



STATE OF ILLINOIS
**OFFICE OF THE
AUDITOR GENERAL**

William G. Holland, Auditor General

SUMMARY REPORT DIGEST

REGIONAL OFFICE OF EDUCATION #34
LAKE COUNTY

**FINANCIAL AUDIT (In Accordance with the Single
Audit Act and OMB Circular A-133)
For the Year Ended: June 30, 2011
Release Date: July 10, 2012**

Summary of Findings:
Total this audit: 7
Total last audit: 5
Repeated from last audit: 4

SYNOPSIS

The Regional Office of Education #34:

- did not have sufficient internal controls over the financial reporting process;
- did not apply appropriate accounting principles;
- did not have adequate controls over purchased services expenditures;
- did not have adequate internal controls over cash;
- did not have adequate internal controls over reporting or accurate expenditure reports;
- did not have adequate documentation for payroll expenditures; and
- did not have adequate documentation for expenditure reports.

{ Revenues and expenditures are summarized on the reverse page. }

REGIONAL OFFICE OF EDUCATION #34
LAKE COUNTY

FINANCIAL AUDIT
(In Accordance with the Single Audit Act and OMB Circular A-133)
For The Year Ended June 30, 2011

	FY 2011	FY 2010
TOTAL REVENUES	\$7,835,861	\$8,324,192
Local Sources	\$1,673,575	\$3,060,180
% of Total Revenues	21.36%	36.76%
State Sources	\$3,990,839	\$3,829,324
% of Total Revenues	50.93%	46.00%
Federal Sources	\$2,171,447	\$1,434,688
% of Total Revenues	27.71%	17.24%
TOTAL EXPENDITURES	\$7,885,382	\$8,822,028
Salaries and Benefits	\$3,327,562	\$3,946,483
% of Total Expenditures	42.20%	44.73%
Purchased Services	\$1,176,969	\$1,672,675
% of Total Expenditures	14.93%	18.96%
All Other Expenditures	\$3,380,851	\$3,202,870
% of Total Expenditures	42.87%	36.31%
TOTAL NET ASSETS	\$2,553,220 ¹	\$1,985,331
INVESTMENT IN CAPITAL ASSETS	\$25,970	\$16,776
¹ Includes a restatement of the FY 2011 beginning net asset balance of \$617,410 due to various reasons, including removal of a transfer and excess liabilities, as well as the recording of an interfund receivable. Percentages may not add due to rounding.		

REGIONAL SUPERINTENDENT
During Audit Period: Honorable Roycealee Wood
Currently: Honorable Roycealee Wood

FINDINGS, CONCLUSIONS, AND
RECOMMENDATIONS

**CONTROLS OVER FINANCIAL STATEMENT
PREPARATION**

The Regional Office of Education #34 did not have sufficient internal controls over the financial reporting process.

The Regional Office of Education #34 is required to maintain a system of controls over the preparation of financial statements in accordance with generally accepted accounting principles (GAAP). The Regional Office's internal controls over GAAP financial reporting should include adequately trained personnel with the knowledge and expertise to prepare and/or thoroughly review GAAP based financial statements to ensure that they are free of material misstatements and include all disclosures as required by the Governmental Accounting Standards Board (GASB).

The Regional Office of Education #34 did not have sufficient internal controls over the financial reporting process. The Regional Office maintains their accounting records on the cash basis of accounting. While the Regional Office maintains controls over the processing of most accounting transactions, there are not sufficient controls over the preparation of the GAAP based financial statements for management or employees in the normal course of performing their assigned functions to prevent or detect and correct financial statement misstatements and disclosure omissions in a timely manner.

In their review of the Regional Office's accounting records, auditors noted numerous adjustments were required to present financial statements in accordance with generally accepted accounting principles.

The Regional Office of Education #34 did not have proper controls in place over the preparation of financial statements to ensure that they are presented in accordance with generally accepted accounting principles. (Finding 11-1, pages 13-14)

The auditors recommended that, as part of its internal control over the preparation of financial statements, including disclosures, the Regional Office of Education #34 should implement a comprehensive preparation and/or review procedure to ensure that the financial statements, including disclosures, are complete and accurate. Such procedures should be performed by a properly trained individual(s) possessing a thorough understanding of applicable generally accepted accounting principles, GASB pronouncements, and knowledge of the Regional Office of Education #34's activities and operations.

