

**Recommendations From Forensic Investigation January 7, 2008
Melanson Heath and Company, PC**

Superintendent's Update February 26, 2008

Hiring a Director of Financial Operations

The position of Director of Financial Operations is difficult to fill. The requirements, as contained in the job description, are complex, and finding someone who has that experience and is available at a price consistent with the budget can be challenging. We are making some recommendations to assist in that process.

1. Consider a search committee consisting of School Committee Members and Administration representation. Outside members should be considered to include individuals who have acumen in school related financial matters.

Search committee established January 2008. Committee consists of Chris Feeley/Chair Town Council, Susan Gagner/Comptroller, Jeffrey Roy/Chair School Committee, Susan Rohrbach/School Committee Budget Sub-Committee Chair, Cora Armenio/School Committee member Budget Sub-Committee, Lisa O'Keefe/Director Human Resources, Maureen Sabolinski/Assistant Superintendent, Erica Montiero/Payroll Manager, Mary Jane Mendes/Accounts Payable, Wayne Ogden/Superintendent.

2. Consider School Business Manager Certification as a prerequisite or requirement within a set period of time after hire.

Advertising generated 17 applications for consideration. Interview committee reviewed the resumes and completed background searches. 5 candidates were selected for further consideration. The 5 candidates all comply with criteria set forth by the auditors.

3. Give hiring preference to candidates who have at least three to five years experience in a Massachusetts School Department.

Initial interviews for the 5 candidates will be conducted on Wednesday, February 27, 2008. 4 of 5 candidates have experience as

School Business Administrators and 1 is a Town Finance Director with experience as a Town Treasurer and Comptroller. All have in excess of five years experience and possess MA licensure as a School Business Administrator.

4. Advertise the position through the numerous Massachusetts governmental association's newsletters and websites.

Advertisement was placed in the Boston Globe, January 13, 2008. Position was posted on the Massachusetts Association of School Superintendent's (MASS) web site, the Massachusetts School Business Officials (MASBO) website, the MA Department of Education web site and School Spring, the Franklin Public Schools recruiting web site.

5. Consider re-advertising the position if a qualified candidate is not found during the first round of evaluations.

Upon completion of interviews the committee will recommend candidates to the School Committee for final interviews in a public forum.

Once the position is filled, the School Committee should require the participation of that person in meetings put on by MASBO, The Department of Education and the Department of Revenue. The topics identified in this investigation, such as how to handle Medicaid, School Choice and Circuit Breaker is discussed at length at these meeting. In addition, important contacts are made to provide guidance when there is uncertainty of how to handle certain transactions.

In review of the candidate's resumes, all interviews are members of MASBO and /or members of MA Government Finance Officers Association. All candidates currently or have attended MASBO trainings and DOE trainings in the area of School Finance. The school district will include compensation for professional membership in the contract of the successful candidate.

In addition, the Director of Financial Operations should be encouraged to contact the School's audit firm. There is usually no charge to answer routine questions regarding how to handle certain transactions, and retaining advice from the auditors can help support a transaction that is later questioned.

This will be discussed during the final interview process and an expectation of the position. Additionally, the audit report will be sent directly to the School Committee Chair and to the Superintendent of

Schools. In the past, the reports went to the Director of Financial Operations directly. The audit firm will send to the School Committee and to the Superintendent

Finally, when transactions are considered that are high risk, contact can be made with the Department of Education and Department of Revenue. Their responses should be documented through either emails or other written correspondence.

This will be an expectation of the position and when a new Director is hired the Superintendent and the School Committee will establish Standard Operating Procedures and it will be an expectation that the new director will develop a procedural manual for the finance office as recommended in the FY 06 audit report.

School Committee Approval of Transfers

The School Department budget is a single bottom line appropriation. The authority to spend within the departments, programs and line items of that budget is determined by the School Committee.

The School Committee can set spending limits to be administered by school principals and program directors. Too often, the line item or departmental spending limits are administered by the financial management staff.

In addition to setting departmental and line item limits, there are other actions that impact the total budget that should be voted by the School Committee. Revenues such as Medicaid and School Choice are examples of revenues which increase the spending authority of the School Department.

