

Initial Statement of Reasons

SECTIONS 19815, 19816, 19816.1, 19817.2, 19819, 19820, 19824, 19828.4, 19840, 19843, 19844, 19845.2, 19848, 19849, 19850, 19851, 19852, 19853, and 19855, plus repeal of Section 19839.

Specific Purpose of the Regulations

The regulations to be amended are among those which determine the content of the annual audit guides. Those guides define terms and specify 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 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 2013-14. After review and some amendment, EAAP proposes to adopt, amend and repeal the regulations listed above. Conforming changes to definitional sections are also made.

Necessity/Rationale

These regulations are necessary to implement Education Code Sections 14502.1, 14503, 41020, 47612 and 47634.2; certain new sections are also required by other statutory provisions cited for Reference. The rationale for each amendment or new regulation 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 provide definitions of terms and specification of 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 in 2013 that affected conditions of apportionment.

Section 19839 of the audit guide regulations concerned compliance with the public hearing requirements for former "categorical" funds "flexed" by former Education Code Section 42605. As that statute has been repealed, this rulemaking would likewise repeal Section 19839.

Title 5, Division 1.5

Chapter 3. Audits of California K - 12 Local Education Agencies

Article 2 Audit Reports

§ 19815. Report Components.

This section lists the required elements of an Education Code Section 41020 audit report. Changes to paragraphs (e)(3) and (4) reflect the change in applicable years and terminology

included in the most current edition of the OMB Circular A-133 Compliance Supplement.

§ 19816. Definitions.

This section defines terms used in Section 19815 of these regulations that pertain to state program compliance with reference to the federal publications referenced in Section 19815 and this section. As stated in the introductory paragraph of this section, definitions are drawn from the three publications named there,¹ or are as defined in the subparagraphs of this section. Most of the deletions are language applicable to fiscal years before 2012-13, which is obsolete. Other changes result from the renaming of reference publications by their publishers; the citation of two reference books in the definition now appearing as subdivision (e); rewording of the definition of the “Report on State Compliance,” now appearing as subdivision (f), as supplied by the State Controller; and the addition of a new definition (superseding a definition formerly appearing as paragraph (a)(7) of Section 19824) of the “Schedule of Instructional Time” with language that accommodates the State’s migration to the Local Control Funding Formula (LCFF) enacted in Chapters 47 (AB 97), 49 (SB 91) and 357 (SB 97) of the Statutes of 2013, and codified in Education Code Sections 2574-2579, 37535.1, 42238.01, 42238.02, 42238.03 and 42238.07. In addition, Section 19816(f) [formerly subdivision (h)] specifies the numbers of audit procedures for the compliance requirements included in the revised audit guide, with obsolete material from years before 2012-13 deleted.

§ 19816.1. Applicability of Audit Procedures by Audit Year.

This section specifies which sections of the audit guide are applicable to each audit year. Former paragraph (a)(11) becomes (a)(1) with the deletion of obsolete paragraphs, and paragraph (a)(2) [formerly subparagraph (a)(11)] is updated to reflect the changes discussed below. The changes to paragraphs (b)(2) [formerly subparagraph (b)(11) and (c)(2) [formerly subparagraph (c)(9)] are parallel to those of paragraph (a)(2).

Article 3. State Compliance Procedures: Local Education Agencies Other Than Charter Schools.

§ 19817.2. Attendance reporting.

Education Code Section 42238.02 specifies grade spans (groupings of grade levels) for purposes of implementing the Local Control Funding Formula (LCFF) reforms. Before the reform legislation, grade levels, which carry different funding rates, were grouped variously for different purposes and among different LEAs. The grade span concept is designed to promote uniformity in recordkeeping as well as to specify how an audit report should report any inappropriately reported units of Average Daily Attendance (ADA). The amendments include a provision for allocating among the grade spans any disallowed units that the LEA’s records do not identify by grade level or grade span. In addition, the directive for reporting a finding has been more simply worded.

¹ *Codification of Statements on Auditing Standards*, published by the American Institute of Certified Public Accountants, the *Codification of Governmental Accounting and Financial Reporting Standards*, published by the Governmental Accounting Standards Board (GASB), *Government Auditing Standards* published by the Comptroller General of the United States.

§ 19819. Independent Study.

The grade span concept of Education Code § 42238.02 (discussed above), is to be used in the reporting of any inappropriately reported units of independent study ADA. In addition, the instructions (in subparagraph (a)(3) and subdivision (d)) for reporting a finding have been more simply worded. Finally, subparagraph (c)(7)(E) was reorganized for clarity by separating two different but similar-sounding required elements of independent study agreements.

