

## **Initial Statement of Reasons**

**SECTIONS 19810** and the 2017-18 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting (Supplemented effective March 1, 2018) incorporated by reference.

### **Specific Purpose of the Regulations**

The regulation to be amended, 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 2017-18. After review and some amendment, EAAP proposes to amend Section 19810 and the 2017-18 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. 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 1 General Provisions**

### **§ 19810. Annual Audit Guides.**

The "2017-18 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting," (~~July 1, 2017~~ March 1, 2018), 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](http://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(f)(5), 2574(b)(3)(C), 14501, 14502.1, 14503, 14509, 15286, 41020, 42238.02(b)(3)(B), 46146.5(h), 47612.5, 47634.2 and 48000, Education Code.

### **Audit Guide Amendments**

The proposed Supplemental 2017-18 Audit Guide includes the following amendments to the text of the existing 2017-18 Audit Guide. The rationale for each substantive amendment follows:

- *Section N* adds reference to Education Code 46160(a)(2). This new code section allows governing boards to schedule early and middle college high school students for at least 900 minutes over a 5 school day period or 1,800 minutes over a 10 school day period. This change is necessary to ensure the audit guide accurately reflects procedures currently allowed.
- *Section P Transportation Maintenance of Effort* is technically amended for clarity and to cite to a more appropriate page of the Department of Education’s website (listing the adjusted amount of 2012-13 transportation revenues) than previously cited.
- *Section S California Clean Energy Jobs Act* changes include correcting a typographical error in procedure 1; adding “pursuant to 1 and 2” in procedure 3 to reference the specific law; to remove the reference to the Public Resources Code and eliminate tests included in a-g, in procedure 4, because such elements are not specifically required in the plans; and to remove procedure 7 because the California Energy Commission already performs this review.
- *Section T After School Education and Safety Program* is technically amended to use the defined term “LEA” consistently, replacing “local education agency.” In addition, the words “middle or junior high” are deleted and language is added to reflect the priority given to homeless youth and those in foster care, as stated in Education Code 8483.1(d)(1) and 8483(c)(1). Also, the title to this section is changed as a technical amendment to reflect the inclusion of both programs in section T. Finally, to improve clarity, the directive to report noncompliance is added to each testing step in Sections 1 and 2, and step g in each of those sections is deleted.
- *Section U Proper Expenditure of Education Protection Account Funds* is technically amended to refer to the constitutional provision governing the expenditure of those funds.
- The following sections are amended for a technical change to ensure that the term “LEA” is used consistently throughout the audit guide, rather than the words “Local Education Agency.” Sections C, T and Y reflect these technical changes.

### **Audit Guide Addition**

- *Section Q Apprenticeship: Related and Supplemental Instruction* is a new audit step included to address Legislative directive included in Assembly Bill 1731, which stated that the Chancellor’s Office of the California Community Colleges has the authority to conduct audits of the K–12 local educational agencies’ oversight of apprenticeship training funds.

NOTE: The changes described above, with the exception of *Section P Maintenance of Effort*. are in effect on an emergency basis.

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

EAAP relied upon the Controller's Office letter of November 30, 2017, which proposed changes to the 2017-18 Audit Guide.

### **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 Supplemental 2017-18 Audit Guide clarifies and revises the language used in the 2017-18 Audit Guide to conform to legislation. 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 "Audit Standards" paragraph of the Audit Guide's General Provisions.) 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. (Audit Guide General Provisions, "Scope/Auditor Judgement.")

### **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 EAAP performed an economic impact assessment of the proposed regulations, in compliance with Government Code section 11346.3(b).

### **What would the proposed regulations do?**

This rulemaking adopts the Audit Guide for 2017-18, Supplemented effective March 1, 2018, as “required by Section 14502.1, through incorporation by reference in a revised Education Code 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 ensure adequate review of LEA compliance with new or revised 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**

These regulations make technical and conforming changes to the K-12 Audit Guide to ensure its compliance with existing statutes. As stated under the “Informative Digest/Policy Statement Overview” above, the proposed regulations will update and improve audit procedures of K-12 local education agencies, which would ultimately benefit the welfare of California residents by ensuring that local education agencies are in compliance with regulatory requirements.