New Jersey State Legislature
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Office of the State Auditor

Town of Hammonton School District

July 1, 2004 to June 30, 2006

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State Auditor
The Honorable Jon S. Corzine  
Governor of New Jersey

The Honorable Richard J. Codey  
President of the Senate

The Honorable Joseph J. Roberts, Jr.  
Speaker of the General Assembly

Mr. Albert Porroni  
Executive Director  
Office of Legislative Services

Enclosed is our report on the audit of the Town of Hammonton School District for the period of July 1, 2004 to June 30, 2006. If you would like a personal briefing, please call me at (609) 292-3700.

Richard L. Fair  
State Auditor  
March 5, 2008
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Town of Hammonton School District

Scope

We have completed a forensic audit of the Town of Hammonton School District for the period July 1, 2004 to June 30, 2006. Our audit included financial activities accounted for in the district’s general fund. Total expenditures were approximately $30.5 million and $32.5 million in fiscal year 2005 and fiscal year 2006, respectively. The district provides regular and special education programs to approximately 3,300 students in grades Pre-K through 12, including the Borough of Folsom students in grades 9-12 and the Township of Waterford students in grades 7-12.

Objectives

The objective of our audit was to determine the primary factors that contributed to the district’s fiscal year 2005 and fiscal year 2006 year-end general fund deficits of $454,000 and $2,186,000, respectively.

This audit was conducted pursuant to the State Auditor’s responsibilities as set forth in the “School District Fiscal Accountability Act”, Title 18A:7A–57 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

In preparation for our testing, we studied legislation, administrative code, and policies of the school district. We read school district budgets, reviewed financial trends, and interviewed school district personnel to obtain an understanding of the programs and the internal controls. We interviewed officials from the Atlantic County Superintendent’s Office to gain an understanding of their oversight and monitoring functions. We also interviewed current members of the Hammonton Board of Education. In addition, we reviewed annual audit reports issued by public school accountants contracted by the district.
A nonstatistical sampling approach was used. Our samples of financial transactions were designed to provide conclusions about the validity of transactions as well as internal control and compliance attributes. Sample transactions were judgmentally selected for testing.

**Conclusions**

We found that accounting errors for deferred health benefit payments and budgeting errors related to transportation services and the child study team were the main cause of the general fund deficit in fiscal year 2005.

We found that the preparation and approval of a budget that was insufficient to meet the cost of district programs and services and inadequate fiscal management practices in the district’s business office caused the general fund deficit in fiscal year 2006.
Fiscal Year 2005 General Fund Deficit

In a resolution dated March 24, 2003, the district exercised the premium delay option offered under the State Health Benefits Program (SHBP) which allows for a 60 day delay in remitting payments on monthly bills for active employees. The delay was effective with the May 2003 premium. Districtwide financial statements are prepared using the accrual basis of accounting and expenses should be recognized at the time they are incurred. The total premium delay for May 2003 and June 2003 was $516,135. The district should have recorded this liability in the financial statements for fiscal year 2003. Instead the district deferred the liability recognition to the succeeding year. This practice continued in future years.

The agreement between the SHBP and Hammonton Board of Education clearly states that should the board elect to terminate the SHBP participation sometime in the future, any delayed premiums will become due and payable immediately at the premium rates effective as of that date. The board elected to withdraw from the SHBP in May 2005. The SHBP scheduled the termination date as of August 1, 2005 with all premiums, including the premium delay, due with the district’s final payment on July 1, 2005. Since the district did not recognize the expense for the two month premium delay begun in fiscal year 2003, it had to recognize 14 months of health benefits premiums as a fiscal year 2005 expense. As a result, the actual expenditure for health benefits was $625,000 more than the budgeted amount in fiscal year 2005.

**Recommendation**

We recommend that the district ensure conformity with generally accepted accounting principles by recognizing expenses when they are incurred.
In preparing the 2005 budget, we found that the district included $315,000 as revenue for transportation fees from other local education agencies. The district also used these same budgeted funds to reduce transportation salary expenditures in the budget. The same accounting errors occurred in budgeting $245,000 as revenue for a child study team for shared services with the Township of Waterford. The monies received from these two sources were applied as a reduction of expenditures during fiscal year 2005. As a result, budgeted revenues totaling $560,000 were not realized.

We recommend that the district ensure that anticipated revenues and expenditures are properly budgeted.

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**Fiscal Year 2006 General Fund Deficit**

State regulations require a district board of education to submit a budget application to the county superintendent for review and approval. Prior year expenditures for each budgetary line item account should be considered when preparing a budget. Adjustments should then be made for any programmatic changes, enrollment, and/or staff fluctuations to arrive at the final projected budget for the ensuing school year. In addition, the district should only budget for revenue that has the potential to be realized. The county superintendent shall only approve budgets that contain funding sufficient to meet all existing statutory and regulatory mandates.

