



ADAM H. EDELEN
AUDITOR OF PUBLIC ACCOUNTS

June 3, 2013

Jeff Pettit, Board Chair
Webster County School District
5745 US Highway 41
South Sebree, Kentucky 42455

RE: Findings and Recommendations

Dear Mr. Pettit:

As you are aware this office received concerns regarding certain financial transactions and activities of the Webster County School District (District). We have completed our examination of these matters and are presenting to you, as Board Chair, our findings and recommendations.

To address the concerns expressed to this office, we requested and examined various District documents for the examination period of July 1, 2011 through March 31, 2013, including, but not limited to, Board meeting minutes, Board member and Central Office staff travel and expense reimbursements, and credit card statements. We also conducted interviews with current and former Board members, several current and former Central Office staff, the District's CPA, the District Board Attorney, and a consultant on contract with the District.

After examining the requested documentation and conducting interviews, auditors identified a number of findings and opportunities to strengthen controls or processes. Our findings and recommendations resulting from this examination are presented below:

Finding 1: District travel and expense reimbursements were not adequately approved and supported.

Through examination of travel and expense reimbursements made to District Board members and Central Office staff for the period of July 1, 2011 through March 31, 2013, auditors found reimbursements were not always properly approved and in some instances the supporting documentation lacked sufficient detail to ensure the expenses were necessary or had a business related purpose. While auditors did not identify any significant reimbursements made to District Board members and Central Office staff that we consider highly questionable, controls over this payment process were weak and could lead to abuse if not strengthened.



One particular issue noted involved reimbursements made to the Superintendent. While the Superintendent's reimbursement request documentation indicated that a secondary review and approval was applied to the requests, the review and approval process was performed by various Central Office staff who report to the Superintendent. While the documentation appears to indicate that Central Office personnel conducted thorough reviews to ensure the Superintendent complied with the policies of the District, this process creates a conflict for staff given that staff report to the Superintendent.

Another issue identified was the lack of consistent reviews and approvals of reimbursement requests made by District administrators including the Assistant Superintendents. Reimbursement request documentation from the Assistant Superintendent, who also serves as the District Director of Pupil Personnel, had no secondary review and approval, as necessary on the expense reimbursement form, applied during the entire examination period. This Assistant Superintendent received over \$6,200 in travel and expense reimbursement requests during the examination period. While auditors found the requests for reimbursement by the Assistant Superintendent to be sufficiently detailed, the District is not ensuring a proper review and approval process is completed.

Auditors also found an instance when an expense reimbursement made to a former Board member was not sufficiently supported. On June 20, 2011, the former Board Chair was reimbursed \$56.17 for vehicle repair work while traveling on behalf of the District to pick up school supplies in Indiana. While the supporting documentation did indicate vehicle repair work was performed, the documentation did not include any detailed information pertaining to the vehicle repaired or the reason the District should reimburse for the repair. Auditors confirmed through interviews with a Central Office staff member and the former Board Chair that the vehicle driven and repaired was a District vehicle and not a personal vehicle; however, the documentation should identify the specific vehicle repaired. While the reimbursement may be appropriate, the documentation did not clearly identify the business related purpose of the expense to the District.

Recommendations

We recommend the Board, or a designated committee of the Board, consistently review and approve the travel and expense requests of the Superintendent prior to payment. This should not be the responsibility of the staff reporting directly to the Superintendent but rather should be performed by the Board who is responsible for hiring and overseeing the performance and activities of the Superintendent. We recommend the Board consistently perform a review to ensure that the reimbursement request is adequately supported.

We recommend the Superintendent, or his designee, consistently review and approve travel and expense reimbursement requests of District administrators prior to payment. As recommended to the Board, the reviewer should ensure that the reimbursement request is adequately supported by detailed documentation. If the responsibility for this review and approval is designated to Central Office personnel, the Superintendent should ensure that the designee is given the authority to appropriately question or deny District administrators' reimbursement requests if they do not comply with established District policy.

Finding 2: The credit card review process was not adequate to prevent excessive, questionable, or personal expenditures.

During our examination, we requested statements for credit cards assigned or available to Central Office staff. Auditors were informed that Central Office staff did not have credit cards but that all of the credit cards for the District's departments/schools were kept in the Central Office building. Though the primary focus of our examination was Central Office expenditures, auditors also tested these expenditures to evaluate the review and approval process and to determine whether the District's schools or departments were making excessive, questionable, or personal expenditures. In addition, the District had no policy regarding documentation, review, or approval of credit card transactions.

