

STATE ALLOCATION BOARD
AUDIT SUB-COMMITTEE HEARING

TABLE OF CONTENTS

Public Notice	Left Front Binder Pocket
	TAB
Audit Recommendations	1
Minutes	2
o April 26, 2010	
o May 17, 2010	
o July 19, 2010	
o August 23, 2010	
Work Group Document	3
o EAAP Appeals Process	
o Review of the Current Audit Guide – Document by work group members	
o OPSC Standard Document Request – Question & Answer	
o Sub-Committee Hearing – Background Document	
Legal	4
o Letter from the Attorney General’s Office	
o Legal Authorities	
Background.....	5
o December 2009 Recommendations and Timeline for Developing and Implementing a Sustainable Expenditure Audit Program for SFP	
o December 14, 2009 Audit Sub-Committee Hearing	
o New Audit Practices – District Perspective	
o Notes on August 11, 2009 Audit Sub-Committee	
o November 26, 2007 Letter from Rob Cook, OPSC Executive Officer	
o Management Representation Letter	

Below are the recommendations of the Audit Working Group:

I. SCOPE AND TYPE OF AUDITS

ISSUE	RECOMMENDATION
a. Scope of the audit needs to be defined: the School Facility Program (SFP) was intended to be a “Grant and Go” program.	Define the scope of the audit as a compliance audit. Local educational agencies (LEA) are audited to ensure they are in compliance with laws and regulations of the SFP program. Audit Guide to be revised and updated annually.
b. The audits performed should be consistent with audits that are performed by other state agencies.	Audits should be performed in accordance with Governmental Auditing Standards. Audits should commence within established time periods.
c. Ensure objectivity and independence of the audit; audits should not be conducted by the same entity that issued the apportionments.	Audits should be conducted by an independent entity outside of the OPSC. Examples: State Controller’s office or Independent Auditors. Existing OPSC audit staff and/or resources would be transferred to the responsible entity.
d. Program requirements at the time of application change over the time that an LEA submits their initial application and the time the project is audited.	Review and audit should be a multi-part process (MORE DISCUSSION IN STREAMLINING SECTION): Develop a process to ensure that LEAs understand audit requirements. A subsequent audit at the time of fund release and a separate close-out audit would also be conducted upon project completion.
e. The LEA should know the requirements for the audit at the time of application and ensure they are keeping the appropriate documentation to qualify expenditures.	SFP Handbook and the Audit Guide should complement each other and incorporate the compliance requirements in the handbook that LEAs will be audited on and allow the audits to be audited to the Audit Guide requirements. The Audit Guide should reflect and be consistent with the SFP Program Handbook, which complies with statute, regulation and guidance governing the program.

ISSUE	RECOMMENDATION
f. There is a concern that once an audit is closed out that OPSC has the authority to reopen the audit at any time and re-look at the expenditures.	Audits should not be re-opened. Additional audits may be conducted if there has been a legal finding of fraud, misappropriation of funds or other illegal acts.

II. PROCEDURES ON THE PUBLISHING AND FINDINGS OF THE AUDITS

ISSUE	RECOMMENDATION
a. In accordance with the Governor's Executive Order, audits are posted to the Accountability website.	Audits should only be published after the audit report is final and the LEA has provided a written report. Draft review of audit should be given to the LEA 30 days prior to publishing and the LEA should have 30 days to respond. Responses should be published in their entirety. Audit findings that are on appeal should also be noted with any published audit information.

III. PROCESS FOR YEARLY UPDATE AND COMMUNICATION TO DISTRICTS REGARDING CHANGES WITH AUDIT PROCESS

ISSUE	RECOMMENDATION
a. Changes to the audit requirements are not effectively communicated to LEAs. A transparent process to revise the Audit Guide should be established that is relevant to the time of the audit.	Create a standing audit committee that will do an annual review of the Audit Guide and create a process to address needed changes. The audit committee should be comprised of California Department of Education (CDE), State Controller's Office, facility and fiscal LEA staff, independent auditor, OPSC staff or other appropriate staff.

IV. STREAMLINING ACTIONS WITHIN AUDIT PROCESS

ISSUE	RECOMMENDATION
a. Program requirements can change from the time a district submits an application to the time the project is audited.	Draft an incremental review and audit process: initial consultation with program staff and desk review done immediately after funds are released. Final audit done at the time of the Final Expenditure Report. Process should be collaboration between program staff and audit staff.

ISSUE	RECOMMENDATION
b. OPSC staff does not have a good understanding of the entire cash management process within an LEA.	Provide training to OPSC staff on internal controls, cash management and multi-fund accounting not to take an advisory role but to allow for a better working knowledge of administering the program.
c. Audit requirements related to financial accounting are not coordinated with the requirements of the California School Accounting Manual (CSAM) that affects all LEAs.	OPSC staff to coordinate with CDE staff that maintains the CSAM to assure that financial documentation for audits is an integrated part of the CSAM and does not impose additional accounting burdens on LEAs.

V. AUDIT APPEALS PROCESS

ISSUE	RECOMMENDATION
a. Currently LEAs can appeal issues through the SAB. A process is needed to address audit discrepancies that have a fiscal impact on the district and the State.	Create an Appeals panel as an SAB Sub-Committee to hear fiscally related appeals. Sub-Committee to consist of representatives from the CDE, Department of Finance and the Legislature. Sub-Committee to determine appropriate process and timeline. Consider establishing a more formal appeals structure modeled after the Education Audit Appeals Panel formal process if, in the future, the Sub-Committee approach is insufficient.

REORDER INDEX OF OPSC AUDIT GUIDE

ISSUE	RECOMMENDATION
Audit Guide summarizes the audit requirements for each local educational agency.	The Audit Guide Index should be reorganized to coordinate with a revised SFP Handbook to allow better definition of the subject areas. A sample portion of an example proposed index is attached.

*Working together to improve the educational environment for
California's children*

School Facility Program

Audit Guide

A guide to assist with program reporting requirements

State of California

Arnold Schwarzenegger, Governor

State and Consumer Services Agency

Bill Leonard, Secretary

Department of General Services

Ron Dietrich, Acting Director

Stephen Amos, Chief Deputy Director

Scott Harvey, Chief Deputy Director

State Allocation Board

Office of Public School Construction

Lisa Silverman, Acting Executive Officer – SAB/OPSC

Lisa Kaplan, Assistant Executive Officer – SAB

Prepared on behalf of the

State Allocation Board

by the

Office of Public School Construction

www.opsc.dgs.ca.gov

SAB Audit Working Group

Contents

Section 1 - Reporting Requirements and SFP Audit Overview 1
 Overview 1

- *Include a flow chart detailing the process of building a school.*
- *Discuss audit process*
- *Purpose – defining scope / compliance audit*

Section 2

SFP General Audit Requirement for all Programs

- a. *Information that is applicable to all programs (100%)*
- b. *Audit Procedures related to the following forms*
 1. *Various Stages of Audits*
 - i. *50-04 Application for Funding*
 - ii. *50-05 Fund Release*
 - iii. *50-06 Expenditure Report*
- c. *Eligible and ineligible expenditure principles*
- d. *Material Inaccuracies*

If the current information does not fit in the new sub-sections – look to see if it goes into background or appendix

Section 3

Individual Program Compliance and Audit Specifics

Discussion of the entities: Charter, School Districts, County Offices (Local Educational Agencies)

- a. *Joint-use*
- b. *High Performance Incentive Grant*
- c. *Financial Hardship*
 - *School District*
 - *County Offices (exceptions)*
 - *Automatic qualifier (\$5 million bonding capacity)*
- e. *Facility Hardship*
- f. *Charter School Facility Program*
- g. *Emergency Repair Program*
- h. *Seismic Mitigation*
- i. *Labor Compliance Program*
- j. *Critically Overcrowded Schools*
- k. *Career Technical Education*
- l. *Overcrowded Relief Grant*

Discussion of Certificates of Participation in handbook area.

SECTION 4: APPENDIX

Check list approach

Sample documents

Audit Working Group
State Allocation Board – Subcommittee on Audits
Monday, April 26th
State Capitol Room 2040
9-Noon

Minutes / Notes:

I. Schedule of Meetings

- 1) Monthly – 3rd Monday of the month from 10-1pm.

Next Meeting

Monday, May 17th - State Capitol Room 2040, 10am-1pm

II. Membership of Audit Working Group

FCMAT – Debi Deal

Treasurer’s office – Blake Fowler

CDE – Arlene Matsuro

OPSC – Rick Asbell / Steve Inman

County Office of Ed Schools Consortium - Andrea Sullivan

CA Assoc School Business Officials (CASBO) – Lettie Boggs

Independent School Auditor Expert - Shilo

State Controller’s office – Casandra Moore-Hudnall /

School Facility expert – Kathy Allen

California County Superintendents Education Services Association – Mike Ricketts

III. Objectives

The Working Group agreed to the objectives of the audit working group below.

The charge of the audit working group is to review current and existing junctures of accountability at the state and local level, including at various stages within the State Facilities Program (SFP) in order to avoid potential redundancies and limit inefficiencies within the SFP Expenditure Audit Program.

In this regard it is the objective of the audit working group to provide recommendations to the State Allocation Board (SAB) subcommittee on audits that define the scope of the Office of Public School Construction (OPSC) audit authority and to draft recommendations for the audit subcommittee to consider as to what is the best use of state

and local resources, including the junctures of accountability with the use of state bond proceeds to build a school.

Also, the working group is charged with drafting recommendations for establishing an audit appeals process that ensures a transparent, consistent and equitable appeals process for SAB consideration.

The specific issues that should be addressed in the working group as requested by the SAB Audit subcommittee include, but not limited to:

- Process: law, regulation, policy and procedures
- Scope and types of audits being done and recommended
- Content of audits
- Transition issues
- Addressing redundancies
- Promoting best practices
- Communication with School Districts

IV. Administration of Meetings

1) Rules of Conducts of Working Group

1) Discussion of Working Group Rules of Conduct (*The Working Group adopted the following rules of conduct*)

- **CHAIR BEGINS MEETINGS ON-TIME:** Out of Respect for all involved in the working group, the meeting will begin on-time or no more than 5 minutes late.
- **DECORUM:** Questions maybe asked or comments given after the AEO has recognized the working group member who has raised their hand. The order of the questions will go in the order the Chair visualizes those members who wish to speak.
- **MATERIAL INFORMATION:** In order for document to be considered by the working group, the documents that contain material information pertinent to the discussion of meeting the objective of the working group, including those documents presented to any or all of the SAB shall be submitted to the Assistant Executive Officer (AEO), no less than seventy-two (72) hours prior to the next working group meeting, of which the AEO will then send on to the working group for review.
- **GUEST COMMENTS:** The working group membership was selected by the State Allocation Board audit subcommittee; this is not an open working group. The

2) **Discussion of Ground Rules** (*See Attached Document*)

1) Adoption of Ground Rules (**Adopted rules**)

3) **Guiding Principles**

1) Adoption of Guiding Principles (**Adopted principles**)

- **Purpose:** Begin each meeting with an agenda and vision of what the committee wants to accomplish and what a successful meeting would look like. Set clear expectations by creating agendas that ask questions to focus the work and lead the working towards a positive and productive meeting.
- **People:** Arrive to the meeting prepared and ready to work together on finding a solution. Be prepared to offer solutions, not just complaints. Make sure everyone has a clear understanding of their role and feels confident in how they can best contribute to a productive working group. If a member is going to miss a meeting, please have one set alternate member and inform the AEO that the alternate will be serving in the members' absence at least 48 hours ahead of time.
- **Process:** Everyone gets the chance to be heard and share ideas. Time will be spent on answering questions, problem solving, and drafting solutions. At the end of the meeting, everyone should be clear on how to move forward, what stands in the way of resolving an issue and what is expected of them.
- **Progress:** Revisit the meeting purpose, role and process frequently to make sure that it leading towards a productive working group. At the end of each meeting the Chair will summarize the direction and to-do list for the next meeting and send out meeting minutes within two weeks.

V. **Discussion on Meeting Charge of Audit Working Group**

1) **Define Scope of OPSC Audit**

a) **Issues to Address with Scope**

- (i) **Process:** law, regulation, policy and procedures
- (ii) **Scope and types of audits** being done and recommended
- (iii) **Content of audits**
- (iv) **Publishing findings of audits**
- (v) **Transition issues**
- (vi) **Addressing redundancies**
- (vii) **Promoting best practices**
- (viii) **Communication with School Districts**

2) Review current and existing junctures of audit accountability at the state and local level

- a) Plan to accomplish the task – seeking Working Group Suggestions

3) Audit Appeals Process

- a) Plan to accomplish the task – seeking Working Group Suggestions

Discussion:

How can you define the scope of the OPSC audit? What is the objective of an OPSC audit?

- Name the objective
- Name the type of audit
- How does this fit with Prop 39

What was OPSC communication process in going from desk to field audits?

- consensus from the field was that there was no communication and took all districts by surprise regarding new standards and scope of audit

Overview of the different types of audits

- OPSC (construction)
- Independent Audit (yearly required by law)
- County Audit (financial)

OPSC states that they do a “program compliance” audit – following statutes and regulations. OPSC is now looking at internal controls and assessing the staff process to assure fiscal accountability.

Concerns about changes without notification regarding the documents needed for the new audit process. Rules at OPSC seem to be constantly changing without proper notification to districts so that they can comply.

FCMAT: 3 types of audit

- Fraud audit
- Mgmt assistance audit: spending guidelines to expenditures
- Prop 39 audit Performance audit

OPSC AUDIT

- Specific SFP program criteria

- Policy and statute and regulations audit
- Fund release compliance
- Expenditures
- Internal controls
- Required match and savings
- New field audits – includes everything included in desk audits before, but now includes financial stmts rather than ad hoc docs
- First hand access to staff and source documents
- Compliance is the main focus, with constr program in perspective, new internal control examination for instructions at the staff level (desk guide), int contr req documentation

Comments about OPSC audit:

- The rules have always seemed subject to change, which has built mistrust from school districts to OPSC.
- How can the working group simplify the audit process and expectations so that districts can be in compliance
- Concerns about gotcha and Material Inaccuracy (MI) applying, Working Group discussed that the same weight applies to various level infractions.
- Concern that there are no layers within mistake at OPSC, where as with yearly independent audit there are several layers of deficiencies: “control deficiency” or “material weakness deficiency”
- How is OPSC handing internal control verification? The controls and people change over the course of the 5-7 year process for building a school?
- How is OPSC going to handle if during the internal control review OPSC determines there are perceived deficiencies? How is this handled if the District is still in compliance with SFP but OPSC determines there are internal control deficiencies? (i.e. the District is in compliance with the proper use of all state funds)
- SFP does not give OPSC authority over local contracts, so why would OPSC be reviewing them?

Independent Audit: In a financial audit there are minor, significant, material weakness which can result in a material misstatement. The layers allow communication that promotes appropriate response. Is this something that can be applied to OPSC and MIs? Currently, the yearly independent audit conducted with every school district reviews the internal controls, why does OPSC have to review this as well? The annual audit is compliance with federal auditing standards, in which documentation is reviews and tested against controls the district has in place.

OPSC Response:

OPSC gathers information from initial audit interview whether there are controls in place currently and if district staff is aware of them. For example, do districts have contract monitoring? Looking for degrees of reliability. Review competitive bid process.

Stakeholder Comments:

- Recommend line in the sand for new practice. Does district size matter with standards?
- Do the internal control determine the scope of the audit?
- Would it be better to include those components in the annual audit when in the state program? That would shift cost to districts.
- There is always an internal control element when you develop the scope of the audit.
- What are the internal controls meant to verify? Validate controls or determine compliance?
- Do the internal controls lead the OPSC audit? Is the proper local internal audit controls a factor or condition of funding by the state?

ROLES OF DIFFERENT GOVERNMENTAL AGENCIES IN AUDITS

TREAS OFFICE – determines bond sales, type and quantity.

Treasurer sells bonds, Finance determines which bond acts get the money, OPSC determines which projects get the funds from which source and work with Treasurer's office on tax compliance certificates. Treasurer's office cares that districts use the funds consistent with how they qualified for the money. Care about savings/interest, impose some reporting requirements. Per state law, grant document retention is required for 35 years. Their main concern is to make sure projects get funded that OPSC said would get funded.

CONTROLLER OFFICE – Oversight of all LEA audits, quality of audits, compliance with standards and quality control. Controller's office is responsible for the yearly update of the annual audit guide for the Education Audit Appeal Panel. All Districts know what to expect with the scope of the audit and if there are new guides they are outlined in the audit guide when updated yearly.

