

Financial Management Practices Performance Audit Report

Montgomery County Public Schools

January 2009



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA
Legislative Auditor

January 15, 2009

Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee
Senator Verna L. Jones, 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 Montgomery County Public Schools (MCPS) in accordance with the requirements of the State Government Article, Section 2-1220(e) of the Annotated Code of Maryland. MCPS is the largest public school system in Maryland based on the number of students enrolled. The educational services are delivered in 199 schools, with fiscal year 2007 expenditures of \$2.19 billion. The objectives of this audit were to evaluate whether MCPS procedures and controls were effective in accounting for and safeguarding its assets and whether its policies provided for the efficient use of financial resources.

Our audit disclosed that, in many cases, MCPS had procedures and controls in place to ensure the safeguarding of assets and the efficient use of financial resources. Nevertheless, our report contains 19 recommendations to MCPS to enhance controls in its existing financial management systems and processes in such areas as payroll, accounts receivable, and credit cards. For example, management should ensure that access to human resources and payroll information is adequately restricted and any related changes are reviewed for propriety, and that all purchasing card transactions are properly recorded, reviewed, and approved. MCPS also needs to ensure that certain industry best practices are used when implementing new IT applications, automated bus routing software is fully used, equipment records are accurate and complete, and health care costs are verified.

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 65. We wish to acknowledge the cooperation extended to us during our audit by MCPS.

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 Montgomery County Public Schools (MCPS) in accordance with the State Government Article, Section 2-1220(e) 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. Since the Committee approved the audit process in September 2004, we have issued audit reports related to 13 school systems; MCPS represents the fourteenth to date. The approved process included 11 areas to be audited at each system. The following are summaries of the findings in these areas at MCPS.

Revenue and Billing Cycle (see pages 9 through 13)

According to the audited MCPS financial statements, \$2.17 billion in revenue was received from all sources during fiscal year 2007, the vast majority of which was received via electronic fund transfers from other governmental entities. Procedures and controls for these revenue sources and accounts receivable were found to be adequate. However, based on our audit, controls over certain other revenues received could be improved. These revenues totaled \$8.8 million during fiscal year 2007. In addition, controls over accounts receivable, which had a balance of \$9 million as of June 30, 2007, and related collections should be improved.

Federal Funds (see pages 15 through 17)

Annually, MCPS is subject to an audit of its federally-funded programs (often referred to as the Single Audit, and required by Circular A-133, which is issued by the U.S. Office of Management and Budget). Due to parallels between that work and the scope of our audit, we placed significant reliance on the results of the independent audit of the fiscal year 2007 grant activity, for which reported expenditures totaled \$89 million. The related

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

Although MCPS has an adequate process for the identification of children eligible for Medicaid-subsidized services, additional measures could be taken to ensure that MCPS recovers all such costs and that payments to the third party administrator, which processes the claims, are accurate.

Procurement and Disbursement Cycle (see pages 19 through 23)

According to MCPS records, non-payroll disbursements totaled \$938 million during fiscal year 2007. MCPS used a number of contract procurement best practices and had established adequate controls over its automated purchasing and invoice processing systems. However, MCPS needs to improve controls and policies governing the use of credit cards and travel. For example, new MCPS credit cards were sent directly to the employee who placed the card order with the bank rather than to an independent employee. Also, certain credit cards purchases were not logged nor subject to supervisory review.

Human Resources and Payroll (see pages 25 through 28)

MCPS employed about 20,350 employees as of October 2007 and payroll costs during fiscal year 2007 totaled \$1.25 billion (not including benefits). MCPS had implemented a comprehensive workforce planning process to address its staffing needs. MCPS should address certain deficiencies within payroll processing. Specifically, certain MCPS personnel had unnecessary and excessive access capabilities on the MCPS human resources and payroll system, and certain transactions processed on the system were not subject to supervisory review.

Inventory Control and Accountability (see pages 29 through 31)

MCPS has formal policies governing the control and accountability of materials and supplies and property. However, MCPS did not utilize just-in-time ordering for materials and supplies. In addition, record keeping for equipment was not adequate. According to MCPS records, as of June 30, 2007, the book value of its capital totaled \$64 million.

Information Technology Services (see pages 33 through 38)

MCPS maintains and administers a computer network, computer operations, and a number of significant financial and academic information system applications. MCPS developed and periodically updated written technology plans. However, we identified several areas in need of improvement, including the strengthening of policies over passwords and accounts. In addition, MCPS should ensure that it uses best practices when implementing new IT applications and determine if it would be more beneficial to use in-house resources for certain support services (such as ongoing maintenance) that it currently outsources.

Facilities Construction, Renovation, and Maintenance (see pages 39 through 44)

MCPS maintains 199 schools and a number of other administrative and support facilities with a staff of approximately 1,650 custodial and maintenance personnel. MCPS had implemented a number of best practices to help reduce construction and maintenance costs for its facilities, such as a comprehensive process to plan for construction and renovations and an energy management program.

While long-term planning included factors such as student population and age of facilities, it did not include periodic assessments of school facilities and major mechanical systems (such as HVAC). In addition, while MCPS used an automated work order system to track maintenance and repairs performed,

it did not use the system to compare actual costs to predetermined estimates or to analyze employee productivity. Furthermore, preventive maintenance tasks performed were not adequately documented.

Transportation Services (see pages 45 through 49)

MCPS is responsible for the safe transportation of approximately 96,000 eligible students, of which five percent are disabled. MCPS used a number of recognized best practices to increase student transportation efficiency, such as staggering school arrival and dismissal times to enable certain buses to perform multiple runs. Nevertheless, MCPS should address all appropriate factors to properly plan and develop bus routes (for example, student ride times and bus capacities) and fully use its automated bus routing software. Furthermore, MCPS should implement adequate controls over billings and collections of fees charged for transportation services provided to non-MCPS entities, such as county recreational programs.

Food Services Operations (see pages 51 through 54)

MCPS had implemented a number of best practices to help reduce food service costs, such as preparing meals for all schools at a central location and using performance measures to gauge operational efficiency. MCPS also has adequate procedures in place to identify students eligible for free and reduced-price meals under the federal national school meals programs. However, MCPS needs to improve the controls over processing of cash receipts in the cafeterias.

School Board Operations and Oversight (see pages 55 through 59)

Oversight of MCPS operations included the seven-member Board receiving financial updates, such as monthly budget variances to assist it in monitoring the efficient use of funds. The Board is also extensively involved in a comprehensive budgeting process and has adopted a detailed ethics policy. Furthermore, MCPS has an active audit committee and an internal audit unit, engaged primarily in conducting audits of

student activity funds. However, several opportunities exist for the Board to improve oversight and effectiveness of MCPS operations. For example, the Board should consider focusing the work performed by its internal auditor on auditing significant MCPS operations and establishing a confidential hotline and whistleblower policy.

Other Financial Controls (see pages 61 through 63)

While MCPS had procedures in place to govern its risk and certain cash management practices, it did not have written policies governing its use of long-term liabilities, such as capital lease agreements, or cash management policies for investing excess funds from routine operations. In addition, MCPS should take additional steps to ensure it controls health care costs, such as by verifying the eligibility of program participants and conducting audits of paid claims.

Table of Contents

Executive Summary	i
Background Information	7
Oversight	7
Statistical Overview	7
External Audits of Fiscal Year 2007 Activity	8
Chapter 1: Revenue and Billing Cycle	9
Background	10
Revenue and Billing Cycle Activity Was Generally Adequate	11
Controls Over Funds Received at Various Locations Need to Be Improved	11
Controls Over Certain Accounts Receivable and Related Collections Should Be Improved	12
Recommendations	13
Chapter 2: Federal Funds	15
Background	16
MCPS Established Adequate Internal Controls Over Federal Grants and Complied with Federal Grant Requirements	16
Improvements Should Be Made to Ensure All Costs for Medicaid-Subsidized Services Are Recovered	16
Available Funding Was Obtained from the Federal E-Rate Program	17
Recommendation	17

Table of Contents

Chapter 3: Procurement and Disbursement Cycle	19
Background	19
MCPS Used Several Best Practices to Address Its Procurement Needs	20
MCPS Had Established Adequate Controls Over Its Automated Purchasing and Invoice Processing Applications	20
Documentation and Processes Related to Credit Cards Need Improvement	21
MCPS Should Ensure that All Employees Comply with Existing Travel Policies	23
Recommendations	23
Chapter 4: Human Resources and Payroll	25
Background	25
Workforce Planning Addressed Future Critical Needs	26
Human Resources and Payroll Internal Controls Need to Be Strengthened	27
Recommendation	28
Chapter 5: Inventory Control and Accountability	29
Background	29
Formal Textbook Procedures Have Been Established	30
Modifications to the Current Inventory Ordering Process Could Improve Operating Efficiency	30
Existing Controls Over Equipment and the Related Record-keeping Should Be Improved	30
Recommendations	31

Table of Contents

Chapter 6: Information Technology Services	33
Background	33
Technology Plans Were Developed to Address Current and Future Needs of MCPS	34
Data Processing Functions Should Be Better Safeguarded	34
MCPS Should Use Additional Recognized Best Practices for System Development	35
Costs and Benefits of Outsourcing IT Maintenance and Implementation Need to Be Evaluated	37
Recommendations	38
Chapter 7: Facilities Construction, Renovation, and Maintenance	39
Background	40
A Number of Best Practices Were in Place to Enhance the Effectiveness of the MCPS Facility Construction and Maintenance Department	41
Long-Term Planning Processes Could Be Improved	41
The Work Order System Should Be Fully Used	43
Recommendations	44

Table of Contents

Chapter 8: Transportation Services	45
Background	45
Several Best Practices Were in Place to Enhance Bus Route Efficiency and to Control Related Costs	46
Policies and Practices for Planning and Revising Bus Routes Should Be Enhanced	47
Controls Over Transportation-Related Accounts Receivable Should Be Improved	48
Recommendations	49
Chapter 9: Food Services Operations	51
Background	51
Certain Best Practices Were in Place	53
Controls Over Food Service Cash Operations Need Improvement	54
Recommendation	54
Chapter 10: School Board Operations and Oversight	55
Background	55
Certain Oversight Had Been Put in Place Regarding MCPS Operations	56
The Board Should Consider Additional Steps to Assist It in Governing MCPS	57
Recommendation	59

Table of Contents

Chapter 11: Other Financial Controls	61
Risk Management Best Practices Were in Place	61
Capital Lease and Cash Management Policies Need to Be Established	62
MCPS Should Take Additional Steps to Control Health Care Costs	62
Recommendations	63
Audit Scope, Objectives, and Methodology	65
Response of Montgomery County Public Schools	Appendix

Background Information

Oversight

Montgomery County Public Schools (MCPS) is governed by a local school board, consisting of seven elected voting members and a student representative. The vast majority of MCPS funding is provided by the Montgomery County and State 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 MCPS to comply with the requirements and mandates of the federal No Child Left Behind Act of 2001. Oversight by the Montgomery County government is limited, although the MCPS annual operational and capital budgets require County approval.

Statistical Overview

According to MSDE student enrollment records, MCPS has the highest student enrollment among the 24 public school systems in Maryland. From fiscal year 1998 to 2007, the average annual full-time regular and special education pupil population has increased 15 percent from 119,843 to 137,727, with MSDE projecting further increases to an enrollment of 145,340 in 2016. Presently, MCPS has 199 schools and a number of other facilities (including alternative schools and administrative facilities). A review of the budget history for fiscal year 1998 to 2007 disclosed an increase in the MCPS total operating expenditures from \$1.15 billion in fiscal year 1998 to \$2.19 billion in fiscal year 2007. Salaries and wages, excluding benefits, accounted for 58 percent of the fiscal year 2007 expenditures, which supported 20,346 full-time positions (13,548 instructional and 6,798 non-instructional).¹

¹ The primary source for this background data is MSDE statistical data, including the annual Fact Book.

Certain statistical information contained in this report was taken from unaudited reports distributed by MSDE and represents the most current comparable information available at the time of our audit. These MSDE reports are based on self-reported data from the 24 Maryland public school systems, and MSDE does not warrant the comparability or completeness of the data.

External Audit of Fiscal Year 2007 Activity

Annually, MCPS engages a certified public accounting firm to independently audit its fiscal year end financial statements. Additionally, the auditor conducts what is referred to as a Single Audit of MCPS federal grant programs (as required by federal regulations). The two resulting audit reports for the 2007 fiscal year were issued in September 2007. Neither report disclosed any material weaknesses or significant deficiencies on MCPS record keeping, processes, and controls.

