

Initial Statement of Reasons

SECTIONS 19810, and that section’s incorporation by reference of the 2015-16 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting (March 1, 2016).

Specific Purpose of the Regulations

The regulation to be amended, Education Code Section 19810, is that which incorporates the audit guide by reference. The audit guide defines terms and specifies procedures to guide accountants in the conduct of statutorily required financial and compliance audits of local education agencies (LEAs). (Ed. Code §§ 14502.1, 14503, 41020.) The Education Audit Appeals Panel (EAAP) must adopt the audit guide by July 1 of the fiscal year to be audited, and must adopt any supplement to address legislative changes to the conditions of apportionment before March 1 of the audit year. (Ed. Code § 14502.1(b)).

The Controller, pursuant to Education Code Section 14502.1, has proposed amending and supplementing the audit guide for fiscal year 2015-16. After review and some amendment, EAAP proposes to amend Ed. Code section 19810 and the 2015-16 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting.

Necessity/Rationale

These amendments are necessary to implement Education Code sections 14502.1, 14503, 41020, 47612 and 47634.2. Also, the addition of new section R, concerning the development of expenditure plans for educator effectiveness, follows express Legislative direction in Stats. 2015, ch. 13, §58(d) (A.B. 104); as amended by Stats. 2015, ch. 324, §8 (SB 103). The rationale for each amendment is provided below, the overall purpose being to guide the conduct of audits and the content of audit reports consistent with Legislative intent and the Controller’s proposals.

Problem to be Addressed in this Rulemaking

The proposed regulatory changes will make clarifying revisions and specify audit procedures to guide accountants in the conduct of the statutorily required financial and compliance audits of K-12 LEAs to address issues resulting from new legislation that affected conditions of apportionment.

Title 5, Division 1.5 **Chapter 3. Audits of California K - 12 Local Education Agencies** **Article 2 Audit Reports**

§ 19810. Annual Audit Guides.

The “2015-16 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting,” (~~July 1, 2015~~March 1, 2016), adopted by the Education Audit Appeals Panel, is incorporated by reference. The guide provides the audit steps, reporting requirements, and other guidance, for the required annual financial and compliance audits, subject to auditor judgment where alternative or additional audit steps may be appropriate. The annual guide is superseded by a supplemental audit guide, if needed, adopted before March 1 of each fiscal year.

Each annual guide and any applicable supplement are available on www.eaap.ca.gov/audit-guide, with paper or electronic copies available on request.

Note: Authority cited: Sections 14502.1 and 47612, Education Code; California Constitution, Article XIII, Section 36, subdiv. (e), subpara. 7, and Article XIII A, Section 1, subdiv. (b), subparas 3(C) and 3(D). Reference: California Constitution Article XIII B, Section 1.5; and Sections 8482.3(e)(5), 2574(b)(3)(C), 14501, 14502.1, 14503, 15286, 41020, 42238.02(b)(3)(B), 47612.5, ~~and~~ 47634.2 and 48000, Education Code.

Audit Guide Amendments

The proposed supplemental 2015-16 Audit Guide includes the following substantive changes:

- *Section R Educator Effectiveness* adds audit steps to address new legislation which provides funding for educator effectiveness, and requires LEAs to develop and adopt expenditure plans (Assembly Bill 104, Statutes of 2015, ch. 13, §58, and Senate Bill 103, Statutes of 2015, ch. 324, §8). The cited legislation appropriates \$490,000,000 to fund teacher and administrator support, such as training, coaching, and mentoring, to enhance educator effectiveness (A.B. 104, ch. 13, §58(a)); provides that the funds may be spent in fiscal years 2015-16, 2016-17, and 2017-18 (A.B. 104, ch. 13, §58(b)(3)); provides that as a condition for such funding each LEA must develop a spending plan presented in a public meeting and adopted in a later public meeting, and report on forms prescribed by the Department of Education no later than July 1, 2018 the specific expenditures made from the funds and the persons benefitted (A.B. 104, ch. 13, §58(b)(2)); and specifies that the funds and their expenditure be subject to the annual audits required by Education Code Section 40120 (A.B. 104, ch. 13, §58(d)). Accordingly, Section R of the audit guide seeks to verify that each LEA has developed a plan and is tracking the benefitted teachers and administrators, and recording expenditures, in a manner that will enable accurate reporting on or before July 1, 2018.
- *Section U Proper Expenditure of Education Protection Account Funds* is revised to make a technical adjustment to remove the word “disbursed” to make the audit step a determination of whether funds have been properly expended.
- *Section W Unduplicated Local Control Funding Formula Pupil Counts* is revised to exclude from audit testing any transitional kindergarten pupils who had their 5th birthday after Dec 2. New legislation allows enrollment in TK prior to a child’s 5th birthday (Assembly Bill 104, Statutes of 2015, ch. 13, §28, amending Ed. Code §48000(b)); however, such a pupil will not generate average daily attendance or be included in the Unduplicated Local Control Funding Formula Pupil Count (“LCFF Count”) until the child attains age five (Assembly Bill 104, Statutes of 2015, ch. 13, §28, amending Ed. Code §48000(c)(3)(B)(ii)). Further, a technical correction is made to exclude juvenile court schools from audit testing, as all juvenile court school students are included in the LCFF Count. (Ed. Code §2574(c)(4)). The amendments will ensure that auditing of records supporting the LCFF Count, which determines an LEA’s eligibility for supplemental and concentration grants, complies with new legislation.
- *Section Z Immunizations* is amended to reflect legislation that excludes independent study and special education pupils from compliance with vaccine requirements (Senate Bill 277,