CDE – AUDIT RESOLUTION AUDITS – resolution of annual audit issues, and the annual audit guide. Guide comes out prior to the fiscal year. Process includes representative group meeting several times a year to address audit issues and produce audit guide annually. Controllers office is the tie breaker. The group meets 2-3 times a year from Sept to Jan/Feb and publish the finished product for district to rely on for their annual audit.

OPSC – clarified “audit guide” terminology. OPSC rarely changes the audit guide and believes current document is in compliance with the new audit procedure the OPSC has implemented. OPSC stated that they review timing of the fund release, reconcile the reports and district contributions and check internal controls. OPSC believes that the audit guide should not be updated because the guidelines are proprietary.

INDEPENDENT AUDITOR – looks at the audit guidelines as minimum standards, and internally each auditor has their own methodology, but the steps of the audit are public information. Independent auditors tend to go beyond the guide, but always imbed it in the audit. It is known and very transparent to all involved.

OPSC reiterated that the OPSC audit guide lays out the basic compliance features, but everything else is proprietary.

Stakeholder comments:

- Would like to look at the Independent auditor guide, before that existed we had very similar issues in annual audit issues that exist now in the OPSC audits. The annual audit guide produced for districts has solved those issues, and allowed input from the field. Can this be done with OPSC’s audit guide?
- The inconsistency of the audit guide presents a challenge. If it is just posted as outreach, it isn’t that helpful for district. And if it is interpreted differently by the district and auditor, there is no way to bring that together because there is no proper appeal or notification process with new audit procedures.
- Concern about lack of training of new OPSC staff and understand the program. Districts fell like they spend too much time training OPSC staff on the program to understand it, so they know what they are auditing.
- Working Group recommended that professional development training is given to all new OPSC staff regarding school construction, and the different SFP programs.
- Communication of changes to the document would be very helpful. There is no transparent revision practice. Changes to wording in regularly issued letters to districts raises concerns and issues of transparency by OPSC.

In response to OSPC’s concern about proprietary information: the Controller’s office indicated that the methodology of the audit is not shared, but the concept of what to expect is known and should be shared. No reason to be concerned about a proprietary approach.

Question: who is responsible for the procedures in that audit guide at OPSC and keeping it up to date? OPSC should look to EAAP audit guide as underlining the new steps and processes that OPSC should adopt.

OPSC response: If the district has complied with the fund release provisions, and the expenses reconcile to the financial statements, there is clear documentation of the funds used = a good short audit. Timing, fund release, reconciled reports, district contribution are the criteria.

Comments:

- Compliance objectives should reflect best practice to promote good work all along. Having OPSC explain “why” is important and this is not being done?
- Changes made by OPSC need to be highlighted so that districts can respond. This is not districts primary job, so training and workshops need to be a focus so that people know what to do, when OPSC changes audits and this way not done with the most recent change from desk to field audits.

RECOMMENDATIONS FOR NEXT MEETING:

- 1) **Review Procedures for Audits of California K-12 Local Education Agencies 2008-09 at guide as a model for OPSC audit guide.**
- 2) **Look at streamlining audit process where audits can be done throughout the construction timeline and close out specific portions** (i.e. audit after site purchase and close out and not wait until the construction project is complete).
 - This is a concern because 99% of the baseline SFP audit guideline is post fund release and after the project is finished which could be up to 6 years after the district received the funding
- 3) **Look at a process for keeping audit procedures relevant and what the process should be for keeping Districts up to speed with changes to programs and how they will be audited before the audit process begins.**
 - Rules and procedures should be developed when programs are created or changed.
 - Need to look at new programs and make sure that the changes in programs are acknowledged in the audit process too. The audit rules should come out with the program. And program rule changes should run through audit too. Changes cause confusion and mistrust.
- 4) **Create Transparency with in OPSC**
 - Comment: At the end of the day, most school district are trying to get the job done right. Transparency works to provide a sense of relief and knowing what to do. OPSC folks have never worked in schools. We need

ASSIGNMENTS

LETTIE ANDREA CATHY MIKE – WITH OPSC – review the OPSC / CDE EAPP audit guide plus other relevant data that should be used to update the OPSC audit guide

CONTROLLER, CDE, INDEPENDENT AUDITOR, FCMAT – draft what an appropriate appeals process should look like

ALL - Discussion of all or nothing audit findings, MI's and giving the money back. Bring back additional alternatives other than the current process being handled by OPSC.

BACKGROUND FOR MEETING

Reviewed both the May 2008 Audit Guide prepared by OPSC and the Standards and Procedures for Audits of California K-12 Local Education Agencies 2008-09 and offer the following comments:

- May 2008 Audit Guide (OPSC)
 - This guide was prepared approximately 4 years following the commencement of the ERP program. Prior to this guide, I do not recall if there was anything other than the reporting forms available as a resource for school districts. This would be a good question for the OPSC staff.
 - On page 5 under “Expenditure Audit Reporting Requirements – Specific Guidelines, there is a reference to SAB 61-03, Part A, Number 8. When I look at the on-line form, Part A only goes to Number 4. Perhaps I’m missing something.
 - Overall, it is my opinion that the guide is vague and leaves much to interpretation.
 - I have heard from professionals completing the 61-03 grant request forms that OPSC staff have requested districts to go back to the original assessment form (which was completed by a licensed architect) to justify the estimated cost 4 years after the assessment was prepared. First, the costs then and now have changed dramatically. Secondly, this was not communicated to districts when the assessments were prepared. Third, districts may have new architects since that time. Lastly, this is an additional cost now to the districts whereas the assessment costs were advance funded to prepare the original assessment cost and OPSC is not paying this additional costs.

- What is frustrating to districts really is this “after the fact” or “change the rules or add new rules along the way” mentality that seems to resonate with OPSC staffers/auditors.
- Standards and Procedures for Audits of California K-12 Local Education Agencies 2008-09
 - This is a very comprehensive guide that offers specific audit procedures for each audit component. For example, Section 19828.3. Instruction Materials, has very specific steps that the auditor will use to verify compliance with Education Code:
 1. Verify that the district passed a board resolution
 2. Verify that the district provided a 10-day notice of public hearing
 3. Determination of time, place and purpose of the hearing
 4. Determine that the meeting was held at a time that encouraged parental involvement
 5. Determine that the resolution statement included certain language
 6. Verify that the governing board made written declarations
 7. Verify that that governing board determined availability of labs

It is important that districts know exactly what the auditors will be testing so they can be in compliance. The audit guideline and verification process should be as transparent as possible.

Audit Working Group

State Allocation Board – Subcommittee on Audits

Monday, May 17th
State Capitol Room 2040
10am – 1pm

Notes From Audit Working Group:

I. Schedule of Meetings

- 1) Monthly – 3rd Monday of the month from 10-12:30pm.

Next Meeting

Monday, June 21st - State Capitol Room 2040, 10am-12:30pm (**Cancelled**)

II. Membership of Audit Working Group (Attendance) ✓ = *in attendance*

✓_ CA Assoc School Business Officials (CASBO) – Lettie Boggs

California County Superintendents Education Services Assoc – Mike Ricketts

CDE – Arlene Matsuro

✓_ County Office of Ed Schools Consortium - Andrea Sullivan

✓_ FCMAT – Debi Deal

✓_ Independent School Auditor Expert - Shilo Gorospec

✓_ OPSC – Rick Asbell / Steve Inman

State Controller’s office – Casandra Moore-Hudnall / Walter Barnes

✓_ School Facility expert – Kathy Allen

Treasurer’s office – Blake Fowler (*on as needed basis*)

III. Discussion on Meeting Charge of Audit Working Group

- 1) **Look at Controller / CDE EAAP guide as a model for updating OPSC audit guide.**

- Identify areas of weakness in OPSC audit guide that needs to be updated

- 2) **Create a Process for handling the following items with OPSC audit**

(i) Scope and types of audits being done and recommended

(ii) Publishing findings of audits (Material Inaccuracies)

(iii) Process for yearly update and communication to district of changes within audit process

- 3) **Streamline current and existing junctures of audit accountability at the state and local level**

- Look at streamlining audit process where audits can be done throughout the construction timeline and close out specific portions.
- Identify redundancies and address them in drafting what the scope of OPSC audit should be.

4) **Audit Appeals Process**

- a) Review Education Audit Appeals Panel appeal process and draft process similar for OPSC
- b) What should an appropriate appeals process at OPSC look like / what is the proper timeline to address?

Discussion:

Review of the Current Audit Guide In Comparison with the New Audit Practice

Provided for the Audit Working Group Meeting, May 17, 2010, by:

Andrea Sullivan, Orange County Office of Education

Lettie Boggs, CASBO

Cathy Allen, Western Placer Unified School District

Mike Ricketts, CCSESA

We were tasked with reviewing the current OPSC Audit Guide. We focused our discussion on the variance between the current audit guide and the current audit practice. The comments in this review are for the regular program, not necessarily the Financial Hardship program, which legitimately includes a more rigorous scrutiny. However some elements of the review will apply to both.

We did not provide a line by line assessment as the broad concept discussion seems to need to precede that lengthy process.

Site Visits

Previous audits were not in-district unless there was an issue that brought the district to a very detailed audit level. A recent change has been the shift from desk to field audits where OPSC is coming to the districts. This probably facilitates faster audits and is appropriate. Districts just need to know that this is routine practice now.

With respect to actually going to sites to verify that the work granted is work completed, DSA already has a very well qualified person on site throughout the project who verifies that the DSA plans have been constructed. The Inspector of Record is state licensed by DSA. They have personal knowledge of the job and verify at project end that all components were constructed. A slight addition or modification to the final verification document could assure OPSC that the DSA plans which were the basis of the grant are legitimately done.

To have a person unfamiliar with plans verify from the basis of a map, via cursory visit/review that the approved plans were constructed is duplication at a less appropriate level than already exists.

WG Discussion:

- Concern that there were no prior notices to districts regarding the new adjustment with the audits from field audit to site audit.
- Districts were concerned because it was sudden change made without any input from districts or SAB.
- OPSC currently is giving districts a 15 to 21 day notice of intent to begin a field audit in the district, but will grant extensions. 15 to 21 days is not sufficient notice to a district before the field audit begins.
- **Working Group Recommendation:** The working group recommended a longer notice timeline – 60-90 day notice, because Districts need time to make sure staff has the time to dedicate to auditor visiting since OPSC may be in the district anywhere from 1 day to 1 week, which significantly impairs the ability of district staff to complete their normal workload. Requesting OPSC recognize districts schedules and is sensitive and works with district to accommodate meeting schedules and calendar timelines. Districts need to know how long OPSC is going to be on-site.
- **Working group recommendation:** Requesting outreach by an OPSC auditor (45 to 6 days prior to arrival) to the District detailing the list of documents needed for OPSC to conduct the audit to help streamline the process.
 - **Add to Audit Guide:** select sample documents that OPSC is requesting from districts. However, allow for OPSC to due sampling of documents that are still within the defined scope of the audit.
 - **Add to Audit Guide:** add a sample checklist to the audit guide that districts need to keep and have for the field audit.
 - **Add to Audit Guide:** Include an introduction in the field guide as to what the field visit is going to entail.
- OPSC stated that audits have not changed, audit have always been required, just that this is allowing for source document review, can have a visual inspection and verification of number of classrooms built, but that a review of internal controls is new.
 - OPSC indicates the audit process is continually developing and changing to expedite the process, thus it is difficult to work constantly request feedback from the districts with any change, but that OPSC really wants to work with the district.
- In general - auditors want to see originals vs. copies – field audit is the norm unless required specifically they do not focus on compliance
- What is the designated scope of the field audit and site visit? Are district's aware of that?
 - Evaluation of controls and risk a good thing; keep audit more focused
- **Question re:** clarification of what District's need to do now regarding making the 50-06 match the general ledger. Is this now a norm with the field audit? Past practice was to account for the grant and the match with a little extra in case something is disallowed. This is of concern because, if the only place the change is mentioned by OPSC is in the instructions, not all districts will read that. A discussion then ensued as to why the general ledger might not match 50-06 specifically explaining the scope of the audit needs to be explained so that new rules and procedures are not made up on the spot that have nothing to do with the compliance / field audit. The parameters of the audit must be defined.
- **Working group recommendation:** An overview of the process of communication between OPSC and District should be in the overview part of the guide. This should include the scope of the field audit.

- **Working group recommendation:** goes back to account code structure. Perhaps we need to define in the account code structure how we track the programs. As I went through the Audit Guide, looking for streamlining, spell it out and say what the documents that you want to see are.
- **Scope of Site Visit Discussion:**
 - Districts do not report over 50% of how they spend their money. Now OPSC wants districts to report all of it.
 - Past practice is that districts just reported 50% with new construction to show accountability on the state money received
 - OPSC indicated that it is good for them to know what everything costs.
 - Questions included why the shift in policy....what problem is OPSC looking to resolve?
 - **Recommendation:** there should be a process implemented whenever there are any changes with the auditing process. OPSC should not have the authority to audit issues outside of the state share of 50% of money received. This needs a definition to refine / define the scope of the audit.
- Discussion of **Incremental Audit** ~ the WG expresses interest in the concept of an incremental audit. (i.e. audit when site /design [plan approval stage] is finished and close that out and 2nd audit is for funding and construction)
 - **Recommendation:** put this in the audit guide as a potential change for the SAB subcommittee to discuss and give direction on.
 - **Discussion** ~ there were questions as to whether this would undo the self-certification process – and the WG discuss that no it would not undue the self-certification process, nor would it slow the process down – it will allow error to be discovered and corrected sooner rather than 6-8 years later when the project is getting a full audit and you bought the site possibly 8 years earlier.
 - Other WG members agreed that this would prevent districts from duplicating the error unknowingly. There would be a higher comfort level in districts moving forward, knowing they were good to go.
 - Checks and balances are built into the independent audit the district yearly goes through were auditors may work with DSA to verify that a project was actually built.

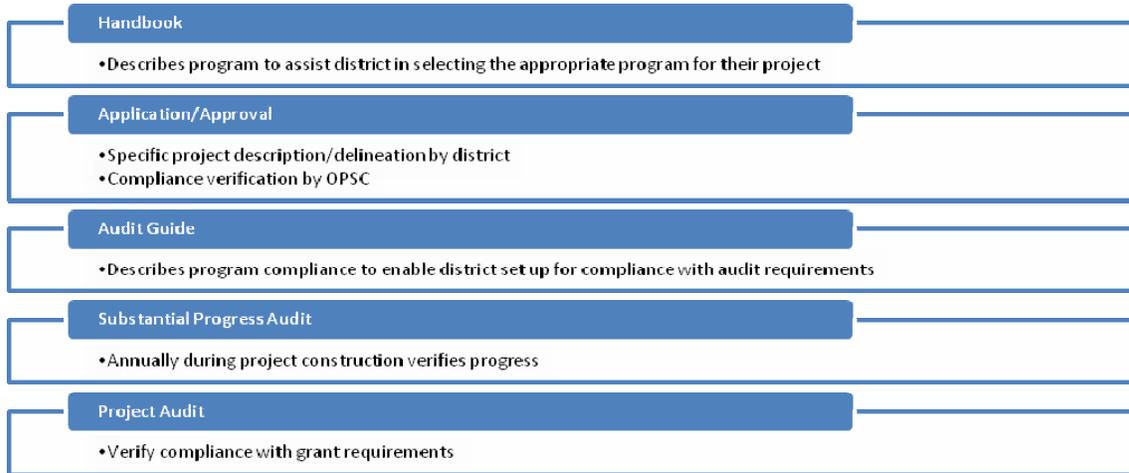
Entrance Interview

OPSC is saying that they inform districts of the elements of the audit at the time of the entrance interview. Districts are saying that they need to know before they account for the project, which is much earlier. Districts must rely on the Audit Guide for rules of compliance.

The current guide does not describe the current process, so districts are unaware of the requirements of compliance. OPSC's Advisories Actions/Building Blocks should be incorporated into the guide so that there is a comprehensive documentation that districts can refer to in developing their compliance documentation.

Advisories in general are frequently provided because of new program elements or the provided guidance is unclear or inadequate. The need to further explain should trigger updates to the guide. Guidance should also be accurate, for instance the Advisory Action of May 24 regarding SFP F&E, incorrect guidance is given stating the inventory rules of the CSAM rather than the Capital Outlay guidelines as the rules of the audit for F&E. So the source they are referencing is not the correct section and very different rules should actually apply.

This particular example shows how this lack of understanding on the part of OPSC could result in different rules within the program than for all other capital outlay funding. This creates issues regarding consistent training of staff, etc. Not to mention calling into question most of the F&E appropriate to a project with respect to being allowed by audit. The typical process of information and verification previously followed and still in place is illustrated below:



When the project audit significantly differs from the guidance, districts cannot anticipate the audit process. This causes the program to lose the effect of the audit guidance promoting good practice, and it makes the districts vulnerable to audit exceptions that could have been prevented if the process was coordinated.