In fiscal year 2006, we found the budget was inaccurate for teaching and aide salaries, health benefit costs, and revenue for transportation fees from other local education agencies, as discussed below.

- Eleven teaching positions totaling approximately $562,000 were not included in the budget. No formal position control table existed which
identified each position, salary, and account. An informal spreadsheet was used to support the budget for teaching salaries. In preparing the budget, eleven teaching positions were not included on this spreadsheet.

- The actual cost for aide salaries exceeded the original budget by approximately $559,000. The district had intended to cut aide positions when the budget was prepared. However, it appears that no aide positions were ever eliminated.

- The district did not provide sufficient funding in its fiscal year 2006 budget for health benefit costs. The actual cost for health benefits exceeded the original budget by $921,000.

- In preparing the fiscal year 2006 budget, the district included $388,000 as revenue for transportation fees from other local education agencies. The district also used a majority of these same funds to reduce transportation salary expenditures in the budget. We found reimbursements to the transportation salary accounts for $277,000 during fiscal year 2006 and $97,000 was recognized as revenue. Therefore, the remaining $291,000 in budgeted revenue could not be realized.

**Recommendation**

We recommend that the district prepare an accurate position control table to be used during the preparation of the budget. We also recommend that the board and county superintendent perform a comprehensive review of proposed budgets and verify the legitimacy of any cost reduction plans prior to approval. Documentation obtained and verified for salary reductions should include position control tables.
that identify annual cost savings for each eliminated or replaced position. Follow-up reviews should be undertaken to verify that positions have been eliminated or savings have been achieved. In addition, the district should ensure that anticipated revenues and expenditures are properly budgeted.

Accounting/Reporting Issues Impacting the Deficits

Funds were not properly encumbered in the accounting system and payments to vendors were significantly delayed.

An encumbrance is established to obligate funds within an account for a specific future use. The purpose and main benefit of encumbrance accounting is to avoid budgetary overspending. State regulations require the board secretary to prepare a monthly report that shows the financial activity of each budgetary line item account. When funds are not properly encumbered, these reports become misleading and available funds are overstated.

In our testing of transactions, we found the following:

- Purchase orders were not encumbered timely in the accounting system. In 17 of the 29 cases tested, the encumbrance was entered in the system after the goods or services were received.

- Annual contracts including utilities were not encumbered at the beginning of the year. For example, we found a $28,000 medical contract for fiscal year 2005 encumbered on June 30, 2005.

- The business office canceled purchase orders and later reinstated them. To illustrate, we reviewed a purchase order dated July 2005. The goods were received in August and September 2005. The encumbrance
was entered on the accounting system in December 2005, cancelled in May 2006, and subsequently re-entered in June 2006 in order to process a check for payment. This check was not cashed for an additional two months.

- Payment was not prompt for 17 of the 29 purchase orders tested. We found a time lag, ranging from three to fifteen months, between the receipts of goods to a cancelled check. In 15 of these 17 cases we found an approximate three month time lag between when the check was printed and cashed. This evidence supports that the district held processed checks prior to disbursement. In addition, conversations with district personnel indicated that vendors were complaining about late payments.

A monthly bill payment list is presented to the board for approval. After approval, payments are processed through the accounting system which results in a printed check. By not releasing checks, the business office misled the board to believe that payments to vendors were timely. The treasurer prepares an outstanding check list, however this list is not provided to the board. The reoccurrence of the same outstanding checks for months at a time may have prompted board members to question the district’s ability to make payments.

**Recommendation**

We recommend that the district ensure that all contracts and other known obligations are encumbered at the beginning of the fiscal year. In addition, the business office should provide the board with the outstanding check list and make full disclosure of the district’s ability or inability to pay bills.
Board Secretary
Reports are not properly analyzed.

State regulations require the board secretary to prepare a monthly report that shows the financial activity of each budgetary line item account. We found that the board and the county superintendent do not properly utilize the monthly Board Secretary Reports to adequately assess the financial position of the district.

We found that halfway through the school year, the district had expended more than half of its appropriation in a number of accounts. For example, in fiscal year 2006 Grades 1-5 Salaries had appropriations of approximately $2 million. As of the end of January, the district expended approximately $1.3 million in this account with only $700,000 available for the second half of the year. At the same point in time, sufficient funding was not available in the other regular program salary accounts to cover this shortfall.

In addition, the Board of Education should approve all transfers from any general fund appropriation account. When the total amount of such transfers, on a cumulative basis, exceeds 10 percent of the amount of the account, the district should request written approval from the county superintendent. We found that the business office did not obtain proper approvals for fund transfers. A proper review of the Board Secretary Reports would have identified the increases or decreases in appropriations (transfers). The board and county superintendent should have questioned these transfers.

Recommendations

We recommend that the board and county superintendent review the Board Secretary Reports and investigate transfers and accounts with insufficient funding. In addition, transfers should be approved by the board.