Statutes of 2015, ch. 35, §2, adding new subdivision (f) to Health and Safety Code §120335), so that the audit testing for immunization compliance will be consistent with that change.

Technical, Theoretical, or Empirical Studies, Reports, or Documents

In preparing the proposed regulations, EAAP did not rely on any technical, theoretical, or empirical studies or reports.

Reasonable Alternatives to the Regulations, Including Alternatives that Would Lessen Any Adverse Impact on Small Business, and the Agency's Reasons for Rejecting Those Alternatives.

The audit guide regulations are applicable only to certified public accountants and public accountants who audit LEAs, and indirectly to the LEAs themselves. No alternatives to these amendments have been proposed which would reduce any impact on small business; in any case, no adverse impact on small business has been identified. No other alternatives were presented to or considered by EAAP. Particularly where the Legislature has ordered that specific matters be included in the audit guide and/or stated that compliance is a condition of apportionment, there is no alternative consistent with legislative intent.

Alternatives Proposed as Less Burdensome and Equally Effective in Achieving the Purposes.

No other alternatives were presented to or considered by EAAP.

Prescribed Audit Procedures.

The proposed amendments clarify, revise, and make additions to, the 2015-16 audit guide to conform to legislation enacted in 2015. The guide covers annual K-12 audits performed by licensed public accountants who must conduct the audits in accordance with generally accepted auditing standards. (Ed. Code §§ 14501, 14503, and 41020; Title 5, §§ 19811.) The audit guide includes provisions that authorize an auditor to use alternative procedures if, in the exercise of professional judgment, the auditor determines other procedures are more appropriate in particular circumstances. (Title 5, § 19810; Audit Guide, segment entitled "General Provisions," p. 1).

Evidence Supporting Finding of No Significant Adverse Economic Impact on Any Business.

EAAP has prepared the following Economic Impact Assessment pursuant to Government Code Section 11346.3(b) and has made an initial determination that adoption of the proposed regulations would not have a significant adverse economic impact on any business in the State of California. The regulations direct accountants to perform the steps necessary for the annual audits required by Education Code Section 41020. Education Code Section 14503 requires the use of this audit guide in the performance of those audits of LEAs. In brief, any economic impact derives from the statutory audit requirement and changes in substantive law already subject to audit.

Economic Impact Assessment

Staff of the Education Audit Appeals Panel (EAAP) have performed an economic impact assessment of the proposed regulations amending section 19810 and revising the Audit Guide which is incorporated by reference. This assessment was performed in compliance with Government Code section 11346.3(b).

What would the proposed regulations do?

This rulemaking adopts the supplemental Audit Guide for 2015-16, required by Section 14502.1, through incorporation by reference in a revised Title 5, Section 19810. The audit guide provides guidance, through definitions of terms and specification of procedures, to auditors in the conduct of the annual financial and compliance audits required of K-12 local education agencies by Education Code Section 41020. The guidance facilitates auditors in conducting audits and readers of audit reports by directing the manner of presenting findings.

Creation or Elimination of Jobs within the State of California

The activities specified in the regulations, or auditor-selected alternative activities, are necessary to implement existing Education Code sections. There will be no jobs created or eliminated as a result of these proposed regulations.

Creation of New or Elimination of Existing Businesses within the State of California

These regulations will make only technical and conforming changes to Section 19810 and the K-12 audit guide. There will be no businesses created or eliminated as a result of these regulations.

Expansion of Businesses or Elimination of Existing Businesses within the State of California

The proposed regulations will not expand or eliminate business. Education Code Section 41020 requires that these audits be conducted by professional accounting firms under contract to local education agencies, and requires that those firms use the standards and procedures developed pursuant to Section 14500 and following.

Benefits of the Regulation to the Health and Welfare of California Residents

EAAP does not anticipate that these proposed amendments would create specific benefits for the protection of public health and safety, worker safety, or the environment, the prevention of discrimination, the promotion of fairness or social equity, nor the increase in openness and transparency in business and government. EAAP has determined that the proposed amendments will ultimately benefit the welfare of California residents by ensuring that local education agencies are in compliance with regulatory requirements.