Chapter 1

Revenue and Billing Cycle

According to the MCPS audited financial statements for the fiscal year ended June 30, 2007, \$2.17 billion of revenue was received by MCPS during fiscal year 2007. Due to similarities between the work of the independent certified public accounting firm that audited MCPS financial statements and the scope of our audit in this area, we place significant reliance on the results of the external audit of revenues and certain accounts receivable (for example, amounts due from other governments). The firm's procedural review and testing disclosed that collection activity for the most significant revenue types, the majority of which was received via electronic fund transfers from other government entities, and related accounts receivable was adequate.

However, MCPS should improve controls over certain revenues received by the central accounting office. MCPS should also improve controls over the billing and related collections of certain accounts receivable.

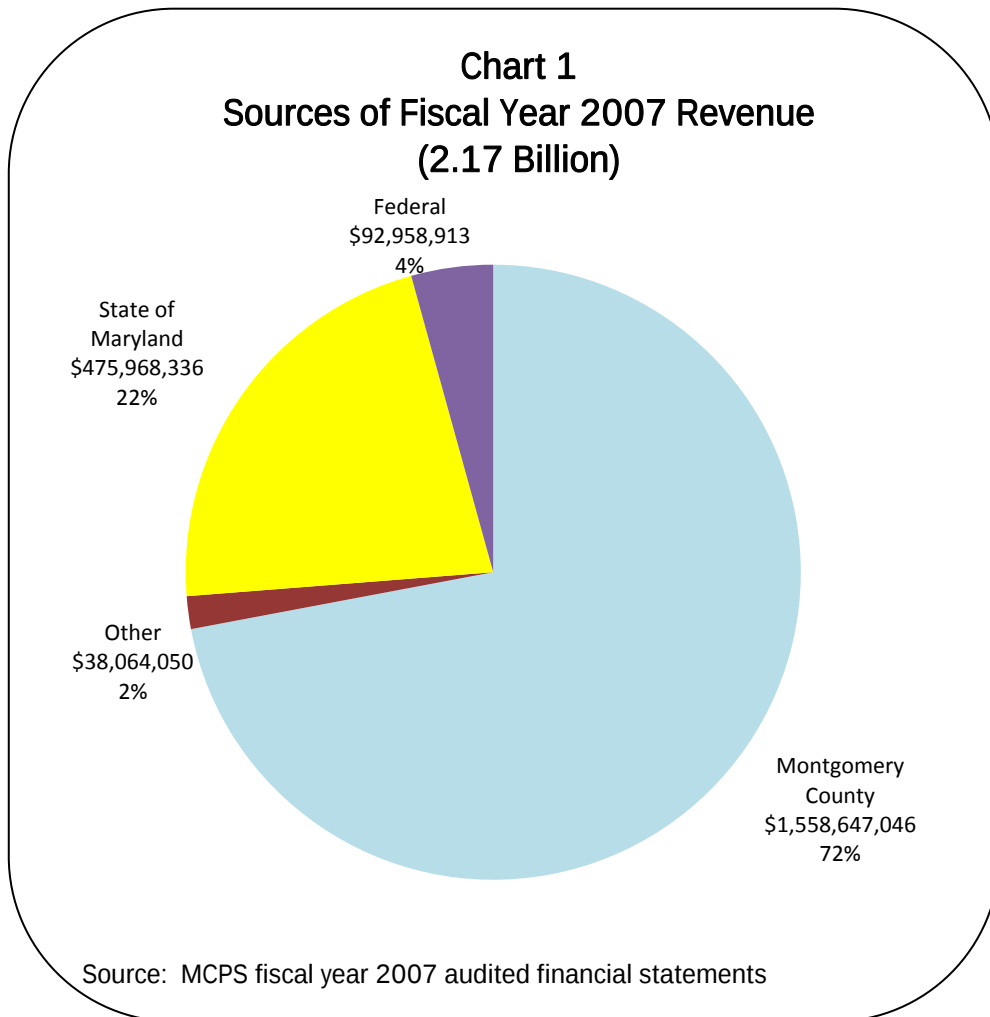
For school activity funds², we placed significant reliance on audits of these funds by MCPS' Internal Audit Unit. The MCPS internal auditor conducts audits of school activity funds. The internal auditor's review and testing of the school activity funds at MCPS schools identified some control weaknesses at certain schools. However, the control weaknesses identified did not appear to be prevalent and were appropriately addressed by school management. In addition, MCPS' external auditor performed procedural reviews and testing of student activity funds in

² The Board has a fiduciary responsibility to ensure that the school activity fund is used only for intended purposes by those to whom the assets belong. Receipts for the school activity fund, which totaled \$38.2 million during fiscal year 2007, are not included in the \$2.17 billion revenue total because the Board cannot use these assets to finance its operations.

conjunction with its fiscal year 2007 audit. The audit disclosed no material control weaknesses or accounting errors related to these funds.

Background

MCPS revenues consist primarily of funds received from Montgomery County, the State, and the federal government, the vast majority of which were received via electronic funds transfer. Other sources include federal grant funds, receipts from the sale of food, facility use reimbursement fees, and interest income. Chart 1 (below) shows MCPS fiscal year 2007 revenues of \$2.17 billion by major source.



In addition to the revenues in Chart 1, schools also collected funds for various purposes, such as for student activity groups including yearbook and band. These school activity funds are accounted for separately by each school and are reported, in summary, in the audited financial statements. According to the audited financial statements, fiscal year 2007 school activity fund revenues totaled \$38.2 million, and the June 30, 2007 balance was \$16.3 million.

Revenue and Billing Cycle Activity Was Generally Adequate

Due to similarities between the work of the accounting firm that audited the MCPS financial statements and the scope of our audit in this area, we placed reliance on the results of the independent audit. The auditor's procedural review and testing disclosed that collection activity for significant revenue types (local, State, and federal aid, plus other sources, such as food service operations), the majority of which was received via electronic fund transfers, and related accounts receivable was adequate.

In addition, MCPS' external auditor performed procedural reviews and testing of student activity funds in conjunction with its fiscal year 2007 audit. The audit disclosed no material control weaknesses or accounting errors related to these funds. Finally, school activity funds were also subject to periodic audit by MCPS internal auditors. The internal auditor's review and testing of the school activity funds at MCPS schools identified some control weaknesses at certain schools. However, the control weaknesses identified did not appear to be prevalent and were appropriately addressed by school management.

Controls Over Funds Received at Various Locations Need to Be Improved

Controls over certain receipts received by other departments, and subsequently processed and deposited by the Controller's Office, were not adequate. Cash and check receipts received by other units and deposited in this manner totaled \$8.8 million during fiscal year 2008. While MCPS had established cash receipts procedures, those procedures did not include how funds received by other

locations should be handled (such as recording receipts and forwarding them for deposit in a timely manner to the Controller's Office). Consequently, we noted the following:

- Cash receipts were not recorded when initially received by other locations to establish immediate accountability over receipts. As a result, MCPS lacked assurance that all receipts received by these locations were subsequently deposited.
- The transfer of funds from the receiving department to the Controller's Office was not consistently documented to establish accountability for the funds, and neither the departments nor the Office had assurance that all amounts received were deposited.
- Checks received by other locations were not restrictively endorsed 'for deposit only' until they were received by the Controller's Office.

Controls Over Certain Accounts Receivable and Related Collections Should Be Improved

Controls over accounts receivable (such as for nonresident tuition, facilities rentals, and field trips) and the related collections processed by the central accounting office need to be improved. According to MCPS records, this accounts receivable balance totaled approximately \$9 million as of June 30, 2007, of which \$1.7 million was more than 90 days old. We noted that MCPS did not have written policies and procedures governing this activity. In addition, the following was noted:

- The employee who maintained the accounts receivable records also had access to the related cash receipts.
- Non-cash credits, which totaled approximately \$2.8 million during fiscal year 2007, were not reviewed and approved by independent supervisory personnel. Although we were advised that most adjustments to accounts receivable were reviewed and approved, the employee who approved the adjustments

also had the ability to process such adjustments. In addition, approvals were not documented.

- MCPS did not have a formal debt collection policy. Specifically, while the department that authorized the invoice contacted the debtor, MCPS had not established procedures that provided for follow-up notices on unpaid accounts to be sent at predetermined intervals. In addition, although MCPS used a collection agency to collect past due accounts, MCPS had not established procedures to determine when an account should be considered delinquent and forwarded to the collection agency. In this regard, as of January 2008, no accounts had been forwarded to the agency since November 2006. Our test of 10 accounts totaling \$89,000, outstanding at least 120 days as of January 2008, disclosed that, for 4 accounts totaling \$43,500, MCPS could not provide any documentation of collection efforts (such as late notices or referral to the collection agency). For four other accounts, although MCPS had forwarded the account to the collection agency, there was no documentation that MCPS had attempted to collect the amount due prior to referring the account.

Recommendations

1. MCPS should establish procedures for collections received at locations other than the Controller's Office to ensure that these funds are accounted for. Such procedures should include initially recording collections and restrictively endorsing checks immediately upon receipt, and documenting transfers from the receiving departments.
2. MCPS should develop policies and procedures governing accounts receivable, including a formal debt collection policy. The policies and procedures should address the proper separation of duties and progressive collections steps to be performed to pursue outstanding accounts. In addition, non-cash credit adjustments should be approved by independent supervisory personnel.

Chapter 2

Federal Funds

Annually, MCPS is subject to an audit of its federally-funded grant programs (often referred to as the Single Audit, and required by Circular A-133, which is issued by the U.S. Office of Management and Budget). The report on the audit of fiscal year 2007 federal grant activity was issued by an independent certified public accounting firm on September 26, 2007.

In that report, the auditor stated that MCPS 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 significant deficiencies³ and no matters considered to be material weaknesses⁴.

MCPS has a process in place to identify children eligible for Medicaid-subsidized⁵ services and to recover the related costs. However, MCPS did not monitor the third party claims administrator to ensure that the vendor properly submitted for reimbursement all claims for services provided and that the vendor's billings for its services were accurate.

MCPS applied for and obtained available funding under the federal E-Rate program.

³ Significant deficiencies are control deficiencies that adversely affect the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected.

⁴ Material weaknesses are significant deficiencies that result in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.

⁵ The Federal Medical Assistance Program, or Medicaid, is not a grant program under Circular A-133 and is not included in the Single Audit.

Background

MCPS receives funds primarily from Montgomery County, the State, and the federal government. Most funds received from Montgomery County and the State are unrestricted; however, federal funds are generally restricted for use for a specified program (such as the School Lunch Program or Special Education). According to the audited Schedule of Federal Awards, fiscal year 2007 expenditures of federal award funds totaled \$89 million.

MCPS Established Adequate Internal Controls Over Federal Grants and Complied with Federal Grant Requirements

Because of the accounting firm's work on MCPS federal fund expenditures, we relied on the auditor's results. Besides expressing an opinion on MCPS 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 2007 required Schedule of Federal Awards (which includes claimed and reported grant-related expenditures). In its report, the firm stated that MCPS 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 significant deficiencies and no matters considered to be material weaknesses.

Improvements Should Be Made to Ensure All Costs for Medicaid-Subsidized Services Are Recovered

Although MCPS had adequate processes in place to identify students eligible for Medicaid-subsidized services (for example, it made use of listings of all children whose families are participating in Medicaid as determined by the Department of Human Resources and conducted outreach to families using the MCPS website), our review disclosed certain deficiencies. Specifically, MCPS did not ensure that its third party administrator was remitting claims information for all eligible services to the State Department of

Health and Mental Hygiene (DHMH) for Medicaid reimbursement, and that fees paid to this administrator were accurate.

While the third party administrator compiled individual claim forms prepared by MCPS schools and submitted this data in an approved format so that MCPS could be reimbursed, MCPS did not verify that claim information submitted to DHMH was accurate and complete. As a result, MCPS may not be recovering the maximum amount of costs associated with provided Medicaid-subsidized services. In addition, while the third party administrator was paid based on the number of claims submitted, MCPS did not ensure that invoices received from this administrator for its services accurately reflected the number of claims actually submitted to DHMH.

According to MCPS records, as of June 30, 2007, approximately 2,800 students were eligible and receiving these services. Those records also indicate that, in fiscal year 2007, MCPS received approximately \$4.4 million in recovered costs for Medicaid claims and paid the third party administrator approximately \$160,000 for its services.

