

**DEPARTMENT OF EDUCATION
INCLUDING
DIRECT AID TO PUBLIC EDUCATION**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2011**



AUDIT SUMMARY

Our audit of the Department of Education and Direct Aid to Public Education for the year ended June 30, 2011, found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System;
- no matters involving internal control and its operation that require management's attention and corrective action; and
- no instances of noncompliance with applicable laws and regulations or other matters that required reporting.

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DEPARTMENT OVERVIEW

The Department of Education (Education) has three functional areas, described in more detail below:

- Direct Aid to Public Education
- Central Office Operations
- Comprehensive Services Act for At-Risk Youth and Families

Education provides funding to localities for elementary and secondary public education through the Direct Aid to Public Education program. During fiscal year 2011, Education transferred over \$6.5 billion in state and federal funds to local school divisions. State funds make up approximately 80.8 percent of these funds, which support the Standards of Quality and other state programs.

Education's Central Office assists the 136 local public school systems by providing training, technical assistance, and monitoring their compliance with laws and regulations. Education helps teachers and other staff improve their skills by assisting school divisions, colleges, and universities in developing educational programs, and provides certain licensing and certification to school personnel. Education also serves as the pass-through agency for state and federal funds and determines the allocation of state money to local school divisions.

Education is the designated fiscal agent for the Comprehensive Services Act for At-Risk Youth and Families (CSA). Central Office staff process pool fund payments to localities for services performed assisting at-risk youth. We will include CSA in the 2011 Agencies of Secretary of Health and Human Resources audit report.

FINANCIAL INFORMATION

Education primarily receives General Fund appropriations, which represent its share of state sales tax and other state tax revenues. Education also receives federal grants and collects fees for teacher licensure.

The following table summarizes budget and actual operating activity for fiscal year 2011 by Education's functional areas, and we provide more detailed financial information for each area in this report.

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenses</u>
Direct Aid to Public Education	\$ 6,279,724,961	\$7,069,964,468	\$6,522,526,183
Central Office Operations	<u>116,239,517</u>	<u>111,415,186</u>	<u>84,930,772</u>
Total	<u>\$ 6,395,964,478</u>	<u>\$7,181,379,654</u>	<u>\$6,607,456,955</u>

Source: Commonwealth Accounting and Reporting System

Direct Aid to Public Education

Education acts as a pass-through agency for state and federal funds and determines the allocation of funds to local school divisions. Essentially \$6.5 billion in state and federal funding went to local school divisions primarily for public education and local school functions. The following table summarizes these expenses by fund.

Analysis of Budget and Expenses for 2011

	<u>Original Budget</u>	<u>Adjusted Budget</u>	<u>Actual Expenses</u>
General	\$4,739,288,334	\$4,710,904,185	\$4,706,095,192
Special	795,000	895,000	848,462
Commonwealth Transportation	2,173,000	2,173,000	2,173,000
Trust and Agency	21,804,100	360,844	190,521
Literary Fund	125,000,000	139,575,000	139,575,000
Lottery Proceeds	430,200,000	435,200,000	427,124,725
Federal	834,092,100	834,025,376	761,959,530
Federal Stimulus (ARRA)	<u>126,372,427</u>	<u>946,831,063</u>	<u>484,559,753</u>
 Total	 <u>\$6,279,724,961</u>	 <u>\$7,069,964,468</u>	 <u>\$6,522,526,183</u>

Source: Commonwealth Accounting and Reporting System

General Fund appropriations make up approximately 72 percent of the Direct Aid expenses. The decrease in the original budget is a result of adjusting the budget to reflect Central Appropriation amounts to cover the cost of items such as changes in retirement and other benefit contribution rates, as well as the distribution of other centrally funded items. The budget also adjusts funding for local school divisions based on updated sales tax projections, it adjusts the state share of health care premium support, and it includes policy changes to the Standards of Quality (SOQ), which include eliminating payments for accrued annual and sick leave for terminated employees and contract buy-outs. Education also received additional federal funds under the American Recovery and Reinvestment Act (ARRA), which helped offset General Fund budget reductions.

The decrease in the original budget of \$21.5 million for Trust and Agency funds and increase in the Literary and Lottery Proceeds of \$16.5 and \$5.0 million, respectively, is due to a miscoding error in the original budget. The final budgets reflect the proper funding amounts.

The increase in the original appropriation in Federal Stimulus Funds (ARRA) is a result of appropriating \$547 million for all remaining funds Education received under Title I, Individuals with Disabilities Education Act, and State Fiscal Stabilization Fund programs. The increase was also due to Education receiving \$249 million in ARRA funds under the Education Jobs Fund program and approximately \$23 million in several other smaller federal programs for the first time. We discuss the ARRA State Fiscal Stabilization Fund in further detail below.