§ 19820. Continuation Education.

The grade span concept of Education Code § 42238.02 (discussed above), is to be used in the reporting of any inappropriately reported units of ADA in continuation schools. In addition, the directive for reporting a finding has been more simply worded.

§ 19824. Instructional Time.

Existing Sections 19824 and 19824.1 reflect the optional reductions of instructional time requirements over the period 2009-10 through 2014-15 made by Education Code Section 46201.2 and 46201.3 due to the State's budget problems. The shorter year reduction that remains in effect for 2013-14 operates differently for a small number of districts depending on their past participation in Longer Year and/or Longer Day funding incentives, as reflected the tests set out in paragraph (a)(7)(B), (C) and (D), which name the districts to which they apply for clarity. Paragraph (a)(6) reflects the sunset of the remaining shorter year provision for districts which attain full funding under the LCFF. Thus, the amended section reflects transition to the LCFF which will eventually eliminate the different calculations necessitated by the retained shorter year authorization. In addition, the revised definition of the "Schedule of Instructional Time" has been relocated to Section 19816(l) for consistency, replacing the older and obsolete definition previously at that location. Finally, county offices of education are exempted from these audit tests because the time reductions do not apply to many of their educational programs, so that material audit findings were considered unlikely.

§ 19828.4. Instructional Materials.

Because the Instructional Materials Funding Realignment program is no longer operational, the end year for disallowance of funds (subdivision (b)) is changed to 2012-13.

§ 19839. Public Hearing Requirement – Receipt of Funds – REPEAL

This section directed auditors to determine whether school districts and county offices of education complied with the public hearing requirements of the former Education Code Section 42605. Repeal of Section 19839 is necessary, because Education Code Section 42605 has been repealed.

§ 19840. Juvenile Court Schools.

The grade span concept of Education Code § 42238.02 (discussed above), is to be used in the reporting of any inappropriately reported units of ADA in juvenile court schools. In addition, the directive for reporting a finding has been more simply worded, and the reference to obsolete uncodified law has been deleted.

§ 19843. Local Control Funding Formula Certification.

This section is added to direct the auditor to determine whether a school district, county office of education, or charter school has confirmed in writing its awareness of the requirements of the LCFF pursuant to Education Code Sections 2574, 2575, 42238.02, 42238.03, and 42238.07, as applicable, for the 2013-14 fiscal year. The State Controller recommended a written certification by the LEA attesting to the knowledge of new LCFF recordkeeping and associated compliance requirements prior to the initiation of compliance testing in the 2014-15 fiscal year. Among the LCFF requirements is progress toward K-3 class size reduction which by statute is to commence with the 2014-15 year. The alternative of providing no audit step related to the LCFF requirements was rejected in light of the extent and complexity of those reforms.

Article 3.1. State Compliance Procedures: School Districts, County Offices of Education and Charter Schools.

§ 19844. California Clean Energy Job Act.

This section complies with Public Resources Code Section 26240 which requires audit review of California Clean Energy Job Act expenditures for consistency with plans approved by the Energy Commission and compliance and Energy Commission guidelines. Audit tests are needed to verify proper use of the funds and to verify that only the planning portion of the funds are spent on planning. This section also calls for verification of compliance with the Public Resources Code Section 26235(f) in the manner in which the LEA contracts out such expenditures.

§ 19845.2. Class Size Reduction.

The class size reduction program was not funded for fiscal year 2013-14; thus the end year has been revised to 2012-13, thus making it inapplicable to fiscal year 2013-14 (and beyond).

19848. Common Core Implementation Funds.

The Education Finance trailer bill for the 2013 Budget provides funds for implementation of the “Common Core” academic content standards through professional development, instructional materials, and the use of technology-based instruction and assessment. The bill further requires the development of a plan, explained in a public meeting before its adoption in a subsequent meeting, for these expenditures. This provision would require auditors to verify compliance with the public meeting requirements and the statutorily specified uses of the funds. The section sets forth an adjustment option as an alternative to a finding of noncompliance for any of the funds appropriated by Section 85 of A.B. 86 (2013) that were inappropriately spent.

§ 19849. Unduplicated Local Control Funding Formula Pupil Counts.

An important part of the LCFF reforms involves increased appropriations to LEAs with a substantial percentage of pupils who are Foster Youth, English Learners, or eligible for free or reduced price meals (FRPM). This new audit procedure calls for verification that such increased appropriations were correct according to the LCFF law. Doing so requires the auditor to verify that no pupil in any of the three eligible categories is counted more than once, that the LEA has maintained adequate documentation for English Learner and FRPM eligibility, and that the unduplicated pupil counts reported on specified forms are consistent with the data that the LEA reported to the California Longitudinal Pupil Achievement Data System. This section requires the auditor to calculate any indicated adjustments to apportionments.

