routes are adjusted to meet ACPS' needs but are not eliminated until the end of a bus' life, essentially as a concession to the contractor for investing in the bus. Such an arrangement reduces ACPS' flexibility to adjust rapidly to a declining student population and school consolidations.¹⁶

ACPS continues to believe that contracting out for these services benefits the school system since it does not require an up-front

¹³ We analyze and explain the PVA payment more fully in the next comment.

¹⁴ Contractors are also paid \$10 per hour for bus drivers' in-service training.

¹⁵ ACPS monitors the contractors' performance and can terminate a contract if necessary, but has not needed to do so in at least the last 11 years.

¹⁶ ACPS has eliminated 3 contract routes in recent years due to these factors, but only after expiration of the buses' useful life.

capital outlay for buses or certain ongoing costs for health care, taxes and other personnel related costs for drivers and additional maintenance and administrative personnel that may be required. However, without proper study and analysis, this conclusion is not necessarily justified. Actual experiences in other states and at least one other Maryland LEA (Frederick County) have indicated that outsourcing of bus services can be more expensive than providing student bus services in-house.

Also, two Maryland LEAs which brought their bus services in-house did so primarily as a result of Internal Revenue Service (IRS) determinations and penalty proposals.¹⁷ IRS concluded that the hourly rates paid to bus contractors were wages from the LEA that were subject to employer's social security and Medicare taxes, and that the LEA was responsible for paying the employer taxes and employee withholding taxes to the U.S. Treasury. ACPS could be subject to a similar IRS determination since, like other LEAs where this issue has arisen, ACPS' provides extensive control, detailed direction, and close oversight of its bus contractors' operations.

Certain payments to bus contractors did not reflect market conditions – ACPS did not adjust a component of the “per vehicle allowance” (PVA) that provides a return on investment to bus contractors. Specifically, payments applicable to that component were not adjusted to reflect prevailing market interest rates at the time new buses were purchased; therefore, ACPS has been paying more than appears necessary for bus services.

As mentioned earlier, the PVA is one of several elements used to determine payment amounts to bus contractors. Bus contracts have one-year terms but are renewable from term to term without either party being required to give notice of renewal and generally are renewed for the same length of time as the approved useful life of the bus (12 years). Also, ACPS' bus contracts have generally been renewed from year to year without changes in contract

¹⁷ These are not the only two Maryland LEAs about which the IRS has made such determination. At least one other LEA has executed a settlement agreement with the IRS and paid a negotiated sum for the years questioned and agreed going forward to treat all hourly rates paid to school bus contractors as wages subject to employment taxes.

provisions, such as the PVA, although such changes are not precluded by the contract provisions.

ACPS had not changed the return on investment rate used in its annual PVA calculations to reflect changes in interest rate conditions. Instead, ACPS has consistently used an 11.67 percent rate since fiscal year 2003 and a 13.17 percent rate for at least the 8 years prior to 2003. When questioned about the rates, ACPS personnel did not attempt to justify the rate but merely indicated that they represented "current loan rates."

We calculated the PVA for each of the past 11 years (1996 to 2006) using the prime interest rate¹⁸ in ACPS' PVA formula and compared our PVA results to ACPS' PVAs that were calculated using the 11.67 percent and 13.17 percent rates. This comparison showed that ACPS' annual PVA payments per bus were from \$1,877 to \$4,291 higher than the payments would have been had the prime rate that existed at the time of purchase been used in the calculation.¹⁹ The effect is that over the 12-year life of the 95 new buses put into service by contractors during the last 11 years, ACPS will pay out approximately \$3.4 million more than appears justified. Of the \$3.4 million, \$1.4 million has already been paid out through fiscal year 2006 and, unless changes are implemented, the remaining \$2 million will be paid out during fiscal years 2007 to 2017. This analysis does not include the effect for any new bus purchases that may be made after fiscal year 2006 or the lost interest income that could be earned by ACPS on the excess funds paid.

Timely Independent Verification of Bus Services Received Is Needed to Ensure Proper Payments

ACPS did not ensure that the services paid for were actually provided by the bus contractors. During the first two weeks of school, the contractors' drivers complete a manifest, which includes

¹⁸ We used prime rate since this rate was recommended in a November 1999 study commissioned by another Maryland LEA that used the same PVA formula, and it was suggested as a reasonable prevailing interest rate in a 1978 Maryland State Department of Education study on the PVA. The prime rates during 1996 to 2006 ranged from 4.00% to 9.50%.