WG Discussion:

- **Working Group Recommendation:** OPSC to send the required document list so that people are aware of the process ahead of time, give districts a 60-90 day notice, negotiable with district schedule. A more efficient upfront communication process will allow sampling to be more effective, thereafter the depth of audit is determined by the sampling findings.
- How will OPSC deal with small districts? Full audit with them? Everyone on the audit panel stated that all districts no matter size should expect the full audit always. That’s the logistics of it.
- Discussion of why vetting is needed and process needs to include stakeholders. Methodology of including new audit processes without obliterating the old information is needed to allow folks to know which guidelines will apply depending on when the project was started. Living record of changes is imperative.
- **Working Group Recommendation:** Audit guide needs to keep reference to old guidelines as a base then update with new rules within the audit guide and SAB must create a process for updating guides / rules and how to communicate with districts.
- **Working Group Recommendation:** Establish an upfront communication plan from OPSC to the District, which includes
 - List of docs required by district
 - Timeline – notification 45-90 days before audit is going to begin and request a sampling of the documents needed.
 - Process for requesting an extension if needed
 - How long OPSC plans to be at the district to allow for district to plan accordingly

- If you have only one project expect full audit or discussion on how to handle a multiple project audit at once
- Discussion occurred that indicated just putting out new processes in the OPSC communication tool Building Blocks is insufficient and that should not be considered “communication” with districts – especially when a new policy is put in place without any prior feed back from districts.
- **Working Group Recommendation:** establish a process where audit guide book is updated yearly – suggest modeling process similar to Education Audit Appeals Panel process.

Internal Controls and Fraud Policy

These elements are already routinely audited by the Fiscal Audit. Inclusion in the OPSC compliance audit is redundant with the other audits already performed. We acknowledge that in a risk based audit, it is standard practice for each auditor to determine risk for themselves. And this appears to be the level of review now in the OPSC process. However, if the purpose of the OPSC audit is to verify compliance with the grant requirements, then the risk assessment for the compliance audit should be in relationship to the risk of non-compliance, which is of more limited scope.

When auditing the use of state bonds, it is important to verify the use based on the state bond criteria. However, if the granting complies with state bond language, then the verification would need to represent compliance with the grant. (Savings methodology could use a restricted reserve approach, and use of restricted funds could be routinely audited for compliance with the restriction. But that is another issue, though related.)

We would like to explore a more coordinated approach that does not involve multiple redundant analyses for the districts and that targets the risk assessment of the OPSC audit to the projects being audited. This would result in time savings for all.

- Questions were asked about OPSC’s new policy to test internal controls and the fraud policy...what is the appropriate scope for OPSC to have during audits?
 - **WG Recommendations:** Scope of grant should define scope of audit, and that OPSC should only be allowed to request to see that there are internal controls in place. However, it needs to be defined what will be required, ex: internal controls. Scope should be specific.
- What are the guidelines OPSC has to follow with the government auditing standards? Current practice is that CDE is silent regarding the controls they use, and an independent auditor applies their own tests as well. The feds care, so they define it. Should OPSC define it as well?
- Question regarding if there an opposition here to define the audit features here that OPSC uses? Internal controls are not defined, but maybe it should be clarified. Auditors look for consistency of accounting/records and staff (particularly key man change structure generally with internal controls – so why would OPSC have to re-review and test internal controls if already tested with yearly independent audit.
 - OPSC claimed that in some reviews they found that the fiscal auditor comments showed a lack of knowledge of the SFP program.
- Most of the working group expressed a desire for OPSC to have– clear communication of acceptable documentation, and process.

Audit Reports, Comments, and Responses

Requirement of audits and related comments and responses also goes to the risk assessment and the appropriate type of risk assessment for a compliance audit.

WG Discussion:

- Discussion surrounded the process by which OPSC releases audit reports and allowing districts to respond.
- **WG Recommendation:** set up a process similar to that of responding to a grand jury report before it is published and released.

Unique Coding String

This is a good practice and OPSC audit should require it to encourage good practice. Methodology should be coordinated with the SACS office and verified during regular audit so that it will be there when they get to the OPSC audit. There is a wide variance of accepted practice in the location of the unique identifier within the coding string as the ultimate form and length of the string varies by county, and the number of projects varies by district.

It is not possible to go back and require this of projects that did not implement it during the project. There are ways to track a project in a subsidiary system to the GL so that full data by project is known.

WG Discussion:

- **Recommendation for OPSC to adopt unique coding string and coordinate with CDE Sacramento office.**

General Ledger Transfers

Absent any guidance regarding why they are looking at transfers, districts don't know what criteria is being assessed by the look at their G/L. Is this to determine cash management? If so, it is unclear why OPSC looking into this is of any value to the state. There are several methods of managing cash, they are not right or wrong, they are just different. They typically reflect the location of the management within the district departs. That is, it looks different when use of cash source is determined at the PO level, the CBO level, or the Facilities Dept level.

For Financial Hardship districts the full G/L review is appropriate, but may not be necessary for the regular program. The G/L component may be more appropriate to evaluation by the fiscal auditors as a component of the overall analysis of the management of the funds of the district.

Conclusion Discussion / Thoughts:

- Regulations and guidelines seem to have been modified in the Guide without retention of the previous knowledge. They come out later after people have been in the process. And they appear to occur without stakeholder input. This is a problem that needs to stop.
- From professionals in the field filling these forms out that OPSC has created, the issue of the guidelines not being timely is problematic. (ERP example) Level of detail was not communicated at the time. Can result in increased costs if new assessments are required – from different architect

- OPSC need to be clear regarding the rules / procedures / guidelines and they are not
- EAAP -Standards & Procedures for Audits, is a very specific guide – OPSC should use their instruction manual as an example of how to do of compliance audits
- Everything in the guide has been discussed with districts between the EAAP and the standards so that everything is clear and the rules are fair before they go in the guidelines. Why can't OPSC do this?
- Sample testing in an audit is one of the more difficult things to define and explain. We want auditors to apply consistently, so it needs to have that level of clarity in the audit guideline and trained to OPSC staff
- Any changes to audit guides and procedures needs to be on a timeline that makes sense with the calendar with the district.
- OPSC should only audit projects based on the regulations / guidelines in place in which the project received funding
- Please draft a sample appeal item document and bring it back to working group to discuss
 - For example a school district in the past had an appeal item re: a funding release. The process wasn't very kind to the district nor was it transparent; it took three trips and then the SAB appeal. Staff to public forum, no in-between or attempt to find consensus or talk to the district.
 - The audit guideline should set out a process that requires the district, OPSC, AEO, with EO to have a meeting to reach a final agreement before the item is appealed and heard at the SAB.
 - There are no levels in-between with an audit – either it is fine or an MI. Since staff really does not have authority to adjust, audit guidelines should set forth a process the district needs to go through with an appeal.
- All - The EAAP process would provide a better option, and should be explored for the re-write of this audit guide.
- Perhaps needs coordination with the Rules Sub-C.
- Are the audits now requiring districts to pay back funding? Yes.
 - Issue of “Auditors are the grantors” and whether that is an issue of inappropriate agency to audit, what about a 3rd party? OAH, Administrative law judge, FCMAT, or someone else not tied to DGS.

Audit Working Group

State Allocation Board – Subcommittee on Audits

Monday, July 19, 2010
State Capitol Room 2040
10am – 1pm

Notes From Audit Working Group:

I. Schedule of Meetings

- 1) Monthly – 3rd Monday of the month from 10-12:30pm.

Next Meeting

Monday, Aug. 23rd (note it is the 4th Monday of the month)

II. Membership of Audit Working Group (Attendance) ✓ = *in attendance*

✓_ CA Assoc School Business Officials (CASBO) – Lettie Boggs

✓_ California County Superintendents Education Services Assoc – Mike Ricketts

✓_ CDE – Arlene Matsuro

✓_ County Office of Ed Schools Consortium - Andrea Sullivan

✓_ FCMAT – Debi Deal

✓_ Independent School Auditor Expert - Shilo Gorospec

✓_ OPSC – Rick Asbell / Steve Inman

✓_ State Controller's office – Casandra Moore-Hudnall / Walter Barnes

✓_ School Facility expert – Kathy Allen

Treasurer's office – Blake Fowler (*on as needed basis*)

III. Charge of Audit Working Group

- 1) **Look at Controller / CDE EAAP guide as a model for updating OPSC audit guide.**
 - Identify areas of weakness in OPSC audit guide that needs to be updated
- 2) **Create a Process for handling the following items with OPSC audit**
 - Scope and types of audits being done and recommended
 - Publishing findings of audits (Material Inaccuracies)
 - Process for yearly update and communication to district of changes within audit process
- 3) **Streamline current and existing junctures of audit accountability at the state and local level**
 - Look at streamlining audit process where audits can be done throughout the construction timeline and close out specific portions.
 - Identify redundancies and address them in drafting what the scope of OPSC audit should be.
- 4) **Audit Appeals Process**

- Review Education Audit Appeals Panel appeal process and draft process similar for OPSC
- What should an appropriate appeals process at OPSC look like / what is the proper timeline to address?

IV. Action Item

- 1) **Amend the OPSC Audit Guide to reflect the Charge of the Working Group to resolve the issues discussed in prior Audit Working Group meetings.**

Comments:

The meeting opened with the AEO indicating that the SAB appreciates the amount of time and work everyone has put into this, and this process will continue and hopes to wrap up at the September meeting.

The first two meetings the Working Group (WG) has established a base on the audit, and the next step is to update and modify the audit guide.

Audit Working Group Focus

- New guide with field audit info
- Guide update process
- Audit and appeal process/standards

Discussion:

Lettie, Andrea, Cathy, Mike –along with OPSC – were asked to review the OPSC / EAPP audit guide plus other relevant data that should be used to update the OPSC audit guide. Lettie presented on behalf of the groups discussion and recommendation in the following 2 documents.

1. OPSC Standard Document Request
2. Audit Working Group – Input Draft July 19, 2010

Checklist Discussion:

- Potentially putting a checklist in the guide
- Establish Standards but not an all inclusive list that is rigid
- Review Suggested checklist of any additions or deletions
- List of primary documents and breakout new and modernization with documents needed.
- Keep primary background documents as an information item and not part of the audit guide.

The reasoning behind the discussions and check list documents is to remember the purpose of this WG is because communication is missing between OPSC and the district. The reasoning behind the check list is because of the mis-communication that often occurs between the school district

and OPSC regarding what documents may or may not be needed for an audit. There needs to be an index to the audit guide that would inform a school district of what they have to have for an audit.

Incremental Audit Discussion:

- The working group has had substantial discussion regarding incremental audits and the concept has been received favorably.
- Comments regarding that there may be issues that an incremental audit might not necessarily work with new construction because of all the changes that occur with new construction..
- How do we handle site closeout?
- Expenditure – construction
 - a) Can we audit every 18 months?
- Finalize a recommendation and get SAB feedback.
- Suggestion of auditing based on percentage of money expended
- Annual submittal of 50-06 by district to OPSC
 - a) Can this be the audit?
 - b) Issues: Corrections prior to submittal (DLOP)
 1. DLOP – OPSC look as consistency with yearly report. OPSC review them.

Discussion occurred regarding making the working group more effective, and members looked at composition of who's working on what so working group is more productive with a variety of members taking part of the discussion. There were reminders regarding:

- What is our task
- What is auditable
- How does 50-04 work with audits
- What is a district looking for and what do they certify?

OPSC expressed apprehension as defining the audit guide, as what auditors use to define their work, it should be used as more of expenditure guide to assist the district.

Introductory Section:

- Include a flow chart detailing the process of building a school.

Organization of Project:

- We need to start with the table of contents
 - Trying to explain at each stage the critical pieces required.
 - Group agreed to review the table of contents.

Agreed upon table of contents:

- Section 1: Overview
 - a. Background (include flowchart)

b. Purpose

- Section 2: SFP General Audit Requirement for all Programs
- a. Information that is applicable to all programs (100%)
 - b. Forms (in numerical order 50-04, 05, 06)
 - c. Eligible and ineligible expenditure principles
 - d. Material inaccuracies

- Section 3: Individual Program Compliance and Audit Specifics
- a. Joint-use
 - b. HPI
 - c. Financial Hardship
 - d. Facility Hardship
 - e. ERP
 - f. Seismic
 - g. LCP
 - h. COS
 - i. Charter Schools
 - j. CTE

Section 4: Appendix

- Would like see audit guide provide guidelines on expenses.
- Districts need to see what they can and can not do.
- Creating a base/foundation and then building upon it.
 - For example in 2006 this was allowed in 2009 this is what is allowed, creating a living document.
- What if expenditures were taken out of the picture?

Next Steps:

- Lisa to go through what the index looks like and assign workload.
 - What specifics should and should not be included - *see notes above*
- Goal is to finish audit guide recommendations / index by the September Working Group meeting in order to present to the SAB

A working group member also expressed concern about the goal of the group and the time commitment.

The goal is to have a draft of the audit guide for the Board Members by the September Board meeting.

OPSC's standard document request letter is a letter template designed to assist auditors in drafting a letter to a school district to request documentation to support certifications made by the school district, verify the eligibility of expenditures reported, and confirm the accuracy of the grants provided. OPSC auditors always modify the request to the specific project(s) being audited. Further, documentation already available will naturally be deleted.

School districts are reminded that the auditor's contact information is included in every letter and should there be any question as to the documents requested they are welcome to contact the auditor.

OPSC Standard Document Request – *Comments from Committee*

1. District's closing escrow settlement statement(s) and supporting documentation.

Q: Escrow statements are good documents, easily submitted. Request for supporting documentation should be case by case. As this is a significant volume of documentation.

A: Yes, these requests are already case by case. Depending on the documents reviewed to provide site acquisition funding, the documents requested may vary. For example, a project funded based on estimated escrow documents, the auditor will request a copy of the final escrow settlement statement. If the project was funded while in the condemnation process, the auditor will ask for the final court judgments outlining the amounts owed to the existing property owner. The auditor may already have access to some of the information, therefore will modify the request to only documents needed.

2. Supporting documentation for all site relocation expenditures.

Q: The relocation consultant does a calculation sheet, this should be sufficient initially and if something needs further clarification, request the supporting docs. Again, this can be a huge volume of docs.

A: It is rare that an auditor will request supporting documentation. They will usually sample expenditures and request all supporting documentation to support the specific expenditure. Providing just the generalized calculation sheet for the expenditure could potentially delay the audit while we wait for the additional detail, rather than receiving it up front. Relocation costs can be complex, especially the cost basis for "comparable facilities", which should include legal documents and other pertinent information. Auditors must have source documents to support their findings.

3. Construction bid announcement that includes Disabled Veteran Business Enterprises (DVBE) language. If the bid announcement does not include DVBE language, provide the bid announcement and supporting documentation to verify that the District made a good faith effort to meet its DVBE participation goals.

Q: *This is more challenging when the delivery method is not Design-Bid-Build. It would be helpful to know what is an acceptable level of effort when using other methods, such as Lease-Lease Back.*

A: This section of the “general document request” again depends on the project. In the case of a lease-lease back project, the auditor would modify the request based on circumstances. The auditor often doesn’t know the construction delivery method prior to obtaining contracts. The District may call the auditor to explain the circumstances regarding their projects. As an alternative, many school districts have an annual school board item indicating a DVBE goal for that year.

4. Bid summary which reflects all submitted bid proposals and supporting documentation for non-responsive bidders.

Q: *The bid summary we understand, but why documentation regarding non-responsive bidders. This is thoroughly vetted by the marketplace.*

A: The auditor would want to know in certain cases why the lowest bidder wasn’t used. Usually, the auditor will receive a copy of letters to the lowest bidder indicating that they were disqualified. On occasion the auditor may receive copies of board items indicating this as well.

5. Notice to Proceed and Notice of Completion for **all** construction contractors.

Q: *NOC is not legally required, it is best practice as it shortens the statute of limitations and keeps project timelines clarified. Some misunderstanding of the NOC as end of project seems to be in evidence in the Audit Guide (pg. 7). Projects should routinely be held open for one year beyond NOC to enable full F&E purchasing. (See also Handbook page 83, Audit Guide page 9). Additionally, in Multi-Prime environments, the CM often controls NOC. What is the objective of this element? Letters in lieu of NOC have worked in the past.*

A: The Notice of Completion helps the auditor determine when a project was completed, especially for districts that are extremely late in reporting. They are not necessarily requested on every project. Expenditures are not permitted after the 3 / 4 year construction timelines, unless they were contracted for within those time frames. In addition, the OPSC has an abundance of districts that have never submitted final expenditure reports for projects that were funded up to 10 years ago. From an audit standpoint, this information helps establish when a project was completed and the integrity of costs reported. There is no limitation on the documents needed by the OPSC to fully understand a project. SFP Regulation 1859.106 allows auditors access to all relevant documents. Auditors on the audit subcommittee panel have reiterated the fact that auditors have the right to request relevant documents.

