

**Education Audit Appeals Panel
State of California**

Appeal of Fiscal Year 2002-03 Audit Finding 03-6 by:

Martinez Unified School District,

Appellant.

EAAP Case No. 04-13

OAH No. N2005040114

Decision

The Education Audit Appeals Panel has adopted the attached Proposed Decision of the Administrative Law Judge as its Decision in the above-entitled matter.

Effective date: November 28, 2005.

IT IS SO ORDERED.

November 28, 2005

Date

(Original Signed)

Thomas E. Dithridge, Chairperson
for Education Audit Appeals Panel

BEFORE THE
EDUCATION AUDIT APPEALS PANEL
STATE OF CALIFORNIA

In the Matter of:

MARTINEZ UNIFIED SCHOOL DISTRICT,

Appellant,

v.

OFFICE OF THE STATE CONTROLLER,

Respondent,

And

CALIFORNIA DEPARTMENT OF
FINANCE,

Intervenor.

Case No. 04-13

OAH No. N2005040114

PROPOSED DECISION

This matter came on for hearing¹ before Jaime René Román, Administrative Law Judge, Office of Administrative Hearings, in Sacramento, California, on August 31, 2005.

Banks & Watson, Attorneys at Law, by John C. McCarron, represented appellant Martinez Unified School District.

Kelly W. Ching, Staff Attorney, State Controller's Office, represented Steve Westley, California State Controller.

Roy S. Liebman, Deputy Attorney General, Department of Justice, State of California, represented the California Department of Finance.

Evidence was received and, to permit the submission of written argument, the matter was deemed submitted as of October 11, 2005.

¹ This is a proceeding conducted pursuant to the administrative adjudication provisions of the Administrative Procedure Act. Education Code section 41344.1, subdivision (b).

FACTUAL FINDINGS

1. On September 24, 2003, Stephen Roatch Accountancy Corporation, Certified Public Accountants, completed and submitted an Audit Report of the general purpose and financial statements of respondent Martinez Unified School District (the District), as of and for the year ended June 30, 2003.

2. The Audit Report set forth Finding 03-6/10000, relating to Attendance – Extended Year Special Education Program. That finding noted, “The District incorrectly computed ADA² for the Extended Year Special Education Program by dividing the number of hours of apportionment attendance by the fixed divisor of 175 days.” Having found this computation error for fiscal year 2002 – 2003, the auditor, Stephen Roatch, CPA, examined prior years’ records for fiscal years 1999 – 2000, 2000 – 2001, and 2001 – 2002. Mr. Roatch found that ADA computational errors extended through those prior years.

3. The cause of the ADA computational errors reportedly arose from an earlier communication misunderstanding between a District official and a State representative. That communication error was repeated in successive years.

4. The communication error resulted in an ADA overstatement, with a concomitant fiscal overpayment from the State to the District, as follows:

<u>Fiscal Year</u>	<u>ADA Overstatement³</u>	<u>Overpayment</u>
1999-2000	8.92	\$ 39,596
2000-2001	13.07	59,821
2001-2002	13.23	62,855
2002-2003	17.11	82,880

The combined overpayments amount to \$245,152. This sum is owed the State of California by the District.

5. The District, a small unified school district with a student population of approximately 4,000 students, filed a timely appeal to Audit Finding 03-6/10000, pursuant to Education Code section 41344.1.

6. The District does not contest the Audit Finding or concomitant deficiency, as it pertains to fiscal year 2002 – 2003. The January 2003 employment of a new District Assistant Superintendent, Timothy Rahill, subsequently resulted in a correction to the 2002 – 2003 ADA computation. That amended ADA submission by the District to the State, through the Contra

² ADA denotes Average Daily Attendance.

³ Education Code section 14503, subdivision (a), states, “If a local education agency is not in compliance with a requirement that is a condition of eligibility for the receipt of state funds, the audit report shall include a statement of the number of units of average daily attendance, if any, that were inappropriately reported for apportionment.”