The Regional Office of Education #34 responded that it agrees with the finding and will continue to implement comprehensive preparation and review procedures to insure that financial statements including disclosures are complete and accurate. The Regional Office noted that included in the corrective activities are contracting with a private Certified Public Accountant firm to provide independent review, consulting services and training to Lake ROE finance staff regarding preparation of financial statements (including review for completeness and accuracy). In addition, the Lake ROE has conducted additional training regarding successful use of the Lake ROE's financial management software and has contracted with a part-time business consultant who is reviewing Lake ROE business procedures and controls. Finally, in an effort to streamline preparation of comprehensive financial statements, the Lake ROE has begun consolidating multiple installations of the financial management software into one cohesive system by the end of Fiscal Year 2013.

FAILURE TO APPLY APPROPRIATE ACCOUNTING PRINCIPLES

The Regional Office of Education #34 did not apply appropriate accounting principles.

Generally accepted accounting principles (GAAP) require that a lease be capitalized if any one of the following four criteria is a characteristic of the lease transaction: 1) the lease transfers ownership of the property to the lessee by the end of the lease term, 2) the lease contains bargain purchase options, 3) the lease term is equal to 75% or more of the estimated economic life of the leased property, or 4) the present value of the minimum lease payments at the inception of the lease, excluding executor costs, equals at least 90% of the fair value of the leased property. Capital leases are treated as an acquisition of assets and the incurrence of obligations by the lessee. In addition, sound internal controls require that an inventory of all fixed assets and depreciation schedules for assets meeting the capitalization threshold for reporting be properly maintained.

The Regional Office of Education #34 did not properly record several transactions and, as a result, did not properly apply the appropriate generally accepted accounting principles (GAAP). The Regional Office of Education #34 capitalizes items costing \$5,000 or more. The capitalization of assets and related depreciation expense were recognized in the governmental and business-type activities of the government-wide Statement of Net Assets. Based on review of the schedule of capitalized assets and related depreciation (schedule), auditors noted the following:

- Items costing less than \$5,000 were included in the schedule.

- An item costing more than \$5,000 was not included in the schedule.
- Three of the five capital lease equipment items tested were listed at cost equal to the total lease payments and not at the present value of the lease obligations.
- Two of the five capital lease equipment items were not included in the schedule.

Auditors proposed adjusting entries to record the above transactions in accordance with GAAP.

For monitoring purposes, the Regional Office of Education #34 maintains a fixed asset listing with equipment items costing \$500 and above. The Regional Office of Education #34 did not properly include and exclude items above and below the capitalization threshold of \$5,000 when calculating and recording fixed asset additions and depreciation expense. In addition, the Regional Office of Education #34 did not have personnel with adequate training and knowledge to record capital lease transactions in accordance with GAAP. (Finding 11-2, pages 15-16)

Auditors recommended that the Regional Office of Education #34 should establish procedures to ensure that transactions are properly accounted for and reported in accordance with generally accepted accounting principles. If necessary, accounting and reporting guidance should be obtained from technical resources to be in conformity with GAAP. The fixed asset schedule should also be completed to include all capital lease items, and only capital assets above the capitalization threshold.

The Regional Office responded that it agrees with the finding and will post recommended adjusting entries to record transactions in accordance with GAAP. The Regional Office noted that in addition, previous adjustments made to the fixed assets/inventory schedule and reporting procedures will be further reviewed and refined as a part of a recently contracted business consultant's scope of work. The ROE also noted that this review and refinement will be accompanied by desk-side training of staff involved with fixed assets/inventory schedules and/or calculation of depreciation schedules.

INADEQUATE CONTROLS OVER PURCHASED SERVICES EXPENDITURES

The Regional Office of Education #34 did not have adequate controls over purchased services expenditures.

Good internal controls require that all contracts be executed prior to services being performed and payments being made to contractors. In addition, the Regional Office of Education #34 is responsible for ensuring that contractors maintain

documentation of the hours worked and services provided under the contract.

