

STATE OF MAINE
DEPARTMENT OF AUDIT

66 STATE HOUSE STATION
AUGUSTA, MAINE 04333-0066

TEL: (207) 624-6250
FAX: (207) 624-6273



POLA A. BUCKLEY, CPA, CISA
STATE AUDITOR

MARY GINGROW-SHAW, CPA
DEPUTY STATE AUDITOR
MICHAEL J. POULIN, CIA
DIRECTOR OF AUDIT and ADMINISTRATION

August 20, 2013

8-22-13, PAB
Unit

Regional School Union 19
Kevin Bowman, Chairman of the School Board
P.O. Box 40
Newport, ME 04953

Dear Mr. Bowman:

As I am sure you are aware, the Department of Audit has been reviewing RSU 19 financial information for the period July 1, 2009 to March 31, 2013. We have completed our report and the superintendent's office has responded to our concerns in writing. These documents are attached to this letter.

Our report will be available on the Department of Audit website at <http://www.maine.gov/audit/reports.htm>, in the section for Other Reports.

We thank Superintendent Potter and Business Manager Nault for their assistance and their efforts to realign the financial structure of the RSU.

Sincerely,

A handwritten signature in cursive script that reads "Pola A. Buckley".

Pola A. Buckley, CPA, CISA
State Auditor

Enclosure

STATE OF MAINE
DEPARTMENT OF AUDIT

66 STATE HOUSE STATION
AUGUSTA, MAINE 04333-0066



POLA A. BUCKLEY, CPA, CISA
STATE AUDITOR

TEL: (207) 624-6250
FAX: (207) 624-6273

MARY GINGROW-SHAW, CPA
DEPUTY STATE AUDITOR
MICHAEL J. POULIN, CIA
DIRECTOR OF AUDIT and ADMINISTRATION

August 22, 2013

Regional School Unit 19
Kevin Bowman, Chairman of the School Board
P.O. Box 40
Newport, ME 04953

RE: Our Report Dated August 20, 2013

Dear Mr. Bowman:

I spoke to Brian Jellison this morning and he indicated that some participant(s) in last night's meeting had expected a statement in our report regarding fraud. As you know, our report did not make a statement about fraud.

The two auditors that were assigned to this engagement were given clear direction and repeated reminders to be absolutely on alert for fraud. I believe they were. We had a large sample size for invoice payments going back as far as FY11. The auditors assigned were not being rushed by management to get the job done quickly. Both auditors are certified, Brian as a Certified Internal Auditor, and Randy as a Certified Fraud Examiner and Certified Public Accountant. They are very conscientious and have conservative views on government spending.

We cannot provide absolute assurance that no fraud occurred since the RSU was formed. We use sampling methods to conduct our work. Absolutely nothing came to our attention that we thought was a fraudulent expenditure.

Thank you for your commitment to public service.

Sincerely,

A handwritten signature in black ink that reads "Pola A. Buckley". The signature is written in a cursive style with a long, sweeping underline.

Pola A. Buckley, CPA, CISA
State Auditor

cc. Greg Potter, School Superintendent
Jerry Nault, Business Manager

State of Maine
Department of Audit
Report On Regional School Unit # 19
Report Issued on August 20, 2013

Summary

The Department of Audit performed a limited procedures engagement of Regional School Unit (RSU) 19. This engagement pertained to fiscal years 2011, 2012, and 2013 through April 30, 2013. Our procedures included:

- determining the nature of RSU 19's financial difficulties,
- verifying, on a test basis, that expenditures were properly authorized and paid,
- testing the accuracy of accounts payables to determine whether all outstanding invoices had been properly recorded in the financial statements,
- testing controls for payroll expenditures,
- examining bank statements to ensure that they were properly reconciled to the general ledger, and
- other procedures as deemed necessary.

Our procedures identified the following areas of concern:

- significant errors related to the preparation of the school budget,
- significant billing errors involving local assessments to the towns,
- financial transactions that were not recorded in accordance with Generally Accepted Accounting Principles (GAAP),
- inadequate controls over payments,
- untimely payments to vendors, and
- inadequate controls over employee timesheets.

Background

RSU 19 was formed in 2009 by consolidating School Administrative Districts 38 and 48. State law pertaining to regional school units is contained in 20-A MRSA Chapter 103-A.

