

Controller: Tougher auditing of district

6.2.11
Inquirer

Releasing an audit of 2010, he urged "enhanced measures" to fix problems.

By Martha Woodall
INQUIRER STAFF WRITER

City Controller Alan Butkowitz said Wednesday that the Philadelphia School District should be required to present a five-year financial plan to an independent authority to address accounting problems his office found in an audit.

Butkowitz, who spoke as he released an audit his office performed on the district's annual financial statement for fiscal 2010, also said he believed the city finance director should be involved with the district's budget and accounting practices. And, he said, his office should be given expanded authority to examine the district's books.

"With poor budgeting practices and inadequate attention to accounting principles and procedures, I believe enhanced measures must be implemented to ensure that the School District gets [its] financial house in order," he said.

Some recommendations, including giving the Controller's Office access to the district's books before they are closed at the end of the fiscal year, would require changing state law, he said.

Butkowitz, who has tangled with the district since the administration of former schools chief Paul Vallas, has called for presenting five-year plans to an independent authority before.

He said the independent body would be similar to the Pennsylvania Intergovernmental Cooperation Authority, which oversees the city's finances. With such a board, Butkowitz said, the district could have avoided the \$629 million shortfall it was facing.

See **SCHOOLS** on B6

■ Students urge continued funding of programs that helped make city schools safer. Story, B6.

6.2.11 Inquirer

Stricter School District audit urged

SCHOOLS from B1

The district said in a statement Wednesday evening that it "disagrees in the strongest possible terms with the city controller's depiction of the district's financial statement for the fiscal year 2010 and the district's internal financial controls."

Mark McDonald, Mayor Nutter's press secretary, said the Nutter administration had not seen a copy of the controller's report and could not comment on the recommendations.

As The Inquirer has reported, the controller's audit uncovered several serious accounting errors known as "material weaknesses" that — if not corrected — could have resulted in higher borrowing costs for the district.

In response to concerns about errors raised in preliminary versions, changes and corrections were made before the district issued its formal financial statement Jan. 31.

That report is used by bonding agencies to grade the district's ability to repay debts. The City Charter requires the Controller's Office to perform the audit.

In its examination of the statement for the fiscal year, which ended June 30, auditors found a lack of documentation to support accounting decisions for several significant transactions. They said that the district's reviews of the accounting practices were not always documented and that procedures had failed to detect some major errors. And auditors said the district had not circulated a completed manual on preparing the annual financial report to the offices that worked on it.

The issues, Butkowitz said, were serious and showed that the district's accounting procedures had not been able to spot the mistakes.

"The last time ... the Philadelphia City Controller's Office found material weaknesses in the School District's financial statements was in 1999 and 2000 — right before the collapse of the school system," he said. The district was facing a \$200 million deficit when legislation was passed that enabled the state to take over city schools in 2001.

Butkowitz, who was elected controller in 2005, had said last week that he believed the 2010 audit was the first time a material weakness had been found in a district financial statement.

The district has downplayed the significance of the errors auditors highlighted. Michael Masch, the district's chief financial officer, has challenged the language in the audit and said none of the questioned areas was serious enough to be called a "material weakness."

The district's statement Wednesday said the controller's findings were based on preliminary documents "that were provided with the understanding that the documents were preliminary, not final, and would be amended and finalized prior to being considered final and subject to audit findings."

Butkowitz said in his report that his auditors found a \$6 million error in a payroll account on the day the district was required to release the final version of its statement.

The report of accounting problems comes as the district seeks more state and city money to help plug the \$629 million shortfall and only days after The Inquirer reported that the Internal Revenue Service has launched a separate, comprehensive audit of the district's finances in the 2009 calendar year.

Contact staff writer Martha Woodall at 215-854-2789 or martha.woodall@phillynews.com.

The Philadelphia Inquirer

Philadelphia School District's accounting procedures questioned in controller's report

May 31, 2011 | By Martha Woodall, Inquirer Staff Writer

Only days after the Internal Revenue Service began a detailed audit of the School District of Philadelphia, the city Controller's Office is poised to release a report that raises questions about district accounting procedures.