The District requires credit cards for schools and departments to be checked out from the Central Office to control the use of the card; however, this process does not protect the District from the credit card being used for excessive, questionable, or personal expenditures. Based on our review of the period July 1, 2011 through March 31, 2013, the credit card sign-in logs were either incomplete or the credit card was kept by the employee for such an extended time that this procedure is ineffective. Though this process existed, it was not consistently followed to ensure credit cards were adequately controlled.

Credit cards were used for travel and other purchases instead of requiring employees to use an expense reimbursement form that would provide the need and business purpose for the expenditures. In our review of these invoices and the credit card process, we reached the following conclusions:

- The procedure to check out a credit card from the Central Office does not control or document the use of a credit card or prevent questionable expenditures from being made. Online or phone purchases can be made without having the actual credit card if the individual placing the order knows the credit card number, security number on the card, and the expiration date which can be obtained from the credit card. Signing a credit card log to gain access to a credit card would

only be effective when an actual credit card is needed for purchases such as gasoline or other routine items. Though a credit card is checked out and the log is completed, no time limit to keep the card exists, which increased the risk of the card being shared with unauthorized employees to use.

- While the credit card transactions tested were supported by some form of documentation, the documentation was not always adequate. The expenditure's business purpose was rarely documented and restaurant receipts did not identify the number of employees participating in the meal. Further, auditors found restaurant charges were routinely only supported by a summary credit card receipt that provides the total and the tip amount but does not provide an itemized list of purchased items.

Without detailed documentation and the purpose for the transaction, it could not be determined whether certain purchases were allowable expenditures. Party supplies were periodically purchased by schools and may have a legitimate business purpose, but without sufficient documentation it could not clearly be determined. The departments that primarily use credit cards are Special Education, Family Resource and Youth Service Center, and Transportation. Special Education used the credit cards most frequently at conferences, training, and for special equipment.

- In addition to restaurant receipts not being detailed and not documenting the reason for the meal, travel, or other expenditure, the policy for meals was not clear. While the District does require an overnight stay for meal reimbursement, the Travel Reimbursement Claim Guidelines states that "[a]ll meal expenses must be accompanied by a receipt and will be limited to \$40 per day unless otherwise approved by the Superintendent, with the exception of convention/meeting luncheons/dinners for which full reimbursement shall be made." The exception to the \$40 per day was confusing because it appeared that an individual could exceed the \$40 if attending a convention or meeting. Without an explanation as to the reason for the overnight stay and the number of employees included in the meal purchase, it cannot be determined whether the guideline was being violated. Further, given that conventions, training, or other business related activities frequently provide certain meals when attending the event, it is unclear why the \$40 limit would not apply in these situations. For example, on March 6, 2013 a meal was purchased on a District credit card at Bella Notte for \$53.99 and the supporting documentation did not state the purpose for the travel, what items were purchased, or the name or number of employees present at the meal. In addition to this concern, it is also not known whether other meal purchases were reimbursed by the District through using a travel reimbursement form. Using both a credit card and expense reimbursement request form would possible allow an employee to exceed the \$40 day limit.

Recommendations

We recommend the Board review the need for credit cards for the District's schools and departments. If the Board decides that credit cards are needed, we recommend that the Board consider the use of a procurement card that can limit the types or categories of purchases that can be made. This control should reduce the risk of unallowable expenditures being made. Further, we recommend the Board consider discontinuing the use of credit cards for purchases related to training, conferences, or other travel. We recommend these expenditures should be requested using a reimbursement form that requires explanations for the travel and requires documentation to be reviewed and approved. By eliminating the use of a credit card for these types of expenditures, the District will reduce the risk of travel expenditures, such as the \$40 maximum allowable for meals, not to exceed the established amounts for the day.

Related to the District's policy that meals not exceed \$40 daily, we recommend that the Board review this policy to ensure that it is clear how conferences and meetings impact the daily amount allowed for meals per employee. We recommend the Board consider applying the daily \$40 maximum amount for meals to conferences and other over night events stipulating that necessary exceptions are documented and approved by the Superintendent or Board.

We further recommend, if credit cards continue to be used by the District, the Board establish a specific credit card policy to require supporting documentation for credit card expenditures to include a business purpose, the number and name of employees involved in the purchase, as well as a detailed invoice or other appropriate documentation that identifies the need for the items purchased. This information should be available for the review process.