Available Funding Was Obtained from the Federal E-Rate Program

MCPS has a process in place to request and receive reimbursement for technology expenditures from the federal School and Libraries Universal Service Program (E-Rate). The E-Rate program provides funding to schools for telecommunications expenses (such as Internet access). The funding is based on the level of poverty and the rural status of the school district. MCPS received approximately \$1.7 million of E-Rate funds for fiscal year 2007.

Recommendation

3. MCPS should ensure that all costs associated with providing Medicaid-subsidized services are recovered by verifying, at least on a test basis, the accuracy and completeness of claims submitted by the third party administrator. MCPS should also verify that billings received from the third party administrator are accurate.

Chapter 3

Procurement and Disbursement Cycle

MCPS followed certain procurement best practices such as purchasing items through contracts already procured by the State and other local governments (referred to as “piggybacking”) when it is beneficial to do so. In addition, MCPS had established adequate controls over its automated purchasing and invoice processing systems. However, we found that processes over credit cards need to be strengthened. Specifically, our review disclosed significant weaknesses in internal controls over the procurement card program. These weaknesses included (1) a lack of monitoring over card usage and credit limits, (2) the employee who requested the procurement cards also initially received the cards from the vendor and (3) employees did not always complete card transaction logs, and other logs were not reviewed and approved. We also noted certain potentially questionable credit card purchases. Finally, for certain employees, travel was not approved in advance, as required by MCPS policy.

Background

MCPS uses an automated system for procurements and disbursements. Requisitions are prepared electronically by departments and are forwarded to the purchasing department. Requisitions must be approved by supervisory personnel within the requesting department. Based on the requisition, the centralized purchasing office will solicit bids and award the contracts. Purchase orders are created in the automated system based on the vendor selected in the bid process. Purchases anticipated to cost more than \$7,500 require bids from multiple vendors. Board policy requires that all contracts over \$25,000 are to be approved by the Board.

The receipt of goods and services are recorded in the automated system or on hardcopy documentation by the receiving school or department and payments are processed by the finance office using the automated system after appropriate matching of original invoices to purchase orders and receiving documents. According to MCPS records, non-payroll disbursements totaled \$938 million in fiscal year 2007.

During fiscal year 2007, MCPS records indicated that its employees used credit cards to make a total of \$5.6 million in purchases (including textbook purchases). According to MCPS records, during fiscal year 2007, 1,209 employees used credit cards with the monthly charges being paid directly by the school system to the credit card bank.

MCPS Used Several Best Practices to Address Its Procurement Needs

MCPS had instituted certain best practices that should enhance the cost effectiveness of its procurements. These include “piggybacking” onto contracts already procured by the State and other local governments, and participating in cooperative purchasing organizations. These practices save MCPS certain costs associated with the procurement of the contracts and may provide larger discounts as a result of the combined purchasing power of multiple entities.

MCPS Had Established Adequate Controls Over its Automated Purchasing and Invoice Processing Systems

MCPS had established adequate controls over its automated purchasing and invoice processing systems. Specifically, electronic approvals were established over purchase requisitions and invoice payments to prevent one individual from creating and approving purchases or approving the payment of invoices. In addition, MCPS had written policies and procedures for the procurement of goods and services and the disbursement of funds. Also, our tests

disclosed that bids were obtained when necessary, the lowest acceptable bid was selected and awards were properly documented.

Documentation and Processes Related to Credit Cards Need Improvement

MCPS should improve controls and monitoring over credit

cards – Although MCPS had developed policies and procedures to help ensure the proper usage of its credit cards, our review disclosed certain deficiencies. Specifically, our tests of controls disclosed the following conditions:

- The duties over the ordering and initial receipt of credit cards from the bank were not adequately segregated. The individual responsible for ordering new credit cards also initially received these cards from the issuing bank prior to their distribution to MCPS personnel named on the cards. This condition could allow unauthorized purchases to be made on improperly obtained cards. Although this individual had been issued two credit cards and made purchases totaling \$9,800 in calendar year 2007, our review indicated that the purchases appeared to be for appropriate school business.
- Although MCPS periodically determined the continued need for cards (based on surveying cardholder supervisors), MCPS did not evaluate the need for cards based on actual usage or the adequacy of card spending limits to reduce exposure and risk of inappropriate charges. For example, our test of usage disclosed that, for 15 cards with monthly credit limits of \$20,000 or greater, total transactions for 6 cards never exceeded 10 percent of the assigned credit limit in any month of calendar year 2007, and 2 cards were never used. In addition, nine of these cards had single transaction limits exceeding \$7,500, MCPS' threshold for obtaining competitive bids.
- MCPS did not ensure that credit card documentation was maintained that adequately supports all purchases and establishes proper supervisory review of every transaction. Our review of 161 calendar year 2007 transactions totaling \$55,000 disclosed that 50 transactions totaling \$22,800, applicable to 9

cardholders, were not included on transaction logs for subsequent review.

Of the remaining 111 transactions, there was no documented approval on the logs pertaining to 41 transactions (applicable to 6 cardholders) to indicate a supervisory review and approval of the related charges. MCPS policy requires that cardholders record all purchasing card transactions on a monthly transaction log and that supervisors review and approve the logs and related documentation in a timely manner.

Credit card activity should be more closely monitored to verify appropriate use – Certain controls were not in place to ensure that MCPS employees used procurement cards to make appropriate purchases. Specifically, we noted the following conditions:

- MCPS policy over procurement card use did not specifically address the permissibility of certain categories of transactions. For example, our review of fiscal year 2007 credit card purchases identified 512 purchases totaling \$39,400 from vendors that did not appear to have an obvious relationship with the mission of MCPS. Based on documentation available, we could not determine the propriety of these transactions, nor did the credit card manual provide any guidance as to the validity of such purchases. For example, we noted 119 purchases totaling \$8,290 from department stores and 121 purchases totaling \$5,571 from party supply stores.
- Our review disclosed that, during calendar year 2007, 10 different schools made purchases of food for meetings in excess of approved limits without obtaining the required approval of the Chief Operating Officer. For example, one school spent a total of \$21,000 on food (using credit cards) without obtaining such approval. The MCPS Independent Activity Fund Manual sets dollar limits on food transactions (such as \$4,200 per year for a high school) that can be purchased by schools-based personnel without the prior approval of the Chief Operating Officer.

MCPS Should Ensure that All Employees Comply with Existing Travel Policies

MCPS has established adequate policies and procedures designed to control travel expenditures. These policies define the conditions under which employees may be reimbursed for travel, including the requirement that all travel be approved in advance by appropriate supervisory personnel. However, the policies and procedures did not establish adequate controls over travel expenditures charged on credit cards. Approximately 26 individuals (that is, upper management employees and Board members) had been issued credit cards that did not have travel-related restrictions, such as for air fare and hotel accommodations. Use of credit cards for travel expenditures may allow cardholders to incur such expenditures without obtaining advance approval, as required by MCPS regulations. Our tests of 32 calendar year 2007 travel expenditures charged to credit cards totaling \$19,028 disclosed 30 expenditures totaling \$17,930 that were not recorded on monthly activity logs and, therefore, were never approved. In addition, no documentation could be located to support 10 meal expenditures totaling \$2,172 that were recorded on credit card statements. According to MCPS records, during fiscal year 2007, travel expenditures totaled \$2.5 million, including \$80,465 charged on credit cards.

Recommendations

4. MCPS should enhance its policies and controls over its credit cards and transactions. Specifically, MCPS should segregate the responsibilities for ordering and receiving the cards, ensure that adequate documentation and approvals exists for all credit card purchases, and conduct periodic spending and credit limit reviews. MCPS should also ensure that the credit card manual includes clarification regarding the appropriate uses of credit cards. Furthermore, MCPS should review past credit card charges, such as those we identified, for propriety and recover any inappropriate charges.
5. MCPS should ensure that all travel is approved in advance, in accordance with existing policy.

Chapter 4

Human Resources and Payroll

MCPS had implemented comprehensive workforce planning, which adequately addressed long-term trends in all critical operational areas. However, MCPS should address certain procedural deficiencies with respect to payroll processing. These deficiencies include unnecessary and excessive access capabilities given to certain personnel on the MCPS human resources and payroll system and a lack of supervisory review of certain human resources and payroll transactions.

Background

Payroll costs are the largest single expense in the MCPS budget, with fiscal year 2007 salary and wage costs totaling \$1.25 billion (not including benefits). MCPS uses an automated system to maintain human resources information, process payroll, and track leave usage. Manual time records, including leave taken, are entered onto the system every two weeks by designated employees at each MCPS site. Leave accumulation is automatically calculated by the system which is also used to process and record all payroll transactions.

Payroll information is downloaded from the automated system into a separate check writing program to produce payroll checks and direct deposit advices. Payroll checks and deposit advices are delivered to employees independent of the timekeepers at each MCPS site for distribution.

As of October 2007, MCPS had approximately 20,350 employees. The 6.8 to 1 ratio of MCPS students to full-time equivalent employees is reasonable when compared with similarly-sized school systems (see Table 1 below).

Table 1
Comparison of Student to Employee Ratios – Fall 2007
Unaudited

School System	Number of Students (as of September 30, 2007)	Number of Full-Time Equivalent Employees (as of October 1, 2007)	Student to Employee Ratio
Montgomery Co.	137,727	20,346	6.8 to 1
Anne Arundel Co.	73,400	9,310	7.9 to 1
Baltimore Co.	104,283	14,221	7.3 to 1
Prince George's Co.	129,752	18,689	6.9 to 1
Baltimore City	81,284	12,021	6.8 to 1

Source: MSDE Student/Staff Publications

Workforce Planning Addressed Future Critical Needs

MCPS monitors data related to portions of the workforce approaching retirement, and forecasts the number of retirements in order to determine their impact on hiring decisions. The MCPS Master Plan sets the strategic direction of the school system and provides coordination and focus for initiatives to address challenges faced by MCPS. The Plan includes a number of objectives and strategies to address human resource needs—which is evidence of workforce planning. It addresses the recruitment and retention of highly qualified instructional staff (that is, teachers and certain instructional aides). MCPS implements alternative methods to address non-instructional personnel employed by MCPS, such as central office and critical support staff. Staff prepared an annual analysis, which identified all employees eligible or likely to retire during the next five fiscal years. This allowed MCPS to tailor its recruitment and retention efforts.

Human Resources and Payroll Internal Controls Need to Be Strengthened

MCPS did not adequately restrict access to its automated personnel and payroll system. Specifically, numerous employees had access to personnel and payroll menus in the automated system, including menus that provided the ability to make changes to critical data or generate checks. While some of these employees needed access to certain components of the menus to perform their jobs, MCPS had not developed a process to restrict employees' access to only those components necessary for them to perform their specific job duties. Specifically, we noted the following conditions:

- Of the 116 employees that could modify employee salary and benefits information in the human resources system, only 7 of these individuals required such access for their job duties.
- Of the 35 employees that could add new employees and/or update employee information such as name, address, and social security number in the human resources system, only the aforementioned 7 employees required such access.
- Twenty-one employees could process manual payroll check transactions (used for non-regular payments such as leave balance payoffs, tax shelter program refunds, and retroactive pay adjustments); however, only three of these employees needed such access to perform their job duties. In addition, these three employees could individually generate the actual manual checks and submit the related information to the bank confirming the checks' validity without any oversight. According to MCPS records, manual checks processed in fiscal year 2007 totaled \$21.2 million.

In addition, MCPS had not instituted any compensating controls, such as an independent review of transaction or exception reports. Although we found no evidence of unauthorized additions to the payroll or unauthorized payments for the items tested, the improper separation of duties and access to the system could be used to process unauthorized payroll payments.

Recommendation

6. MCPS should take the necessary corrective actions to ensure that adequate internal controls are in place over its automated human resources and payroll system. Specifically, employees should be provided only the system access capabilities needed to perform their job duties. In addition, MCPS should segregate duties related to processing manual payroll checks. Finally, MCPS should establish an independent review and approval process to ensure, at least on a test basis, the propriety of payroll-related changes recorded in the automated system.

Chapter 5

Inventory Control and Accountability

MCPS has formal policies and procedures governing the control and accountability of materials and supplies and property, including textbooks; however, MCPS could reduce the costs of maintaining the on-hand materials and supplies inventory by revising its ordering system. Furthermore, MCPS should improve its control over equipment and the related recordkeeping.