¹⁹ For example, the PVA for a bus purchased in 2005 was calculated by ACPS as follows: \$55,940 bus purchase price X (8.33% depreciation + 11.67% return on investment) = \$11,188. Using the prime rate of 4.0% for the return on investment, the calculation would be: \$55,940 X (8.33% + 4.0%) = \$6,897. \$11,188 - \$6,897 = \$4,291.

the total time and miles driven on each route. The data recorded on these manifests are used by ACPS to calculate the payments to the contractors, but without timely independent verification. School officials advised us that the time and mileage reported on the manifests are verified approximately every two years, at the same time that ACPS' evaluates each bus driver. However, there was no documentation available to show that the manifest verifications were performed timely and no documented adjustments could be provided for any discrepancies found.

The Efficiency of Bus Routes Needs to Be Evaluated Regularly

Our review of the student ridership count sheets prepared in the Fall of 2005 for the 2005-2006 school year disclosed that 53 (28 percent) of ACPS' 186 bus routes²⁰ operated at less than 65 percent of bus capacity and that another 47 (25 percent) operated at less than 40 percent of capacity (most runs were on 66-passenger conventional school buses). LEAs do not always intend to run buses at manufacturers' stated capacity since fewer older students can be comfortably seated. For example, ACPS deems bus capacity for middle school and high school students to be 44 (67 percent of the 66 rated capacity) on a conventional school bus. Many school systems take a similar position on bus capacity. We noted that ACPS did not regularly evaluate whether each bus route could be handled more efficiently (for example, by rerouting or using smaller buses) and did not revise bus routes unless there was an overcrowding problem. Also, ACPS had not established any performance measurements or goals to assess the efficiency of its bus routes.

The current planning for bus routes is a year-round process that is very time-consuming and relies heavily on the experience and knowledge of the ACPS transportation department staff using input from the ACPS' Student Information System, bus contractors, school officials and the community. ACPS has recently purchased automated bus routing software that can assist in designing efficient routes, but it is still in the process of being implemented.

²⁰ Contractor routes plus routes run by ACPS directly.

We were informed that, due to conditions in Allegany County (such as the size of school zones and the distances between stops), it may not be possible for some buses to run at desired capacities without increasing the length of time certain students would be on the bus. ACPS attempts to keep one-way student ride times to 1 hour or less.

Recommendations

8. ACPS should prepare a documented cost benefit analysis to determine whether continued use of outside vendors to provide student bus services is cost beneficial for the school system. This analysis should also evaluate each pay element (including the PVA interest factors) of the current bus contracts to determine if the rates paid by ACPS are reasonable and necessary and future payments should be adjusted as appropriate. ACPS should also evaluate its current relationship with its bus contractors with respect to IRS regulations.
9. ACPS should independently verify bus contractors' manifests on a timelier basis to ensure that the payments to the contractors accurately reflect the actual bus services provided and document any adjustments required.
10. ACPS should implement its automated bus routing software as soon as possible to assist in developing more efficient bus routes, and develop performance goals for bus operations. In addition, because of low ridership on many runs, ACPS should consider mandating the use of smaller capacity buses by contractors, when practical and allowable, to reduce operating costs (that is, lower purchase prices and lower operational costs will result in lower payments to bus contractors).

Chapter 9

Food Services Operations

ACPS uses several best practices to help reduce the costs of its food supplies and materials. However, ACPS' statistical analysis of its food service labor costs, which totaled approximately \$2.8 million during fiscal year 2005, showed that it was not meeting either industry standards or its own established goals for labor costs. ACPS also has one of the higher labor costs per meal when compared to similarly-sized Maryland school systems, although ACPS' average cost per meal is comparable to these systems. The high labor costs have contributed to ACPS' food service expenditures exceeding revenues, resulting in ACPS subsidizing food service operations with general funds.

ACPS also uses several best practices to maintain a high participation rate in its free and reduce priced meals program. See Table 5 on the following page for cost per meal data.

Table 5
Comparison of Cost per Meal
Fiscal Year 2005 (Unaudited)

School System	Total Expenditures	Meals Served ^①			Average Cost Per Meal
		Breakfast (paid, free, and reduced)	Lunch, Snacks and Summer Food (paid, free, and reduced)	Total	
Allegany Co.	\$4,651,819	406,001	1,199,387	1,605,388	② \$2.90
Queen Anne's Co.	1,901,907	66,334	520,824	587,158	3.24
Garrett Co.	2,319,081	251,762	487,273	739,035	3.14
Caroline Co.	2,162,182	159,667	602,887	762,554	2.84
Talbot Co.	1,619,726	162,369	400,712	563,081	2.88
Worcester Co.	2,387,197	199,335	642,867	842,202	2.83
Kent Co.	1,111,775	125,918	307,252	433,170	2.57
Dorchester Co.	1,918,269	226,675	535,165	761,840	2.52
Somerset Co.	1,324,106	210,411	349,865	560,276	2.36
Peer Group Total	\$14,744,243	1,402,471	3,846,845	5,249,316	\$2.81

Sources: MSDE 2004-2005 Selected Financial Data and MSDE 2004-2005 factbook.