In May of 2013, RSU 19 received the proceeds of a \$2.8 million general obligation bond. The purpose of this long term debt was to provide funding for the repayment of a \$ 1.5 million revenue anticipation note that was due; and to pay-off other outstanding payables.

Procedures, Results, Conclusions, and Recommendations

Reconciliation of Bank Statements to the General Ledger

We examined RSU 19 bank reconciliations to ensure that reconciliations are performed on a timely basis, and that they are reconciled to the general ledger.

Based on our testing, it appears that RSU 19's bank reconciliations are performed on a timely basis, and reconciled to the general ledger.

Inadequate Accounting Procedures and Inaccurate Budgetary Data

For fiscal years 2010 through 2012, RSU 19's financial reporting and accounting procedures were inadequate and, as a result, did not provide accurate internal budgetary data.

After performing a review of RSU 19's accounting records, we determined that several factors contributed to the entity's negative financial position. To further illustrate this point, Table 1 shows a comparison of the entity's current assets to current liabilities, for fiscal years 2010 through 2012.

Table 1 - RSU 19's - Current Assets vs. Current Liabilities from the Statement of Net Assets			
	2010	2011	2012
Current Assets	2,710,354	1,408,104	471,185
Current Liabilities	2,394,977	2,560,628	3,822,508
Excess (deficit)	315,377	(1,152,524)	(3,351,323)

Table 1 above illustrates how much money and other current assets are on hand to pay current liabilities.

Table 1A is a comparison of actual revenues to actual expenses on an entity-wide basis (includes all funds), at June 30 for fiscal years 2010 thru 2012.

Table 1A - Actual Revenues vs. Actual Expenses from the Statement of Activities			
	2010	2011	2012
Revenues	29,414,322	26,363,167	26,035,759
Expenses	27,955,649	27,459,093	28,101,901
Excess (deficit)	1,458,673	(1,095,926)	(2,066,142)

Table 1B below is a comparison of actual revenues to actual expenditures for RSU 19's General Fund, as well as fund balances for fiscal years 2010 thru 2012.

Table 1B - Actual Revenues vs. Actual Expenditures (General Fund)			
	2010	2011	2012
Revenues	23,629,276	22,321,074	22,618,794
Expenditures *	23,363,339	23,087,239	24,702,694
Excess (deficit)	265,937	(766,165)	(2,083,900)
Fund balance - June 30	367,766	(565,154)**	(2,649,054)
* Includes net transfers			
** As restated			

We noted several reasons for RSU 19's negative financial position:

- **Lack of a merger settlement statement** - On July 1, 2009, SAD 38 and SAD 48 merged and formed RSU 19. At the time of the consolidation, SAD 48 failed to provide RSU 19 with a merger settlement statement that would have provided a detail of their financial position at June 30, 2009.

Title 20-A MRSA §1481-A and §1506 provides the basis for: (a) the distribution of reorganizational costs associated with the new regional school unit; and (b) the distribution of debt liabilities between the existing school units.

Further, SAD 38 financial statements for June 30, 2009, reported a positive fund balance of \$515,957 in their General Fund. Accounts payable was presented as \$128,862.

SAD 48 financial statements for the same period reported a negative fund balance of \$414,128. Accounts payable was presented as \$1,811,650.

At the time of the merger, funds provided by former SAD 48 towns were not sufficient to meet their respective share of liabilities and the negative fund balance. As a result, there was an inequitable distribution of liabilities between SAD 38 towns and SAD 48 towns.

- **Warrants not issued in accordance with statutory requirements** - Title 20-A MRSA §1486 and §1489, state that the regional unit school board must issue warrants to each municipality in a school district, based on the total amount of the articles adopted at the region-wide budget meeting.

For fiscal year 2012, warrants issued by RSU 19 to the towns were \$650,000 less than the local share as approved by the voters in the adopted school budget. It was noted that a similar situation occurred in fiscal years 2011 and 2013.

- **Actual General Fund expenditures exceeded budgeted General Fund expenditures** – Title 20-A MRSA §15690, provides the basis to be used by RSUs for budget authorizations.

In fiscal year 2012 actual expenditures exceeded budgeted expenditures by \$192,571.

- **Non-billing of local assessments** - RSU 19 did not have documentation to support the basis for allowing reductions to local assessments for fiscal years 2011 through 2013. These reductions (credits) totaled \$1,882,000. As a result, RSU 19 collected less revenue than the amount presented in the adopted budget. Table 2 shows local assessments according to the budget, the amount of credits applied to the assessments, and actual revenue collected.