Costa County Office of Education, was never received by the State.⁴

7. The District submits no obligation should be owed for prior year deficiencies. To that end, the District contends:

- A. The State Controller is not authorized to retroactively apply audit findings to collect money for errors in prior years;
- B. The District relied on a State representative's erroneous advice; and
- C. Each prior year's deficiency is fiscally immaterial.

8. Districts are required to maintain records for no less than three years.⁵ In conducting a District audit, an auditor largely applies Generally Accepted Government Auditing Standards (GAGAS).⁶ In addition, an auditor utilizes a State Controller Agency Guide.⁷ The purpose of a District audit is to ascertain the District's compliance with legal requirements.⁸ Such "audit or review" may be conducted by the Controller's Office, a certified public accountant or a public accountant.⁹ No audit purports to review all District documents but, consistent with GAGAS, a representative sample.¹⁰ When, however, a deficiency is discovered, more scrutiny is focused by an auditor in an effort to determine both the scope and extent of the deficiency.¹¹ Such a focused scrutiny includes an auditor's review of prior years' records.¹²

9. Mr. Roatch conducted his audit in accord with, inter alia, GAGAS and the Agency Guide.¹³ Having found the 2002 – 2003 deficiency, it became professionally

⁴ In its Post-Hearing Brief, received September 19, 2005, the District states, "Because it appears that the State did not receive the District's Amended ADA computation from the County, the District withdraws its appeal of the audit finding as to the 2002-03 school year." In sum, the "District does not challenge that it made an error on its ADA computation for Extended Year Special Education. Nor does the District challenge the audit findings regarding the 2002-03 school year."

⁵ California Code of Regulations, title 5, sections 16025 and 16026.

⁶ OMB Circular A-133; see also Education Code sections 14503, subdivision (a), and 41020; California Code of Regulations, title 5, sections 19812 and 19814.

⁷ *Standards and Procedures for Audits of California K-12 Local Education Agencies*, April 2001. See Education Code section 14502.1, and *Modesto City Schools v. Education Audits Appeal Panel* (2004) 123 Cal.App.4th 1365.

⁸ Education Code section 41344.1, subdivision (c).

⁹ Education Code section 41344, subdivision (e).

¹⁰ *Bily v. Arthur Young & Co.* (1992) 3 Cal.4th 370, 382: "[A]n audit rarely, if ever, examines every accounting transaction in the records of a business."

¹¹ *Bily*, *supra* at p. 380.

¹² The District's contention that the "State Controller is not authorized to retroactively apply audit findings to collect money for errors in prior years" is summarily dismissed. Its reliance on Education Code section 41610 is inapposite. The legislative mandate that District records be maintained for three years would be clearly impaired, were the undersigned to adopt the District's contention. Education Code sections 14500, 41020, and 41341.

¹³ Education Code sections 14503 and 41020; *Standards and Procedures For Audits of California K-12 Local Educational Agencies* [SCO audit guide], April 2003, Section 310 [*cf.*, California Code of Regulations, title 5, sections 19812 and 19814]. That performance is not, despite the District's contention, an inappropriate delegation of public authority. *People ex rel Lockyer v. Sun Pac. Farming* (2000) 77 Cal.App.4th 619, 633; *Wilkinson v. Madera*

incumbent upon him to consider whether the District had erred similarly in prior years.¹⁴ Employing that professional judgment, Mr. Roatch undertook a further audit that reviewed records for three prior years to ascertain whether the 2002 – 2003 deficiency was an aberration or systemic.¹⁵ Mr. Roatch discovered the District had erred in prior years, and consequently reported his findings in his 2003 Audit Report. To his credit, Mr. Roatch, observing the sum of each prior year's ADA computation error, opined that the sum was immaterial, and that each prior year's audit report was neither substantially nor professionally compromised. On the other hand, the combined scope of the prior years' errors result in an amount that is material.