Background

MCPS maintained one warehouse for non-food service materials and supplies. Inventory records were maintained using an automated system. According to the MCPS audited financial statements, as of June 30, 2007, the book value of its non-food service materials and supplies inventory was \$6.6 million. In addition, according to MCPS records, fiscal year 2007 expenditures for materials and supplies (excluding those for food services) totaled \$58.9 million.

MCPS uses an automated fixed asset system to track property and equipment. According to the MCPS audited financial statements, as of June 30, 2007, the book value of its capital equipment (including furniture and fixtures) was \$64 million and, per MCPS records, fiscal year 2007 expenditures for capital equipment totaled \$16.8 million. For financial statement reporting purposes, equipment items with a cost of \$5,000 or more are capitalized and depreciated. Furthermore, in addition to the aforementioned equipment items, certain items defined in MCPS policy with a lesser value (such as computers, copiers, and cameras), are included in

the centralized fixed asset system. Equipment items that do not meet these criteria are recorded on each individual school's equipment records.

Formal Textbook Procedures Had Been Established

MCPS had established formal procedures for selecting, purchasing, distributing, and disposing of textbooks. All potential textbooks are screened by a selection committee and approved by the Board. Textbooks are inventoried and accounted for by individual schools. Textbooks are sold or disposed of centrally as provided for by MCPS policy.

Modifications to the Current Inventory Ordering Process Could Improve Operating Efficiency

MCPS did not use just-in-time ordering to procure materials and supplies. Just-in-time ordering for supplies allows an entity to order supplies only when needed and can reduce the amount of storage needed and inefficiencies due to excess ordering and related record keeping. Currently, the majority of materials and supplies (such as office supplies) are ordered in bulk during the summer from various vendors based on the annual needs of the schools. The current process results in inefficient cash flow as it requires large cash outlays at one time, rather than several smaller outlays if materials and supplies were ordered throughout the year. In addition, this process increases the chance that supplies could be spoiled and requires more storage space than may otherwise be needed. Although schools have the option to schedule orders throughout the school year, we were advised that this option is rarely employed.

Existing Controls Over Equipment and the Related Recordkeeping Should Be Improved

MCPS centralized inventory records did not accurately reflect all equipment that it owned. Our testing of the detail records for equipment disclosed the following discrepancies:

- The detailed equipment records included 306 items with no tag or serial number recorded (which are required by MCPS policy); as a result, accountability over these items is reduced. In addition, the value of some of these 306 items appeared to be misstated. For example, according to MCPS records, one utility truck purchased in 2005 had been assigned a purchase cost of \$640,000. This could have been due either to an individual record reflecting the cost of multiple items included on a single invoice or to errors that existed in the old equipment records that were transferred to the new automated inventory system when it was implemented on July 1, 2007.
- The detail equipment records often did not agree with what was on hand. Our test of 54 capital equipment items totaling \$144,769, listed in the detail records, disclosed that 28 sensitive items (such as laptop computers and digital cameras) with a total value of \$49,700 could not be located. In addition, our test of 37 equipment items physically sighted at five locations disclosed that 4 items were not included in the detail equipment records.
- Our test of 9 purchases of 6,960 items at a total cost of \$6.5 million (primarily computers) made during fiscal years 2007 and 2008, disclosed that 48 items totaling \$43,600, were not included in the detailed equipment records.

Recommendations

7. MCPS should use just-in-time ordering for routine materials and supplies to reduce the amount of on-hand materials and supplies.
8. MCPS should improve controls over equipment and the related recordkeeping. Specifically, MCPS should ensure that the detail equipment records are complete and accurate.

Chapter 6

Information Technology Services

The MCPS Department of Technology maintains and administers the MCPS's computer network, computer operations and instructional information system applications. MCPS developed and updated a written technology plan that was linked to the MCPS master plan.

Nevertheless, we did identify deficiencies in a number of areas, including user security, critical program change controls, and computer room access. For example, over 13,000 accounts had passwords that were set to never expire and access to the computer room was not terminated for certain former employees. In addition, MCPS did not use certain best practices when it implemented a new IT application, and did not determine if it would be more beneficial to hire additional in-house IT support staff for functions now performed routinely by IT vendors.

Background

MCPS operates a wide area network, with Internet connectivity, which connects the individual schools' local networks to the computer resources located at the MCPS headquarters. The Department of Technology maintains a computer room at the

headquarters location in which numerous computer servers operate to support MCPS Information System applications.

Several significant administrative and academic related information system applications exist. For example, MCPS operates the Financial Management System (FMS) application and the Online Administrative Student Information System application. The FMS application includes modules for budgeting, accounts payable, fixed assets, and purchasing.

Technology Plans Were Developed to Address Current and Future Needs of MCPS

MCPS had developed a written technology plan, which includes a comprehensive assessment of the technical needs of the schools. The plan identifies their IT needs and the actions to be taken to address those needs. The plan also includes measurable goals and objectives. Other areas that are addressed in the plan include professional development and IT related budgets. Finally, the plan is periodically updated and monitored for implementation status of identified actions.

Data Processing Functions Should Be Better Safeguarded

Steps Should Be Taken to Ensure that Access to IT Software Applications Is Appropriate and Controlled – Certain

computer security vulnerabilities existed with respect to various MCPS automated systems, programs, and data. For example, when compared to industry standards, automatic password expirations were set for excessive periods (such as 999 days). Also, for over 13,000 accounts, including high privilege users such as database and network administrators, passwords were set to never expire. In addition, there was no standard as to the complexity of passwords (to make them more difficult to hack). Furthermore, significant system security-related activities (such as account logons and failed access attempts) for one critical system were not always logged for review and, as a result, unauthorized or inappropriate activities affecting the integrity of critical production application program and

data files could occur and remain undetected. We also found that, as of December 2007, one critical system had not been updated for security related software updates since March 2007, leaving this system vulnerable to security exploits addressed by these updates. Finally, production program changes to critical MCPS applications were not adequately documented. For example, requests for changes were often not documented and, for two critical applications, there was no formal process to acknowledge user approval of program changes.

Physical security over the computer room should be

improved – Physical access to the computer room was not adequately controlled. Specifically, 20 users, including 11 former employees, had unnecessary access to the computer room, via identification cards.

MCPS Should Use Additional Recognized Best Practices for System Development

In July 2007, MCPS began implementing a new financial management system (FMS) for financial operations and reporting, including general ledger, accounts payable and accounts receivable. FMS implementation began in July 2006 with an original contract cost of \$6.7 million for programming and implementation and \$2.4 million for purchasing hardware and commercial off-the-shelf software. As of May 2008, these contracts had been amended to a total of \$10.6 million and actual contract expenditures per agency records totaled \$10.5 million.

Although MCPS initiated the use of the system on time, it did not use certain system development best practices⁶ to ensure successful project implementation. Although these best practices will not necessarily guarantee a successful implementation (a project completed on time, on budget, and with the intended functionality), the more those best practices are used, the likelihood

⁶ The most widely accepted best practices in IT application development have been disseminated by the Standish Group International, Inc., a private industry leader in collecting and analyzing data on IT projects. These best practices are referred to as the Chaos 10. These best practices have resulted from a study of over 40,000 projects as well as interviews with executives, project managers, IT providers, and users.

of a successful outcome increases. Our review of the implementation process disclosed that MCPS followed certain of these best practices (such as having the support of executive personnel with the authority to obtain needed funding and resources and having an experienced project manager). However, other practices were not followed.

- Best practices specify that the upfront and continual involvement of the end users of any system is the most critical aspect for any application development project. Users must be involved from concept to final implementation and the application must be implemented on par with real users' capabilities and desires. Proper user involvement throughout a project typically significantly reduces the amount and extent of training needed when new systems are actually put into use.

While MCPS provided documentation of meetings between end users and the implementation team, the documentation did not substantiate sufficient end user involvement in designing system requirements and ensuring project functionality. For example, weekly progress reports prepared by the implementation team (which included few actual end users) were submitted only to the Chief Operation and Chief Information Officers. Furthermore, pilot sessions between the implementation vendor and end users only highlighted FMS capabilities instead of reviewing end user needs and expectations.

An external review of FMS implementation by a consultant that MCPS hired in May 2008, at a cost of \$22,700, noted that MCPS needed to "... evaluate how end users were actually using the application. For example: are end users looking for data in the right fields and forms, comparing related data, entering data properly – correct value ..." The review also indicated a need for additional staff training and noted that end users were often unaware of reporting capabilities and available reports. MCPS project staff also noted in April 2008 (10 months after implementation) that, while the vendor conducted "train-the-trainer" sessions, MCPS primary users received limited system training, resulting in users in various areas, such as grant accounting and public sector budgeting, not being comfortable

that they were using the new system properly and to its fullest capabilities.

- When MCPS determined that the functionality specified in the original contract would not be achieved, it modified the scope of the project without assessing the costs and benefits. Specifically, although FMS was to be used for budgeting purposes, MCPS determined during the implementation phase that the budget module would not interface with its existing human resources and payroll system. MCPS then eliminated this requirement from the contract deliverables; however, it did not reduce the contract costs for the deliverables that were eliminated. Instead, MCPS amended the contract, at an additional cost of \$1.2 million, to obtain several applications not specified in the original contract that MCPS believed would extend project functionality. This action was taken without formally evaluating the costs and benefits associated with the eliminated deliverables and the additional applications to determine whether MCPS received appropriate value.

Best practices state that project scope should be kept as focused as possible (known as “minimizing scope” within the Chaos 10 best practices) while still yielding a very useful end product.

In addition, MCPS did not ensure it received certain functionality specified in the amended contract. According to a report of system defects prepared by MCPS in April 2008, 95 implementation issues were identified that had not yet been corrected. Of these 95 issues, MCPS classified 15 of them as critical. For example, MCPS staff noted a number of significant reporting deficiencies. Subsequent to our audit, we were advised that functionality continues to be an issue and, to help address the problems, MCPS hired the aforementioned consultant at a contract cost of \$190,500.

Costs and Benefits of Outsourcing IT Maintenance and Implementation Need to Be Evaluated

The majority of ongoing IT maintenance and system implementation services are currently outsourced by MCPS. MCPS performs various IT functions with in-house resources, including training and

equipment replacement services. Although MCPS uses a competitive procurement process when contracting for IT services, it has not formally assessed the costs and benefits of continuing to contract for these services, rather than perform more IT functions internally. According to MCPS records, IT contract services requested for fiscal year 2009 totaled \$8.4 million, or 28 percent of the IT budget.

Recommendations

9. MCPS should implement appropriate security measures to safeguard its applications and data systems, including enhancing its IT security by establishing and enforcing stricter password requirements, logging all significant security-related events, and conducting documented reviews of logged system activity. MCPS should also improve controls over physical access to its computer room.
10. MCPS should use industry-recommended best practices for future IT development projects. Specifically, MCPS should ensure that users of new IT applications are sufficiently involved, that the cost benefits of contract modifications are formally assessed, and that full system functionality is achieved during the implementation phase.
11. MCPS should formally evaluate the extent of its outsourcing of ongoing IT services to ensure it is cost beneficial.

Chapter 7

Facilities Construction, Renovation, and Maintenance

MCPS has the a number of best practices to help reduce construction and maintenance costs for its facilities, including: (1) the use of a six-year Capital Improvement Plan (CIP) based on a comprehensive and public process to plan for construction and renovation of school facilities, (2) extensive use of relocatable classrooms to minimize new construction requirements, (3) a comprehensive energy management program, and (4) an annual survey process to solicit feedback from both customers and staff.

However, long-term planning could be improved because it did not include a periodic comprehensive assessment of the condition of school facilities and major mechanical systems. In addition, although it maintains a detailed and comprehensive work order system, MCPS did not make full use of it. For example, data from the system was not accumulated and analyzed to determine overall efficiencies or used as a tool for evaluating individual performance. Furthermore, the performance of preventive maintenance was not adequately documented.

Background

MCPS maintains 199 schools and a number of other facilities (such as administration and support offices) with a staff of approximately 1,650 custodial and maintenance personnel.

MCPS uses a six-year CIP to identify ongoing and projected needs for new buildings and major renovations. The annual CIP was developed using student demographic data and input from various sources, including public meetings, and was approved by the Board. In the fiscal year 2007 CIP, necessary major renovations, repairs, and systemic improvements to existing schools over the next six years were estimated to cost \$1.5 billion.

