

## **Initial Statement of Reasons**

**SECTIONS 19810** and the 2019-20 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting (Supplemented effective March 1, 2020) 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, 41024.) 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, proposed by letter dated December 13, 2019, amending and supplementing the Audit Guide for fiscal year 2018-19. (Later, the Department of Education proposed, and the stakeholders discussed in a January 13, 2020 meeting, changes to Sections P [Transportation Maintenance of Effort] and T [Clean Energy Jobs Act], both of which are technical changes included in this Rulemaking). After review and some amendment, EAAP proposes to amend Section 19810 and the 2019-20 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 affects conditions of apportionment.

## **Title 5, Division 1.5** **Chapter 3. Audits of California K - 12 Local Education Agencies** **Article 1 General Provisions**

### **§ 19810. Annual Audit Guides.**

The “2019-20 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting,” (~~July 1, 2019~~ March 1, 2020), 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 2574(b)(3)(C), 8482.3(f)(5), 14501, 14502.1, 14503, 14509, 15286, 41020, 41024, 42238.02(b)(3)(B), 47612.5, 47634.2 and 48000, Education Code.

*Document incorporated by reference:* 2019-20 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting (March 1, 2020). After a number of years' experience, it proved cumbersome to set out the parts of the audit guide in regulations, some of which applied to different sets of fiscal years, and some applicable to past audit years. Incorporation by reference simplified the process of adopting annual audit guides and annual supplements, by putting the guide directly in usable format. Annual audit guides, audit guide supplements, and the steps of the rulemaking progress are readily available on EAAP's website.

### Audit Guide Amendments

The proposed supplemental 2019-20 Audit Guide includes the following changes:

- *Section E. Continuation Education*, relocates procedure 6(a) to new step 7, as the requirement that no more than 10% of continuation high school ADA at P2 (excluding pupils who are pregnant or a child's primary caregiver) was generated through independent study applies to all continuation high school pupils, and not just those from whom the step 6 requires a sample, i.e., regardless of which pupils are earning work experience credit. As a result, the step requiring a finding is renumbered to Step 8.
- *Section F. Instructional Time*, recognizes the exemption from the ordinary minimum instructional days requirement for the three districts named in Ed. Code section 37700, and potentially others pursuant to subdivision (c) of that section, to operate on a four days per week schedule; and provides, in a sentence added to Step 9, that those districts are only subject to penalties for insufficient instructional days if they fail to offer the required number of educational minutes required by Ed. Code section 46208. This amendment conforms to the amendment to Ed. Code section 37700(b)(2).
- *Section O. K-3 Grade Span Adjustment* deletes language applicable only to the period when some or all districts had not met their Local Control Funding Formula (LCFF) targets, thus making the requirement for each schoolsite's average class enrollment no greater than 24 unless a collective bargaining agreement provides a different limit. **All districts have met their LCFF targets.** Consequently, the reference to Education Code section 42238.02(d)(3)(B) or (C) is replaced with a reference to section 42238.02(d)(3)(D). Previously, this audit guide section referenced "maximum average class enrollment" as adjusted by section 15498.1(g) of this Title.

- *Section P. Transportation Maintenance of Effort* technically amend Item 2 to make clearer the steps auditors can follow to access the exhibit on the California Department of Education’s website, which details pupil transportation revenue received by the LEA during the benchmark fiscal year of 2012-13.
- *Section T. California Clean Energy Jobs Act* takes language requiring a finding and disallowance of construction project funds when there has been no timely final completion report of expenditure from Step 6, which applies only in specific circumstances, and restates that requirement to apply to all projects failing this requirement. In Step 6 a technical amendment changes “include a finding” to “report a finding,” for clarity.
- *Section U. After School Education and Safety Program* is amended to provide an exception to the release time requirement (5:00 pm rather than 6:00 pm) for schools located in an area with population density of less than 11 persons per square mile, because many pupils in such areas will travel relatively greater distances after the after school program. The change implements amendments effective January 1, 2019 to Education Code section 8483(a).
- *Section W. Unduplicated LCFF Pupil Counts* makes a technical amendment to update the references to date maintained on the California Department of Education web site which reflects LEA reporting of the numbers of students applicable to the Unduplicated LCFF Pupil Count. Specifically, it defines “certified” data as data satisfying the “SELPA approved” filter, available only if both the LEA and the SELPA approved their data.

NOTE: The changes described above are already in effect on an emergency basis.

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

EAAP relied upon the Controller’s Office letter of January 2, 2019, which proposed changes to the 2018-19 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 2019-20 Audit Guide clarifies and revises the language used in the original 2019-20 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 2019-20, Supplemented effective March 1, 2020, 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. 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. 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.