When administrators and School Committee members make spending decisions during the course of the school year, there are often decisions that are made informally, but are never documented through budget transfers. For example, if a school boiler breaks down and needs an emergency repair, there is an unexpected cost that is not in the budget. There is usually discussion about where the money is coming from to cover the cost, but that transfer is never voted and recorded. With the number of line items to administer and the complexity of spending decisions throughout the year, it is near impossible to recall and keep track of these decisions without documenting them through budgetary transfers.

For these reasons, we recommend that the Director of Financial Operations submit transfer requests to the School Committee for any cost that will over expend a budget cost center established by the School Committee.

In addition, when there are revenue shortfalls that impact the level of spending, a vote should be taken by the School Committee as to where the budget will be cut to cover the deficits. For example, when it was projected that a \$ 600,000

revenue shortfall was expected in October of 2006, a vote should have been taken to reduce specific line items to cover that expected deficit.

The School Department instead instituted a spending freeze, which is an arbitrary and often ineffective method of addressing a deficit problem. Without going through each cost center, and identifying specific items in the budget that can be eliminated, it is not possible to give assurance that a spending freeze will be sufficient to cover the deficit. In this case, the spending freeze did create surplus balances in some accounts, which mitigated, but did not eliminate the deficit.

A spending freeze can be implemented through budgetary transfers that take money from accounts which have discretionary surplus balances, and transferring to accounts that are projected to be in deficit. Finally, when there is a projected deficit that is going to be covered by a Town Council transfer, the amount of the deficit needs to be determined and voted before the School commits to the related expenditures. See the recommendation on the Town's role in monitoring the School's budget.

Budget Transfers FY 2007

FY 2007 budget transfers and the closing of the FY 2007 books will be discussed publicly and voted on at the February 26, 2008 School Committee meeting.

(see School Committee agenda and minutes)

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Concerns over 2008 Budget

The deficits in 2006 and 2007 raise concerns over the School Department's level of spending in fiscal 2008. There will be more circuit breaker available in 2008 than in 2007, as there is no carry over deficit to be applied to the 2008 expected receipts. However, there was a deficit in Special Education Tuitions even with full Circuit Breaker receipts for both fiscal 2006 and 2007.

In addition, certain other accounts have been in deficit during both fiscal 2006 and 2007. We have prepared the three-year budget analysis, and provided a copy to the interim Director of Financial Operations. That analysis will assist in identification of potential budget shortfalls. However, the schedule is prepared based on the inclusion of negative revenue items, which needs to be taken into consideration in evaluating the 2008 budget.

Due the holdback of 15% of the FY08 budget by the Superintendent in July, 2007, the successful contractual negotiations by the School Committee and by some cost reductions implemented by the special education department, at this time the school department does not anticipate a deficit. We are monitoring the budget and areas of concern are the funds budget for snow removal, legal costs and unanticipated special education increases.

Integration of Payroll Schedule into the Budget

Compensation for personal services represents the vast majority of the School's operating budget. Accordingly, the budget cannot be monitored without determining the status of payroll related accounts during the year.

When we reviewed budget documents contained in the School's budget books for 2005, 2006 and 2007, we were unable to locate any detail related to amounts that supported budgeted amounts in the payroll line items.

There were schedules maintained by the Payroll Manager and Director of Financial Operations that monitored actual activity during the year. The proposed payroll schedule supporting the budgetary accounts should be incorporated into the budget workbook, and then compared to the actual payroll that is paid each pay period.

Interim Finance Director Paul Funk has developed a budget workbook that includes salary and FTE data aggregated to each individual school. The salary funds have been encumbered and balances are reviewed as part of each pay cycle. This data is incorporated into the annual budget information and School Committee budget workbooks.

Negative Line Items

It is our belief that the use of negative line items for various revenues and other budgetary items such as attrition are confusing and difficult to administer. We understand that the Interim Director of Financial Operations has eliminated these items in the 2008 budget accounts.

We recommend that the School continue to eliminate the negative line items in future budgets.

Through the practices implemented by the School Committee, the Superintendent, the Interim Finance Director and the Business Office staff this practice has been discontinued as evidenced in the budget presentation on February 26, 2008.

Budget vs. Actual Analysis in Budget Workbooks

The budget schedules contained in the budget workbooks that we reviewed for fiscal 2005, 2006 and 2007 contained a comparison of the prior year budget to the proposed current year.