Table 2 below compares MCPS fiscal year 2006 plant costs (that is, maintenance and operational costs) with other similarly-sized school systems in Maryland. The table presents two cost measures used to assess plant costs—cost per student and cost per square foot. These statistics show that MCPS facilities operation and maintenance costs are in line with its peer group and its square footage per student is in line with other similarly-sized school systems.

Table 2 Plant Cost Comparison Per Student and Per Square Foot Fiscal Year 2006 (Unaudited)					
School System	Plant Costs			Square Footage Per Student	Total Gross Square Footage
	Total	Per Student ❶	Per Square Foot		
Montgomery Co.	\$125,854,615	\$904.96	\$6.15	147.2	20,466,878
Prince George's Co.	124,425,153	942.55	7.12	132.3	17,466,878
Baltimore Co.	94,015,905	878.55	6.08	144.6	15,472,933
Anne Arundel Co.	59,188,511	811.18	5.07	159.9	11,666,226
Baltimore City	83,176,509	1,001.09	4.54	220.3	18,301,832
Average of Comparable Schools	\$90,201,520	\$913.26	\$5.74	159.2	15,726,967

Sources: MSDE Financial Data, MSDE Fact Book, Maryland Public School Construction Square Footage Data

❶ - Based on Average Daily Enrollment 2005-2006

A Number of Best Practices Were in Place to Enhance the Effectiveness of the MCPS Facility Construction and Maintenance Department

MCPS has instituted several best practices to enhance project results and cost effectiveness in its facilities and maintenance department, beyond the previously noted six-year CIP:

- Use of a construction consultant to review building design and make appropriate cost savings suggestions prior to hiring general contractors. The purpose of this process is to keep change orders to a minimum.
- Use of various methods to reduce the need for additional construction. The periodic evaluation of space utilization included consideration of capacity, enrollment projections, redistricting students among schools, and the use of relocatable (portable) classrooms.
- Use of a comprehensive program for energy conservation and management. MCPS has instituted two programs (one of which dates back to 1991) to continually promote and reward a culture of conservation in the schools. MCPS also works with Montgomery County to identify measures to comply with countywide practices for resource conservation. As part of this process, MCPS has identified and implemented projects, including increased use of energy management systems and modifying lighting systems.
- Use of an annual survey of school based personnel for customer satisfaction of maintenance and repair services provided. Results are compared to previous years' data and staff are directed to provide feedback to both school based and administrative personnel.

Long-Term Planning Processes Could Be Improved

Long-term planning did not include a periodic comprehensive assessment of the condition of school facilities and major mechanical systems. MCPS developed a schedule for modernizing schools using a facility assessment tool, but has not used this

process since 1999. The State of Maryland Public School Construction Program (PSCP) performs annual inspections of selected schools throughout the State, but these inspections are not meant to be a substitute for periodic inspections by the school system. During fiscal years 2006 and 2007, PSCP had inspected 51 of MCPS' 199 schools. In a number of other school system audits, we noted that either staff conducted periodic facility assessments (such as bi-annually) or an outside vendor was contracted to perform a comprehensive facility survey.

These inspections provide specific details on the unique needs of facilities as they age and allow MCPS to incorporate preventive maintenance into their long-term planning that could delay or avoid the need for a large investment in new construction. The average age of the MCPS' 199 schools is 41 years, with 61 schools being more than 50 years old. MCPS advised us that, based on high costs of such assessments, annual facility assessments would not add value to long-term planning that is included in the CIP. However, it is significant to note that the applicable data in the CIP is based on previous inspections by MCPS, which are generally over eight years old.

Since the condition of all schools was not periodically assessed, there was a lack of documentation on the current condition, maintenance needs, and replacement backlog of HVAC systems, a major system component. Although HVAC replacements have been included in the most recent CIP, MCPS maintenance personnel advised that projects are often addressed on an emergency basis. MCPS was in the process of addressing the lack of centralized records on HVAC systems and expected to automate the care and replacement process for HVAC systems by the beginning of fiscal year 2010. Although MCPS estimated that deferred maintenance totaled \$34.2 million, this amount did not include costs associated with replacing HVAC systems.

The Work Order System Should Be Fully Used

Certain capabilities of the automated work order system were not used to control costs and assess performance –

MCPS did not fully use its automated work order system when assigning significant maintenance work and tracking the completion of assigned tasks to help it control costs and assess performance. We noted that, although all work orders along with information related to actual resources used to perform the task (that is, time and materials) are logged, no information was entered indicating resources expected to be used to perform the task, based on either past history or industry guidebooks. As a result, completed work orders could not be evaluated for efficiency or used to assess the performance of both individual employees and the entire Facility Construction and Maintenance 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. MCPS advised that they were in the process of developing such measures using the existing data.

In addition, work orders were often not completed timely. According to MCPS records, of 4,675 work orders open as of March 31, 2008, 3,257 (or 70 percent) were over 90 days old. For internal performance measurement purposes, MCPS utilizes a 15-day response time as the standard for routine (as opposed to shorter time frames for emergency and urgent) work orders.

Comprehensive preventive maintenance was not

adequately documented – A comprehensive preventive maintenance plan had been developed by MCPS, but the plan had not been updated since 1997. As a result, many of the procedures described were no longer relevant to current operations. For example, this manual has not been updated to include the current automated work order system. In addition, MCPS could not provide us with documentation that all required preventive maintenance had been completed since it did not use the current work order system to track required and performed preventive maintenance. Although periodic inspections of work are conducted by supervisors, this documentation was inconsistent and did not provide a record that all preventive maintenance required by the plan had been performed. MCPS was in the process of compiling preventive

maintenance information in the automated work order system so that work required and performed could be better tracked.

Recommendations

12. MCPS should establish a process to periodically assess the physical condition of its facilities, including all major systems, and use this information for planning purposes.
13. MCPS should maximize its use of the automated work order system so that actual costs can be compared to estimated costs for significant projects, and the productivity of staff can be measured. In addition, MCPS should update its preventive maintenance plan and use the work order system to track maintenance required and performed.

Chapter 8

Transportation Services

MCPS used a number of recognized best practices to increase student transportation efficiency, such as staggering school arrival and dismissal times to enable certain buses to perform multiple runs and assigning bus routes to drivers based on their proximity to the route to limit the number of deadhead miles (miles traveled with no students on the bus). Nevertheless, we noted areas where improvements could be made, such as addressing all appropriate factors for properly planning and developing bus routes (for example, student ride times and bus capacities), fully using its automated bus routing software, and implementing controls over fees charged for transportation services provided to non-MCPS entities.

Background

MCPS is the largest school system in Maryland and transports more students than any other school system in the State. Approximately 96,000 students, of which 5 percent are disabled, are eligible to ride each day on one of over 1,100 buses owned and operated by MCPS. Fiscal year 2007 pupil transportation operating costs totaled approximately \$92.7 million. Forty-eight percent of the 18.4 million reported route miles for the 2006-2007 school year represented mileage for transporting disabled students.

As seen in Table 3 below, the cost per rider is reasonable when compared with similarly-sized school systems; however, the cost per mile is higher than the average of similarly-sized school systems. According to MSDE Factbooks, MCPS transportation costs have

increased 29.5 percent since fiscal year 2005, significantly more than other similarly-sized systems. This increase is primarily attributable to salary and wage costs.

Table 3
Comparison of Transportation Costs per Rider and per Mile
Fiscal Year 2007 (Unaudited)

School System	Number of Eligible Riders		Miles (in thousands)		Expenditures (in thousands)	Average Annual Cost per	
	Non-Disabled	Disabled	Non-Disabled	Disabled		Rider	Mile
Montgomery Co.	90,560	5,151	9,604	8,798	\$92,691	\$968	\$5.04
Prince George's Co.	83,246	5,323	12,445	8,475	107,137	1,210	5.12
Anne Arundel Co.	53,512	1,597	6,042	3,535	36,231	657	3.78
Baltimore Co.	60,052	2,872	8,651	5,720	50,261	799	3.50
Average of Comparable Schools	65,603	3,264	9,046	5,910	\$64,543	\$937	\$4.32

Sources: MSDE 2006-2007 Fact Book

Several Best Practices Were in Place to Enhance Bus Route Efficiency and to Control Related Costs

The MCPS transportation department had numerous practices in place to help reduce student transportation costs:

- Staggering school arrival and dismissal times to enable certain buses to perform multiple runs on the same day, thereby reducing the need for MCPS to obtain additional buses.
- Assigning bus routes to drivers based on their proximity to the routes to reduce the amount of miles driven with no students on the bus (deadhead miles).
- Using central collection locations and transfer stops for regional programs and magnet schools to minimize the number of bus trips and stops.
- Using smaller buses for special education routes, which generally carry only a few students at a time. Smaller buses are less costly to purchase and generally less costly to operate.
- Piggybacking with other governmental units to purchase fuel.

Policies and Practices for Planning and Revising Bus Routes Should Be Enhanced

Current bus route scheduling policies do not include all appropriate factors necessary to properly plan bus routes. For example, current policies do not address maximum student ride times or set bus capacity limits.

Also, automated routing information was not correlated with actual ridership counts and, as a result, did not provide assurance that buses were being used in the most efficient manner. The automated system showed that approximately 90,000 students rode MCPS buses, but the load manifests of actual ridership (completed by the bus drivers in the winter of 2007/2008) showed that only 71,000 students actually rode MCPS buses on the day of the count. In February 2008, the automated routing system showed that, for many routes, the number of students eligible to ride a specific bus significantly exceeded that route's capacity. For example, of MCPS's 1,866 bus routes, the automated routing system showed that 390 routes were each over capacity by more than 20 students, which could indicate that the buses on those routes, as planned, were overcrowded. Conversely, the load manifests showed 119 routes each with less than 32 actual riders, well below MCPS' lowest desired capacity (a minimum of 40 students).

The full capabilities of MCPS' system routing software, to establish efficient routes on a system-wide basis, were not utilized. Instead, MCPS relied on school administrators and bus drivers to notify the Transportation Department of specific problems with existing bus routes for which subsequent adjustments were made. Efforts to improve overall route efficiency were limited to an annual planning procedure which merely incorporated new students into already established bus routes. MCPS used the routing software primarily to visually show current bus routes as an aid to manually developing new routes and changing existing routes. The system also was not being updated for current student enrollment data, which would be needed to effectively run the routing software. We were informed

that, as of February 2008, current student enrollment data, including address changes, had not been uploaded since November 2007. During that period, 2,566 student records had been modified.

The ability to fully use the automated routing software was hindered by certain policy decisions. Since MCPS policies do not require students to ride a specific bus route, the MCPS Transportation Department has difficulty using the available data to accurately estimate the actual ridership on a bus, to plan appropriately, and to determine the cost impact. This policy forces personnel from the Transportation Department to correct problems reactively without necessarily ensuring the most efficient solution is found. Moreover, not assigning a student to a specific bus route creates a safety concern since MCPS may not readily be able to determine the location of a particular student. In other school systems, we have noted that students are assigned a specific bus route, which allows, among other things, bus route planning to be more efficient.

Controls Over Transportation-Related Accounts Receivable Should Be Improved

Controls over accounts receivable and the related collections processed by the Transportation Department were not adequate. Specifically, MCPS had no written procedures to control processing and collection of amounts billed to non-school entities (such as county recreation programs). Billings for these services totaled \$780,000 for the period from July 2006 to February 2008. We noted the following conditions:

- The employee responsible for receiving cash receipts and preparing the deposit also had access to the related accounts receivable records. As a result, funds could be misappropriated without detection.
- Receipts were not processed timely. Our test of 10 field trip charges, totaling approximately \$45,500, disclosed that the collections applicable to 8 of these charges were not recorded into the accounting records for periods ranging from 4 to 23 days following transfer to the central accounting office by the Transportation Department. Based on available records, we

could not readily determine when receipts were first received by the Transportation Department. These 10 field trips were properly billed and recorded in the Transportation Department's automated accounts receivable records and the related payments were deposited intact.

- Checks were not immediately restrictively endorsed 'for deposit only' or recorded in a mail log.
- The Controller's Office did not provide the Transportation Department with any verification that receipts forwarded by that Department were deposited. (See Chapter 1)

Recommendations

14. MCPS should enhance existing policies to address all appropriate factors that impact bus routing, such as bus loads. MCPS should also use the automated routing software in conjunction with other relevant information to help improve the efficiency of bus routes. In this regard, MCPS should consider changing its policy by requiring students to ride a specific bus route.
15. MCPS should develop specific procedures that establish adequate controls over the Transportation Department's accounts receivable and the processing of related collections.