An audit by the Controller's Office of the comprehensive financial statement the district prepared for fiscal year 2010 found several serious accounting errors that if not corrected could have resulted in higher borrowing costs for the district.

According to a copy of the report The Inquirer obtained, City Controller Alan Butkovitz's office found four "material weaknesses" in the district's preliminary financial report for the fiscal year that ended June 30, 2010. The audit is scheduled for release Wednesday.

In response to concerns the audit raised, changes and corrections were made before the district issued its formal report Jan. 31.

Butkovitz said it marked the first time his office had found such serious problems with accounting procedures during its yearly review of district reports.

"When you wave a flag and say there is a 'material weakness,' that's like saying you can't automatically trust these statements," Butkovitz said. "You have to kick the tires and examine them."

Michael Masch, the district's chief financial officer, challenged the language in the controller's audit and said none of the questioned areas rose to the level of a "material weakness."

"A material weakness would misrepresent the actual financial condition of the school district," Masch said.

Among other things, the district's annual report is used by bond-rating agencies to grade its ability to repay debts. The City Charter requires the Controller's Office to audit the statement.

The report was due Dec. 31, but the Government Finance Officers Association of the United States and Canada, which reviews government reports, granted a 30-day extension.

Masch said the transactions the Controller's Office questioned included esoteric accounting technicalities that did not affect the statement of the district's assets or liabilities.

"I am completely perplexed at the Controller's Office decision to report this the way it did," Masch said.

He also said that in the past, the Controller's Office has understood that the preliminary documents the district provides are drafts subject to change.

But Deputy City Controller Gerald V. Micciulla, who oversaw the audit, said the problems auditors found were serious and increased the risk that other errors could slip by.

"On a scale of 1 to 10, this is a 10," he said. "When they give us these statements, these statements are supposed to be correct."

Butkovitz said the fact that the district had not spotted the errors was one of the factors that heightened auditors' concerns and figured in their decision to describe them as serious weaknesses.

"There are accounting rules that require us to broadcast to the world material weaknesses because of their significance in terms of the reliance the outside world puts on these accounting procedures," he said.

According to the copy of the controller's report The Inquirer obtained, auditors highlighted several issues, including a lack of documentation to support accounting decisions for several significant transactions. They said that the district's reviews were not always documented and that the procedures had failed to detect some significant errors. And auditors said the district had not circulated a completed manual on preparing the annual financial report to the offices that worked on it.

As one example of the lapses, the controller's report said the district improperly recorded a \$15.3 million loan from its general fund to a food-service account.

With the approval of the Government Accounting Standards Board, the School Reform Commission in January approved a five-year repayment plan to restore the money to the general fund. Masch said the district had been working for three years to reduce the debt, which stems from an ill-fated experiment to privatize food service during the administration of former schools chief Paul Vallas.

The report also found that the district improperly recorded a \$42 million adjustment from 2009 under new government accounting requirements related to payments the district made as part of a debt-restructuring deal to exit risky interest-rate swaps.

The district said it had followed the recommendation of a consultant hired specifically to deal with the new reporting requirements. Masch called the issue "a very esoteric dispute with the adjustment" that did not affect the district's bottom line.

The auditors in Butkovitz's office also said that on the day the district was required to submit its financial statement, they spotted a \$6 million error in a payroll account.

In a May 13 letter responding to the controller's report, Masch said: "I would like to note the seriousness with which this administration treats the findings and recommendations." He said the district had made changes to resolve all the issues.

But the district's response to the audit repeatedly disputes the controller's characterization of the seriousness of the issues.

"The school district does not concur that there is a material weakness in the review of accounting entries," the response said.

The final report received certificates of excellence from the Association of School Business Officials and the Government Finance Officers Association of the United States and Canada. The certificates - which the district has received each year since the mid-1980s - indicate it has met the highest public accounting standards and help it obtain lower interest rates on debt.

Masch said the district has a high investment rating, "but not the very highest."

As of Dec. 31, Moody's gave the district a rating of Aa3 on one series of long-term debt; Standard & Poor's gave it an AA- rating.