① - The number of meals served does not include meals served to non-school entities.

② - ACPS cost per meal is \$2.69 when non-school entity meals are factored in.

Background

Twenty-two of the 23 ACPS schools have cooking cafeterias. The remaining school receives prepared food from another school. ACPS also prepares similar meals for non-school entities, such as the Allegany Senior Center, the Head Start Program, and the City of Cumberland Summer Camp. During fiscal year 2005, billings for the meals prepared for non-school entities totaled approximately \$414,000. See Table 6 on the following page for information regarding fiscal year 2005 food services.

Table 6
Food Service Facts for Fiscal Year 2005

Average Cost per Meal (including non-school entity meals) **\$ 2.69**

Number of Meals Served:

Breakfast	Paid	102,797		
	Free	250,108		
	Reduced Price	53,096		
			406,001	
Lunch	Paid	488,190		
	Free	512,238		
	Reduced Price	163,864		
			1,164,292	
Snacks			26,851	
Summer Meals			8,244	
Non-School Meals			120,870	

Total Meals Served **1,726,258**

School locations served	23
Full-time employees	82
Part-time employees	100

Revenues:

Federal	Cash payments	\$2,059,204		
	USDA Commodities	268,883		
			\$2,328,087	
Sales and other sources			1,895,288	
State aid			134,391	

Total Revenue (all sources) **4,357,766**

Total Expenditures **4,651,819**

Excess of Expenditures over Revenues **\$(294,053)**

Sources: MSDE 2004-2005 Factbook, ACPS FY 2005 Audited Financial Statements, ACPS Payroll/Personnel Records.

Best Practices Were in Place to Reduce Certain Costs and Maintain High Participation in Meal Programs

ACPS uses several best practices to help reduce food

supply and materials costs—ACPS uses several best practices to lower its food supply and material costs. The best practices include:

- using USDA commodities;
- standardizing its serving sizes;
- participating in a food cooperative, which includes 12 other Maryland school systems; and,
- monitoring menus, adjusting food production, and reheating certain leftover items to reduce waste.

When compared to other Maryland school systems, ACPS food supplies and materials costs per meal are one of the lowest. For example, ACPS' fiscal year 2004 food supplies and materials costs per meal were second to lowest among the comparable, similarly-sized systems.

ACPS uses several best practices to maintain high

participation in its free and reduced meal programs—ACPS uses several best practices to maintain high participation in its free and reduced priced meal programs. These include using a family application instead of individual student applications to simultaneously qualify more students for the free or reduced priced meal programs, and using a keypad system in cafeterias to eliminate the easy identification of students in the free and reduced meal programs, which in turn helps reduce any stigma of participating in the programs. These practices have resulted in ACPS having relatively high participation rates for the free and reduced price meal programs shown in Table 7 on the following page.

Table 7
Percentages of Paid, Free and Reduced Price Meals Served
Fiscal Year 2005 (Unaudited)

School System	% Paid Lunches and Breakfasts Served	% Free Lunches and Breakfasts Served	% Reduced Price Lunches and Breakfasts Served	% Free and Reduced Price Lunches and Breakfasts Served
Allegany Co.	37.64%	48.55%	13.82%	62.36%
Somerset Co.	25.26%	63.81%	10.94%	74.74%
Dorchester Co.	33.13%	56.91%	9.95%	66.87%
Caroline Co.	37.72%	48.79%	13.50%	62.28%
Garrett Co.	40.79%	42.60%	16.61%	59.21%
Kent Co.	45.16%	43.97%	10.87%	54.84%
Worcester Co.	45.23%	45.46%	9.31%	54.77%
Talbot Co.	56.16%	35.20%	8.64%	43.84%
Queen Anne's Co.	65.74%	26.53%	7.73%	34.26%

Source: MSDE 2004-2005 Factbook

Labor Cost Per Meal Was High Which Necessitated Subsidizing the Food Service Program With General Funds

ACPS regularly calculates the meals per labor hour (MPLH) for the food service operations in each of its cafeterias. However, it has not used this information to make adjustments that will reduce the per meal labor costs, and continues to experience high labor costs in the food service program. These high labor costs have contributed to ACPS having to subsidize food service program operating deficits with general funds. In fiscal years 2003, 2004 and 2005, ACPS transferred \$497,100, \$487,100, and \$497,100 of general funds, respectively, to the food service program.