Chapter 9

Food Services Operations

MCPS has implemented a number of best practices to help reduce food service costs, such as preparing meals for all schools at a central location, using performance measures, and participating in the United States Department of Agriculture (USDA) commodity program. MCPS also has adequate procedures in place to identify students eligible for free and reduced-price meals under the federal national school meals programs. However, MCPS needs to improve internal controls over the processing of cash receipts.

Background

MCPS has one central location that prepares all meals for its 199 schools. Although the MCPS food service operation is intended to be self sustaining, it operated at a loss in fiscal year 2007; MCPS has taken certain actions in an attempt to correct this situation. See Table 4 on the next page for information regarding fiscal year 2007 food services.

Table 4
Food Service Facts for Fiscal Year 2007

Average Cost per Meal **\$ 2.83**

Number of Meals Served:

Breakfast	Paid	625,268	1,881,714
	Free	968,107	
	Reduced Price	288,339	
Lunch	Paid	4,911,112	9,442,495
	Free	3,257,059	
	Reduced Price	1,274,324	
Ala carte Sales			3,129,110
Snacks			21,303
Summer Meals			206,783
Non-School Meals			212,752
Total Meals Served			<u>14,894,157</u>

Schools	199
Kitchens	1
Full-time employees	602

Revenues:

Federal	Cash payments	\$15,717,693	\$17,781,124
	USDA Commodities	2,063,431	
Sales and other sources			22,895,402
State aid			1,017,320
Total Revenue (all sources)			\$41,693,846
Total Expenditures			<u>42,145,103</u>
Excess of Expenditures over Revenues			<u>\$ (451,257)</u>

Sources: MSDE 2007 Data and MCPS Fiscal Year 2007 Audited Financial Statements.

Certain Best Practices Were in Place

MCPS has implemented several practices to contain food

services costs – These measures helped to both increase operational efficiency and reduce food supply and material costs.

- MCPS used a Central Production Facility to prepare the meals for its 199 schools. On a daily basis, these prepared meals were delivered to the schools, where they are reheated.
- MCPS used performance data, such as meals per labor hour, inventory turnover, and satisfaction surveys to track and monitor the operating efficiency at each of its school cafeterias. In addition, MCPS periodically reviewed the financial results of its food services operation and took appropriate actions (such as increasing meal prices) after it incurred a loss for fiscal year 2007.
- MCPS participated in the USDA commodities free food program. Per MCPS records, \$2.1 million in USDA commodities were received in fiscal year 2007.
- MCPS used standard serving sizes and recipes to economize on food purchases, as well as monitoring waste and reheating items where possible to reduce waste.

MCPS used several best practices to encourage

participation in the national school meals programs – Best practices used by MCPS include the use of a family application process—instead of individual student applications—to simultaneously qualify more students for the programs, and the use of a keypad system in cafeterias to eliminate the easy identification (and any perceived stigma) of students in the free and reduced-price meal programs. For fiscal year 2007, over 73 percent of MCPS students eligible to receive free and reduced price lunches actually participated in the program, which was commensurate with other school systems audited.

Controls Over Food Service Cash Operations Need Improvement

The internal controls over certain transactions processed by cafeterias were not adequate. Specifically, MCPS' written cash handling procedures allow cashiers to both deposit funds to a student's cafeteria account (that is, up to \$10 for a secondary school student and up to \$5 for an elementary school student) and record a meal purchase in the same transaction. In addition, cashiers can void transactions. However, for voids involving these combined transactions, the respective managers did not retain supporting documentation or justification to explain these adjustments. Without adequate supporting documentation, MCPS is unable to determine which part of the transaction—the deposit or the purchase—was incorrect, or whether the void transaction was proper. According to MCPS staff, void transactions processed from September 1, 2007 through March 31, 2008 totaled \$251,800.

Recommendation

16. MCPS should improve controls over its cash receipts processing. Specifically, MCPS should require that adequate documentation be retained to support all voided transactions.

Chapter 10

School Board Operations and Oversight

Oversight of MCPS operations includes a comprehensive budget process. The Board also receives financial updates, including monthly budget variances, to assist it in monitoring the efficient use of funds as well as performance indicators for financial and academic operations. The Board has adopted a detailed ethics policy. Annually, the Board meets with the MCPS certified public accounting firm to review the results of the annual financial statement and the federal Single Audits. Also, MCPS has an internal audit department and the Board has an active audit committee.

Several opportunities exist for the Board to improve operations and oversight. For example, the Board should consider expanding the work of its internal auditor into areas beyond student activity funds. Also, consideration should be given to establishing a confidential hotline to enable employees and others to report operational concerns and suspected fraud, waste, and mismanagement.

Background

MCPS is governed by a seven-member board elected by the voters of Montgomery County. The Board generally operates several committees (such as Policy and Audit). To assist in oversight, the Board contracts for independent audits of the MCPS financial statements and federal programs, has an internal audit department, and receives regular updates from MCPS management personnel on a broad range of financial, administrative, and academic topics. The Board is ultimately accountable for the success of MCPS in

providing the children of Montgomery County with a quality education, while wisely spending local, State, and federal funds. Following is the MCPS stated policy on educational philosophy:

Vision

A high-quality education is the fundamental right of every child. All children will receive the respect, encouragement, and opportunities they need to build the knowledge, skills, and attitudes to be successful, contributing members of a global society.

Mission

To provide leadership and oversight for a high quality educational system with community-supported goals, policies, and resources committed to benefit our growing and diverse student population.

System Goals

- Ensure success for every student
- Provide an effective instructional program
- Strengthen productive partnerships for education
- Create a positive work environment in a self-renewing organization

Source: www.MCPS.org

Certain Oversight Had Been Put in Place Regarding MCPS Operations

The Board uses a number of methods to oversee the operations of MCPS

- The Board is actively involved in the development of the budget, including public work sessions. As part of the budget process, the Board receives and reviews performance measures for each MCPS department.

- The Board receives monthly expenditure data, including budget variances, and is provided with financial updates, including information such as projections of financial activity, by MCPS personnel.
- The Board hires 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.

A detailed ethics policy has been established – The MCPS Board has adopted a detailed conflict of interest policy that covers Board members as well as all MCPS employees, and specifically identifies those supervisory employees (including certain employees with procurement responsibility) required to file annual financial disclosure statements. This policy also covers conflicts of interest and conforms to State law. MCPS maintains an Ethics Panel (composed of three persons not affiliated with MCPS and appointed by the Board) to interpret ethics policies and provide advice on policy implementation. The Panel also reviews and rules on any reported complaints of ethics violations. We reviewed the related statements for calendar year 2007. All persons required to file disclosure statements did so, and our review did not disclose any issues of potential audit significance.

The Board Should Consider Additional Steps to Assist It in Governing MCPS

MCPS internal auditor's work should be expanded to include areas beyond student activity funds and that unit should be made more independent – Although MCPS has an internal audit unit and an active Board audit committee that oversees the work of the auditor (both of which are deemed best practices), the scope of the auditor's work should be expanded to include more significant areas within MCPS. Approximately 80 percent of the unit's work plans for fiscal year 2007 and 2008 were allocated to performing audits of student activity funds. Although there are unique risks associated with student activity funds, which are not always subject to review by other auditors, the dollar amounts involved are not as significant as with other MCPS

operations, such as payroll, procurements, and disbursements, which should be regularly reviewed by the internal auditor. Student activity fund expenditures totaled \$37 million, while MCPS expenditures totaled \$2.19 billion for fiscal year 2007 per audited financial statements.

In addition, the unit does not organizationally report directly to the Board or its audit committee as a means to promote audit independence. Instead, the unit reports to the Superintendent through the Chief Operating Officer. We further found that the unit only rarely presents its findings formally to the audit committee. Our review of audit committee meeting minutes for the period from November 2005 to July 2007 disclosed that the unit presented findings at only one meeting. Subsequent to the audit, MCPS provided us with documentation that the audit committee reviewed and approved the fiscal year 2009 audit plan and indicated that it would review future internal audit results, and include appropriate comments in the minutes of its meetings.

The MCPS Board should consider establishing a confidential hotline — MCPS had not established a process, such as a confidential hotline, to enable employees and others to confidentially report operational concerns and suspected fraud, waste, and mismanagement. While the Montgomery County Office of the Inspector General had a county-wide hotline, this Office has no authority to investigate allegations involving MCPS. Current Board policy requires employees to report suspected incidents, preferably in writing, through existing supervisory channels. However, routing such matters through intermediary parties could result in allegations not being properly handled. Typically, confidential mechanisms bring to light matters and issues previously unknown and unsuspected by organizational managers. If such a process was established, in conjunction with the establishment of a whistleblower policy, the internal audit unit could conduct the initial reviews of information received via the hotline or direct the information to other appropriate officials, such as law enforcement.

Recommendation

17. The Board should consider expanding the scope of the internal auditor unit's work and should require the unit to organizationally report directly to the Board's audit committee. In addition, the Board should consider the feasibility of establishing a confidential hotline, with formal follow-up procedures and an employee whistleblower protection policy.

Chapter 11

Other Financial Controls

This chapter addresses the management of risk, cash, and debt (for example, long-term lease-leaseback agreements) within MCPS. While MCPS had procedures in place to govern its risk and cash management for certain types of investments, it did not have written policies governing its use of long-term liabilities, such as lease agreements. In addition, MCPS had not taken certain actions to verify the propriety of health care costs.

Risk Management Best Practices Were in Place

MCPS used a combination of commercial insurance and self-insurance to manage its risks. MCPS insured its liability, property, and workers' compensation coverage through participation in the Montgomery County Liability and Property Coverage Self Insurance Program. The notes to the fiscal year 2007 audited financial statements stated that settled claims had not exceeded coverage in any of the past three fiscal years.

To reduce its workers' compensation costs, MCPS contracted with a loss prevention firm to analyze claims data. MCPS used this data to develop accident investigation and safety training for departments identified as having a history of high-dollar losses. MCPS also established a Case Management Team that reviews individual cases and employee return-to-work schedules. The Team has the discretion to temporarily assign employees to light duty tasks to speed up their return to the same pre-injury work schedule.

Capital Lease and Cash Management Policies Need to Be Established

MCPS had not adopted a policy to govern its use of long-term lease obligations to finance operations. Long-term liability levels and their related annual costs are important obligations that must be managed within available resources. An effective policy should provide guidelines to ensure MCPS manages its long-term liabilities accordingly. By law, MCPS is not authorized to issue bonds or similar debt instruments to finance capital or operational needs. However, MCPS used capital leases to purchase equipment such as buses and computer hardware. According to MCPS audited financial statements, capital lease payments through 2012 had a present value of \$45.9 million at June 30, 2007, with \$19.5 million due within one year.

Although MCPS had cash management policies for areas such as the pension trust and student activity funds, it did not have a policy for investing excess cash from routine operations. Cash and investments from governmental activities totaled \$50.2 million as of June 30, 2007. The notes to the fiscal year 2007 audited financial statements indicate that MCPS' deposits had been sufficiently collateralized so that the deposits were not subject to custodial or credit risk.

Policies to govern the use of long-term obligations to finance operations and manage cash and investments are recommended by the Government Finance Officers Association.

MCPS Should Take Additional Steps to Control Health Care Costs

Although MCPS had implemented certain practices designed to control health care cost (such as procuring medical and prescription services under cooperative arrangements), it had not taken certain substantive actions to control costs. Specifically, MCPS did not verify the eligibility of program participants and their listed dependents or audit the propriety of claims paid by program administrators. MCPS provides health benefit coverage to active and retired employees through a program self-insured by the

Employee Benefit Plan Trust Fund (in conjunction with Montgomery County and several other local government units). MCPS paid approximately \$175.8 million in claim payments for 57,000 employees, retirees, and their dependents during fiscal year 2007.

Recommendations

18. MCPS should adopt formal policies governing long-term obligations and cash management.
19. MCPS should enhance its procedures to verify health care costs by ensuring the eligibility of program participants and the propriety of paid claims.