The accounting concerns raised by the Controller's Office are one more bit of bad news for the district as it looks for more city and state aid to help address a \$629 million shortfall.

The IRS last week began a wide-scale audit of the district's financial practices for the 2009 calendar year, The Inquirer reported Friday. As the audit began, the district abruptly fired its payroll director, Eileen Pelzer.

According to sources, the district blamed Pelzer for not informing top administrators about the audit's broadened scope. Sources said Pelzer, who has declined to comment, told them she had informed her supervisor about the IRS audit.

The IRS seeks information about reimbursements for travel and meals, use of district automobiles and credit cards, and "checking account data for payments that are processed outside the district's general fund," according to a document The Inquirer obtained that lists 28 separate areas of inquiry.

The district has downplayed the significance of the probe, calling it "a random, routine audit."

Contact staff writer Martha Woodall at 215-854-2789 or martha.woodall@phillynews.com.



Posted on Thu, Jun. 2, 2011

Council at a loss without schools stats

By DAFNEY TALES
Philadelphia Daily News

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Many have asked, but few have seen actual figures that show the progress that district officials say they've made with the reform initiatives launched under Superintendent Arlene Ackerman.

At least that's how City Councilman Bill Green, and many like him, see it. They say that district officials have yet to show data validating their claims that daily attendance at Promise Academies is up while serious incidents are on a downward slope.

In its \$2.75 billion budget, approved on Tuesday by the School Reform Commission, district officials earmarked money to expand the district's Renaissance Schools initiative to turn around struggling schools and its 18-day summer school, but slashed full-day kindergarten, school budgets and transportation.

City officials, union leaders and education advocates were stunned by the district's budget decisions, and have asked officials to explain their reasoning, but to no avail.

Green, never one to shy away from criticizing the district, said that the district's behavior has left him sour.

"I think that while people are looking to try to find a way to provide resources, it's only if they treat us like adults to begin with," he said.

Green noted that he has yet to receive information about summer school and other programs that he requested last week during the district's hearings in front of City Council.

District officials last week requested up to \$110 million in additional funds from the city to stave off cuts.

"And to expect us to take any kind of votes to increase revenues in that case, I don't think that's likely," Green said.

Fellow Council member Jannie Blackwell agreed.

"Nobody knows anything because we don't know what the district has done," she said on Tuesday, the day the district's provisional budget was adopted.

"We're not informed. I have not seen a plan or a process, and I'm the chair of the Education Committee. We're very worried."

A district spokeswoman said that the district has answered many questions and will continue to. "The answers to the remaining questions will be provided [today]," said spokeswoman Shana Kemp."

Council isn't alone in its skepticism. City Controller Alan Butkovitz released an audit of the district's financial statements yesterday that found "serious financial errors."

He called for more oversight of the district, including giving the city's finance director involvement in district finances and giving wider auditing power to the controller's office.

Cindy Clark, whose son Caleb will attend kindergarten at Meredith School next year, is also skeptical of the district's budget.

"They talk about transparency and what the district is doing with the money, but we're not seeing it," she said.

The Philadelphia Inquirer

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Controller urges 'enhanced measures' in auditing of Philadelphia School District

By Martha Woodall

Inquirer Staff Writer

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The Philadelphia Inquirer

Posted on Thu, Jun. 2, 2011

Nutter pitches more taxes to aid schools

His proposals included raising property rates and parking fees - and reviving his push for a soda levy.

By Troy Graham

Inquirer Staff Writer

With time running out to raise about \$100 million for city schools, Mayor Nutter proposed in private meetings Wednesday to raise property taxes, resurrect the long-dead soda tax, and increase prices at parking meters and kiosks.

City Council members, who largely were opposed to raising taxes last week when Philadelphia School District officials first asked for \$75 million to \$110 million in city money, were just as cool Wednesday to Nutter's specific plans.

A property-tax increase, several members noted, would come on the heels of last year's 10 percent increase - and that hike, while unpopular, was a compromise after they shot down Nutter's previous attempt to create a soda tax.