While localities did not take advantage of all of the federal funding available (stimulus and non-stimulus) in fiscal year 2011, some of these funds are still available into fiscal year 2013. After December 2012, most federal stimulus funding will not be available, at which time, if General Fund revenues do not return, policy makers will need to decide if the Commonwealth should provide the same level of aid to localities or discontinue services in other areas.

The following table shows Direct Aid transfer payments by program:

Direct Aid to Public Education Expenses by Program

	<u>Expenses</u>	<u>Percent</u>
State Education Assistance Programs	\$5,268,847,434	80.8%
Federal Education Assistance Programs	1,246,519,283	19.1%
Financial Assistance for Cultural and Artistic Affairs	<u>7,159,466</u>	<u>0.1%</u>
Total	<u>\$6,522,526,183</u>	<u>100.0%</u>

Source: Commonwealth Accounting and Reporting System

The majority of the expenses under the State Education Assistance Programs are transfer payments to localities for several different programs, of which the Standards of Quality funding makes up 89 percent. Funding for the Standards of Quality is comprised of roughly 24 percent from Education's net revenue from the state sales and use tax and the remaining portion funded with other General Funds. Lottery profits from special state revenue sharing make up another eight percent of the State Education Assistance expenses. The Federal Education Assistance Program includes \$248 million of State Fiscal Stabilization Funds expenses.

The Stabilization Fund is an ARRA grant designed to assist states in filling budget deficits. Localities may use the grant for a wide variety of educationally related goods and services while targeting the following four specific areas:

1. Increase teacher effectiveness and address inequalities in the distribution of highly qualified teachers.
2. Establish and use a pre-kindergarten-through-college-and-career data system to track progress and foster continuous improvement.
3. Make progress towards rigorous college and career standards and highly qualified assessments that are valid and reliable for all students, including those with limited English proficiency and disabilities.
4. Provide targeted, intensive support and effective interventions to turn around schools identified for corrective action and restructuring.

Education also distributed four other ARRA grants in fiscal year 2011. Education received and allocated the remainder of \$125.6 million in Title I ARRA in fiscal year 2011. Localities expensed approximately \$70.1 million of these grants, designed to assist children who are at risk of not meeting challenging academic standards and who reside in areas with a high concentration of children from low-income families.

Education also received and allocated the remainder of the \$217.7 million of stimulus funding to school divisions under the Individuals with Disabilities Education Act to assist in providing a free and appropriate public education to all children with disabilities. Localities used \$114.6 million of these funds in fiscal year 2011. Education received a one-time grant of \$249.5 million under the Education Jobs Fund in fiscal year 2011 to assist in saving or creating education jobs for school year 2010-2011. Localities used \$42.3 million of these funds in fiscal year 2011. The Education Jobs fund grant does not end until September 30, 2012.

Education received and allocated \$8.7 million in Education Technology State Grants in fiscal year 2011. The main objectives of this grant are to improve student academic achievement through the use of technology in schools, assist all students in becoming technologically literate by the end of eighth grade, and encourage the integration of technology with teaching training and curriculum development to establish research-based instructional methods. Localities expended almost \$3.8 million of these grants in fiscal year 2011.

Localities have until September 30, 2011 to obligate IDEA State Grants funds and December 31, 2011 to spend the funds, or they will revert to the Federal Government. The Federal Government granted Education a waiver for the Title I and Education Technology funds, extending the date to obligate funds until September 30, 2012 and the date to spend funds until December 31, 2012.

The Standards of Quality set minimum standards for programs and services each local school board must provide. Education allocates funds to each locality based on demographic and census information gathered from local school divisions, following the provisions outlined in the Appropriation Act and Code of Virginia. Sales and use tax disbursements go to each school division using census data of school-age children within the school divisions. The school divisions receive lottery profit allocations based on the funding formulas of the Direct Aid programs appropriated in the Lottery Service Area of the Appropriation Act.

Education calculates most state payments using the Average Daily Membership (ADM) for each school division and the total agency appropriation. Local divisions receive these payments twice per month throughout the fiscal year. At the beginning of the fiscal year, Education makes a preliminary calculation of 24 equal installment payments for each school division. After each school division reports its actual ADM as of March 31, Education adjusts the remaining installment payments to reflect each school division's actual ADM. The following table shows expenses in Direct Aid over the last four fiscal years.