Finding 3: The lack of segregation of duties in District Central Office weakened financial controls.

The District's Central Office has multiple fiscal responsibilities such as receiving and depositing funds, establishing vendor accounts, paying vendors, printing checks, making bank deposits, performing bank reconciliations, preparing the annual budgets, and making the necessary postings and adjusting entries in MUNIS, the District's accounting system. While the District employs a Payroll Clerk, these duties appear to be performed solely by the District's Treasurer with minimal oversight by the Superintendent who also serves as the District's Chief Financial Officer.

The District has had frequent turnover in the Treasurer's position. During the examination period, the District has employed three Treasurers. The causes for the departures were reportedly due to an inadequate salary and the fact that the job duties were overwhelming. Auditors identified that the duties assigned to the Treasurer's position did not allow for adequate segregation of duties. To provide for strong financial controls, the best practice is for the District to have certain duties and responsibilities performed by different employees.

Segregation of duties is a critical component of an entity's internal controls because it reduces the risk of errors, inappropriate or questionable activity, and is a fundamental aspect of fraud prevention. In general, the concept of segregation of duties is to separate the following functions among employees:

- Asset custody;
- Record Keeping/Accounting;
- Disbursements; and
- Reconciliations.

If an organization cannot reasonably separate these functions due to the limited size of the agency, it is essential that a consistent and detailed supervisory review of related activities be required as a compensating control.

During the examination, auditors were informed that the Treasurer position had the access and opportunity to perform all financial activities in the District. The Treasurer can print checks using a signature card that has both the Treasurer and Superintendent's signature thereby not requiring the Superintendent to actually review or sign any checks. Given that District policy does not require the review of the Treasurer's work activities, it appears that the Treasurer has sole discretion to perform financial activities with no or limited review. The extensive financial responsibilities performed by the Treasurer appear to increase the District's level of risk and weaken financial controls. A single employee should not perform the majority of the financial duties especially without consistent oversight to ensure controls and processes are performed properly.

According to the Kentucky Department of Education (KDE), a finance officer is defined as follows:

The finance officer serves as the financial leader of the school district and is responsible, with the assistance of the superintendent, school councils, and other finance staff, for creating a sound financial climate that reflects the district needs and expectations. The finance officer must have an understanding of generally accepted financial practices and of the financial reporting and budget processes recommended by the Governmental Accounting Standards Board and required by the Kentucky Revised Statutes, Kentucky Administrative Regulations, and the Kentucky Department of Education.

Considering that the Superintendent is identified as the Chief Financial Officer and the District employs a Treasurer that actually performs the majority of the District's financial activities, it is unclear which position actually functions as the District's Finance Officer as defined by KDE. According to KDE, a Finance Officer is the leader that receives support from the Superintendent and other staff; however, the District did not establish a financial position that can clearly be defined in this manner.

According to a former District Treasurer, she was told by a finance officer from another school district that it was the Chief Financial Officer that signed off or approved everything in other districts. Therefore, as a new Treasurer, she did not feel comfortable assuming the responsibility of performing activities she did not understand.

Another financial concern involved the balance of the District's Federal and State Grant Fund, otherwise known as Fund 2. The concern was that Fund 2 could not be reconciled to the bank statement or account balance. Due to the turnover in the Treasurer's position, it was difficult to determine a date when Fund 2 could no longer be reconciled. The District has provided assistance to the Treasurer in reconciling Fund 2 by hiring a consultant, as well as a finance officer from another school district. However, it was clearly the responsibility of the Treasurer to perform this reconciliation as part of this position's various job responsibilities.

According to the District Treasurer, Fund 2 was recently reconciled and the District believes this issue has been resolved. However, the District has not yet established a process for oversight of the monthly reconciliations to ensure they are consistently and appropriately completed.

Recommendations

We recommend that the Board clarify whether the Treasurer or the Superintendent acts as the Chief Financial Officer for the District as defined by KDE. Once this determination is made and clearly communicated, we recommend that the Board and Superintendent review the financial duties and responsibilities to determine how these activities can be separated between the current employees to ensure segregation of duties and proper oversight exist. We recommend considering expanding the current duties of the Payroll Clerk to perform certain duties currently performed by the Treasurer. This would provide the opportunity for more than one employee to share the financial duties of the District. For those activities that cannot be segregated, we recommend a compensating control be established in policy requiring oversight of work performed, including account reconciliations, to ensure it is accurate, complete, and timely.