6. Supporting documentation verifying that the District conducted a qualification appraisal/selection process for selecting the architect, engineer, and/or construction manager, pursuant to Government Code Section 4526 or a statement, signed by the District Representative, which states that the District procured professional services

in accordance with the requirements of Chapter 10 (commencing with Section 4525) of Division 5, of Title 1, of the Government Code.

Q: *No comment, this is fine.*

A: Agree

7. **All** Department of Industrial Relations letters approving the District's Labor Compliance Program (including initial, extended, and final approval letters, if applicable).

Q: *As applicable, not required for all projects.*

A: Concur. As applicable.

8. A detailed listing of all Labor Compliance Program (LCP) expenditures. If no LCP expenditures were incurred, provide a written explanation.

Q: *The expenditures have their own column on the 50-06 and should not require additional delineation, other than routine sampling.*

A: Correct, we only request the information if LCP appears to be required on a project and zero expenditures are reported by the school district.

9. Architect agreement.

Q: *No comment, this is fine.*

10. A: Construction contract agreement(s), addendum(s), and final billing(s).

Q: *Active construction contracts can only be changed through a change order process. (Agreements, addendums, and amendments are appropriate to other contracts, such as architect and professional services.) This should probably read "contract, change orders, and final billing" as those are the contract documents. Alternative delivery methods may use a blended terminology.*

A: By "addendum" we typically are looking for information on the acceptance of additive and deductive alternates. The auditor can modify the language as necessary since this is just a template letter.

11. Copies of all change orders for main contractor(s). The change orders must include the description of change. If the change orders have not been approved by the Division of the State Architect (DSA), the project architect should provide a letter stating that the change orders submitted to the OPSC represent all change orders for the project and that the change orders will be submitted to the DSA for approval. If the change orders do not require DSA approval, the District Representative should confirm this in a letter to the OPSC.

Q: *This can be the DSA stamped page which also includes the days, dollars, and scope involved in the change. Additional documentation is voluminous and*

should be requested as needed, if for instance a change might have altered the districts qualification for the grant (change in number of classrooms or square footage.) Past practice has been that DSA did not review change orders that did not affect their approval areas (ex: change in color of carpet or paint.) A letter stating that the change did not require review has been sufficient.

A: Agree, typically we receive a page or two for each change order. We are not usually looking for plans and specifications detailing the change.

12. Construction management agreement.

Q: Provide if applicable, not all projects use CM. These services may apply to more than just the construction phase, depending on the delivery method and project particulars.

A: Agree, again this is a template letter and this item is only requested if CM expenditures are reported by the District. Often times, even if CM expenditures are reported, the CM agreement is not requested.

13. General ledgers and other source documents supporting expenditures and warrants listed on the Detailed Listing of Project Expenditures (DLOPE).

Q: Historically the audit has depended primarily on warrant registers as verification that the expenditure was made. Use of the GL's is new to non-FH districts. It would be helpful to clarify to what purpose they are using the GL.

A: Historically, desk reviews have not required GLs for either FH or non-FH districts. As indicated in our audit outreach presentations the use of GLs is more reliable accounting information. In addition, districts typically find it easier to provide the GL than individual warrants and invoices. Most auditors trace expenditures from reports and ad hoc documents to the general ledgers as the auditors on the working group can attest. GLs should reconcile to the expenditures reports on the Expenditure Report. If they do not, it is an indicator of potential issues. Warrant listings are not much better than ad hoc documents because they may not have been corrected for refunds or misclassified costs. A district's financial statements are the only acceptable record from which to pull samples.

14. A copy of the budget summary (usually referred to as the Form 01 or Form J01) that shows the Fiscal Year (FY) XXXX/XXXX budget for total general fund expenditures, and the transaction ledger for the ongoing major maintenance account for FY XXXX/XXXX.

Q: Why verify the General Fund? Major Maintenance contribution can be verified from Section 7 of the SACS Standards and Criteria, one for each year of the project.

A: District's are required to make a deposit equal to a percentage of the total general fund restricted (or unrestricted account) depending on the fiscal year. Without showing the General Fund amount, we don't know what the minimum deposit should have been. Yes, we can verify if a contribution was made, what we can't

determine from just looking at the major maintenance account is whether it was enough.

15. Documentation identifying the project savings remaining in the restricted facility fund (Fund 35).

Q: Not all remaining funding or savings will be in F35. This depends on the cash management style of the district, which is not subject to OPSC purview. (Typically only applicable to FH.)

A: Education Code 17070.63(c) states that project savings shall remain in the county fund for expenditure by the district for other high priority capital outlay purposes. The OPSC is aware that limitations on some school district's bond funds prohibit the transfer of bond funds to other funds. In cases where school districts have this limitation, then the OPSC would also request documentation identifying where the district's share of savings is being held.

16. Documentation supporting the interest reported on the District's *Expenditure Report* (Form SAB 50-06).

Q: The interest reporting required by OPSC does not reflect the means by which interest is generated and requires each district to make a consistent yet inaccurate guess as to the interest applied to each project. Alternative approaches should be considered.

A: The OPSC is currently reviewing alternatives; however it should be noted that all County Office of Educations have been able to allocate interest on a "per project" basis and provide supporting documentation for the deposit of interest as a whole and the method of distribution to individual SFP projects. The OPSC advises school districts to contact their local COE for additional guidance.

Restricted reserve of interest for purposes appropriate to the funding (state bond) could satisfy fiduciary bond requirements, yet improve reporting, auditing, and use of these monies.

17. The District's legal counsel's approval or opinion stating that the District complied with all applicable laws and regulations pertaining to the Force Account Labor expenditures.

Q: When applicable. By definition this is a very small component of the project.

A: Agreed, again this is a templated list of potential requests by the auditor and if no force account labor is reported, then the information would not be requested.

The enclosed *Management Representation Letter* completed and signed by the authorized District Representative (only an *original* signature will be accepted).

Q: Some districts have been advised by legal counsel not to sign this letter as it requires them to attest to items that were not within their control.

A: Only one district has not returned the Management Representation Letter. The district should have control because they are assigned responsibility to safeguard SFP funds, ensure they are accounted for appropriately, and ensure they were used for the intended purpose. The certifications indicate the district representative is providing information “to the best of their knowledge”.

Audit Working Group
State Allocation Board – Subcommittee on Audits
Monday, Aug 23rd
State Capitol Room 2040
10:30am – 3pm

AGENDA - NOTES

I. Membership of Audit Working Group

CA Assoc School Business Officials (CASBO) – Lettie Boggs
California County Superintendents Education Services Assoc – Mike Ricketts
CA Dept Education – Arlene Matsuura
County Office of Ed Schools Consortium - Andrea Sullivan
FCMAT – Debi Deal
Independent School Auditor Expert - Shilo Gorospe
OPSC – Rick Asbell / Steve Inman
State Controller’s office – Casandra Moore-Hudnall
School Facility expert – Cathy Allen
Treasurer’s office – Blake Fowler (*on as needed basis*)

II. Objectives

The charge of the audit working group was to review current and existing junctures of accountability at the state and local level, including at various stages within the State Facilities Program (SFP) in order to avoid potential redundancies and limit inefficiencies within the SFP Expenditure Audit Program.

In this regard the objective of the audit working group is to provide recommendations to the State Allocation Board (SAB) subcommittee on audits that have recommendations in the following categories and answer the questions laid out in the agenda.

The specific issues that should be addressed in the working group as requested by the SAB Audit subcommittee include, but not limited to:

- Process: law, regulation, policy and procedures
- Scope and types of audits being done and recommended
- Content of audits
- Transition issues
- Addressing redundancies
- Promoting best practices
- Communication with School Districts

III. AGENDA ITEMS FOR DISCUSSION & RECOMMENDATION

Discussion on Meeting Charge of Audit Working Group

Keep intent of SB 50 in mind as we are doing this process – keep flexibility

- 1) Define the scope of the Office of Public School Construction (OPSC) audit authority,
 - a) Recommend changes to the scope and types of audits being done
 - i) Defining the Scope - OPSC is a compliance audit
 - (1) Direct OPSC (CDE, Controller's office discusses and discloses this) – i.e. make very clear in audit guide what it is the district is required to comply with (no hidden gottcha regarding with compliance)
 - ii) Reco. Stages of audits (2 or 3) – more than 1 stage
 - (1) Include program to lay out requirement of program
 - iii) Reco. Gov Auditing Standards should be complied
 - iv) Reco. Desk v/s Field audit
 - (1) Need to Flesh out re: when we figure out who does the audit and how many audits – i.e. 50-04 stage desk???
 - v) Reco: Audit should be based use of state funds and related matching funds
 - vi) Reco: Scope re: separation b/w program and audit
 - (1) Dispute: If controller does audit – publish finding w/ district response, but could recommend the issue is readdressed at OPSC. Or Controller's office would work with program staff regarding a program dispute
 - vii) Reco: Audit to the Audit Guide - which are general audit guidelines –
 - (1) don't make the guide regulations or so specific. (allow auditor judgment and don't audit less than the guide)
 - viii. Reco: Audits are not allowed to be re-opened unless for fraud or illegal acts
 - xi. Reco: Define different type of audits regarding 50-60% audit vs. financial audit 100% funded – should they be audited at the same level

NOTES

- Differences b/w grant program or LPP
- Grant and go but have to meet these requirements – then that is what should be audited.
- Program folks lay out the requirements
- Performed with Governmental Audit Standards
 - Field and desk audit (compliance audit)
- 05 – maybe a desk audit
- Stage audit – depending on the stage

Intent of SB 50 scope vs LPP

- Is a District supposed to be audited on every expenditure (b/c it is a grant)

- Scope depends on agencies risk analysis of the school district or project. There is not a one-size fits all process.

- Discuss at audit working committee –

b) Recommend changes and a procedures for SAB consideration on the publishing and findings of audits (Material Inaccuracies)

i) **Should** the audits be published once final? Should it be on our website or the Gov's website

(1) OPSC claims it was not published under governmental auditing standards

(2) Controller's office – says this is illegal – should always allow district to respond.

ii) Reco: Audit should always follow Governmental Audit Standards (Yellow book standards)

iii) Reco: Draft review to district a minimum of 30 days prior to publishing – extensions will be allowed – Auditor is allow a final rebuttal based on district response.

iv) Reco: Allow district response to be published – exactly how the district writes the letter w/o OPSC influence to re-draft

v) Reco: Audits are only published when they are final

(1) Mutually agreed upon date is generally how it is handled

(2) SAB should not get involved at this stage – it would compromise potential appeals and objectivity etc..

vi) Is there a way for Districts to work with OPSC to address problems with audit regarding their process being wrong? Should be a program issue – create a process for a program review – annual update of handbook.

(1) Issues are reviewed to the annual audit committee These are program issues and it would work if audits were removed from OPSC – if it is an issue regarding audit findings –

(2) Application of policy problem? How are we recommending resolution? File a form 189 – audit should go forward

c) Recommend a process for yearly update and communication to district regarding changes within audit process

i) Create a standing audit committee

ii) Annual review update redraft of audit guide

iii) Changes are then put in the audit guide - which addresses problems within the audit that were discovered.

iv) Create a process

v) Audits should be conducted based on the guidelines in place upon approval of the application.

- 2) **Draft recommendations for the audit subcommittee to consider as to what can be done to streamline current and existing junctures of accountability with the use of state bond proceeds to build a school, and**
- a) Recommend streamlining actions within audit process where audits can be done throughout the construction timeline and close out specific portions.
- i) **Reco: Draft a multi-part audit process**
- (1) Desk audit done immediately after 05 (fund release form)
 - (a) Should it be looked into at 04 process (work load process)
 - (b) 04 – authorizes the project (project application)
 - (i) Do an entrance audit interview at the 04 stage – with program personnel on required documentation needed.
 1. Re-staff OPSC so that program staff are giving them this information. Front-end review.
 - (ii) Management representation letter – should be presented at this stage not at 06 stage – should this be a legal document?
 - (iii) 04 – have where program personnel present all the information on documents needed for the audit at the 06 level.
 - (2) Final audit being done after 06 ~ main reason is because a lot of people leave b/w 05-06 – *if there is a problem it is better to know it right away before the end.* 06 ~ expenditures -
 - (3) OPSC – looking at front-end interim and back end audits – there are positives to an interim function. A lot of this centers around the districts internal controls (maybe do that at the front end) *staffing issues*
- ii) **Reco: Issue: Internal Controls** – OPSC has very little understanding of how to build a school and program staff need training regarding multi-fund accounting. Have program staff get cash management training as well. Develop staff to have a good understanding of entire process.
- (1) **GAS audit** – requires internal controls. Independent auditor should do the internal controls and OPSC could build upon it or just use independent auditors review– but consider the work the independent auditor.
- iii) **Reco: Coordination - CA State Accounting School Manual** (CDE manages) staff should meet with OPSC staff regarding codes. Whenever CSAM structure changes there should be a discussion with OPSC staff. Training OPSC staff on CSAM and creating a streamlined structured. How do we make this a trigger for discussion? Coordinate accounting – coding standards
- (1) CSAM / Standardized Accounting Code Structure (SACS)
 - (a) Example is 6170 – CSAM change, but OPSC needs more detail than what can be put in 6170 – **this needs to be discussed and figured out.**
 - (b) All districts uses CSAM
- Recommendation** ~ SAC forum – make sure that OPSC knows about this – forum topics are published for meetings – CDE there is a trigger ...Get OPSC on that distribution list.

- iv) **Reco: Develop program staff that deal with project application and process once it is approved (team of program staff going out and meeting with the districts – regarding 04 entrance interview) – that understand program requirements and multi-fund / cash management training**
- v) **Recommendation that OPSC is the program staff and the audit is conducted by another agency (Independent auditors – they pick up parts of school construction with the annual audit / State Controllers office / DGS auditors)**
 - (1) Items that come annually that come with the expenditures for independent auditors – and then OPSC does the closeout audit.
 - (2) There needs to be a line b/w the program and audit – and this does not exist at OPSC – would there be enough separation b/w DGS and OPSC
 - (3) If audit conducted by an independent auditor – then there needs to be audit oversight.
 - (4) Goal is independence and separation of the entities. Functions and perceptions.
- vi) **Reco: Standing Audit Committee should be created while OPSC for input on whomever is conducting audits**
 - (1) CDE, Controllers, Facility district staff and CBO district staff, (include County / Financial Hardship / Big & Small Districts) independent auditor, OPSC program and / OPSC audit representative, or whomever the auditing entity is – whether it is OPSC or not.

Recos for split audit

04- entrance interview (done by program staff – with audit guide and check list) – Content of the management letter should be given to staff at this time.

Need: Clear distinction b/w program and audit staff at OPSC

- **Program staff should be responsible for educating district on documentation compliance requirements**
- **Included should be the 4 pages of certifications required and explain what the certifications mean – needs to be part of the program guide**
 - There is an audit process on the 04 – can we close out the certifications
 - Reimbursement or occupancy issues

Have OPSC figure out if there should be an 04 and 05 audit process or whether they should be merged

05- interim fund release audit

Site close out

- **OPSC reviews final escrow document**
- **Court documents**

- Site acquisition is done at 05 and you can do an audit on the 04 certifications

06 – final expenditure audit

- b) Identify redundancies and address them in drafting what the scope of OPSC audit should be.
 - i) Internal controls

3) Draft recommendations for establishing an audit appeals process that ensures a transparent, consistent and equitable appeals process for SAB consideration.