None of ACPS' 22 cafeterias met ACPS' established goal of 18 MPLH, and only 8 cafeterias met the industry guidelines²¹. ACPS'

²¹ Industry guidelines for ACPS-sized cafeterias ranged from 11 to 19 MPLH per *Cost Control for School Foodservices*, Third Edition, by Dorothy Pannell-Martin, revised July 2000. The guidelines relate to on-site production using average automated equipment that was common in the late 1980s, 1990s, and 2000s.

cafeterias averaged 12.3 MPLH, with a range from 10.3 to 16.3 MPLH. This condition adversely impacts the labor cost per meal. ACPS per meal labor costs are higher than many other school systems in Maryland, as seen in Table 8 below.

Table 8				
Food Service Labor Cost Per Meal (Unaudited)				
School System	FY 2003 ❶	Rank	FY 2004 ❶	Rank
Allegany Co.	1.17	2	1.18	1
Caroline Co.	1.14	3	1.18	1
Garrett Co.	1.20	1	1.16	3
Kent Co.	1.02	5	1.10	4
Worcester Co.	1.08	4	1.03	5
Talbot Co.	0.96	6	1.01	6
Dorchester Co.	0.96	7	0.99	7
Somerset Co.	0.95	8	0.89	8
Queen Anne's Co. ❷	0.00	9	0.00	9

Source: MSDE Selected Financial Data Report for FY 2003 and FY 2004.

❶ - Food costs per meal for other LEAs for FY 2005 was not available for comparison purposes.

❷ - Queen Anne's County's food services are totally contracted out to an outside vendor.

Recommendation

- ACPS should analyze its food service operations data to identify inefficiencies in its food service operations, including its labor costs, and make adjustments to help decrease the need for food service operations to be subsidized with general funds.

Chapter 10

School Board Operations and Oversight

Detailed policies have been adopted to govern actual Board operations, and the Board each year meets with ACPS' certified public accounting firm to review the results of the annual financial statement and federal Single Audits. Also, the Board is actively involved in the development of ACPS' budget.

Several opportunities exist for the Board to improve operations and oversight. Although policies to govern actual Board operations were extensive, the Board's policies over financial management generally only assigned responsibilities to key management personnel. The policies did not provide direction and guidance for carrying out responsibilities in areas such as cash receipts, deposits, procurement and accounts payable. In addition to developing better policy and procedural guidance to ACPS' departments, the Board should work toward establishing an internal audit function to act as an independent reviewer of ACPS operations for the Board, and creating performance measures to help monitor ACPS implementation of its budget and Master Plan.

Furthermore, ACPS' finance unit was late in preparing financial statements and other required reports. Staffing shortages in the finance unit appeared to have been the primary cause of the delays.

Also, ACPS did not actively enforce its Code of Ethics requirement for filing financial disclosure statements.

Background

ACPS is governed by a 5-member board elected by the voters of Allegany County. The Board does not have an established committee structure due to its size and generally acts in whole to carry out its oversight duties. The Board, however, may form standing or special committees at its discretion. To assist in oversight, the Board contracts for independent audits of ACPS' financial statements and federal programs, and receives monthly updates from ACPS management personnel on a broad range of financial and academic topics.

The Board is ultimately accountable for the success of ACPS in providing the children of Allegany County with a quality education, while wisely spending local, State, and federal funds. Following is the ACPS stated policy on educational philosophy:

The philosophy upon which the Allegany County Public School system is established recognizes the true worth and dignity of each pupil as an individual, including his/her right to a variety of learning experiences which will permit the fullest development possible within the limits of his/her capacity. The Board of Education of Allegany County accepts the responsibilities incumbent upon all modern public schools to provide thorough academic preparation, adequate and appropriate job training, cultural enrichment activities, exposure to the fine arts, and a well-rounded program of non-academic activities.

Education of the child is a cooperative effort involving the student, the teacher, the home, the school, and the community. In a dynamic evolving relationship, the person is the product and society is the result.

Source: <http://boe.allconet.org>

Certain Oversight Has Been Put in Place Regarding ACPS' Operations

The Board uses a number of methods to oversee the operations of ACPS. For example, the Board contracts with an independent certified public accounting firm to perform audits of its financial statements and federally funded grant programs and annually meets with that firm to review the results. The Board is also actively involved in the development of the ACPS' annual budgets.