Finding 4: The Board did not have a formal written contract with its attorney.

Between January 1, 2003 and March 31, 2013, the District paid over \$150,220 in retainer and other legal fees to the Board's Attorney without a formal written contract for her services. Further, the Board and its Attorney were unaware that a formal written contract did not exist until the document was requested recently by the current Board Chair while discussing renewal of the Attorney's contract.

The Board Attorney has served the Board in this capacity since a former Board initially approved her selection by a vote of 5-0 on December 16, 2002. Approval for the Board Attorney's services was renewed annually by the Board since 2002. The Board Attorney stated that when the current Board requested the contract she initially thought there may have been written documentation of the initial agreement but acknowledged that she and others at the District were not able to find a written contract.

The only written documentation to support the District's initial agreement with its Board Attorney were Board meeting minutes from December 16, 2002, which state that the Board Attorney "is to receive a \$500.00 monthly retainer fee, plus a set hourly rate for services beyond the retainer fee." While these minutes document the amount to be paid for retainer, the minutes do not clearly define the legal services performed for the \$500 monthly retainer, additional services considered to be "beyond the retainer fee," nor the hourly rate the Board Attorney will be paid for those additional services.

According to the Board Attorney, the hourly fee was always to be whatever her hourly charge rate was to her clients. She noted that when beginning her work with the District her hourly charge rate was \$100 but her rate increased and is currently \$150 an hour. While examining invoices for the Board Attorney's services to the District between July 1, 2011 and March 31, 2013, auditors found that invoices included details relating to the work performed and the total fees charged to the district; however, the invoices did not clearly indicate the Board Attorney's hourly charge rate nor the hours of work performed.

While a contract does not have to be in writing to be legally binding, a formal written contract allows for greater transparency and accountability by both parties to the agreement. Furthermore, given the potential for rotation among Board members and key District financial personnel, a written contract would provide documentation of the exact terms of the agreement and would not rely on any individual recollections.

Recommendations

We recommend the Board ensure any agreement entered into is documented in a formal written contract and that the Board discontinue the practice of relying on implied or verbal agreements for contracts. Contracts entered into by the District should specify the services the contractor will perform and the amount to be paid. If the contract allows for the contractor to receive a retainer and an hourly fee, the contract should specify the services provided for the retainer paid and the services performed subject to an additional hourly rate. We recommend the Board include specific language requiring detailed invoices from a contractor to include a description of the work performed, the number of hours associated with each work step and the rate at which the services are being charged.

Finding 5: Superintendent's annual evaluation was not consistently performed or reported according to District policy, contract, and state statute.

District Board policy 02.14 and the Superintendent's contract requires the Board to conduct an annual evaluation of the Superintendent. However, according to the Superintendent, the Board did not perform an evaluation for fiscal years 2009 and 2010. Further, auditors found a summative evaluation of the Superintendent was also not discussed and adopted in an open meeting of the Board during the examination period as required by the amended District Board policy and Kentucky Revised Statute (KRS) 156.557.

The Superintendent stated that the full Board had difficulty meeting to conduct the evaluation, noting that the former Board Chair wanted all Board members involved in the evaluation process. One former Board member made similar statements noting that the Board had discussed performing the Superintendent's evaluations many times while in closed session; however, the Board did not perform the evaluations. Although the Superintendent stated that he had not received an evaluation in 2009 and 2010, the former Board Chair stated that the Board had completed the evaluations of the Superintendent but the Board did not make a written report of the evaluations.

In 2010, the Kentucky Legislature revised KRS 156.557 by adding specific language to address the issue of superintendent evaluations and open meetings. The new language found in KRS 156.557(4) states:

- (a) Each superintendent shall be evaluated according to a policy and procedures developed by the local board of education and approved by the department.
- (b) The summative evaluation of the superintendent shall be discussed and adopted in an open meeting of the board and reflected in the minutes.
- (c) If the local board policy requires a written evaluation of the superintendent, it shall be made available to the public upon request.
- (d) Any preliminary discussions relating to the evaluation of the superintendent by the board or between the board and the superintendent prior to the summative evaluation shall be conducted in closed session.