10. An administrative proceeding need not "be conducted according to technical rules relating to evidence and witnesses."¹⁶ Hearsay is admissible. However, upon a properly interposed objection, hearsay evidence may be limited in scope.¹⁷ In balancing the respective evidence provided by each party,¹⁸ the undersigned applied, in part, the criteria set forth at Evidence Code sections 412¹⁹ and 413.²⁰

- A. The District's auditor, aware of the cause for the ADA deficiency reporting, ascribed such error to one of two reasons: either a prior employee who suffered from some cognitive deficiency that contributed to miscommunication, or that prior employee's replacement mistakenly relied on the prior employee's errant guidance. While the District competently established the local cause (i.e., an employee) underlying its repeated deficiencies, such cause was not competently shown to have arisen by any act by a State representative.
- B. As set forth above, the District auditor observed that each prior year's ADA overpayment was sufficiently immaterial. However the review necessitated by accounting principles revealed a systemic error that occurred over successive years and amounts to a sum that becomes both significant and material.²¹

Community Hospital (1983) 144 Cal.App.3d 436, 442; *Kugler v. Yocum* (1968) 69 Cal.2d 371, 384.

¹⁴ *Bily, supra*; GAGAS, section 4.14: "Auditors should consider the results of previous audits...and follow up on known significant findings..." Section 4.17: "auditors should apply audit procedures specifically directed to ascertain whether violations...have occurred." Section 4.18: "auditors should apply audit procedures specifically directed to ascertain whether violations have occurred..."

¹⁵ GAGAS, section 4.15.

¹⁶ Government Code section 11513, subdivision (c).

¹⁷ Government Code section 11513, subdivision (d).

¹⁸ *Fresno County Office of Education*, Case No. 00-03 (OAH No. N2000050273), May 25, 2001, factual finding 27, p. 8.

¹⁹ Evidence Code section 412 provides, "If weaker and less satisfactory evidence is offered when it was within the power of the party to produce stronger and more satisfactory evidence, the evidence offered should be viewed with distrust."

²⁰ Evidence Code section 413 provides, "In determining what inferences to draw from the evidence or facts in the case against a party, the trier of fact may consider, among other things, the party's failure to explain or to deny by his testimony such evidence or facts in the case against him, or his willful suppression of evidence relating thereto, if such be the case."

²¹ Education Code sections 14501, 14503, 41344, and 41344.1; and California Code of Regulations, title 5, section 19816.

LEGAL CONCLUSIONS

The State of California, its political subdivisions, including school districts, possesses limited resources. The Education Audit Appeals Panel (the Panel) has a constitutional, statutory and regulatory obligation to properly ascertain that the State's limited resources are properly disbursed and expended as required by both law and regulation.²²

The District submits, "The sole issue on this appeal is whether, under the circumstances of this case, the Controller's office is allowed to require the District to amend its ADA computations for the three previous years (1999-2000, 2000-2001, and 2001-2002) and to require the District to repay certain funds that it received those years." To that end, it is determined that the Controller is allowed to require the District to amend its ADA computations for prior fiscal years and to require reimbursement.²³ Further, it is consistent with the professional responsibilities of a public accountant conducting an audit to examine prior extant records to ascertain both the scope and extent of a currently discovered deficiency, to ascertain its current and historic significance or materiality. Those prior year audit reports did not reveal the subsequently discovered deficiency. This does not function to preclude the Controller from meeting his or her statutory obligations.²⁴ Cause accordingly exists to deny the appeal of appellant, pursuant to the provisions of Education Code sections 14500, 14501, 14503, 41020, 41341, 41344, and 41344.1, in conjunction with California Code of Regulations, title 5, section 19814, as set forth in Findings 1 through 10.

ORDER

The appeal of appellant Martinez Unified School District is DENIED.

Dated: 11-14-05

(Original Signed)
JAIME RENÉ ROMÁN
Administrative Law Judge
Office of Administrative Hearings

²² *Visalia Unified School District*, Case No. 02-13 (OAH No. N2002100180), Feb. 28, 2005; Education Code sections 14501, subdivision (b); 41344, and 41344.1; and California Code of Regulations, title 5, section 19814.

²³ Education Code sections 14500 – 14507, 41020, and 41341 – 41344.1.

²⁴ *Western Surgical Supply v. Affleck* (1952) 110 Cal.App.2d 388, 392 – 393; *Martin v. Alcoholic Beverage Control Appeals Board* (1959) 52 Cal.2d 287.