Costs per Pupil for Fiscal Years 2008-2011 (All Funds)

	<u>Fiscal Year 2008</u>	<u>Fiscal Year 2009</u>	<u>Fiscal Year 2010</u>	<u>Fiscal Year 2011</u>
Direct aid to localities expenses*	\$6,655,258	\$7,040,234	\$6,694,657	\$6,522,526
Total students**	1,191,836	1,195,326	1,203,823	1,208,902
Per pupil expenses***	\$ 5,584	\$ 5,890	\$ 5,561	\$ 5,395
Total teachers****	100,438	100,908	99,524	98,792

* Dollars in thousands

** Final March 31, adjusted average daily membership (ADM)

*** Direct Aid to localities expenses divided by total students

**** Reported from the Instructional Personnel Report for corresponding school years

In fiscal year 2011, total Direct Aid expenses decreased about \$172 million from fiscal year 2010 levels primarily due to General Fund budget reductions. While Education allocated approximately \$323 million of the Stabilization Fund in fiscal year 2011, school divisions only used approximately \$248 million. Localities have until September 30, 2011 to obligate these funds and December 31, 2011 to spend the funds, or they will revert to the Federal Government. Once these funds are no longer available, localities may experience dramatic cuts unless the economy improves or other funding sources materialize.

Central Office Operations

Analysis of Budget and Expenses for 2011

	<u>Original Budget</u>	<u>Adjusted Budget</u>	<u>Actual Expenses</u>
General	\$ 50,158,139	\$ 49,728,764	\$46,881,788
Special	5,193,165	5,193,165	1,391,759
Commonwealth transportation	240,942	240,942	238,106
Trust and agency	279,663	279,663	119,847
Indirect cost recoveries	1,287,254	1,287,254	904,754
Federal	59,080,354	38,180,744	32,937,494
Federal Stimulus (ARRA)	-	16,504,654	2,457,024
Total	<u>\$116,239,517</u>	<u>\$111,415,186</u>	<u>\$84,930,772</u>

Source: Commonwealth Accounting and Reporting System

Central Office's expenses were approximately \$26 million less than budgeted. This reduction occurred primarily due to a reduction in federal funds appropriations due to modifications to certain grant reimbursement accounting procedures and the termination of several federal grant awards. In addition, Education received a new, multi-year federal grant totaling \$15.1 million to cover costs related to the development and administration of a longitudinal data system expansion. However, Education only spent \$1.8 million of that grant during fiscal year 2011.

Most of Central Office Operation expenses are for contractual obligations associated with the Standards of Learning testing contract with NCS Pearson, Inc. In fiscal year 2011, NCS Pearson, Inc. received \$38.3 million in combined state and federal funds. Payroll and other personal services costs consist of roughly 30 percent of the total expenses for the Central Office Operation in fiscal year 2011.

Central Office Operation Fiscal Year 2011 Expense Analysis

Contractual Services	\$ 51,380,567
Personal Services	25,167,500
Transfer Payments	6,465,700
Continuous Charges	1,537,365
Equipment	198,304
Supplies and Materials	<u>181,336</u>
Total	<u>\$ 84,930,772</u>

Source: Commonwealth Accounting and Reporting System



Commonwealth of Virginia

Auditor of Public Accounts

Walter J. Kucharski
Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

January 3, 2012

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable Charles J. Colgan
Chairman, Joint Legislative Audit
and Review Commission

We have audited the financial records and operations of the **Department of Educating, including Direct Aid to Public Education** (Education) for the year ended June 30, 2011. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Audit Objectives

Our audit's primary objective was to evaluate the accuracy of the Department of Education's financial transactions as reported in the Comprehensive Annual Financial Report for the Commonwealth of Virginia for the year ended June 30, 2011 and test compliance for the Statewide Single Audit. In support of this objective, we evaluated the accuracy of recording financial transactions in the Commonwealth Accounting and Reporting System and in Education's accounting records, reviewed the adequacy of Education's internal control, and tested for compliance with applicable laws, regulations, contracts, and grant agreements.

Audit Scope and Methodology

Education's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered significance and risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

- Federal grant revenues and expenses
- Contractual services expenses
- Financial assistance and incentives payments
- Appropriations
- Information systems security

We performed audit tests to determine whether Education's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of Education's operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

Conclusions

We found that Education properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and in Education's accounting records. Education records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted no matters involving internal control and its operation that we consider necessary to be reported to management. The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Exit Conference and Report Distribution

We discussed this report with management on January 3, 2012.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

DBC/alh

DEPARTMENT OF EDUCATION

Patricia I. Wright
State Superintendent of Public Instruction

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