	2010	2011	2012	2013
Assessments (per budget)	6,726,910	7,252,080	7,686,229	7,588,492
Less: Credits	-	(390,000)	(829,999)	(662,000)
Actual Revenue collected	6,726,910	6,862,080	6,856,230	6,929,492*

* Unaudited

In addition, in fiscal year 2012, RSU 19 did not bill towns for their full share of RSU 19's debt service. The total of debt service not collected, but paid by RSU 19 on behalf of the towns was \$ 363,000.

- **Budgeted expenditures exceeded budgeted revenues** - For fiscal years 2010 thru 2013, RSU 19's budgeted expenditures consistently exceeded budgeted revenues. Table 3 shows a comparison of budgeted revenues vs. budgeted expenditures.

	2010	2011	2012	2013
Revenues	21,957,640	20,508,040	21,860,534	21,892,688
Expenditures	22,323,399	21,238,040	22,610,790	23,496,296
Excess (deficit)	(365,759)	(730,000)	(750,256)	(1,603,608)

- **Budgetary preparation errors** – The RSU 19 General Fund budget for fiscal year 2012 indicated that \$830,000 from the prior year fund balance would be used to reduce the local share of town assessments. Since the prior year fund balance as restated was a negative \$565,154; the difference of \$1,395,154 was not available to reduce local assessments.

As a result, the 2012 budget included the use of \$1,395,154 that was not available to pay 2012 expenditures.

- **Financial transactions not recorded in accordance with GAAP** – For fiscal years 2010 through 2012, RSU 19 did not always record financial transactions in accordance with Generally Accepted Accounting Principles (GAAP). The effect of not complying with GAAP resulted in RSU 19's independent auditors making material adjustments to the financial statements.

We recommend that RSU 19's management take the following actions:

- Analyze the financial impact associated with the merger of SAD 38 and SAD 48 to ensure that all financial obligations associated with SAD 48 are properly assessed to the applicable towns, in accordance with the provisions of the RSU 19's Reorganizational Plan.
- Implement or strengthen budgetary controls to include:
 - issuing warrants to RSU 19's towns in accordance with articles passed at the region-wide budget meeting,
 - monitoring controls to identify variances between budget and actual amounts in order to implement corrective action, and
 - controls to ensure the accuracy of presented budgetary data.
- Implement a control process to ensure that financial transactions are recorded in accordance with GAAP.

Inadequate Internal Controls over Voucher Payments

We performed an examination of RSU 19 payment vouchers for fiscal years 2011 and 2012, and fiscal year 2013 through April 2013. Approximately 3,600 checks totaling \$9.6 million are issued each year. We examined a total of 230 voucher payments. We noted the following:

- During fiscal years 2011 and 2012, purchase orders were not approved on a consistent basis by authorized personnel. In addition, instances were noted where purchase orders were issued subsequent to the invoice date. Starting with the 2013 fiscal year, purchase orders were approved by the Superintendent's office prior to the purchase of goods or services.
- There was inadequate support for mileage reimbursements. Eight of thirteen reimbursement forms examined did not contain sufficient documentation to support the reimbursement.
- Invoices were not consistently approved by a supervisor prior to payment.
- Invoices were not consistently paid on a timely basis.
- Invoices were not always matched up to a purchase order and a receiving report; and then retained by the RSU 19's Business Office.

We reviewed the controls for processing and approving vendor contracts. Based on our testing, these controls appear to be properly designed and in place.

We recommend that RSU 19:

- implement procedures to ensure purchase orders are approved by the Business/Superintendent's Office prior to the purchase of goods or services,
- reimburse mileage and other travel expenses only if they have been properly approved and documented, and
- match the purchase order and receiving report up to the invoice prior to the payment being made.

Invoices Not Paid on a Timely Basis

As part of the voucher examination for fiscal years 2011 through 2013, we noted instances where payments to vendors were not submitted on a timely basis. The sample for 2011 and 2012 was drawn by randomly choosing five transactions for each month, and adding any unusual items. For fiscal year 2013 (through April 2013), we chose ten transactions randomly for each month. The chart below illustrates the number and percentages of late payments as compared to the sample size for the voucher test.

Payments in the Arrears			
Fiscal Year	No. Tested	No. Late	% Late
2011	68	8	12%
2012	62	7	11%
2013	100	42	42%
Total:	230	57	25%

An analysis of voucher payments made to Anthem Insurance for fiscal years 2011, 2012, and fiscal year 2013 (through April 2013), showed that payments were overdue from 30 to 90 days.