Nutter acknowledged that he had "a lot of work to do" to persuade at least nine Council members to pass whatever combination the administration endorsed - and just two weeks until the summer recess.

"We have a very limited time frame here," the mayor said. "But there is enough time to accomplish these very important goals. . . . What it requires is leadership, political will, and the commitment to get things done."

Nutter and School District officials, who face a \$629 million budget gap, have described terrible consequences if the money isn't raised.

District officials have said they would be forced to make cuts to full-day kindergarten, transportation services, and alternative schools and increase class sizes.

Some critics on Council have questioned whether the district has adequately trimmed the fat from its budget, or eliminated programs less effective than full-day kindergarten. They have described the district's targeting of such essential services for cuts as a kind of blackmail.

"They're fearmongering," said Councilman Bill Green. "Until they stop engaging in that kind of behavior, I see no reason to be supportive of their efforts."

The district's cash request also has come amid questions about its financial stewardship: City Controller Alan Butkovitz called for more oversight and auditing power Wednesday after finding what he called "serious financial errors" in the district's accounting procedures. Butkovitz also advocated that the district be required to submit a five-year financial plan to an independent authority, as the city does.

"It's pretty dire here. This is a very tough situation," Council Minority Leader Brian O'Neill said. "I don't think anybody has any confidence in the School District's budgeting and finance, their accountability."

Nutter met in the morning with about a dozen education advocates, presenting his plans and asking for their support. He then met with Council leadership in President Anna C. Verna's office.

"I didn't see anybody smiling in that room," Council Minority Whip Frank Rizzo said after the meeting.

Nutter emerged about noon and said he hoped to reach "more of a consensus" with Council members before Thursday's 10 a.m. Council meeting.

There was no word Wednesday night on any possible deals, but with just three Council meetings before the recess, Nutter said any new revenue bills would need to be introduced Thursday.

Nutter could introduce measures now and attempt to garner support during the next two weeks. A property-tax hike would come as an amendment to an existing bill.

Several of the education advocates, including Philadelphia NAACP president J. Whyatt Mondesire, said they would back the mayor.

"If we don't stand with this mayor and push some kind of legislative package through Council in the next several days, the consequences will be dire," Mondesire said.

Debra Weiner, with Public Citizens for Children and Youth, said Nutter had told her a property-tax increase that would raise \$100 million would cost the average taxpayer \$120 a year.

"Ten dollars a month, maybe \$2.50 a week. That's like a movie ticket and a Coke," she said. "I think that's affordable to sustain the momentum the schools have demonstrated in the last eight years."

Weiner said she expected the advocates to mobilize a huge swell of supporters for the mayor's proposals.

While the numbers are subject to negotiation, Council members described the mayor's current package as including:

A 10 percent property-tax increase. Property taxes are divided between the city and the schools. The hike would be accomplished by raising the school's share. Last year's 10 percent increase was done solely on the city's portion.

A tax of 2 cents per ounce on sugary beverages, the same as Nutter proposed in 2010. Council killed the soda tax last year amid opposition from the soda industry, store owners, and Teamsters. Councilman William K. Greenlee said he was concerned about whether the tax could be legally enforced: "We'll get ourselves in trouble if we rely on that . . . I think certainly the soda people will go to court right away."

An increase in prices at city parking meters and kiosks that would raise about \$6 million a year. The price hikes could be concentrated in high-traffic zones such as Center City and University City.

Nutter might be able to make this move administratively, with the cooperation of the Philadelphia Parking Authority.

If the city increases its funding of the schools, the city must provide that money every year. That notion has troubled several Council members who have complained that the district is controlled by the state and doesn't have to answer to Council.

Nutter acknowledged that the city cannot obligate the district to spend money on his priorities, such as full-day kindergarten.

But he said any additional city funding would come with more accountability and a "closer relationship" between city and schools - possibly through a memorandum of understanding or directive from the School Reform Commission.

He said it would be easy to determine if the district wasn't upholding its end of the bargain.

"Some of these are pretty obvious," Nutter said. "You either have full-day kindergarten or you don't. You'll know by day two."