During their review of expenditures, auditors noted that for 1 of 6 contracts selected for testing, the Educational Services Division (ESD) was unable to provide a signed contract that covered the period selected for testing. In addition, for 1 of 6 contracts selected for testing, the Regional Office of Education #34 did not maintain documentation to support the hours worked and services provided. The amount paid totaled \$35,584 and was paid from local funding. The contract was executed with the Assistant Regional Superintendent under a consultant agreement to act as the Executive Director for the Regional Office of Education #34's blended component unit, Education Services Division (ESD). The ESD is responsible for providing a variety of in-service training and staff development opportunities to improve the knowledge and skills of educators, and for serving as the primary regional delivery system for State and federal grant supported programs and services in education. The Regional Office of Education #34 is the administrative and fiscal agent for the ESD.

Failure to maintain contracts or documentation of the hours worked and the services provided, may result in services being provided that are inconsistent with program goals and activities, inadequate protection of the Regional Office of Education #34's interests, and unallowed costs charged to programs.

Proper controls have not been established to ensure that all contractual payments are supported by signed contracts and that documentation of hours worked and services provided are maintained. (Finding 11-3, pages 17-18) **This finding was first reported in 2008.**

The auditors recommended that the Regional Office of Education #34 should establish procedures to ensure all program costs are sufficiently documented and adequately supported. Auditors noted that all consultant agreements should be supported by a current written contract with detailed scope of services and rates of compensation. The ROE #34 should also maintain documentation to support hours worked and the services provided.

The Regional Office of Education #34 responded that it agrees with the finding and will refine internal procedures to ensure all consultant agreements are supported by a current, timely written contract with scope of services and rates of compensation. The ROE noted that it has developed a system to document and generate supporting materials to track hours worked and services provided. (For previous Regional Office response, see Digest Footnote #1.)

INADEQUATE INTERNAL CONTROLS OVER CASH

The Regional Office of Education #34 did not have adequate internal controls over cash.

Adequate internal controls over cash require that all cash in the custody of the Regional Office of Education #34 be recorded in the general ledger and that each month's bank statement be reconciled to the related general ledger account balances.

The Regional Office of Education #34's Educational Services Division (ESD) was not performing monthly bank reconciliations appropriately. Auditors noted that the ESD's ending adjusted general ledger balance for their operating cash account was not properly reconciled to the bank account as of June 30, 2011. Material transactions were not included in the original trial balance received by the auditors. Subsequent to auditors' inquiry of the material cash variance, the ESD reviewed their general ledger accounts, recorded transactions previously unrecorded in the general ledger, and reconciled their cash account.

Lack of appropriately reconciled monthly bank statements could result in unintentional or intentional errors or fraud, where the errors or fraud could be material to the financial statements and may not be detected and corrected in a timely manner by employees in the normal course of performing their assigned duties.

The Regional Office of Education #34 has inadequate internal controls in place to ensure that bank statements are reconciled to the related general ledger cash accounts and that all activity occurring during the year is actually recorded. (Finding 11-4, pages 19-20)

The auditors recommended that the Regional Office of Education #34's management should review and document in writing that each of their bank accounts reconcile to their related general ledger account balances on a monthly basis. Reconciliations should be completed in a timely manner and management should ensure that all reconciling items are reviewed with the appropriate follow-up. The bookkeepers should reconcile all activity that takes place in the account and track reconciling items to ensure proper treatment.

The Regional Office of Education #34 responded that it agrees with the finding and has re-instated a system of reconciling all bank accounts to the related general ledger on a regular and recurring (monthly) basis. The Regional Office noted that as a result of independent review by a contracted Business Consultant, internal control procedures are being developed to ensure reconciliations are completed in a timely manner. These procedures include redundant reviews and management will ensure that all reconciling items are reviewed with the appropriate follow-up. The ROE also noted that bookkeepers

are tasked to reconcile all activity that takes place in the accounts and track reconciling items to ensure proper treatment.

INADEQUATE INTERNAL CONTROLS OVER REPORTING AND INACCURATE EXPENDITURE REPORTS

The Regional Office of Education #34 did not have adequate internal controls over reporting or accurate expenditure reports.

Good business practices dictate that proper internal controls, such as management review and approval of expenditure reports submitted to granting agencies, should be in place. Amounts submitted on grant expenditure reports should be in agreement and reconcile with the general ledger.