- a) RECO: Review draft Education Audit Appeals Panel appeal process - should the same process for OPSC appeals?
 - i) Reco: Type of NON-compliance -
 - (1) Reco: Limit appeals to material fiscal impact – repayment of funds
 - (2) Reco: Material Inaccuracy what does it mean – clarify this
 - ii) **Should the SAB be determining appeals?** Is it appropriate for SAB to review determinations – should it go to an ALJ or EAAP?
 - (1) **Reco: creation of an Audit subcmte to hear audit appeals fiscally related appeals**
 - (a) Representation CDE, DOF, Legislative representative – to hear formal appeal (informal process) if Dist disagrees then after decision by subcmte – could go to ALJ process or it could go to EAAP. (who hires the ALJ – SAB or EAAP)
 - (b) Final determinate is determined by the appealing entity
 - (c) District then can file suit with the superior court
- b) Suggest Recommendations for the SAB subcommittee on Audits to consider for appeals.
 - i) What should an appropriate appeals process at OPSC look like?
 - (1) Appeals should be limited to Fiscal – b/c per SB 50 allowing program flexibility and intent – issue with programmatic interpretation
 - (2) If fiscal impact district has right to appeal
 - ii) What is the proper timeline to address?
- c) **Policy Appeal vs. Fiscal Appeal**
- d) **Recommendation that you cannot re-open an audit after close out. (regulation change) – allows for fraud to re-open etc..**

- 4) **Redraft Index of OPSC Audit Guide – See Table of contents on attached document..**
 - a) Audit guide lays out the program
 - b) OPSC defines compliance with audit committee
 - c) Audit requirements are built within the guide
 - d) Coordination b/w the audit guide and the program (handbook)
 - i) Handbook
 - (1) Include checklist in the program handbook
 - ii)
 - e) Appeals – clearly define

EAAP Appeals Process

Question: Should this process be mirrored at OPSC for audit appeals?

The Education Code provides that a local education agency that is required to repay an apportionment significant audit exception, or to pay a penalty arising from an audit exception, may appeal a finding. (Educ. Code §§ 41344(d), 41344.1.)

The Health & Safety Code provides that amounts reported to local education agencies in a certain required notification issued by the State Department of Education shall be deemed apportionment significant audit exceptions and may be appealed pursuant to the above-cited Education Code provisions. (H&S Code § 33684(h)(1), (2), (3).) The reported amounts are prior year adjustments based on corrections to previously reported redevelopment agency (RDA) pass-through payments, and are to be deducted from the total Principal Apportionment in the year indicated in the notification letter. The date of receipt of the notification letter is deemed the date of receipt of the final audit report for purposes of determining the time to request a repayment plan by applying to the State Department of Education, and the time to request summary review by EAAP's Executive Officer or to file a formal appeal with EAAP. (H&S Code § 33684(h)(3), Educ. Code §§ 41344(a), (d), 41344.1(d).) In the following explanations, all references to "audit exceptions" or "audit findings" are applicable to the adjustments set out in the State Department of Education notification letter.

Please refer to "Filing Deadlines and Procedures" under Related Links, below.

Summary Reviews

Grounds

The EAAP statutes provide for a "summary appeals process," conducted by the executive officer acting independently of the panel, if the audit exceptions involved "clearly constitute substantial compliance" (see below). The law further provides that "if the conditions for finding substantial compliance are not clearly met or involve substantial questions of fact, the executive officer may deny the request for summary review."

Process

The law provides that the summary review process is "voluntary [and] informal" and that the executive officer may seek comment from the Department of Finance and

Superintendent of Public Instruction. Summary review is not subject to the provisions of the Administrative Procedure Act and does not involve a hearing.

Outcomes

The law provides that if the total audit exceptions for which an agency seeks summary review involve less than 150 units of average daily attendance (ADA) or \$750,000, whichever is less, “the executive officer may waive or reduce the reimbursement or penalty upon a finding of substantial compliance and that other remedial measures are sufficient to induce full compliance in the future.” For exceptions involving larger total amounts of ADA/funding, “the executive officer may waive or reduce the reimbursement or penalty upon a finding of substantial compliance and order other remedial measures that are sufficient to induce full compliance in the future, if he or she has the written approval of the Department of Finance and the Superintendent.”

Relationship of Summary Reviews and Formal Appeals

The EAAP statutes provide that the summary review process is “in addition to the normal appeal process,” further stating that the right to a formal appeal to the panel is “independent” of the summary review provisions, and that “an appellant may pursue his or her appeal [to the panel] regardless of the result [of summary review].” If an appellant first requests summary review and then, dissatisfied with the outcome, chooses to pursue a formal appeal, the formal appeal is *de novo*, as if the summary review had never taken place.

Formal Appeals

Grounds

The EAAP statutes provide three grounds on which K-12 local education agencies may formally appeal audit findings to the panel itself:

- errors of fact
- errors of interpretation of law
- substantial compliance

The first two grounds are not explained further in the EAAP statutes.

With respect to the third, one of the EAAP statutes provides that:

“Substantial compliance” means nearly complete satisfaction of all material requirements of a funding program that provide an educational benefit substantially consistent with the program's purpose. A minor or inadvertent noncompliance may be grounds for a finding of substantial compliance provided that the local educational agency can demonstrate it acted in good faith to comply with the conditions established in law or regulation necessary for apportionment of funding. The panel may further define “substantial compliance” by issuing regulations or through adjudicative opinions, or both.

Process

The law provides that a hearing shall be held in each appeal to the panel, and that the panel shall consider appeals pursuant to the provisions of the Administrative Procedure Act. As standard practice, the panel delegates the hearing to an administrative law judge from the state's Office of Administrative Hearings, who then proposes a decision for the panel's consideration. After reviewing the law and the record, the panel may adopt the decision as proposed or reject it and adopt a different one. The panel is specifically authorized to “approve settlements and make findings of fact and interpretations of law.” The Controller is automatically a party to every appeal to the panel, and the State Department of Education and Department of Finance are empowered to intervene as parties if they choose to do so.

Outcomes

With regard to the first two grounds, the law provides that if the panel determines that the appealing agency is correct in its assertion of error with regard to an audit finding, the agency is freed of its obligation to repay the penalty or apportioned funding associated with the finding. If the panel finds there was substantial compliance, it may waive or reduce the payment otherwise required “and may also order other remedial measures sufficient to induce full compliance in the future . . . includ[ing] restoration of a reduction or penalty amount if full compliance is not rendered in the future, ordering special audits, and requiring special training.”

Settlements

Education Code Section 41344.1(b) provides in part that EAAP may approve settlements. Section 1028 of Title 2, California Code of Regulations, provides that any party to an action that is proceeding pursuant to the Administrative Procedure Act (APA), as is the case with all of EAAP's formal appeals, may request settlement discussions at any time. The APA itself provides that the possibility of settlement may occur at any time.

Review of the Current Audit Guide

In Comparison with the New Audit Practice

Provided for the Audit Working Group Meeting, May 17, 2010, by:

Andrea Sullivan, Orange County Office of Education

Lettie Boggs, CASBO

Cathy Allen, Western Placer Unified School District

Mike Ricketts, CCSESA

We were tasked with reviewing the current OPSC Audit Guide. We focused our discussion on the variance between the current audit guide and the current audit practice. The comments in this review are for the regular program, not necessarily the Financial Hardship program, which legitimately includes a more rigorous scrutiny. However some elements of the review will apply to both.

We did not provide a line by line assessment as the broad concept discussion seems to need to precede that lengthy process.

Site Visits

Previous audits were not in-district unless there was an issue that brought the district to a very detailed audit level. A recent change has been the shift to coming to the districts. This probably facilitates faster audits and is appropriate. Districts just need to know that this is routine practice now.

With respect to actually going to sites to verify that the work granted is work completed, DSA already has a very well qualified person on site throughout the project who verifies that the DSA plans have been constructed. The Inspector of Record is state licensed by DSA. They have personal knowledge of the job and verify at project end that all components were constructed. A slight addition or modification to the final verification document could assure OPSC that the DSA plans which were the basis of the grant are legitimately done.

To have a person unfamiliar with plans verify from the basis of a map, via cursory visit/review that the approved plans were constructed is duplication at a less appropriate level than already exists.

Entrance Interview

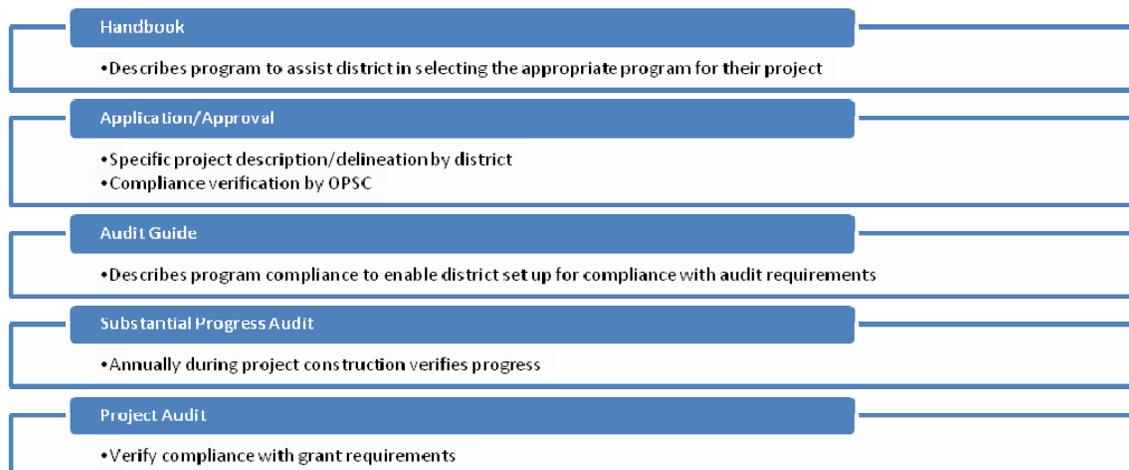
OPSC is saying that they inform districts of the elements of the audit at the time of the entrance interview. Districts are saying that they need to know before they account for the project, which is much earlier. Districts must rely on the Audit Guide for rules of compliance.

The current guide does not describe the current process, so districts are unaware of the requirements of compliance. OPSC's Advisories Actions/Building Blocks should be incorporated into the guide so that there is a comprehensive documentation that districts can refer to in developing their compliance documentation.

Advisories in general are frequently provided because of new program elements or the provided guidance is unclear or inadequate. The need to further explain should trigger updates to the guide. Guidance should also be accurate, for instance the Advisory Action of May 24 regarding SFP F&E, incorrect guidance is given stating the inventory rules of the CSAM rather than the Capital Outlay guidelines as the rules of the audit for F&E. So the source they are referencing is not the correct section and very different rules should actually apply.

This particular example shows how this lack of understanding on the part of OPSC could result in different rules within the program than for all other capital outlay funding. This creates issues regarding consistent training of staff, etc. Not to mention calling into question most of the F&E appropriate to a project with respect to being allowed by audit.

The typical process of information and verification previously followed and still in place is illustrated below:



When the project audit significantly differs from the guidance, districts cannot anticipate the audit process. This causes the program to lose the effect of the audit guidance promoting good practice, and it makes the districts vulnerable to audit exceptions that could have been prevented if the process was coordinated.

Internal Controls and Fraud Policy

These elements are already routinely audited by the Fiscal Audit. Inclusion in the OPSC compliance audit is redundant with the other audits already performed. We acknowledge that in a risk based audit, it is standard practice for each auditor to determine risk for themselves. And this appears to be the level of review now in the OPSC process. However, if the purpose of the OPSC audit is to verify compliance with the grant requirements, then the risk assessment for the compliance audit should be in relationship to the risk of non-compliance, which is of more limited scope.

When auditing the use of state bonds, it is important to verify the use based on the state bond criteria. However, if the granting complies with state bond language, then the verification would need to represent compliance with the grant. (Savings methodology could use a restricted reserve approach, and use of restricted funds could be routinely audited for compliance with the restriction. But that is another issue, though related.)

We would like to explore a more coordinated approach that does not involve multiple redundant analyses for the districts and that targets the risk assessment of the OPSC audit to the projects being audited. This would result in time savings for all.

Audit Reports, Comments, and Responses

Requirement of audits and related comments and responses also goes to the risk assessment and the appropriate type of risk assessment for a compliance audit.

Unique Coding String

This is a good practice and OPSC audit should require it to encourage good practice. Methodology should be coordinated with the SACS office and verified during regular audit so that it will be there when they get to the OPSC audit. There is a wide variance of accepted practice in the location of the unique identifier within the coding string as the ultimate form and length of the string varies by county, and the number of projects varies by district.

It is not possible to go back and require this of projects that did not implement it during the project. There are ways to track a project in a subsidiary system to the GL so that full data by project is known.

General Ledger Transfers

Absent any guidance regarding why are they looking at transfers, districts don't know what criteria is being assessed by the look at their G/L. Is this to determine cash management? If so, it is unclear why this is of any value to the state. There are several methods of managing cash, they are not right or wrong, they are just different. They typically reflect the location of the management within the district depends. That is, it looks different when use of cash source is determined at the PO level, the CBO level, or the Facilities Dept level.

For Financial Hardship districts the full G/L review is appropriate, but may not be necessary for the regular program. The G/L component may be more appropriate to evaluation by the fiscal auditors as a component of the overall analysis of the management of the funds of the district.

OPSC Standard Document Request Question & Answer

OPSC's standard document request letter is a letter template designed to assist auditors in drafting a letter to a school district to request documentation to support certifications made by the school district, verify the eligibility of expenditures reported, and confirm the accuracy of the grants provided. OPSC auditors always modify the request to the specific project(s) being audited. Further, documentation already available will naturally be deleted.

School districts are reminded that the auditor's contact information is included in every letter and should there be any question as to the documents requested they are welcome to contact the auditor.

OPSC Standard Document Request – Comments from Committee

1. District's closing escrow settlement statement(s) and supporting documentation.

Q: Escrow statements are good documents, easily submitted. Request for supporting documentation should be case by case. As this is a significant volume of documentation.

A: Yes, these requests are already case by case. Depending on the documents reviewed to provide site acquisition funding, the documents requested may vary. For example, a project funded based on estimated escrow documents, the auditor will request a copy of the final escrow settlement statement. If the project was funded while in the condemnation process, the auditor will ask for the final court judgments outlining the amounts owed to the existing property owner. The auditor may already have access to some of the information, therefore will modify the request to only documents needed.

2. Supporting documentation for all site relocation expenditures.

Q: The relocation consultant does a calculation sheet, this should be sufficient initially and if something needs further clarification, request the supporting docs. Again, this can be a huge volume of docs.

A: It is rare that an auditor will request supporting documentation. They will usually sample expenditures and request all supporting documentation to support the specific expenditure. Providing just the generalized calculation sheet for the expenditure could potentially delay the audit while we wait for the additional detail, rather than receiving it up front. Relocation costs can be complex, especially the cost basis for "comparable facilities", which should include legal documents and other pertinent information. Auditors must have source documents to support their findings.

3. Construction bid announcement that includes Disabled Veteran Business Enterprises (DVBE) language. If the bid announcement does not include DVBE language, provide the bid announcement and supporting documentation to verify that the District made a good faith effort to meet its DVBE participation goals.

Q: This is more challenging when the delivery method is not Design-Bid-Build. It would be helpful to know what is an acceptable level of effort when using other methods, such as Lease-Lease Back.

A: This section of the “general document request” again depends on the project. In the case of a lease-lease back project, the auditor would modify the request based on circumstances. The auditor often doesn’t know the construction delivery method prior to obtaining contracts. The District may call the auditor to explain the circumstances regarding their projects. As an alternative, many school districts have an annual school board item indicating a DVBE goal for that year.

4. Bid summary which reflects all submitted bid proposals and supporting documentation for non-responsive bidders.

Q: The bid summary we understand, but why documentation regarding non-responsive bidders. This is thoroughly vetted by the marketplace.

A: The auditor would want to know in certain cases why the lowest bidder wasn’t used. Usually, the auditor will receive a copy of letters to the lowest bidder indicating that they were disqualified. On occasion the auditor may receive copies of board items indicating this as well.

5. Notice to Proceed and Notice of Completion for all construction contractors.

Q: NOC is not legally required, it is best practice as it shortens the statute of limitations and keeps project timelines clarified. Some misunderstanding of the NOC as end of project seems to be in evidence in the Audit Guide (pg. 7). Projects should routinely be held open for one year beyond NOC to enable full F&E purchasing. (See also Handbook page 83, Audit Guide page 9). Additionally, in Multi-Prime environments, the CM often controls NOC. What is the objective of this element? Letters in lieu of NOC have worked in the past.

A: The Notice of Completion helps the auditor determine when a project was completed, especially for districts that are extremely late in reporting. They are not necessarily requested on every project. Expenditures are not permitted after the 3 / 4 year construction timelines, unless they were contracted for within those time frames. In addition, the OPSC has an abundance of districts that have never submitted final expenditure reports for projects that were funded up to 10 years ago. From an audit standpoint, this information helps establish when a project was completed and the integrity of costs reported. There is no limitation on the documents needed by the OPSC to fully understand a project. SFP Regulation 1859.106 allows auditors access to all relevant documents. Auditors on the audit subcommittee panel have reiterated the fact that auditors have the right to request relevant documents.