Comparison to the prior budget does not provide for identification of the sufficiency of that budget for the purpose of establishing the new budget. As a minimum, we recommend the prior years budget and actual, the current year budget and projected actual, and the proposed budget all be presented in the worksheets. The software system currently used by the Town can provide historical data easily, as well as create worksheets for budget modeling.

The Interim Finance Director has been revising all methods of reporting and development of the school department budget. Budget documents will include salary data, and information as to expenditures from past years and current financial data.

With the hiring of a new Director procedures and processes will be put in place to make the school budget transparent and clear to all stakeholders.

Director of Financial Operations Participation at School Committee Meetings

We found that budget to actual reports were submitted to the School Committee with an attached memo from the Director of Financial Operations. The complexity of activity in the School's operating budget is such that a more detailed scrutiny, and discussion at the School Committee should ensue.

The School Committee and the Superintendent's Office rely on the Director of Financial Operations to monitor financial activity, and alert them as to any areas of concern. That process cannot be accomplished through a one page memo.

We recommend that the contract with the new Director of Financial Operations contain a requirement that attendance at School Committee meeting is mandatory.

The School Committee in its hiring of a new School Business Administrator will require the individual to be in attendance at all School Committee meetings and at all meetings whereby the school budget is discussed. The reporting of financial information will be a collaborative process defined by the School Committee, the Superintendent and the School Business Administrator to provided informative financial data to the administration and to the community.

Town's Role in Monitoring the School's Budget

The School Department's budget is a single bottom line appropriation of which the School cannot exceed in total. The line item detail is administered by the School, and in many cases, as in the past in Franklin; the Town records do not contain the line item detail of the School.

Prior to fiscal 2007, the School Department maintained their own financial management system with line item detail. The Town maintained a minimum of detail necessary for the Comptroller to complete the Town's Schedule A for the Department of Revenue. During fiscal 2007, the Town migrated to a new financial accounting software package, and the School brought on the line item detail to that system and abandoned the previous system used exclusively by the School.

Up to the identification of the inappropriate entries at the end of fiscal 2007, the Town Comptroller did not examine line School's line items for potential over expenditures. This was based on past practices since line item detail was not made available in prior years and on the knowledge that the Town does not have authority over the School's line items detail anyway.

The Town Comptroller has the responsibility as set forth in MGL to approve bills for payment by their signature on a warrant only when there is sufficient appropriation available to pay for the cost. Even though the School's appropriation is a single bottom line, the Comptroller may become aware of a deficit in a line item, which is so material as to possibly cause the bottom line to be in deficit at the end of the year. In that case, the Comptroller needs to request an action from the School Department to assure that a deficit will not ensue, and should not approve invoices for payment until satisfied that the line item deficit will be covered.

The Town and School Department should work out parameters with which the Town Comptroller can fulfill her responsibilities to monitor the budget without causing undue stress and conflict between the Town and School.

In the end, the Town is responsible for covering a deficit in any department in the Town. Accordingly, there is a due diligence that must be applied during the year to identify and prevent deficits from occurring, even in the School Department.

With the hiring of a new Director and some of the changes and checks and balances put into place by the Interim Director (cost centers) the administration and the School Committee will articulate a more comprehensive set of procedures as the new financial administration assumes responsibility for the department. The School Committee will be

kept informed if all procedural changes and further updates to the audit recommendations will be made during the summer of 2008.

School Department Making Journal Entries

With the integration of the School's detailed records into the Town's accounting system, the School Department was given authorization to enter journal entries into the Town's accounting system.

Although this is meant to accommodate the School's authority over their records, it causes access problems for the Town. The accounting records, including the School's, is the responsibility of the Town. The Town Comptroller therefore is responsible for any entry made by the School Department. She currently relies on the School Department to provide her with a copy of the entry but is at risk if an inappropriate entry is made.

We recommend that the Town discontinue access by anyone outside of the Comptroller's office into the Town's accounting records. This however, places responsibility of the Comptroller's Office to enter journal entries timely when received.

Effective November, 2007 the School Department no longer makes any journal entries. Requests to make journal entries are made to the Office of the Comptroller and the Town Finance personnel makes the entry. When adjustments to the salary line item are requested they are made by the School Department Payroll Manager. An email to the Comptroller is sent to alert the Town to the adjustment. This seems to be working well.