District policy 02.14, pertaining to the evaluation of the superintendent, was amended on August 9, 2010 to reflect the new language found in KRS 156.557, including the requirement that a "summative evaluation shall be discussed and adopted in an open meeting of the Board and reflected in the minutes." Despite the new language adopted into District policy, a review of Board meeting minutes from July 1, 2011 through March 31, 2013 found no such evaluation discussion was recorded. The former Board Chair stated he did not think it was appropriate to publically evaluate the Superintendent, noting that other staff within the District and public officials, in general, are not publically evaluated.

Recommendations

We recommend the Board ensure its compliance with District policy and KRS 156.557(4). This will require the Board to perform an annual evaluation of the Superintendent and present a summative evaluation in an open meeting and document its action in the official minutes of the meeting.

We further recommend the Board consider revising District policy 02.14 to specifically state that the evaluation of the Superintendent is to be made in writing and the time period by which the evaluation process will be completed.

Finding 6: The Superintendent's employment contract lacked specific detail regarding benefits for vacation and sick leave and did not clarify additional duties.

The Superintendent's employment contract provided few specifics related to his leave benefits. For our examination period, we reviewed the Superintendent's employment contract for the period July 1, 2010 through June 30, 2014. While the contract includes the stipulation that the Superintendent will receive 25 calendar days of vacation annually, it does not identify specific days to be worked so that it can be clearly determined when leave should be taken. Further, the contract does not address how the Superintendent's vacation or sick leave will be accumulated or reported to the Board for its review. The contract does not address sick leave or how the balance will be reported to and reviewed by the Board. In addition, the contract outlines the Superintendent's job description but did not address his dual role as the Chief Financial Officer.

According to the Superintendent's employment contract effective July 1, 2010, he receives 25 calendar days of vacation annually. However, there are other issues related to this benefit that have not been addressed in the contract. First, the contract does not state if there is a maximum number of unused days that can be accrued. Second, there is no specified procedure that the Superintendent should follow to report his use of vacation days to ensure the Board is aware of leave taken allowing the Board an opportunity to monitor his vacation leave balance at regular Board meetings.

In addition, the employment contract does not contain a provision regarding the number of sick days to be awarded annually to the Superintendent. While this may simply be the same number of days provided other teachers or certified staff, a clause stating the actual amount of sick days approved could prevent any confusion and assist in preventing a higher number of sick days than anticipated being awarded to the Superintendent.

If the Superintendent's use of vacation and sick days is not monitored, there is a risk that large payouts will result when the Superintendent terminates his employment or retires. The Board had not ensured checks and balances were in place to monitor the Superintendent's use of leave.

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As stated previously, the Superintendent also has the title of Chief Financial Officer yet this role is not clearly defined in the employment contract. Specific responsibilities related to this role should be listed in the contract so that it is understood what is expected from the employee. The only financial tasks required in the Superintendent's job description are for him to prepare the annual operating budget recommendations and maintain a system of financial accounts.

Recommendations

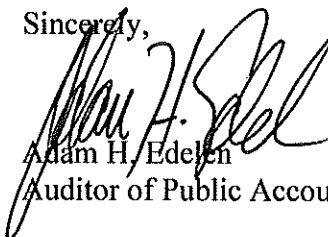
We recommend that the Board review the Superintendent's employment contract to strengthen the sections of the contract pertaining to leave benefits. For vacation leave, a maximum number of accrued vacation days should be specified, along with how unused vacation days will be valued when the position is terminated. Related to sick leave, the annual number of sick leave days awarded to the Superintendent should be specified. In general, we recommend that the contract contain a requirement that the Superintendent notify the full Board, Board Chair, or a designated Board committee when vacation or sick leave is taken to ensure that the Board has the needed information to monitor the Superintendent's leave balances. We also recommend the Board receive an independent report of the Superintendent's leave activity from the District's Central Office.

We further recommend that the Board determine what duties are required related to the Superintendent's dual role of Chief Financial Officer. These roles should be explicitly written into the contract or the Superintendent's job description.

We would like to thank the District for its assistance throughout the examination process. We trust that the findings and recommendations presented in this letter will assist the Board in strengthening its controls and oversight of the District's financial activities.

If you have any questions regarding this letter, please contact me at (502) 564-5841. Thank you, in advance, for your attention to these matters.

Sincerely,



Adam H. Edelen
Auditor of Public Accounts

cc: James Kemp, Webster County School District Superintendent