6. Supporting documentation verifying that the District conducted a qualification appraisal/selection process for selecting the architect, engineer, and/or construction manager, pursuant to Government Code Section 4526 or a statement, signed by the District Representative, which states that the District procured professional services in accordance with the requirements of Chapter 10 (commencing with Section 4525) of Division 5, of Title 1, of the Government Code.

Q: No comment, this is fine.

A: Agree

7. **All Department of Industrial Relations letters approving the District's Labor Compliance Program (including initial, extended, and final approval letters, if applicable).**

Q: As applicable, not required for all projects.

A: Concur. As applicable.

8. **A detailed listing of all Labor Compliance Program (LCP) expenditures. If no LCP expenditures were incurred, provide a written explanation.**

Q: The expenditures have their own column on the 50-06 and should not require additional delineation, other than routine sampling.

A: Correct, we only request the information if LCP appears to be required on a project and zero expenditures are reported by the school district.

9. **Architect agreement.**

Q: No comment, this is fine.

10. **A: Construction contract agreement(s), addendum(s), and final billing(s).**

Q: Active construction contracts can only be changed through a change order process. (Agreements, addendums, and amendments are appropriate to other contracts, such as architect and professional services.) This should probably read "contract, change orders, and final billing" as those are the contract documents. Alternative delivery methods may use a blended terminology.

A: By "addendum" we typically are looking for information on the acceptance of additive and deductive alternates. The auditor can modify the language as necessary since this is just a template letter.

11. **Copies of all change orders for main contractor(s). The change orders must include the description of change. If the change orders have not been approved by the Division of the State Architect (DSA), the project architect should provide a letter stating that the change orders submitted to the OPSC represent all change orders for the project and that the change orders will be submitted to the DSA for approval. If the change orders do not require DSA approval, the District Representative should confirm this in a letter to the OPSC.**

Q: This can be the DSA stamped page which also includes the days, dollars, and scope involved in the change. Additional documentation is voluminous and should be requested as needed, if for instance a change might have altered the districts qualification for the grant (change in number of classrooms or square footage.) Past practice has been that DSA did not review change orders that did not affect their approval areas (ex: change in color of carpet or paint.) A letter stating that the change did not require review has been sufficient.

A: Agree, typically we receive a page or two for each change order. We are not usually looking for plans and specifications detailing the change.

12. Construction management agreement.

Q: Provide if applicable, not all projects use CM. These services may apply to more than just the construction phase, depending on the delivery method and project particulars.

A: Agree, again this is a template letter and this item is only requested if CM expenditures are reported by the District. Often times, even if CM expenditures are reported, the CM agreement is not requested.

13. General ledgers and other source documents supporting expenditures and warrants listed on the Detailed Listing of Project Expenditures (DLOPE).

Q: Historically the audit has depended primarily on warrant registers as verification that the expenditure was made. Use of the GL's is new to non-FH districts. It would be helpful to clarify to what purpose they are using the GL.

A: Historically, desk reviews have not required GLs for either FH or non-FH districts. As indicated in our audit outreach presentations the use of GLs is more reliable accounting information. In addition, districts typically find it easier to provide the GL than individual warrants and invoices. Most auditors trace expenditures from reports and ad hoc documents to the general ledgers as the auditors on the working group can attest. GLs should reconcile to the expenditures reports on the Expenditure Report. If they do not, it is an indicator of potential issues. Warrant listings are not much better than ad hoc documents because they may not have been corrected for refunds or misclassified costs. A district's financial statements are the only acceptable record from which to pull samples.

14. A copy of the budget summary (usually referred to as the Form 01 or Form J01) that shows the Fiscal Year (FY) XXXX/XXXX budget for total general fund expenditures, and the transaction ledger for the ongoing major maintenance account for FY XXXX/XXXX.

Q: Why verify the General Fund? Major Maintenance contribution can be verified from Section 7 of the SACS Standards and Criteria, one for each year of the project.

A: District's are required to make a deposit equal to a percentage of the total general fund restricted (or unrestricted account) depending on the fiscal year. Without showing the General Fund amount, we don't know what the minimum deposit should have been. Yes, we can verify if a contribution was made, what we can't determine from just looking at the major maintenance account is whether it was enough.

15. Documentation identifying the project savings remaining in the restricted facility fund (Fund 35).

Q: Not all remaining funding or savings will be in F35. This depends on the cash management style of the district, which is not subject to OPSC purview. (Typically only applicable to FH.)

A: Education Code 17070.63(c) states that project savings shall remain in the county fund for expenditure by the district for other high priority capital outlay purposes. The OPSC is aware that limitations on some school district's bond funds prohibit the transfer of bond funds to other funds. In cases where school districts have this limitation, then the OPSC would also request documentation identifying where the district's share of savings is being held.

16. Documentation supporting the interest reported on the District's *Expenditure Report* (Form SAB 50-06).

Q: The interest reporting required by OPSC does not reflect the means by which interest is generated and requires each district to make a consistent yet inaccurate guess as to the interest applied to each project. Alternative approaches should be considered.

A: The OPSC is currently reviewing alternatives; however it should be noted that all County Office of Educations have been able to allocate interest on a "per project" basis and provide supporting documentation for the deposit of interest as a whole and the method of distribution to individual SFP projects. The OPSC advises school districts to contact their local COE for additional guidance.

Restricted reserve of interest for purposes appropriate to the funding (state bond) could satisfy fiduciary bond requirements, yet improve reporting, auditing, and use of these monies.

17. The District's legal counsel's approval or opinion stating that the District complied with all applicable laws and regulations pertaining to the Force Account Labor expenditures.

Q: When applicable. By definition this is a very small component of the project.

A: Agreed, again this is a templated list of potential requests by the auditor and if no force account labor is reported, then the information would not be requested.

18. The enclosed *Management Representation Letter* completed and signed by the authorized District Representative (only an *original* signature will be accepted).

Q: Some districts have been advised by legal counsel not to sign this letter as it requires them to attest to items that were not within their control.

A: Only one district has not returned the Management Representation Letter. The district should have control because they are assigned responsibility to safeguard SFP funds, ensure they are accounted for appropriately, and ensure they were used for the intended purpose. The certifications indicate the district representative is providing information "to the best of their knowledge".

STATE ALLOCATION BOARD AUDIT SUB-COMMITTEE HEARING

STATE SCHOOL FACILITY PROGRAM JUNCTURES OF ACCOUNTABILITY

BACKGROUND DOCUMENT

The following is a chronological list of audit points that currently exist within the School Facility Program (SFP). It is important to remember that funding is established through formulas and calculations that exist in statute and regulation. The funding derived from these calculations is full and final and verified and audited by the OPSC throughout the funding application process. SFP funding is not determined by what the District is constructing beyond the estimated cost of construction (60% commensurate rule) and the number of classrooms included in the project in the case of new construction applications only.

It is also important to note that there are several other State Agency junctures of accountability before the District can even apply to the SAB for funding. Both the Department of Education (CDE) and the Division of the State Architect must review and approve the District's plans for the project and the CDE and the Department of Toxic Substance Control must review and approve the District' site as a precondition of applying for funding through the SFP.

1. Eligibility Applications

- Enrollment information -- OPSC reviews CBEDS and Special Day Class enrollment reports to verify student counts presented by the District.
- Student Capacity – OPSC reviews site diagrams, detailed 1-A school building schematics and square footage calculations. OPSC also visits school sites to verify accuracy of site diagrams, detailed 1-As, etc.
- Age and Ownership Status of Facilities – OPSC reviews DSA approval date information to verify the age of school buildings for modernization eligibility and lease and portable purchase documentation.
- Housing projections – OPSC reviews Tentative and Final Tract maps, City Council and Planning Commission meeting minutes and letters from local Planning jurisdictions to verify housing estimates presented by the District.
- Student Yields – OPSC reviews Board adopted reports and calculations of student yield calculations to verify validity of student yields claimed that are higher than State averages.

2. Funding Applications

- DSA and CDE approved Plans – OPSC reviews plans for classroom counts, type of construction and site development work.
- Cost Estimates – OPSC reviews and verifies architect cost estimates for construction and cross references with estimates on file with the DSA. OPSC reviews and audits funding requested for site development costs by reviewing project DSA site plans locally approved off-site plans, local ordinance and fee schedule information, geotechnical and geohazard reports and Saylor Cost Estimating guidelines.
- Site Acquisition – OPSC reviews site purchase documentation (Purchase Agreements, Escrow instructions and statements, condemnation documents and current professional appraisals).
- Career Technical Education (CTE) – OPSC requires and reviews letters, meeting minutes and reports from CTE advisory committees to ensure that their needs are being met in the District.

3. Fund Release Applications

- Construction Contract and Notice to Proceed (NTP) – OPSC reviews construction contract and NTP to ensure that the District has met the requirements for the release of funds.
- Labor Compliance Program (LCP) – OPSC reviews the District's LCP approval letters and third party contract to make sure that they have a valid LCP.
- Bid Documentation -- OPSC reviews the District's accepted bid documents including additive and deductive alternatives.

4. Expenditure Audit

- Program Certifications – OPSC requests and reviews documents to validate certifications made by the District throughout the application process (i.e., routine restricted maintenance account balance, bid results, architect selection process).
- Project Expenditures – OPSC requests and reviews construction and services contracts, invoices and warrants.
- Project Scope – OPSC requests and reviews project change orders and requires evidence of DSA approval when required.

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January 25, 2010

Lisa Kaplan
Assistant Executive Officer
State Allocation Board
1130 K Street, Suite 400
Sacramento, CA 95814

RE: Establishing or Changing SAB/OPSC Audit Processes

Dear Ms. Kaplan:

On behalf of the State Allocation Board (SAB) you have tendered the questions presented below to this office. The essential inquiry is whether California's Administrative Procedures Act (APA) applies when the SAB and/or the Office of Public School Construction (OPSC) establish or make changes to audit procedures, and whether the SAB and OPSC have authority to contract for outside auditing services.

The short answers to these questions are:

1. No, the APA does not mandate formal rulemaking if an agency's audit process serves as a guide and an auditor retains discretion as to how to perform an individual audit. Under such circumstances the audit guide is considered a flexible tool rather than a "rule of general application" for purposes of the APA, and the guide need not be adopted as a formal regulation.

2. Yes, the OPSC may contract for auditing services. The OPSC is the arm of the Department of General Services (DGS) responsible for administering the Leroy F. Greene School Facilities Act of 1998 (the Act)¹ and for providing assistance to the SAB, and it may contract for outside auditing services with or without express direction to do so from the SAB. As to the SAB, because the statutory scheme directs the DGS director to provide the administrative services needed to carry out the state's school facilities program, it would appear inconsistent with the statutory scheme for the SAB to directly "administer" the school facilities program by taking such an operational action as independently engaging an outside auditor.

¹ Ed. Code, § 17070.10, et seq.

QUESTION 1: Does Establishing a New Auditing Process or Changing the Audit Process Fall Under the Requirements of Government Code § 11340.5?

Government Code section 11340.5 prohibits a state agency from issuing, using, or enforcing "any guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule" (hereafter collectively referred to as a "standard") unless such standard has been adopted as a regulation in accordance with the provisions of the APA. (Govt. Code, § 11340 et seq.) A standard falls within and must be adopted in accordance with the formal rulemaking provisions of the APA if it meets the following two criteria: (1) the agency intends it to apply generally rather than in a specific case; and (2) the standard implements, interprets, or makes specific the law enforced by the agency. (*Tidewater Marine Western, Inc. v. Bradshaw* (1996) 14 Cal.4th 557, 571.)

Education Code section 17070.35 grants the SAB authority to adopt regulations for the administration of the Act. And Education Code section 17076.10 provides that the SAB may require an audit of a school district's reports and records concerning the expenditure of state school construction grant funds in order to ensure compliance with the Act. The Act itself provides no additional guidance concerning how such audits specifically shall be performed, and provides no guidance as to whether audit processes are contemplated to be established by regulation.

Given the above legislative grant of authority, the SAB has adopted School Facility Program (SFP) Regulations. (Cal. Code Regs., tit. 2, § 1859 et seq.) SFP Regulation 1859.106 authorizes the OPSC to conduct an audit of a district's expenditures under the Act, including compliance with site acquisition guidelines. If the OPSC does not conduct an audit within a specified time period, SFP Regulation 1859.106 provides that expenditures are deemed appropriate. SFP Regulation 1859.106 provides no additional guidance concerning the process of performing such audits.

Whether audit guidelines fall within the APA was examined by the Court of Appeal in *Modesto City Schools v. Education Audit Appeals Panel* (2004) 123 Cal.App.4th 1365. Modesto City Schools argued the State Controller's audit guide should be considered an underground regulation and subject to the APA because it was developed to apply generally to the Controller's compliance audits. The Court disagreed, noting that the audit guidelines were suggestive, rather than mandatory in every audit, and that auditors retained discretion to follow alternative procedures. (*Id.* at 1382.)

Given the foregoing, any guidelines developed by the SAB and/or OPSC would become subject to the formal rulemaking provisions of the APA only if strict and routine application of the guidelines were mandated in every audit. If auditors retain discretion as to how individual

audits will be performed, those guidelines, like the Controller's audit guidelines at issue in *Modesto City Schools*, need not be formally adopted as regulations under the APA.²

Here, as noted, neither the Act nor the SFP regulations direct that audits are to be performed in a particular manner. The only specificity set forth in SFP Regulation 1859.106 is that expenditures and a district's adherence to statutory site acquisition guidelines be reviewed. Assuming the OPSC audit processes previously developed or currently being considered allow for flexibility and discretion, those audit processes are not required to be adopted as formal regulations under the APA.

QUESTION 2: What Are the Legal Requirements That OPSC Must Follow for Amending the Audit Process Currently in Place?

Consistent with our answer to the first question, if the audit guidelines or process developed by OPSC provide auditors with flexibility and discretion as to how individual audits will be performed, those guidelines, like the Controller's audit guidelines at issue in *Modesto City Schools*, need not be formally adopted as regulations under the APA. Under these circumstances OPSC may simply amend its audit processes internally as it deems appropriate

² The rule articulated in *Modesto City Schools* is in harmony with cases addressing an agency's obligation to respond to Public Records Act (PRA) requests for information relating to audits. Consistent with the above holding that flexible audit guidelines need not be adopted as regulations under the APA, such guidelines are also not required to be publicly *disclosed* under the PRA. Specifically, an agency may decline to disclose an audit manual that details audit investigation techniques and procedures, as such material falls within the public interest exemption in Government Code section 6255 [public interest in non-disclosure outweighs interest in disclosure] and related federal decisions applying the "law enforcement" disclosure exemption under the federal Freedom of Information Act. (*Eskaton Monterey Hospital v. Myers* (1982) 134 Cal.App.3d 788, 792-794.) As *Eskaton* explains, an agency is not obligated to disclose its "game plan" or strategy for audits, where the effect of disclosure would be to enable law violators to escape detection. (*Id.* at 792-793.)

Further, those portions of preliminary notes, drafts, and memoranda that contain subjective analyses and opinion, and are not retained by the agency in the ordinary course of business, are exempt from disclosure under Government Code section 6254, subdivision (a). (*Citizens for a Better Environment v. Dept. of Food & Agriculture* (1985) 171 Cal.App.3d 704.) This statutory provision applies the deliberative process exemption and protects pre-decisional writings, draft advisory opinions, recommendations, and policy deliberations from disclosure. It does not, however, shield underlying factual material. (*Id.* at 713.) Under this exemption, draft audit reports may be protected from disclosure, provided such drafts are customarily discarded rather than retained. If it is an agency's policy to retain all drafts, they would need to be disclosed.

and need not disclose those guidelines or formally adopt them as regulations.³ If, however, the SAB/OPSC audit processes are written in a manner so as to apply mechanically, invariably, and inflexibly in every case, they would be required to be adopted in accordance with all of the procedures delineated in the APA. (Govt. Code, §§ 11340 et seq.)

QUESTION 3: If There is a Violation of Government Code § 11340.5, What Are the Steps That Must be Taken to Remedy the Problem?

If the SAB and OPSC are utilizing audit processes that are applied mechanically, invariably, and inflexibly in every case, such processes would be considered void as underground regulations not formally adopted in accordance with the provisions of the APA. (See *Tidewater Marine, supra*, 14 Cal.4th at 576.) Under these circumstances, the SAB and OPSC should discontinue their use and the SAB should immediately undertake to adopt the audit processes as formal regulations in accordance with the procedures delineated in the APA. (See *id.*; see also *Morning Star Company v. State Board of Equalization* (2006) 38 Cal.4th 324, 341-342.)