During fiscal year 2013, RSU 19 management negotiated a re-payment plan with some vendors to allow for an extension of payments beyond 30 days.

As of June 30, 2013, RSU 19 was current in regards to accounts payable.

In addition, RSU 19 does not maintain a subsidiary ledger for accounts payable. As part of the audit testing, we were unable to determine whether invoices that were not paid on a timely basis, were properly booked as accounts payable on RSU 19's financial statements.

We recommend that RSU 19 implement appropriate budgetary and monitoring controls to prevent future cashflow issues.

We also recommend that RSU 19 maintain an accounts payable subsidiary ledger to support the payable amount as reported on their financial statements.

Inadequate Controls over Timesheets

We examined forty payroll transactions for fiscal years 2011 and 2012, and fiscal year 2013 (through April 2013). Out of forty items examined, we noted the following:

- Time sheets for transportation garage employees are not signed by the employee; nor are they approved by a supervisor.

In all cases, the pay rate paid to an employee agreed with either the employee's contract or the stated hourly rate for the employee.

We recommend that RSU 19 implement controls to ensure that:

- Hourly employees certify their hours worked.
- All time cards and time sheets are properly approved by a supervisor.

Management's Responses and Corrective Action Plan - as written by RSU 19 personnel

Audit Finding: Inadequate Accounting Procedures and Inaccurate Budgetary Data

Management's Response: The Finance Committee has examined and discussed the provisions of the Reorganization Plan (the "Plan") and the financial transactions associated with the funds provided by MSAD 38 and MSAD 48, from the formation to the RSU to the present. The Committee has recommended that, consistent with the provisions of the Plan, the six former SAD 48 towns be assessed an amount which will provide funds to the former two former SAD 38 towns. The Board is expected to approve the recommendation and direct the Business Office to add the Plan related assessment to the fiscal year 2014 town notifications.

The Business Office has adopted a format for issuing warrants to towns which is consistent with the provisions of 20-A M RSA 15691-A, (1) and (2). Supplemental schedules are also provided to make town treasurers aware of the computations associated with the warrant development and town allocations.

The Business Office publishes "*Financial Highlights*" after each month's revenue and expense transactions are entered into the accounting system. The sheet compares revenue and expense budget to actual amounts as well as other information of a financial nature. The document is presented to the Finance Committee for their consideration, discussion, and reaction. The Superintendent and Business Manager may offer comments on the content including possible alternatives for corrective action should it be appropriate.

The Business Office has examined practices associated with recognizing and recording financial transactions in the course of operations. Changes have been made to recognize fiscal year-end transactions and assign these properly. Instructions have been provided to employees concerning best practices on "year-end close" procedures. These efforts will continue to be examined and changes made on an on-going basis.

Audit Finding: Inadequate Internal Controls over Voucher Payments

Management's Response: The RSU is examining procedures associated with all forms of procurement. In most instances purchase requisitions and purchase orders, components of the accounting system will continue to be used. In some instances it may be necessary to introduce new procedures involving the use of credit cards or other forms of electronic procurement. In all instances the emphasis will be on improving internal controls in the transactions.

The Business Office has designed and distributed new Business Mileage and Business Travel documentation forms. These are for universal use in the RSU replacing a host of ad hoc forms generated locally. Both forms are also electronically available to allow users a more convenient experience associated with completing the information. The forms allow entry of standardized trip documentation and approval.

The Business Office is examining various protocols by which it can produce a system which involves schools and programs throughout the RSU effectively integrating the various elements in the recommendation. A pilot program in a school and department will be implemented during fiscal year 2014 and expanded to the entire organization after evaluation and wholesale adoption.

Audit Finding: Invoices not Paid on a Timely Basis

Management's Response: The Business Office develops a formal cash flow analysis at the start of each fiscal year to forecast periods where revenues will not match planned expenditures. In those instances we're able access temporary financing in the form of a Revenue Anticipation Note from a local bank thereby minimizing late payments.

The RSU will establish an accounts payable subsidiary ledger.

Audit Finding: Inadequate Controls over Timesheets

Management's Response: The RSU will examine alternatives by which employees are able to certify hours worked and identify other approved payroll status. The RSU will clearly define methods by which employee time records are reviewed and approved by supervisors.