Several members also noted that the June 16 summer recess was an "arbitrary deadline," and that they could agree to continue working. Council also has yet to pass the municipal budget and must do so before June 30 or the city won't be able to spend money.

The School District passed a budget Tuesday, but can add any additional city and state funds later.

Nutter and his allies in Harrisburg have said the state would be more likely to restore some school funding if the city acted first. The state's deadline is June 30, but officials anticipate passing a budget early.

"There's a high-stakes poker game going on with the school; with the city, and with Harrisburg," said Councilman Curtis Jones Jr. "At the end of the day, we don't want the kids to be the casualty."

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Butkovitz calls city schools 'the worst'

City controller says district's accounting in dire shape, needs much more oversight District disagrees

A day after the School District of Philadelphia approved a budget that includes massive layoffs and program cuts to close a \$629 million deficit, City Controller Alan Butkovitz released a report that details poor accounting practices and calls for more oversight.

It analyzed the year ending June 30, 2010, and found that staff failed to explain large transactions and did not detect accounting mistakes in a timely fashion. He echoed the call for the Pennsylvania Intergovernmental Cooperation Authority to review the district's five-year plan and have regular in-

30%
Philadelphia School District facilities that are fully air conditioned, according to a spokeswoman. Students were dismissed at 1:30 p.m. yesterday due to the heat and humidity, although it is considered a full day.

volvement with the city finance director.

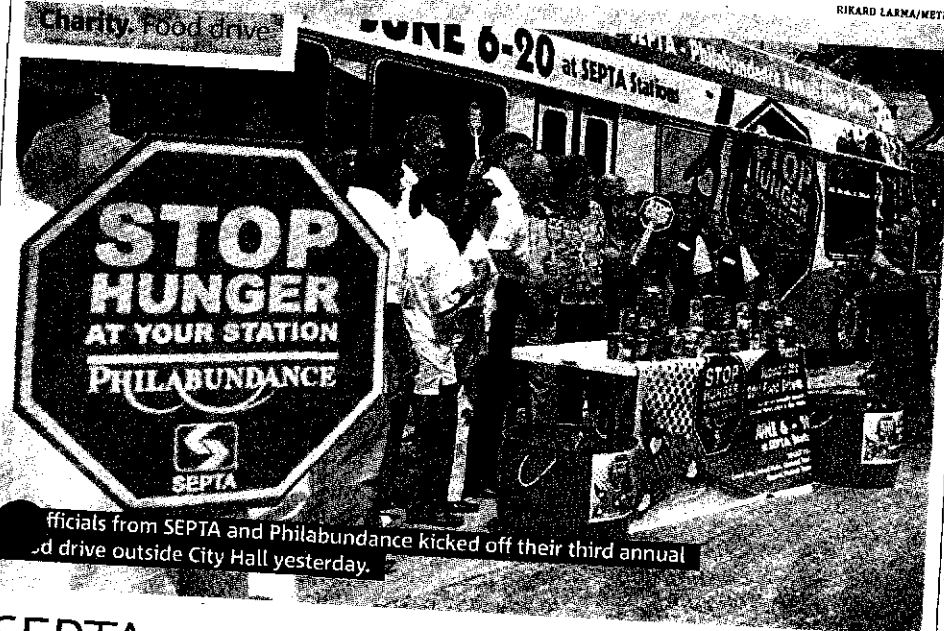
"On a scale of 1 to 10 — where 10 is the worst — the School District's combination of weaknesses registers as a 10," Butkovitz said in a statement.

The district disagrees with much of the controller's report and said it has reviewed its procedures, but it has taken significant criticism from state and local lawmakers and education activists for not doing a better job of managing its finances.

The "interim" budget approved by the School Reform Commission yesterday includes drastic cuts to transportation and full-day kindergarten, and savings from renegotiating union contracts. Some cuts could be avoided with additional state or local funding.

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RIKARD LARNA/METRO



Officials from SEPTA and Philabundance kicked off their third annual food drive outside City Hall yesterday.

SEPTA wants riders' 40 tons of love

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