QUESTION 4; SUBPART A: Does the SAB Have the Legal Authority to Hire an Outside Auditor to do the Audits for OPSC?

Government Code section 15490 establishes the SAB and its membership. Subdivision (c) (1) of section 15490 authorizes the SAB to appoint "an employee to report directly to the board as assistant executive officer," and subdivision (c) (3) authorizes the SAB to "[e]mploy additional staff members, and secure office space and furnishings, as necessary to support the assistant executive officer in the performance of his or her duties." Subdivision (c) also specifies that the DGS director shall provide assistance to the SAB as the board requires. In turn, the OPSC is defined in the SFP regulations as "the State office within the Department of General Services that assists the Board as necessary and administers the Act on behalf of the Director." (Cal. Code Regs., tit. 2, § 1859.2.)

Mirroring Government Code section 15490, subdivision (c), Education Code section 17070.20 provides: "The Director of General Services shall administer this chapter and shall provide assistance to the board as it requires." Next, Education Code section 17070.35 delineates many of the SAB's duties, including the duty to adopt rules and regulations under the APA for the administration of the Act. And Education Code section 17070.40 creates the various state school facilities funds and empowers the SAB to apportion those funds for the purposes of the Act.

³ We observe that the questions presented to this office evidently derive from discussions occurring during a public "SAB Audit sub-committee hearing." There is certainly no *prohibition* against the SAB and OPSC publicly discussing and disclosing its audit processes. However, as this letter opinion explains, if those processes allow for flexibility and discretion in the conduct of audits, the processes are not *required* to be disclosed.

Whether the SAB has authority to contract directly for the services of outside auditors is neither expressly addressed in nor precluded by the Act or the above-quoted Government Code provisions. We believe, however, the overall statutory scheme reveals the Legislature intended to place such operational matters and decisions with the Director of General Services as part of his administrative responsibilities, while reposing the ultimate policy-making, rulemaking, and funding apportionment decisions with the SAB.

Specifically, the above statutory provisions and SFP regulations reveal that the OPSC is created within DGS in order to discharge the DGS director's responsibility for administering the Act and assisting the SAB as required by Education Code section 17070.20 and Government Code section 15490. And the SAB functions as the primary policy and decision-making entity by adopting regulations that govern administration of the Act and by determining how funds are to be apportioned. (Ed. Code, §§ 17070.35, 17070.40.) With regard to audits, consistent with this administration/support versus decision-making statutory scheme, the SAB has adopted regulations that place the responsibility for performing audits with the OPSC, while the SAB retains the power to adopt or reject the OPSC's audit findings and recommendations. (Cal. Code Regs., tit. 2, §§ 1859.106 and 1859.106.1.)

This view of the statutory scheme and entities' respective roles finds support in the Act's Legislative history and in applicable rules of statutory construction. For instance, when 1998 SB 50 was transmitted to then-Governor Wilson, the accompanying Enrolled Bill Report explained at page two: "The State Allocation Board is responsible for setting policy and providing allocations to districts that apply for state building funds." And since the term "administer" as used in Education Code section 17070.20 is not defined, it is appropriate to utilize its commonly understood meaning, as reflected in dictionaries. (See e.g. *Consumer Advocacy Group, Inc. v. Exxon Mobile Corp.* (2002) 104 Cal.App.4th 438,444.) Administer is principally defined in Merriam-Webster's on-line dictionary as "to manage or supervise the execution, use, or conduct of." Established rules of legislative interpretation thus support the conclusion that the SAB is responsible for decision-making, and the OPSC is responsible for executing the Act's provisions and the SAB's policies, rules, and decisions.

Given this scheme and division of responsibilities, we believe it would be outside the SAB's authority for the SAB independently to "hire an outside auditor to do the audits for OPSC." Instead, consistent with the above statutory and regulatory authority, the conduct of audits should be left to the OPSC as it carries out its mission of fulfilling the DGS director's statutory obligation to administer the Act.

QUESTION 4; SUBPART B: Does the Law Allow OPSC to Contract With and Hire an Outside Auditor Without Direction to Do so From the SAB?

As already noted, the DGS director is responsible for administering the Act and providing assistance to the SAB, and does so through the efforts of the OPSC. (Ed. Code, § 17070.20; Cal. Code Regs., tit. 2, § 1859.2.) In discharging that statutory duty, OPSC operates under the general direction and control of the DGS director, the individual statutorily empowered to

January 25, 2010

Page 6

control the operations of the DGS and its administrative subunits. (Govt. Code, §§ 14602, 14605, and 14607.) That administrative authority is of course subject to the lawful rules and regulations adopted by the SAB for administration of the Act. (Ed. Code, § 17070.35.)

There are no provisions within the Act or SFP regulations that purport to limit the DGS/OPSC's lawful authority to contract for services, such as limiting OPSC's contracting authority to those instances where the SAB has directed OPSC to do so. Accordingly, the DGS, acting through the OPSC, may contract for outside services to the extent such contracts are permissible under California's Public Contract and Government codes. (See specifically Public Contract Code sections 10335 through 10381 [relating to contracts for services], and Government Code section 19130 [establishing standards for use of personal services contracts in order to avoid conflict with the civil service mandate set forth in Article VII of the California Constitution]. Indeed, this authority is reflected in SFP regulation 1859.1 which expressly recognizes the DGS director's power to enter into contracts to administer the Act:

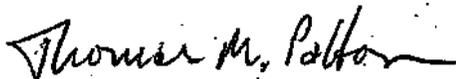
The General Services Director, or his or her legal designee shall perform all acts necessary to carry out the provisions of the Act except such functions as are reserved to the Board and to other agencies by law or by [SFP regulations] 1859 through 1859.107 inclusive. *The acts to be performed include, but are not limited to, entering into contracts to administer the Act.*

(Cal. Code Regs., tit. 2, § 1859.1, emphasis added.)

Accordingly, in administering the Act, OPSC may exercise the DGS director's authority and contract for outside services to the extent provided for and subject to the limitations set forth in the Public Contract and Government codes.

I hope this information has been helpful, and please do not hesitate to contact me if I may be of additional assistance.

Sincerely,



THOMAS M. PATTON
Deputy Attorney General

For EDMUND G. BROWN JR.
Attorney General

TMP:bls

Cc: Rob Cook, Executive Officer,
SAB and OPSC

LEGAL AUTHORITIES

State governors' executive orders

Executive orders as issued by the governors of the states are not laws, but do have the same binding nature.

Executive orders may, for example, demand budget cuts from state government when the state legislature is not in session, and economic conditions take a downturn, thereby decreasing tax revenue below what was forecast when the budget was approved. Depending on the state constitution, a governor may specify by what percentage each government agency must reduce by, and may exempt those that are already particularly underfunded, or cannot put long-term expenses (such as capital expenditures) off until a later fiscal year. The governor may also call the legislature into special session.

The Governor's website on Bond Accountability states...

"The Office of Public School Construction (OPSC) is staff to the State Allocation Board (SAB) and is part of the Department of General Services (DGS). The OPSC implements and administers the School Facility Program that is funded by various state general obligation bonds; including Proposition 1D bond funds, along with other programs for the SAB."

Education Code

17070.20. The Director of General Services shall administer this chapter and shall provide assistance to the board as it requires.

17070.35. (a) In addition to all other powers and duties as are granted to the board by this chapter, other statutes, or the California Constitution, the board shall do all of the following:

(1) Adopt rules and regulations, pursuant to the rulemaking provisions of the Administrative Procedure Act, Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code, for the administration of this chapter...

(2) Establish and publish any procedures and policies in connection with the administration of this chapter as it deems necessary.

(3) Determine the eligibility of school districts to receive apportionments under this chapter.

(4) Apportion funds to eligible school districts under this chapter.

(b) The board shall review and amend its regulations as necessary to adjust its administration of this chapter to conform with the act that amended this section to add this subdivision....

17076.10. (a) A school district that has received any funds pursuant to this chapter shall submit a summary report of expenditure of state funds and of district matching funds annually until all state funds and district matching funds are expended, and shall then submit a final report to the board. The board may require an audit of these reports or other district records to ensure that all funds received pursuant to this chapter are expended in accordance with program requirements.

101022. (a) The bonds authorized by this chapter shall be prepared, executed, issued, sold, paid, and redeemed as provided in the State General Obligation Bond Law (Chapter 4 (commencing with Section 16720) of Part 3 of Division 4 of Title 2 of the Government Code), and all of the provisions of that law, except Section 16727 of the Government Code to the extent that it conflicts with this part, apply to the bonds and to this chapter and are hereby incorporated into this chapter as though set forth in full within this chapter.

(b) For purposes of the State General Obligation Bond Law, the State Allocation Board is designated the "board" for purposes of administering the 2006 State School Facilities Fund.

CALIFORNIA CODES
GOVERNMENT CODE
SECTION **15490**-15492

15490. (a) There is in the state **government** the State Allocation Board, consisting of the Director of Finance, the Director of General Services, a person appointed by Governor, and the Superintendent of Public Instruction. The board shall also include three Members of the Senate appointed by the Senate Committee on Rules, two of whom shall belong to the majority party and one of whom shall belong to the minority party, and three Members of the Assembly appointed by the Speaker of the Assembly, two of whom shall belong to the majority party and one of whom shall belong to the minority party.

(b) The members of the board and the Members of the Legislature meeting with the board shall receive no compensation for their services but shall be reimbursed for their actual and necessary expenses incurred in connection with the performance of their duties.

(c) The Director of General Services shall provide assistance to the board as the board requires. The board may, by a majority vote of all members, do one or more of the following:

(1) Appoint an employee to report directly to the board as assistant executive officer.

(2) Fix the salary and other compensation of the assistant executive officer.

(3) Employ additional staff members, and secure office space and furnishings, as necessary to support the assistant executive officer in the performance of his or her duties.

15492. (a) The Department of General Services shall assign one full-time position within the Office of Public School Construction to the performance of the following functions:

(1) Providing advisory assistance to school districts regarding the process of site acquisition for projects for which the State Allocation Board has approved funding under Chapter 1 (commencing with Section 17210) of Part 10.5 of the **Education Code**.

(2) Formulating recommendations for administrative or statutory revision to the manner in which school sites are acquired under Chapter 1 (commencing with Section 17210) of Part 10.5 of the **Education Code**, and submitting those recommendations to the State Allocation Board.

(b) The Department of General Services shall establish a screening unit or other mechanism within the Office of Public School Construction to ensure that the office responds in a timely manner to any inquiry regarding the status of an application for project funding under Chapter 1 (commencing with Section 17210) of Part 10.5 of the **Education Code**.

(c) The requirements set forth in this section shall not increase the staffing level of the Office of Public School Construction, as that staffing level existed on the operative date of this section.

State Constitution Section 1 of Article XVI...

“Notwithstanding any other provision of this Constitution, Members of the Legislature who are required to meet with the State Allocation Board shall have equal rights and duties with the nonlegislative members to vote and act upon matters pending or coming before such board for the allocation and apportionment of funds to school districts for school construction purposes or purposes related thereto.”

**State Allocation Board
Audit Subcommittee**

December 2009

**Recommendations and Timeline for Developing and Implementing
a Sustainable Expenditure Audit Program for the SFP**

Lisa Kaplan, JD
Assistant Executive Officer

1. The Audit Sub-Committee proposes that the SAB at the January 27, 2010 SAB meeting direct that OPSC suspend the new audit process and resume the previous audit process in effect at the May 2008 publishing of the *School Facility Program Substantial Progress and Expenditure Audit Guide* until a publicly vetted process approved by the SAB is established with written documentation assigning responsibility
2. The Audit Sub-Committee reviews current and existing junctures of accountability at the state and local level, including at various stages within the SFP in order to avoid potential redundancies and limit inefficiencies within the SFP Expenditure Audit Program.
3. The Audit Sub-Committee proposes that the SAB clarifies the role and responsibility of OPSC as directed by the SAB pursuant to Education Code Section 17076.10.
4. The Audit Sub-Committee proposes that a written audit process and guide be developed through an audit review and development workgroup formed to assist the Assistant Executive Officer.
5. The Audit Sub-Committee proposes that the written audit process and guide be presented to the public at one or more special meetings of the Implementation Committee called for that purpose only.
6. The SAB Audit Sub-Committee hold a hearing on the written documents and process.
7. The Audit Sub-Committee propose that the SAB adopt: an audit guide; an audit process with required documentation identified and explicit timelines; an administrative review procedure through which disputed audit findings must be addressed by the Executive Officer prior to appeal and an audit appeals process.
8. The SAB Audit Sub-Committee reviews the process after six months of operation and report finding to the SAB.
9. Develop a timeline for completing items #5 - #8.

State Allocation Board Audit Subcommittee

Report by

Lisa Kaplan, JD
Assistant Executive Officer

DECEMBER 14, 2009 SAB AUDIT SUBCOMMITTEE HEARING

Minutes of the hearing

Monday, December 14th the State Allocation Board (SAB) Audit sub-committee met to further study and discuss the scope of the Office of Public School Construction (OPSC) auditing authority and bring recommendations to the SAB defining that authority.

The sub-cmte is composed of Senator Alan Lowenthal, Kathleen Moore (CDE), and Scott Harvey (DGS).

Rick Simpson, Deputy Chief of Staff for the Speaker of the California State Assembly, and chief architect of the education bonds over the past 12 years provided an overview of the reasons why the Legislature changed from the Lease-Purchase Program (LLP) to the School Facility Program (SFP), and the intent and reasoning behind the SFP.

The change from the LLP to SFP was to instate a formula driven process for the SAB to follow and take out the discretion of which schools got funded as set-up in the LPP. Furthermore, Mr. Simpson indicated that the SFP was set-up to give more discretion to school districts and offer an incentive to be cost effective so that if savings were realized, districts were allowed to keep those savings. Thus, the SFP intended to set-up a partnership between the State and Districts focusing on cost efficiency and a formula driven allocation of funds. Lastly, he indicated that the State oversight and audits were intended to be on the back end of the SFP funds, since the allocation to districts was full and final funding.

In response to questions, Mr. Simpson indicated that the authors of SB 50 never intended for OPSC to second guess Districts use or saving or the need to provide justification. He also mentioned that the SFP is the most successful program the State of California has created, housing over one million students in the last 10 years, thus this program should not be changed or threaten the state-local relationship that works pretty well.

Next the sub-cmte heard from Terry Tao an attorney with Atkinson, Andelson, Loya, Rudd and Romo to discuss who has the statutory authority of audits under the Gov Executive order.

Mr. Tao gave an overview of the Gov Executive Order and together with to Ed Code §17076.10(a), the law indicates that audits from originate from SAB to OPSC. Specifically, direction must be given from SAB to OPSC on the scope and authority of the audit since the SAB administers the State Bond funds. Therefore, since SAB is responsible for audits, any changes to the audit process must go through the rule making process as set-up in Government Code §11340.5, otherwise the SAB could be sued for abuse of discretion in not going through the Administrative Procedures Act (APA).

In response to questions, Mr. Tao indicated in his professional opinion an audit can be done by some other agency besides SAB/OPSC, and that OPSC acts under direction of the SAB and can only administer what the SAB directs it to. Moreover, he indicated any changes to the already existing APA approved audit process must be vetted publicly and go through the APA process again. Only until the new procedure has gone through this process can OPSC then implement the new audit, until then it must continue using its existing audit process.

Thereafter, the sub-cmte heard from OPSC (Rob Cook, Lisa Silverman, Steve Inman and Dennis Mehl) on the Audit Practices (past and current) that OPSC is using. The presentation began with sub-cmte members asking OPSC questions.

In response to questions, Executive Officer Rob Cook responded that the SAB was informed on at least two different times that OPSC was beginning a new audit process, but that the SAB gave no direction on the scope or authority of the audit or took a vote on the information presented. Furthermore, Mr. Cook indicated that according to Regulation §1859.106, OPSC has authority to audit every program SAB has authorized.

When asked if the old audit process met Gov Ex Order requirements for a performance audit, Mr. Cook responded that no it did not and reiterated that in fact the old process was not an audit at all. An SAB member disagreed with Mr. Cook's assessment, indicating that the Hoover Commission singled out the SAB as a shining example of a good audit process, during which Mr. Cook was an SAB member at that time, and kindly requested that Mr. Cook not refer to the Macias report as authority for audits as the report dealt with Facility Hardship and the SAB voted to not accept the report. In response to further questions, Mr. Cook indicated that the audits were "audits in name only" prior to two years ago and anything done prior to that was not an audit.

Another SAB member asked OPSC, how they can have an audit guide if there were no audits conducted? At this point Dennis Mehl (OPSC-retired annuitant who worked for DOF for many years) indicated that the term audit can get confusing and that OPSC is referring to the fact that there was no field audit until 2 years ago only program audits.