Additional Actions Should Be Taken to Provide Guidance to Management

Formal guidance needs to be provided in various financial

areas – The Board needs to develop and adopt policies and procedures to guide staff in routine operations in areas such as cash receipts, deposits, accounts payable, procurement, and other daily financial operations. For example, while ACPS had documented certain Board accounting policies, these policies were not comprehensive and did not detail the procedures necessary to accomplish specific tasks. In this regard, we noted one Board policy stated that annual financial reports should be prepared and submitted to MSDE. However, there were no documented procedures for identifying and processing all year-end transactions to ensure that proper closing of the books and timely reporting is achieved. A comprehensive manual would provide a standard reference to help ensure that transactions were processed correctly and consistently in accordance with established accounting practices. Such a manual would also provide a historical reference guide for ACPS accounting employees in the event of personnel turnover.

The Government Finance Officers Association (GFOA) recommends that an entity document its accounting policies and procedures and that these documents be reviewed and updated on a periodic basis. The GFOA also has identified financial and operational best practices that should be considered when developing such policies and procedures.

ACPS needs to establish performance measures to assist with evaluating the progress of its budget and Master Plan

ACPS did not establish performance measures to evaluate the progress of its budget and Master Plan. The GFOA recommends the use of performance measures linked to an entities budget and strategic planning process to assist with assessing the accomplishments of an organization and aid with the decision making process.

Additional Positions Should Be Considered to Improve Board Oversight and Financial Reporting

The Board should consider establishing an internal auditor position

ACPS does not have an internal auditor. The use of an internal auditor who would report directly to the Board is a recommended best practice of the GFOA. The GFOA notes that internal auditors commonly assist management in monitoring the design and proper functioning of internal controls and procedures and can play a valuable role in conducting performance audits, special investigations, and studies.

While ACPS may not be able to justify an internal audit position based on its size, it could determine if such a position could be shared with other local Boards (such as Garrett and Washington County Boards of Education). The sharing of an internal audit position was also recommended by MGT of America, Inc. in its November 8, 2000 performance audit report on ACPS.

Adequate staffing levels should be maintained in the finance office

Understaffing of ACPS' finance office has contributed to the following problems:

- The issuance of financial statements for fiscal years 2004 and 2005 was delayed.

- Financial reports required by the Maryland State Department of Education were not submitted until 10 months after the due date. As a result, the State Board of Education voted in October 2005 to withhold 10 percent of monthly State aid payments to ACPS until reporting requirements were met. Withheld payments totaled as high as \$5.1 million, all of which was received by ACPS in August 2006.
- Development of the fiscal year 2007 budget was rushed, without all Board-desired information being provided, because the finance office had to manage the budget development tasks and the task of completing the delayed fiscal year 2005 financial statements.
- Monthly financial reports prepared by the finance office for ACPS departments and administrators were not consistently distributed.

We were informed by ACPS management personnel that the ACPS finance office was purposely understaffed to reallocate resources to the classrooms. In testimony to the ACPS' Board regarding the lateness of the fiscal year 2005 financial statements, management admitted that the Board's suggestion to add personnel to the finance office after the fiscal year 2004 financial statements were late would have helped expedite the fiscal year 2005 financial statements if the suggestion had been followed. We were also informed that two employees have been recently hired to perform finance office duties. Our review also noted that the finance office used numerous manual processes instead of utilizing the respective automated functions of its computerized accounting and procurement system, thereby reducing the efficiency of the office such as prolonging the recording of year-end closing transactions in preparation for the ACPS annual financial statements.

We also noted that, during fiscal years 2003 and 2004, ACPS ranked 8th and 9th in administrative cost per pupil and mid-level administrative cost per pupil, respectively, among its nine peer school systems, as shown in Table 9 on the following page. Although it is desirable to maintain low administrative costs, such measures should not result in negative performance in critical areas, such as the finance office.

Table 9

Administrative Cost Per Student (Unaudited)

School System	FY 2003				FY 2004			
	Administration		Mid-level Administration		Administration		Mid-level Administration	
	Cost	Rank	Cost	Rank	Cost	Rank	Cost	Rank
Allegany Co.	\$166.14	8	\$419.27	9	\$179.68	8	\$445.23	9
Kent Co.	399.08	1	770.70	2	391.81	1	745.47	2
Dorchester Co.	276.07	2	618.11	6	216.25	3	712.28	3
Somerset Co.	254.73	3	680.14	4	229.53	2	678.23	5
Worcester Co.	197.60	5	799.77	1	179.16	9	771.08	1
Talbot Co.	207.13	4	683.33	3	201.78	5	707.45	4
Queen Anne's Co.	168.15	7	509.98	7	181.85	7	523.84	7
Garrett Co.	176.46	6	460.95	8	192.84	6	484.69	8
Caroline Co.	159.65	9	620.41	5	206.88	4	653.04	6
Statewide	\$236.97		\$588.51		\$239.95		\$614.78	

Source: MSDE Selected Financial Data Report for fiscal years 2003 and 2004.
 (Administrative cost per pupil data for other LEAs for fiscal year 2005 was not available for comparison purposes.)

