

Initial Statement of Reasons

SECTIONS 19810 and the 2023-24 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting (Supplemented effective March 1, 2024) 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 enacted before March 1 of the audit year. (Ed. Code § 14502.1(b)).

The Controller, pursuant to Education Code Section 14502.1 and by letters dated February 7 and 14, 2024, proposed amending and supplementing the Audit Guide for fiscal year 2023-24. After review and some amendment, EAAP proposes to amend Section 19810 and the 2023-24 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 "2023-24 Supplemental Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting," (~~March~~July 1, 2023~~4~~), 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, including Appendices A, B and C and any applicable supplement, is available on www.eaap.ca.gov/audit-guide, with paper or electronic copies available on request.

Note: Authority cited: Article XIII, Section 36 and Article XIII A, Section 1, California Constitution; and Sections 14502.1 and 47612, Education Code. Reference: Article XIII B, Section 1.5, California Constitution; and Sections 2574, 14501, 14502.1, 14503, 37700, 41020, 41024, 41480, 42238.02, 43500, 43501, 43502, 43504, 43505, 43509, 43520, 43521, 43522, 44258.9, 45037, 46146, 46300, 47605, 47612, 47614, 47634, 48000, 48206, 48306, 48313, 51747, 51749, 52060, 53071, 56026, 56340 and 76004, Education Code.

Document incorporated by reference: 2023-24 Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting (March 1, 2024). Annual audit guides, audit guide supplements, and the steps of the rulemaking progress are available on EAAP's website.

Audit Guide Amendments

The proposed annual 2023-24 Supplemental Audit Guide includes the following amendments:

Report Components Section 4.a, LEA Organization Structure is deleted and moved to new Section 5, Other Information. Also, a technical change is made to section 5.a.2 requiring a statement in instances where there was no change in the school district's boundaries.

Report Components Section 5.b, State Compliance Report is amended to ensure that the audit guide is in compliance with the most recent requirements of the American Institute of Certified Public Accountants.

Section G. Instructional Materials is amended to add a penalty to any finding that the school district or county office of education did not follow required steps to ensure that each pupil would have sufficient textbooks and instructional materials, in accordance with Section 60150(b).

Section P. Transportation Maintenance of Effort is deleted because there are no audit requirements in statute and no fiscal penalty for failing the requirement. Declining enrollment in some LEAs have reduced transportation expenses, and the Home-to-School Transportation Reimbursement program provides new funding for Home to School transportation.

Section TT. Home-to-School Transportation Reimbursement includes a technical change to reflect the fact that plans may have been updated subsequent to the original adoption on April 1, 2023.

Section T. Clean Energy Jobs Act is deleted due to completion of projects and submission of final expenditure reports.

Section T. Art and Music in Schools implements SB 115 (Stats. 2023, Chapter 49), amending sections 8820-8822, which in turn carry out the mandate of Proposition 28, enacted November 8, 2022, by funding a new, ongoing program supporting arts instruction in schools beginning in 2023-24. Section 8830 subdivision (i) requires the program to be included in the

annual audit. Audit steps will review expenditures to ensure they were used to supplement rather than supplant existing services, that after an audit year in which the allocated funds are fully expended or the third year of the program, no more than 20 percent of the expenditures were used for allowable purposes other than certificated or classified salaries and benefits; and that no more than 1 percent of the total funding received in the allocation year was used for administrative expenses, including indirect costs. Other audit steps verify that the LEA certified compliance with Section 8820(g)(1) (or a waiver by CDE), and that the LEA certified compliance with Section 8820(g)(2), concerning the use of art and music funds.

Section Z. Immunizations section is revised to delete review of students in the 1st or 8th grade in the audit year. Review of those grades was necessary because of the disruption caused by the Covid-19 Pandemic. Current immunization rates are approaching rates near pre-pandemic levels and the Department of Public Health is no longer requiring reporting from grades 1 and 8.

Section DZ. Expanded Learning Opportunities Program includes technical amendments to steps 3 and 5 to ensure reference to the correct code section. It is also adding audit procedures that would exempt an LEA from fiscal penalty when it is temporarily prevented from operating the Expanded Learning Opportunities Program because of a school site closure due to emergency conditions, in compliance with Section 46120(b).

Section EZ. Transitional Kindergarten is amended to delay steps 5 and 6 to 2025-26 as a result of deadlines changed by SB114. It would also add a new procedure to audit transitional kindergarten classroom with early enrollment pupils, also resulting from changes made by SB114 to Section 48000.15.

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 letters dated February 7 and 14, 2024, which proposed supplemental changes to the 2023-24 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 2023-24 Audit Guide clarifies and revises the language used in the original 2023-24 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 2023-24, Supplemented effective March 1, 2024, 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.