Article 4. State Compliance Procedures: Charter Schools.

§ 19850. Contemporaneous Records of Attendance.

A new subdivision (e) added to Education Code Section 47612 calls for new procedures to ensure the correct calculation of attendance in charter schools operating on multi-track calendars, to ensure that no pupil is counted for more than one unit of ADA. The continuing five school-day optional reduction is reflected in subparagraph (b)(4)(C). Provisions are added for proper reporting of pupils under age 22 who were continually enrolled in school through age 19, as their ADA remains eligible for apportionment. Finally, the Education Code Section 42238.02 grade span concept discussed above is to be incorporated in the reporting of any inappropriately reported units of ADA, with a provision for allocating among the grade spans any such units not identified by grade level or grade span; and the directive for reporting a finding has been more simply worded.

§ 19851. Mode of Instruction.

The grade span concept is to be incorporated in the reporting of any inappropriately reported units of ADA, with a provision for allocating among the grade spans any such units not identified by grade level or grade span. In addition, the directive for reporting a finding has been more simply worded.

§ 19852. Nonclassroom-Based Instruction/Independent Study.

The grade span concept is to be incorporated in the reporting of any inappropriately reported units of ADA. In addition, the directive (in subdivision (e)) for reporting a finding has been more simply worded. Finally, subparagraph (c)(7)(E) was reorganized for clarity by separating two different but similar-sounding required elements of independent study agreements.

§ 19853. Determination of Funding for Nonclassroom-Based Instruction.

The Section calls for verification that a charter school with more than 20 percent of its ADA generated out of the classroom (independent study) has a funding determination by the State Board of Education in effect for the year audited, and calls for testing the accuracy of the charter school's data submitted in order to obtain the funding determination. (EAAP reviews for

accuracy, but any changes to the funding determination are the province of the State Board of Education.) The grade span concept is to be incorporated in the reporting of any inappropriately reported units of ADA. In addition, the directive (in subdivision (e)) for reporting a finding has been more simply worded.

19855. Charter School Facility Grant Program.

This new section calls for testing, pursuant to Education Code Section 47614.5(k), the proper expenditure of funds received from the Charter School Facility Grant Program, which assists charter schools with facilities rent and lease costs. Beginning in fiscal year 2013-14, oversight for the program is vested in the California School Finance Authority and grant amounts are no longer correlated with categorical grants to other LEAs. Auditors are to verify that expenditures were consistent with the grant program's purposes.

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 add new procedures to the 2013-14 audit guide, remove or modify other procedures in keeping with 2013 legislation, delete the obsolete procedures of Section 19839, and make conforming changes to Sections 19816 and 19816.1. These audits must be 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 and 19812.) 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, §§ 19814 and 19816(h)).

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

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. 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.

Economic Impact Assessment

Staff of the Education Audit Appeals Panel (EAAP) have performed an economic impact assessment of the proposed supplemental regulations adding, amending and deleting the various provisions as enumerated above in Chapter 3 of Division 1.5 of Title 5, of the California Code of Regulations, relating to audits of California local education agencies (LEAs) that serve kindergarten and any of grades 1 through 12 (K-12). This assessment was performed in compliance with Government Code Section 11346.3(b).

What would the proposed regulations do?

These regulations will be part of the audit guide for California K-12 LEAs, as required by Education Code Sections 14502.1 and 14503. 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 (LEAs) by Education Code Section 41020. The proposed supplemental amendments to these regulations for the 2013-14 fiscal year are made pursuant to Education Code Section 14502.1.

Amendments are proposed to Section 19816 subparagraph (f) [formerly (h)] to add and remove audit procedures consistent with the sections that follow. Conforming changes are proposed to section 19816.1. Obsolete provisions of those two sections (for years before 2012-13) are deleted as unnecessary. Article 3, Section 19839 entitled Public Hearing Requirements -- Receipt of Funds, which became inapplicable beginning with 2012-13, is to be repealed.

Creation or Elimination of Jobs Within the State of California

The amendments are minor and/or technical in nature as they prescribe terms only for audits. 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 the K-12 audit guide. No businesses will be 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 LEAs, and requires that those firms use the standards and procedures developed pursuant to Education Code Sections 14500 and following.

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

These regulations make technical and conforming changes to the K-12 audit guide to ensure its compliance with existing statutes. We do 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 openness and transparency in business and government.