Audit Scope, Objectives, and Methodology

Scope

We conducted a performance audit to evaluate the effectiveness and efficiency of the financial management practices of the Montgomery County Public Schools (MCPS). We conducted this audit under the authority of the State Government Article, Section 2-1220(e) of the Annotated Code of Maryland and performed it in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Objectives

We had two broad audit objectives:

1. To evaluate whether the MCPS procedures and controls were effective in accounting for and safeguarding its assets
2. To evaluate whether the MCPS 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 and 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 MCPS 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 MCPS. We also interviewed personnel at MCPS, the Maryland State Department of Education (MSDE), and staff at other local school systems in Maryland (as appropriate⁷). Our audit procedures included inspections of documents and records, and observations of MCPS 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, 2006 through December 31, 2007. For our audit work on revenue and federal grants, we primarily relied on the results of independent audits of fiscal year 2006 and 2007 activity.

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. We also used certain statistical data—including financial and operational—compiled by MSDE from various informational reports submitted by the Maryland local school systems. This information was used in this audit report for background or informational purposes, and was deemed reasonable. For comparison purposes, information provided in this report was generally limited to those Maryland school systems of similar sizes, based on student enrollment and/or system budget.

⁷ During the course of the audit it was necessary to contact other systems to identify policies or practices for comparative purposes and analysis.

In many cases, this information was self-reported by the school systems. The data were neither audited nor independently verified by us. Finally, information provided in this report was obtained from various reports readily available during our fieldwork.

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 MCPS, the results of other auditors 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 Comprehensive 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 reported results of the independent federal grants audits of the MCPS federal financial assistance programs for the evaluation of internal controls and for compliance with federal laws and regulations and of the MCPS financial statement audits. 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

MCPS 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 MCPS that did not warrant inclusion in this report.

Fieldwork and MCPS Responses

We conducted our fieldwork from November 2007 to July 2008. The MCPS response to our findings and recommendations is included as an appendix to this report.

APPENDIX



MONTGOMERY COUNTY PUBLIC SCHOOLS
MARYLAND
www.montgomeryschoolsmd.org

January 12, 2009

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

Dear Mr. Myers:

The response to recommendations made in the Financial Management Practices Audit Report that was issued for Montgomery County Public Schools in December 2008 is enclosed. In addition, an electronic copy was sent to you on January 12, 2009.

We would like to thank the legislative auditors for helping us identify several areas where we can improve our system's performance and efficiency. Staff appreciated the level of professionalism demonstrated by the auditors throughout the audit process. In addition, we appreciate the recommendations, as well as the recognition of best practices within our organization.

Please do not hesitate to contact Mr. Larry A. Bowers, chief operating officer, at 301-279-3626 if you have any questions or need additional information regarding this submission.

Respectfully,

Jerry D. Weast, Ed.D.
Superintendent of Schools

JDW:vnb

Enclosure

Copy to:

Members of the Board of Education
Mr. Bowers

Office of the Superintendent of Schools

850 Hungerford Drive, Room 122 ♦ Rockville, Maryland 20850 ♦ 301-279-3381

Legislative Audit

Recommendation 1

MCPS should establish procedures for collections received at locations other than the controller's office to ensure that these funds are accounted for.

Response

We agree with this recommendation. The Department of Financial Services has developed written procedures that require individual departments to record receipts immediately upon receipt, restrictively endorse checks immediately, and maintain a chain of custody. Appropriate staff in all departments that handle receipts will receive training on these procedures during FY 2009. Stamps for restrictive endorsements have been provided to departments that were not using them. The Department of Transportation, where this issue was identified, has instituted a log of receipts, immediate restrictive endorsement, and a chain of custody process.

Recommendation 2

MCPS should develop policies and procedures governing accounts receivable, including a formal debt collection policy. The policies and procedures should address the proper segregation of duties and progressive collection steps to be performed to pursue outstanding accounts. In addition, non-cash credit adjustments should be approved by independent supervisory personnel.

Response

We agree that Montgomery County Public Schools (MCPS) departments and divisions that have responsibilities for billing and receiving payments should have formal, written guidelines and procedures established concerning their accounts receivable processes. The Department of Financial Services will assist these departments and divisions with their procedures and have them completed by the end of FY 2009. In addition, MCPS will formalize the guidelines for debt collection and will build in a monitoring process to ensure the timeliness of the follow-up to unpaid receivables. MCPS will provide proper segregation of duties in its procedures.

Each department that produces receivables will have its own procedures based on the nature of the billing generated by the department. Receivables are generated in a number of offices for a variety of reasons. Receivables may be for nonresident tuition charged to parents for students who live outside the county or for rental of a school bus by a day care center. Receivables also may be the result of the legislative requirement that teachers be advanced all leave at the start of the year but may leave MCPS prior to earning the leave. Receivables may be bills for health care premiums for employees on unpaid leave or retirees whose pension benefits do not cover their insurance premiums.

Each department's procedures are designed to maximize collection prior to the collection process within the Division of Controller. Typically, the local departmental procedures are most effective. If payment is not made, the service being provided, that the debtor wants to continue,

will be discontinued. For example, in the case of nonpayment of insurance premiums, the individual is notified and coverage is cancelled for nonpayment. These collection procedures precede the procedures followed by the Division of Controller. Although the Division of Controller had a formal debt collection process, it was not being followed during the period of the audit. The monitoring process that will be developed will ensure this does not happen in the future.

MCPS agrees in part to the recommendation about noncash credit adjustments being approved by independent supervisory personnel. Currently, audit adjustments over certain amounts are approved by independent supervisory personnel. MCPS documents all adjustments made to accounts through the accounts receivable workflow in the Financial Management System. Receivable adjustments of \$5,000 or more, credit memos of \$2,500 or more, and receipt write-offs of \$500 or more require separate documented approval of the controller. Adjustments exceeding stated limits cannot be processed without approval, and all approvals are permanently documented. These limits are reasonable and prudent for an operation the size of MCPS, and we do not agree that all adjustments need to be approved by supervisory personnel.

Recommendation 3

MCPS should ensure that all costs associated with providing Medicaid-subsidized services are recovered. MCPS should also verify that billings received from the third party administrator are accurate.

Response

We agree with this recommendation. MCPS is instituting a practice, beginning in January 2009, to verify the accuracy and completeness of claims submitted by the third party biller by surveying 50 random Medicaid eligible students, as defined and identified by the Maryland State Department of Health and Mental Hygiene and the Maryland State Department of Education, for a quarterly fiscal reconciliation. Each quarterly review of 50 students will manually track and reconcile a complete Medicaid-subsidized billing cycle of services recommended, services provided, services billed, and services paid to ensure that all costs are recovered. MCPS has worked with the third party vendor to improve billing transparency and accounting practices through additional reporting, documented communication with MCPS, and enhanced/refined edit processing for Medicaid-subsidized services.

Recommendation 4

MCPS should enhance its policies and controls over its credit cards and transactions. MCPS should also ensure that the credit card manual includes clarification regarding the appropriate uses of credit cards. Furthermore, MCPS should review past credit card charges for propriety and recover any inappropriate charges.

Response

We agree with the recommendation concerning the segregation of duties in the ordering, receiving, and distribution of our procurement credit cards. The duties of ordering new credit cards and the initial receipt and distribution of the cards were segregated before the conclusion of this audit. Although all account managers and card holders have received required training on their responsibilities regarding transaction documentation, credit limit reviews, and approvals, additional reinforcement of these requirements is needed periodically. Therefore, a memorandum has been sent to managers and card holders reminding them of their responsibilities and requirements. The procurement card manual is currently under revision and will be distributed to all card holders by late January 2009.

We agree that all credit card charges should be reviewed for correctness and appropriateness. Each month the Division of Controller and the Division of Procurement will conduct the review to ensure compliance.

MCPS does not agree with the findings concerning the purchase of food and the use of vendors that may not have an obvious relationship with the mission of MCPS. Due to the breadth of our educational programs, we purchase food for Hospitality programs that provide catering, Family and Consumer Sciences classes, school-run stores, and a variety of items from entertainment supply stores that are purchased for the benefit of elementary students.

We also have a provision to provide up to \$800 for clothing or assistance to needy students. Due to the nature of these purchases, we will continue to stress with schools that expenditures in this area must be submitted to the community superintendent. Our Internal Audit Unit will continue to monitor and report schools exceeding the limits. If any inappropriate charges are discovered, those charges are handled and recovered according to the Board policies.

Recommendation 5

MCPS should ensure that all travel is approved in advance, in accordance with existing policy.

Response

We agree that all travel should be approved in advance and comply with Board of Education policies and MCPS regulations. MCPS requires preapproval of staff travel by the appropriate supervisor. Regulation DIE-RB, *Out-of-State Travel on Official Business*, was revised to require detailed receipts for all travel expenditures. Account managers and supervisors will be reminded of these requirements. In order to improve controls, MCPS will ensure that MCPS staff and Board of Education members' travel expenses continue to be well-documented as to the business purpose and nature of expenditures. Specific requirements for travel documentation are included in the Purchasing Card Agreement signed by senior staff and Board of Education members who are issued credit cards which may be used for travel.

Recommendation 6

MCPS should take the necessary corrective actions to ensure that adequate internal controls are in place over its automated human resources and payroll system. In addition, MCPS should segregate duties related to processing manual payroll checks. Finally, MCPS should establish an independent review and approval process.

Response

Although MCPS agrees that it would be ideal to limit the access of employees to only those functions they are required to perform as part of their job duties, this is not possible with the Human Resources Information System (HRIS) utilized by MCPS. The cost to develop this capability for this proprietary software would be prohibitive.

MCPS does not agree that duties related to processing manual payroll checks should be segregated. Only three people have the knowledge and skills to run the entire payroll process. To meet payroll deadlines, it is critical that only one person completes these tasks and activities. Their knowledge of the process is required to complete the complex data input and other system requirements to accurately pay and account for corrections in a timely manner. Since each transaction has an audit trail, someone other than the person who runs the payroll process verifies that the calculations and results are correct.

In order to respond to the intent of this recommendation, MCPS will implement by March 31, 2009, independent reviews of all changes to critical information. In addition, improvements to the segregation of duties for manual check processing will be implemented.

MCPS agrees with the establishment of an independent review and approval process. Since HRIS does not allow MCPS to provide authorization by transaction type (e.g., changing an individual's salary is one transaction and recording the date of a performance appraisal is another transaction), MCPS has implemented a review process to identify any individuals who are processing transactions outside of the scope of their assignment. All transactions processed during FY 2009 have been reviewed.

Recommendation 7

MCPS should use just-in-time ordering for routine materials and supplies to reduce the amount of on-hand materials and supplies.

Response

We agree with the auditors' recommendation to implement this best practice as soon as it is financially possible. The idea is that schools will receive supplies just when needed instead of storing them for later use. This systematic process was presented to the legislative auditors during their field work, and we are extremely pleased that they agree with the efficiency and effectiveness of this future program.

Recommendation 8

MCPS should improve controls over equipment and the related recordkeeping.

Response

We agree with this recommendation. With the recent implementation of the new Financial Management System, it is an appropriate time to revise our procedures for maintaining equipment inventory records. Effective January 2009, all monthly inventory records for new equipment will be validated for completeness and accuracy. Also, our internal auditors will add physical verifications of equipment to its procedures when they visit a school to conduct an audit.

Recommendation 9

MCPS should implement appropriate security measures to safeguard its applications and data systems, including enhancing its IT security by establishing and enforcing stricter password requirements, logging all significant security-related events, and conducting documented reviews of logged system activity. MCPS should also improve controls over physical access to its computer room.

Response

We agree with this recommendation. MCPS is aligning its security policies with the National Institute of Standards and Technology (NIST) Information Security Standards. To enforce these policies, MCPS is implementing the Oracle Identity and Access Management suite that enforces strong passwords, account lockouts, and password expirations for all MCPS staff. The estimated completion date for this implementation is September 2009. Passwords for high-privilege users, such as network and database administrators, are now changed every 45 days.

MCPS has instituted a formal security audit log review process for all IBM AIX servers. These logs run three times per day (once for each operator shift). A written log is maintained in the MCPS data center stating that process was run, the date and time, the person who ran it, and notes if any anomalies were found. If a security event occurs, it is reported to the appropriate system administrator who will initiate further investigation and facilitate resolution of the issue. MCPS is currently exploring and reviewing options to enable auditing subsystems across the AIX enterprise systems.

MCPS limits access to the computer room to individuals whose job responsibilities require such access. However, at the time of the audit, the access list had not been properly updated. MCPS reviewed and strengthened the process for updating the access card list to ensure it accurately reflects the individuals authorized to access the computer room. Since December 2007, MCPS has followed a process of verifying the accuracy of the access list weekly, using termination and transfer data reports from HRIS. An execution log of the weekly process is kept securely in the MCPS data center. This revised process will be formally documented in MCPS computer security procedures.