A SAB member then asked if there have been changes to the audit program. OPSC responded, yes, there have been significant changes in the audit program, but they don't call it a new process, just an update of the current audit.

Then a sub-cmte member then questioned OPSC that if in the audit, OPSC is questioning the savings on a project? Steven Inman (OPSC) responded yes, they review the savings to make sure they were expended on high priority projects within the district. Lisa Silverman (OPSC) also reiterated that in the beginning the audits were a program check, but now OPSC looks at projects savings under the new audit program.

Another sub-cmte member stated that the primary concern from Districts is that they do not know what auditing guide they fall under and that there has been no communication to them regarding what the new process / system is.

Questions:

KM ~ OPSC has had an audit process & guide that existed prior to Gov's executive order – did SAB review those and give OPSC audit authority /

- What is the process for audit authority and defining its scope? When the DOF report came out – it mentioned setting up a pilot program...what is the process that OPSC legally must go through to implement it?

KM to RC ~ what is the report SAB provided to DOF per the 2007 request in the Gov Ex Order? RC yes SAB approved it and on the consent agenda

RC ~ performance audit only related to financial hardship...of which the board did not approve – where did SAB give OPSC authority to change the scope of the audits they conduct?

LS ~ past audits didn't work – OPSC needed to have a risk based model to have an effective audit process

SH ~ wants to hear the fruits of the pilot process...because it now sounds like OPSC is finally doing an audit right – is that what he heard? SAB needs to implement best practices

KM~ indicated that the issue is that SAB must give direction to OPSC for their “new” audit program 1) Field, 2) Risk Assessment and 3) internal controls – procedures need to be written out on the new program to communicate this to district.

Dennis M ~ pilot was his word that he used for setting up an internal audit program prior to the end of a project (i.e. doing a pre-meeting with the district (application stage) about what an audit is and what OPSC's expectations are – i.e. 13 strategies – things that a district needs to have if it gets audited. He explained that the pilot is very different that the new audit process OPSC has implemented.

KM ~ primary concern for the districts is what auditing guide do they fall under and that OPSC needs to communicate more with districts what the process and system is.

DISTRICT PERSPECTIVES ON AUDITS

Peggy Reyes (Desert Sands USD), director of facilities for past 34 years in school districts – has constructed 22 new building with the new audits process and 17 schools with the old process. *Look at her submitted testimony*

Shawn Atlow (LA USD) – new audit process what set forth and given to the district in July 2009 on a project that began in 2006. The new process is not related to the prior SFP audit progress. What is new are the requirements for organizational charts, copies of written internal processes, copies of policies and procedures, requirement of signing the management representation letter, OPSC observing district staff working. Specifically, LA USD felt it was outside of OPSC's scope of authority to ask questions about a FEMA audit where no state money was used.

Lettie Boggs (Colbi)

- prior = compliance audits
- New = financial audit standard – where OPSC looks at internal controls, which is an okay thing to do as long as it is not duplicative of other audits districts undergo.

Audits need to focus on what no one else does

- all school district are required by law to have an independent internal audit every year that looks for fraud and double checks internal controls put into place at the district
- districts are allowed time to comment on the finding in the report before it is released
- each year the audit looks at different programs – so there is a continuous improvement process of auditing new programs and doubling checking on what was audited the prior year

There is already an audit process in place at all Districts – so the question is what is OPSC trying to do? What is their authority? Lettie believes that OPSC's job is to promote efficiency and for school districts being audited on something by 3 different agencies is not efficient

**STATE ALLOCATION BOARD
AUDIT SUB-COMMITTEE HEARING
DECEMBER 14, 2009**

**NEW AUDIT PRACTICES
*DISTRICT PERSPECTIVE***

Newly Instituted Audit Practices Established by OPSC (Pilot Program or New Standards?)

- Risk Assessment for project expenditure audit performed by evaluating district internal controls rather than on deviations from SFP norms. Examples of recent OPSC audit requests include:
 - Review of Non-SFP Projects
 - Review of general ledgers/reconciliation documentation
 - Requirement of certified Management Representation Letter
 - Review prior legal matters (capital & non-capital) and Grand Jury Reports
 - Review of Prior & Independent audit findings
 - Review of settlement agreements with contractors
 - Review of Staff Competence and turnover
 - Review of scope of work
 - Review of contract amounts for consultants

- Audit of project savings beyond verification of district certification that district spent or will spend the savings on other high priority capital outlay projects, including a re-review of the calculation of interest earned on the savings

- Re-opening formerly audited and closed out SFP projects by the OPSC

- Auditing under the new audit guidelines for projects built 5-6 years ago when other audit guidelines were in place

- Audit conferences conducted in district (timeline and standard operating procedures for these conferences do not currently exist)

- Site visit to verify projects were built

Stuart & Associates

Governmental Consultants

TO: Superintendents and Facilities Directors

FROM: Susan Stuart

DATE: August 12, 2009

RE: August 11, 2009
SAB Audit Subcommittee

On August 11th, the SAB held its first hearing of the SAB Audit Subcommittee – what proved to be a very interesting and enlightening hearing. The hearing began with an overview of the audit process by the California State Auditor. OPSC then gave an overview of their process, followed by Lettie Boggs who represented school districts in the OPSC audit process. Public Comment was then taken.

The members of the committee are:

- Senator Alan Lowenthal, Chair
- Kathleen Moore, Director, CDE representative
- Scott Harvey, Department of General Services representative

Susan Ronnback, Assistant Executive Officer, SAB, is staff to the committee.

One of the roles of this subcommittee is to define the scope of OPSC authority as it relates to conducting project audits.

CALIFORNIA STATE AUDITOR

The California State Auditor explained that the first component of an audit is risk assessment. An audit process does not audit all projects, rather only those that might be likely to be of high risk in their accounting procedures.

She explained the Governor's 2007 Executive Order, which clarified fiscal accountability in the audit process and identified three components of the audit protocol:

1. Early planning and Entrance Conference
2. In progress accountability and visits
3. Follow up – close out

It was clarified that the purpose of the audit is to share issues, allowing corrective action and to eliminate surprises. The auditor would provide a preliminary report one to two months prior to publication of the final report to allow corrective action.

Additionally she pointed out that the auditor reviews previous and other concurrent audits, so as not to duplicate information and effort by the agency. The purpose of the audit is make sure the funding agency “got what they paid for”.

Committee Member Questions

It was asked how and when a risk assessment was conducted on school district audits. This process has been absent in OPSC audits, as OPSC audits every project at close-out. When asked what risk assessment criteria were used for districts chosen for audits, OPSC stated two; dollar amount of the project, and prior audit findings. It was suggested that OPSC possibly should not be in the business of auditing, that it might be more valuable to have a contract with an outside auditing agency.

A member of the committee questioned OPSC as to whether and at what point an entrance conference was used in the OPSC audit. It was clear the first contact with the district by OPSC was during the close out portion of the audit. OPSC staff pointed out they first meet with the district to identify a space for the auditor to work.

Another member of the subcommittee asked if the OPSC audit process was the same for 100 percent funded projects and for those where districts contributed local funds. OPSC responded that all districts would be treated the same, although later in the hearing it was clarified that Financial Hardship Districts (100 percent state funded), require much greater scrutiny.

OFFICE OF PUBLIC SCHOOL CONSTRUCTION

Rob Cook described the evolution of OPSC’s audit process for the past two years, while he was Executive Director. He explained that much of the SFP

program includes front end certifications by the applicant district and they are accepted at face value. These certifications were verified at the time of the project closeout, and that prior to 2007, the audits performed were merely a desk audit of the project costs and not a true audit. He described three hallmarks of the audit process; equal access by districts, integrity of funds, and results expected by the voters.

OPSC commented that audit documentation consisted only of a single page form (SAB 50-06) certified by the district, which was refuted later in the hearing by school districts.

After a recent evaluation of the internal audit process, OPSC was advised of audit deficiencies that included:

- Insufficient staff training
- Poor audit practices
- Lack of field audits

New Audit Procedures

OPSC recently implemented measures to address these deficiencies and has updated the audit guidebook. Currently, OPSC has applied these updated audit procedures to four school districts. In the new protocols, there is no differentiation in the audit review of a financial hardship and non-financial hardship project. It was suggested that the OPSC audit guide be made available to school districts.

Committee Member Questions

Senator Lowenthal asked if the guidelines had been vetted at the SAB meeting and the answer was that it had not, nor had it been vetted before the SAB Implementation Committee. Committee members agreed that since OPSC is the staff to the SAB, any audit process of programs administered by the SAB should be approved by the SAB.

Ms. Moore expressed that the goal of an audit is to determine if the funds were spent appropriately. There is concern among school districts that the audit is perceived as being used as a “gotcha”. OPSC responded the new approach is now is to provide front end support and outreach to applicant districts. It was pointed out that when an audit takes place 6 to 8 years after the construction of a project, and at the very end, it is difficult to view this audit as helpful and not a “gotcha”.

Mr. Harvey asked if OPSC had an “Entrance Template” for what school districts could expect. There is none available at the time.

LETTIE BOGGS

Ms. Boggs stated that districts must go through several kinds of audits on facility projects; fiscal audits from an outside auditor, GO bond performance audits by the Citizen Oversight Committee, the OPSC audit, and fiscal audits from the County Office of Education. School districts must follow specific guidelines on how they incur debt and make expenditures. The local governing boards must approve all budgets, contracts, and payments issued while following the State Accounting Code Structure (SACS) Code.

Other internal controls require the district to maintain three basic types of filing systems:

- Alpha – filing system based on contracted entity such as an architect
- Numerical – filing system based on the source code of the expenditure
- Project – filing system tracking the cost incurred on a project-by-project basis. These files cover multiple years and multiple funds.

In addition, the district is required to follow the State Accounting Manual (SAM) with allocations of costs. Ms. Boggs stated that although the multiple controls seem redundant, this is an effective way of checks and balances on public dollars.

OPSC Audit

Although the required annual expenditure document (SAB 50-06) is a one page document, this form must be accompanied with a detailed spreadsheet of warrants issued, purpose of expenditure and type of expenditure, and an additional annual report is required. Until recently the required annual submittals have not been reviewed by OPSC. OPSC’s review was conducted after the district reported 100 percent of the expenditures.

Beginning last year, OPSC required an additional form, a Project Information Worksheet (PIW), which includes a significant amount of information on project costs and scope. In addition to all of the above, another challenge is that the OPSC audit process is not in sync with the CDE required annual audits.

Another major concern is that often the final close-out audit is measured against the current SFP regulations and not the regulations in place at the time of the apportionment. Districts will strive to meet the audit expectations if they knew what information is going to be needed for that audit, however, districts are being asked for documents they didn't know would be required years later. Currently, some audits are not concluded until 6 to 8 years after the apportionments.

Miss Boggs made some suggestions for the system that would include:

- Well explained rules
- Districts would be notified of any changes with a log that is searchable by date
- An audit scope that fits the project scope
- The documents would be available well in advance
- A nexus is provided between the project application and the audit communication
- Projects should not be subject to re-audits of programs that have already been audited by other entities.

State Audit Guide

Arlene Matsuura of the CDE identified the State Audit Guide that was last approved in 2002. In this guide districts are required to have their financial records audited by State approved CPA individuals/firms. Should a district disagree with the audit findings of the independent audit, they can appeal to the Audit Appeals Committee. This Committee membership includes members from DOF, CDE and FCMAT.

An independent audit is usually done at a higher level and not an in depth audit of a specific project. However, a consolidation of information from the various audits already being performed should be considered adequate.

Stakeholder Comments

- Previous "Desk Audits" felt like they were full financial and performance audits of the project to school districts.
- Long Beach Unified stated that districts plan and design projects based upon the rules in place at the time. However, these are not necessarily the rules used at the final close-out audit.
- The method of identifying savings and the method of tracking expenditures of those savings need to be further discussed. Once a

- project savings has been identified, the district should only be required to track how the savings, as deposited into a separate fund, is being appropriately spent.
- The full and final provisions of the SFP appear to apply to the applicant district and not to the SAB. OPSC audits a project and requires adjustments to the full and final apportionment based on final audit findings. Perhaps the districts should also have access to funds found in their favor during the course of the audit.
- School Districts have not been notified that any changes to the audit process were occurring. OPSC was asked to define the changes with an explanation of when the changes will be implemented.
- Small School District staff must multitask and it is difficult for them to keep up to date with incremental changes in the program.

CLOSING

Senator Lowenthal

Considering the presentations, Senator Lowenthal summarized the meeting stating the program must have transparency, openness, and conform to the spirit of SB50. The Senator stated the program should not be an onerous audit process and that the SAB needs to be taking a more active role in deciding the audit process.

The next meeting of the Audit Subcommittee hasn't been announced.



November 26, 2007

To: All School Districts and County Superintendents of Schools

Subject: Office of Public School Construction's Process Improvements – Internal Controls

The Office of Public School Construction's (OPSC) goal is to improve the audit process and reduce the amount of time being spent by OPSC and school district staff in auditing our closeout projects. The OPSC will be adopting a Management Representation Letter (MRL) in our audit process that is a certification by a school district that it has proper internal controls. We are confident that you are following these internal control standards since districts must make this same certification as part of their annual independent audit reports. Providing evidence of sound internal controls will enable us to streamline your audits.

Education Code Section 41020 requires each school district's books and accounts to be audited annually by certified public accountants that comply fully with Generally Accepted Government Auditing Standards (GAGAS). One component of GAGAS requires independent auditors to obtain a sufficient understanding of internal controls.

Proper internal accounting and administrative controls ensure that assets are safeguarded, accounting data is accurate, and that managerial policies are being followed. Some examples of proper internal controls include:

- Separation of duties – This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing transactions, and handling assets. No one individual should control all key aspects of a transaction.
- Controls over Information Processing – This includes edit checks of data entered, accounting for transactions in numerical sequences, comparing file totals with control accounts, and controlling access to data, files, and programs.
- Physical Control Over Vulnerable Assets – This includes security for and limited access to assets such as cash, securities, inventories, and equipment which might be vulnerable to risk of loss or unauthorized use.
- Monitoring conflict of interest – Staff authorized to approve contracts should not hold a financial interest in potential vendors.
- A system of checks and balances – Policies should be in place to ensure that authorization for approvals are in place.

Beginning in January 2008, we will be requesting that an authorized district representative sign and return the MRL. The OPSC must verify this information during its audit of State bond dollars and this certification is essential to ensure the integrity of the audits. By adopting the MRL, we will be able to reduce the amount of time that we mutually spend on your closeout audits.

If you have any questions regarding this matter, please feel free to contact Ms. Lisa Silverman, Fiscal Operations Manager, at (916) 322-0264.

Sincerely,
ROB COOK
Executive Officer
Office of Public School Construction

School District: _____

County: _____

Application Number: _____

School Name: _____

Management Representation Letter

This letter must be signed by the District Representative and/or other Authorized District Official.

Education Code Section 41020 requires each school district's books and accounts to be audited annually by certified public accountants that comply fully with Generally Accepted Government Auditing Standards (GAGAS). One component of GAGAS requires independent auditors to obtain a sufficient understanding of internal controls.

In connection with the audit of the above mentioned project for our school district, I confirm, to the best of my knowledge and belief the following representations made to you during the audit (please check yes or no):

Y N

- The school district is responsible for the fair presentation of the expenditures reported to the Office of Public School Construction.
- The school district has made available to you all -
 - Financial records and related data.
 - Contracts for all vendors.
- There have been *NO* irregularities involving management or employees who have significant roles in the internal control structure.
- There have been *NO* irregularities involving other employees that could have a material effect on the financial statements.
- I am not aware of any instances of actual or potential breaches of or non-compliance with laws and regulations that are central to the School Facility Program.

As the District Representative/Authorized District Official, I confirm that the school district maintains a system of internal accounting and administrative controls within the district. This responsibility includes documenting the system, communicating system requirements to employees, and assuring that the system is functioning as prescribed and is modified, as appropriate, for changes in conditions. I acknowledge that our system of internal accounting and administrative controls includes (please check yes or no):

Y N

- An organization plan that provides segregation of duties appropriate to safeguard state assets.
- A plan that limits access to school district assets to authorized personnel who require these assets in performance of their assigned duties.
- A system of authorization and recordkeeping procedures adequate to provide effective accounting controls over assets, liabilities and expenditures.
- An established system of practices to be followed in performance of duties and functions.
- Personnel of quality commensurate with their responsibilities.
- An effective internal review system.

If any of the above statements are incorrect or you have any concerns, please attach a written explanation.

Signature of District Representative and/or other Authorized District Official

Date

Print Name: _____