ACPS Should Actively Enforce Its Code of Ethics Requirement for Filing Financial Disclosure Statements

ACPS employees had not submitted the financial disclosure statements for calendar year 2005 as required by ACPS' Code of Ethics. Specifically, none of the 58 ACPS personnel who were required to submit a disclosure statement had done so by the January 31, 2006 deadline. ACPS was not aware that the financial disclosure statements had not been filed until we brought it to their attention. On July 5, 2006, ACPS sent out a memo requesting applicable ACPS personnel to submit their disclosures by July 17, 2006. As of October 5, 2006, 56 of the 58 required disclosure statements had been filed.

The Annotated Code of Maryland requires a local school system to be subject to its local government's ethics laws unless the local school board adopts its own ethics regulations. In 1985, ACPS'

Board adopted its own ethics policy. The policy had been subsequently revised in April 2001 and June 2004.

Recommendations

12. ACPS management should develop and adopt policies to guide ACPS' various financial areas. Additionally, ACPS should develop and use performance measures to assist in assessing its budget and Master Plan.
13. The Board should explore the feasibility of establishing an internal audit function, either on its own or in a shared arrangement with other nearby school systems or local governments. The Board should also ensure the ACPS finance office is adequately staffed, and the finance office should use more of the automated capabilities of ACPS' computerized accounting system to increase its efficiency and effectiveness.
14. ACPS should actively enforce its Code of Ethics, including all required financial disclosure requirements.

Chapter 11

Other Financial Controls

This chapter addresses the management of cash, investments, risk, and debt by ACPS. ACPS has appropriate procedures in place to govern its cash and investments. However, ACPS does not have written policies governing its use of long-term lease/purchase agreements. We also noted that ACPS appeared to cover risks adequately through insurance policies, but that the risk management process over workers compensation could be more effective. Finally, ACPS bank reconciliations were not performed in a timely manner nor were they reviewed and approved by supervisory personnel.

Cash Management Best Practices

ACPS cash and investments as of June 30, 2005 totaled \$6,105,147 and \$10,544,751, respectively, and were managed in compliance with its investment policy. Also, ACPS adopted a formal written investment policy on February 13, 1996 and readopted the policy on October 11, 2005. Our review of the policy confirmed that it was in accordance with the Annotated Code of Maryland and the Maryland State Treasurer's regulations for local government investment policies.

Debt Management Policy Should Be Established

ACPS has not adopted a policy to govern its use of long-term lease obligations to finance operations, as recommended by the GFOA. Debt levels and their related annual costs are important long-term obligations that must be managed within available resources. An effective policy should provide guidelines to ensure ACPS manages its debt program in line with its resources. By law, ACPS is not authorized to issue bonds or similar debt instruments to finance capital or operational needs. However, ACPS does use lease/purchase agreements to acquire equipment items, such as photocopiers. According to ACPS audited financial statements, fiscal year 2005 lease/purchase payments totaled \$158,738, with future commitments through June 30, 2010 totaling \$510,366.

Risk Management Practices Could Be Enhanced

ACPS uses a combination of commercial insurance and self-insurance to manage its risks. Most property, vehicle and liability insurance is provided through set premium commercial insurance policies obtained through bids. Since 1992, ACPS has self-insured employee medical and dental benefits, but with commercial stop-loss coverage for individual claims exceeding \$175,000.

ACPS participates in the Maryland Association of Boards of Education's (MABE) risk pool for its workers' compensation insurance coverage. ACPS pays an annual premium into the pool and may participate in refunds or be assessed additional premiums based on claims paid from the pool and ACPS' individual loss experience. However, ACPS has not utilized the workers compensation loss data provided by MABE to enhance safety training in areas with the greatest claims and has not established initiatives such as a return-to-work program to help reduce workers compensation costs. Such programs could reduce workers compensation losses and their associated costs. ACPS management advised us that they plan to eventually establish a return-to-work program.

Bank Account Reconciliation Process Needs Improvement

ACPS did not perform timely reconciliations for any of its nine bank accounts from July 2005 through February 2006 primarily due to a staff vacancy that was filled during January 2006. As of August 15, 2006, ACPS had prepared reconciliations of its two main bank accounts (general checking and payroll) through April 2006 and July 2006; however, the seven other accounts (food service and construction funds) had still not been reconciled. Furthermore, none of the new reconciliations for the general checking and payroll accounts had been reviewed and approved by supervisory personnel. According to ACPS records, the nine bank accounts had balances totaling \$8.6 million as of June 30, 2006.