Recommendation 10

MCPS should use industry-recommended best practices for future IT development projects. Specifically, MCPS should ensure that users of new IT applications are sufficiently involved, that the cost benefits of contract modifications are formally assessed, and that full system functionality is achieved during the implementation phase.

Response

We agree with this recommendation that specifically addresses information about the implementation of the new MCPS Financial Management System (FMS). As a standard practice, MCPS uses cross-functional application development project teams to ensure that the users' requirements are identified and incorporated in all systems, where appropriate. Stakeholders are involved throughout the development and implementation of all new applications.

User requirements are prioritized and evaluated for design feasibility, benefit and usability, and process improvement impact. In the case of FMS implementation, several conference room pilots were held to gather a wide range of user input and feedback. During these structured, hands-on worksessions using the system, end users were able to critique and validate how the written requirements were translated into specified system features. This environment provided users with the opportunity to provide feedback on the usability of the product. In addition, every functional area had staff representation on the project team, including a functional manager.

By choosing an established vendor for implementing FMS, with a proven track record of successfully implementing the Oracle Financial suite, and contracting a separate industry leader to work with district staff to develop the system requirements and scope of work, MCPS took appropriate, industry-standard steps to ensure that the implementation was successful. The limited number of contract modifications was thoroughly assessed for the benefit of the requested modifications and the cost.

During the evaluation of the Requests for Proposal for the FMS, both the grant accounting and public sector budgeting modules were judged to meet MCPS requirements. During implementation, however, MCPS discovered these modules would not satisfy MCPS requirements. The funds originally earmarked to support the implementation of the budget module were reassigned to higher priority tasks. MCPS is currently negotiating with the vendor to replace the original budgeting module with a module with the functionality that meets the school system's requirements.

Recommendation 11

MCPS should formally evaluate the extent of its outsourcing of ongoing IT services to ensure it is cost beneficial.

Response

We agree with this recommendation. MCPS evaluates on a case-by-case basis, whether it has the resources internally to develop and maintain required systems. Systems such as FMS, that employs technologies new to MCPS staff and is designed to combine many legacy systems, required outsourced implementation services until additional MCPS IT staff is either hired or trained to support the specific off-the-shelf solution. MCPS IT resources for both development and support are limited. To develop all new systems internally would require significant new staffing in the application development area, which would then require hiring and retaining significantly more staff that would not be needed after the initial implementation period.

Of the \$8.4 million of contractual services in the MCPS IT budget, \$4.3 million fund mainframe and enterprise business systems licensing and business continuity and security services, \$3.2 million fund externally hosted instructional and assessment management systems, and less than \$900,000 supports external consultant services. Work is under way in MCPS to bring even more development efforts in-house.

Recommendation 12

MCPS should establish a process to periodically assess the physical condition of its facilities, including all major systems, and use this information for planning purposes.

Response

We do not agree with this recommendation. MCPS uses an extensive facilities assessment tool to prioritize the major modernization of its facilities. The Facilities Assessment with Criteria Testing (FACT) tool was developed in the early 1990s in cooperation with the state and others to evaluate facility condition and program capability for buildings in need of major modernizations. Comprehensive FACT assessments are very costly to conduct. To be accurate and of value, an assessment team must be staffed with professional architects and engineers and cost between \$5,000 and \$15,000 per building. To do this biannually for every building, as suggested in the audit, would cost MCPS at least \$1 million per year. We do not believe the benefit would justify the cost.

In the early to mid-1990s, MCPS conducted a large number of FACT assessments and established a priority list for modernizations that is still being used today. For stability in long-range planning, the prioritized list of modernization projects has remained unchanged since it was established in 1992 and appended in 1996. Additional FACT assessments may be needed in the next few years to extend the priority list for future modernizations. However, to periodically assess all MCPS facilities would be cost prohibitive and would disrupt long-range planning if scheduled modernizations were reordered every year or even every few years based on changing FACT scores.

Staff is reviewing the possibility of utilizing the MCPS facility asset management system completed in August 2008 to develop a facility assessment index. We believe this would more appropriately address the concerns of the auditors. Over the past two years, facility asset

inventory information was collected and entered into Maximo as part of the asset management system. With this information, staff can develop criteria and a scoring system to produce a facility index for all schools in the Maximo database. Based on a range of index scores, schools can be rated on a scale from excellent to poor. MCPS may incorporate the index into its FY 2011 Educational Facilities Master Plan submission to the Interagency Committee for Public School Construction. We believe that this indexing method will satisfy the intent of the recommendation for a comprehensive assessment of school property and equipment without the need for expensive FACT assessments for every school.

Recommendation 13

MCPS should maximize its use of the automated work order system so that actual costs can be compared to estimated costs for significant projects, and the productivity of staff can be measured. In addition, MCPS should update its preventive maintenance plan and use the work order system to track maintenance required and performed.

Response

MCPS agrees with this recommendation and is in the process of developing such measures using the data in its Maximo work order system. MCPS expects to have cost and productivity data reporting for all of its Division of Maintenance depots by the end of December 2009. The next phase of the Maximo system to be implemented is the ability to track required and completed preventive maintenance work orders. If funding is approved, the preventive maintenance work order system will be implemented by the end of FY 2010.

Recommendation 14

MCPS should enhance existing policies to address all appropriate factors that impact bus routing. MCPS should also use the automated routing software in conjunction with other relevant information to help improve the efficiency of bus routes. In this regard, MCPS should consider changing its policy by requiring students to ride a specific bus route.

Response

MCPS agrees and is committed to addressing all factors that will improve the efficiency of bus routes. The Department of Transportation utilizes an annual process of reviewing all routes. This process requires depot supervisors and routers to analyze all regular education bus routes for safety and efficiency. All factors contributing to safety and route efficiency are considered, including student load, mileage, ride time, and stop locations. Information is obtained from a variety of sources, including the computer assisted routing program, MapNet. As these factors are considered, recommendations for safety and efficiency improvements are formulated. Following this process at the depot level, the depot and routing staff are required to present review results to a panel consisting of the director, assistant director, and bus operations manager. When recommended route improvements are approved by the department director, a timeline for implementation is established. A study is under way to determine if this process would be effective in reviewing special education bus routes.

We do not agree with the recommendation that students should be required to ride a specific bus route. The Department of Transportation has previously considered assigning students to specific routes and stops, but has rejected this idea. Accurately assigning students to specific stops would require maintaining data on the pick-up and drop-off address. MCPS has experience doing this with special education students, where students are assigned to specific stops. This is a very labor intensive process. In addition, changes to initial student information are received for 50 percent of the students on an annual basis. In regular education, it is much more efficient to publish stop locations and allow students to use the stop that works best for them. In addition, assigning students to a specific stop is not possible since we do not know about day care arrangements or other places students may be before or after school. One variable that is not known until school starts is how many eligible bus riders will use some other form of transportation to get to and from school. Many parents drive students to school. Because this number is hard to predict, it sometimes leads to over- or under-loaded buses. Adjustments are made shortly after the school year starts. Allowing families to choose a bus stop accommodates family needs and provides greater customer service.¹

Recommendation 15

MCPS should implement adequate controls over billings and collections of fees charged for transportation services provided to non-MCPS entities, such as county recreational programs.

Response

MCPS agrees with this recommendation, and the Department of Transportation has segregated responsibilities for cash receipts from billing. The remittance address on the invoice prepared by the supervisor of the Field Trip Unit has been modified. Checks from non-MCPS entities are mailed to the fiscal specialist at the Department of Transportation's Shady Grove administrative office. The checks are logged in to a cash receipts spreadsheet and restrictively endorsed upon receipt. The fiscal specialist prepares a memo for deposit and forwards the checks and memo to the Division of Controller. The MCPS Department of Financial Services will develop a process to report deposits received by the Division of Controller so that deposits can be independently verified by the Department of Transportation, completing the process and ensuring appropriate controls are in place.

¹ **Auditor's Comment:** The desire to provide accommodating services is acknowledged. However, the additional costs to operate a mass transit-like service for students instead of routes with assigned student riders had not been determined by MCPS and reported to its Board for its consideration. The vast majority of local school systems in Maryland operate routes with assigned student riders due to student safety concerns and the efficiencies that can be gained by operating fewer routes and maximizing bus capacity based on predictable ridership levels.

Recommendation 16

MCPS should improve controls over its cash receipts processing.

Response

MCPS agrees with this recommendation. The Division of Food and Nutrition Services has updated cafeteria manager procedures to require that a report be printed showing all voided transactions. The cafeteria manager must then make handwritten notes on the report justifying the voided transactions and file the report with other daily reports. Internal audit procedures also have been modified to ensure that documentation for voided transactions has been completed.

Recommendation 17

The Board should consider expanding the scope of the internal auditor unit's work and should require the unit to organizationally report directly to the Board's audit committee. In addition, the Board should consider the feasibility of establishing a confidential hotline, with formal follow-up procedures and an employee whistleblower protection policy.

Response

MCPS agrees with the recommendation regarding the scope of the work of the Internal Audit Unit. During the current year, the Internal Audit Unit will conduct 7 payroll audits, 6 audits of professional leave use in schools, and 13 cafeteria audits. It also conducts inventory audits and, as indicated in the response to Recommendation 8, the unit will add the physical verification of equipment to its procedures. However, it is not possible to increase the number of audits as well as audit the work of the other MCPS units without the addition of at least one additional internal auditor. With the current fiscal situation and the priorities facing the Board of Education, it would not be possible to consider adding another auditor position at this time.

MCPS does not agree with the recommendation to have the Internal Audit Unit report directly to the Board of Education Fiscal Management Committee. The superintendent of schools has a fiduciary responsibility for all MCPS resources, including school independent activity funds, and is the person primarily responsible for the fiscal integrity of the school system. In order to accomplish this, he needs to have the Internal Audit Unit report to him rather than to the Board. Although there is a supervisor for this unit, the work of the auditors requires monitoring on a daily basis by an administrator at an appropriate level in the school system. This unit reports to the associate superintendent for shared accountability and the deputy superintendent of schools. It is critical that this supervision be provided to ensure that the unit is effective in its operation and addresses the fiduciary responsibility of the superintendent. Finally, the Internal Audit Unit often needs to work with other offices, such as the Office of Human Resources, the Office of the Chief Operating Officer, and the Department of Financial Services, in order to be effective. Separating the authority of this unit from the superintendent would result in the unit being less effective in these working relationships.

The Board of Education regularly receives many financial and operational audits in addition to the work of the Internal Audit Unit. These audits ensure financial and operational accountability to the Board of Education, the County Council, and the public. These regular audits include:

- An independent certified public accountant audits financial transactions.
- The Maryland State Department of Education audits a variety of areas, including enrollment, program administration, special education, teacher certification, criminal background checks of teachers, and grants monitoring.
- The federal government regularly provides mandated A-133 single audits of federal grant programs.
- The state Interagency Committee on Public School Construction audits the use of state construction funds.
- The county Office of Legislative Oversight conducts comprehensive budget reviews of MCPS programs each year.

MCPS also agrees with the suggestion of establishing a fraud and abuse hotline. Currently, the school system works with the county's inspector general's office that reports hotline issues involving MCPS to the chief operating officer of MCPS. We have pursued the acquisition of a fraud line for MCPS; however, as a result of the current fiscal situation, we have not contracted with any company. When the financial situation improves, it is our intent to do so.

Recommendation 18

MCPS should adopt formal policies governing long-term obligations and cash management.

Response

MCPS agrees that it needs to develop formal, written procedures regarding long-term obligations and cash management. MCPS currently has well-established practices that have been in place for a number of years. The Board of Education approved a resolution in 2004 concerning the use of a master lease to purchase some equipment and vehicles. This Board resolution includes the terms of the lease agreement as well as the amount. Amendments to this resolution have recently been reviewed by the Board's Fiscal Management Committee and approved by the Board of Education.

Recommendation 19

MCPS should enhance its procedures to verify health care costs by ensuring the eligibility of program participants and the propriety of paid claims.

Response

MCPS agrees with the recommendation to conduct a dependent eligibility audit. On December 9, 2008, the Board of Education awarded a contract for an audit that will be conducted during the remainder of FY 2009. MCPS also will explore conducting a claims audit. We will contact other organizations who have conducted such an audit to determine the costs and potential benefits. If we find from these organizations that the benefits exceeded the costs, we will move forward with issuing a request for proposals.

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