Recommendations

15. ACPS should adopt a debt management policy. For example, it should consider using the recommended practices of the Government Finance Officers' Association.
16. ACPS should evaluate its workers' compensation claims to identify and implement cost saving practices.
17. ACPS should reconcile all of its bank accounts each month, with subsequent documented supervisory review and approval of the reconciliations.

Audit Scope, Objectives, and Methodology

Scope

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

Objectives

We had two broad audit objectives:

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

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. Our audit approach, including the specific objectives of our local school system audits, was approved on

September 14, 2004 by the Joint Audit Committee of the Maryland General Assembly in accordance with the enabling legislation. As approved, the audit objectives excluded reviewing and assessing student achievement, curriculum, teacher performance, and other academic-related areas or functions. We also 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. Finally, we did not evaluate the ACPS Comprehensive Education Master Plan or related updates.

Methodology

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 ACPS. We also interviewed personnel at ACPS, the Maryland State Department of Education (MSDE), and staff at other local school systems in Maryland (as appropriate²²). Our audit procedures included inspections of documents and records, and observations of ACPS 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, 2004 through March 31, 2006.

In addition, we contacted a number of other state auditors' offices and legislative program evaluation agencies that had a history of conducting audits or reviews of local school systems. We interviewed those officials and inspected their work programs and resultant reports to identify specific audit techniques and operational practices at schools that could be adapted for our school system audits. Finally, we used certain statistical data--including financial and operational--compiled by the 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. For comparison purposes, information provided was generally limited to those Maryland school systems of similar sizes, based on student enrollment or system budget. In many cases, due to the self-reporting nature of the information, the data were neither audited nor independently verified by us.

²² During the course of the audit, it was necessary to contact other systems to identify policies or practices for comparative purposes and analysis.

Other Independent Auditors

When developing the approach for the audits of school system financial management practices, a consideration was the reliance on the work of other independent auditors to the extent practicable to avoid unnecessary duplication of audit effort. With respect to ACPS, the results of other audits that we considered were reported in two distinct audit reports: one related to the administration of its federal grants and the other, the management letter from the audit of its Annual Financial Report.

During the course of this audit, we relied on these results. We performed certain steps to satisfy ourselves as to the reliability of the work performed with respect to the independent federal grants audit of the ACPS fiscal year 2005 federal financial assistance programs for compliance with federal laws and regulations and the ACPS fiscal year 2005 financial statement audit. Accordingly, we significantly reduced the scope of our work in Chapter 1 "Revenue and Billing Cycle", and in Chapter 2 "Federal Funds".

Limitations of Internal Control

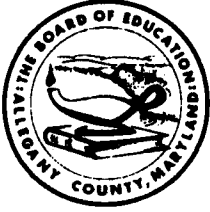
ACPS management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, 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 ACPS that did not warrant inclusion in this report.

Fieldwork and ACPS Responses

We conducted our fieldwork from March 27, 2006 to September 5, 2006. The ACPS response to our findings and recommendations is included as an appendix to this report.



Board of Education of Allegany County

108 Washington Street, P.O. Box 1724
Cumberland, Maryland 21501-1724
Telephone (301) 759-2000

William J. AuMiller
Superintendent of Schools

January 4, 2007

Mr. Bruce A. Myers, CPA
Legislative Auditor
Office of Legislative Audits
Maryland General Assembly
301 West Preston Street, Room 1202
Baltimore, MD 21201

Dear Mr. Myers:

Enclosed are the responses to the recommendations made in the Financial Management Practices Performance Audit Report for Allegany County Public Schools issued December 2006.

If you have any questions regarding this submission, please do not hesitate to call me.

Sincerely,

William J. AuMiller, Ed.D.
Superintendent of Schools

WJA:klr

Enclosure

cc: Mr. Tom Striplin, Board President

1. The ACPS uses the same general ledger system, decentralized purchasing system, and manual purchase orders as Allegany County government. The ACPS will hold future discussions to see if joint training on the system can be held to more fully automate the process and the ACPS will re-examine a proposed purchasing policy to guide staff in the procurement process.
2. Because of the small administrative staff, the ACPS reviews its workforce planning on a case by case basis. On December 1, 2005 the ACPS hired an Assistant Director of Finance to succeed the Assistant Superintendent of Administration and Finance who retired on June 30, 2006. This training proved invaluable to the successor and was a success based upon the efforts of both individuals. This process will be used with hiring a new Director of Information Technology who will be hired in the spring of 2007. The ACPS has also used this same process with the Executive Director of Human Resources who is nearing retirement.
3. The ACPS recognizes the need to improve system documentation and has started the process. Policies of the ACPS are always approved by the elected Board. Procedures though are typically not brought to the elected Board for approval.
4. The ACPS has hired an additional accountant on September 5, 2006 who is a CPA with governmental experience. This additional person will allow the system to place an increase emphasis on upon inventory and fixed assets. The ACPS hopes to have training on the fixed asset system in order to give staff members the tools they need to be successful. Study of the textbook inventory process is being proposed in order to improve the process.
5. Data processing personnel currently note the change date of code changes. Department personnel will begin the process of commenting in code the reason for changes. A new Director of Information Technology will be hired in the spring of 2007 and program change software may be evaluated at that time. Both organizations who share information technology resources will evaluate any proposal carefully that will increase costs.
6. The ACPS recognizes the need to update the disaster recovery plan. This effort was tabled so this audit could be studied. Efforts to update the disaster recovery plan and increase physical controls and safeguards have begun.
7. The Director of Facilities has requested an additional person in the FY08 budget develop performance standards and document preventative maintenance.
8. The ACPS has no interest in operating buses currently operated by outside vendors. Government operations are generally less efficient than privately held

business and such a move would require capital for physical plant as well as the additional of personnel in drivers and support personnel. It should be noted at a recent MABE Workers Comp meeting, Frederick County shared with the group an increase in workers comp claims from bus drivers after those drivers became employees of the system instead of employees of private contractors.

The ACPS is analyzing the PVA formula to make it more objective and reflective of market conditions. A recent study by Carroll County showed ACPS 13th out 18th on a cost per contract of the LEAs who use private contractors and 9th out 18th on the PVA formula. The same study ranked the ACPS as 15th out 18th on the maintenance and operation component of the contractor contract. When current contracts become open, the ACPS has little to no interest in them so the assertion of overpaying bus contractors is not supported by the interest in open contracts. The assertion of overpayment should not be made until all components of the contractor's contract are compared especially since nothing was noted on maintenance and operation. State wide guidance on this would be appreciated

9. The ACPS does verify bus contractors' manifests every two years. Manifests are checked for reasonability. If school bus riders are not being picked up or delivered to their drop off points, schools, the central office, and the transportation office would receive calls about the inadequate service.
10. The ACPS is currently implementing automated routing software. The ACPS has had unfavorable experience with buses under 54 passengers. Those buses typically last no longer than 8 years as compared to the 12 years that buses can run. The weather and terrain in Allegany County is more treacherous as opposed to other areas in the State. With new housing developments being proposed for Allegany County, smaller buses decrease the flexibility of the bus fleet and may not be practical if development should occur.
11. The department is developing a plan to standardize labor and staffing based upon Meals Per Labor Hour (MPLH). The department is also planning to eliminate satellite programs which will ease the burden on supplying schools allowing for a possible reduction in staff while increasing food quality. The department has also requested a maintenance repair position that should save the department money by doing HVAC repairs in house instead of paying local contractors.
12. The ACPS will review financial polices. A new finance director assumed duties on July 1, 2006. On July 6, 2006 the finance department was directed to begin documenting financial procedures. The Board will consider developing and using additional performance measures in the budget.

13. The Board will discuss the possibility of establishing a shared joint internal audit position with the Allegany County Commissioners. The Board has hired two additional Certified Public Accountants (CPAs). It should be noted that Finance handles aspects of workers compensation insurance, health insurance, and Medicare D commonly held by non financial departments. Restructuring will be looked at as the Board re-engineers administrative processes. Joint training with Allegany County Government occurred on the automated ledger package in October 2006. Future sessions on various aspects of the package are planned for 2007.
14. The Board will re-evaluate its Code of Ethics and financial disclosure requirements.
15. The ACPS is not permitted to issue debt by the State of Maryland. Copier leases are controlled by the budget process. All leases have an opt out clause if funding is not available.
16. Allegany County has received support from the MABE Workers Comp Fund for its workers compensation practices. Currently workers comp claims are processed in the human resources department but the workers comp trustee to the MABE Workers Comp Fund is the Finance Director. These functions should be aligned under one department. The FY08 budget will propose a new position of Risk Manager that can focus on workers comp issues.
17. Bank reconciliations are now performed monthly and approved by the Director of Finance. Failure to approve in July and August 2006 was an oversight due to the number of new personnel in the department.

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