The Regional Office of Education #34 did not have adequate controls in place to ensure amounts submitted on grant expenditure reports are in agreement and reconcile with the general ledger. Auditors, during their review of expenditure reports, noted the following:

- The expenditure report submitted for June 30, 2011, for the ROE/ISC Operations grant, which was received from the Illinois State Board of Education, was inaccurately reported. The Regional Office of Education #34 reported budgeted amounts as expenditures on their report. When compared to the expenditures recorded in the general ledger, most categories were under reported while the purchased services category was over reported by \$10,778. In total, actual expenditures recorded were in excess of the total amount reported.
- The expenditure report submitted for June 30, 2011, for the Beginning Teacher Induction Pilot Program grant, which was received from the Illinois State Board of Education, was inaccurately reported. The Regional Office of Education #34 reported budgeted amounts as expenditures on their report. When compared to the expenditures recorded in the general ledger, most categories were over reported while the purchased services category was under reported by \$330. In total, actual expenditures recorded were less than the amount reported by \$10,670.
- The expenditure report submitted for June 30, 2011, for the McKinney Education for Homeless Education grant, which was received from Will County Regional Office of Education #56, was inaccurately reported. When compared to the expenditures recorded in the general ledger, all categories were inaccurately reported. This was due to reclassifications made in the general ledger and not including expenditures for

the entire fiscal year. In total, actual expenditures recorded were in excess of the amounts reported.

The Regional Office of Education #34 has inadequate internal controls in place to ensure that expenditure reports submitted to granting agencies agree and reconcile to the general ledger. Therefore, expenditure reports submitted did not agree and reconcile with amounts reported in the general ledger. (Finding 11-5, pages 21-22)

The auditors recommended that the Regional Office of Education #34's management should review expenditure reports and supporting documentation prior to submission to granting agencies to ensure that expenditures were actually incurred, allowable, and properly classified. Supporting expenditure documentation and indication of management's review should be included with a copy of the report and available for subsequent internal and external review and analysis. In addition, Regional Office of Education #34 should contact the Illinois State Board of Education to determine the need to amend its expenditure reports.

The Regional Office of Education #34 responded that it agrees with the finding. The Regional Office noted that year-end errors in expenditure reports were due to loss of critical expertise in expenditure report preparation, inexperience in both preparing and reviewing staff members regarding expenditure reports, and failures to reconcile (with documentation) expenditures to budgeted categories and amounts. The ROE noted that as a result, management controls have been put in place to ensure full supporting documentation is available for all expenditure reports and that expenditures align with budgeted categories. The ROE will contact the Illinois State Board of Education to determine whether the need exists to amend the expenditure reports.

INADEQUATE DOCUMENTATION FOR PAYROLL EXPENDITURES

The Regional Office of Education #34 did not have adequate documentation for payroll expenditures.

Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, established principles and standards for determining costs for federal awards carried out through grants, cost reimbursement contracts, and other agreements with State and local governments and federally recognized Indian tribal governments. To be allowable under federal awards, costs must meet certain general criteria. Those criteria, among other things, require that expenditures must be allocable, reasonable, and supported by adequate documentation.

Part 4 of the OMB Circular A-133 Compliance Supplement prescribes that employee time and effort distribution records

must be maintained to document the portion of time and effort dedicated to the single cost objective and each program or other cost objective supported by non-consolidated Federal funds or other revenue sources.

During review of payroll expenditures, auditors noted the following:

- Salaries and benefits for salaried employees assigned on multiple programs were allocated and charged to the programs based on budgets. No time allocation sheets or time and effort reports were prepared to account for actual time charged by program.
- Employees who worked solely on federal grant programs did not prepare the required semi-annual certification stating that they had worked full time on those programs.

Failure to prepare time allocation sheets did not provide a sufficient basis for the allocation of actual payroll charges incurred by program, which may result in a program being over or under charged for salary and benefits. Also, noncompliance with the Allowable Costs/Cost Principles of the Circular A-133 Compliance Supplement may result in the federal funds being expended for unallowable purposes. (Finding 11-6, pages 23-26)

Auditors recommended that the Regional Office of Education #34 should develop and implement adequate policies and procedures to ensure compliance with the Allowable Costs/Cost Principles of the OMB Circular A-133 Compliance Supplement and Cost Principles of OMB Circular A-87 for Compensation for Personnel Services. These policies and procedures should include requiring staff involved in multiple programs to submit time sheets by program or time and effort reports by program. The Regional Office should also establish a payroll cost allocation procedure that allows for computation and comparison of actual time charged with budgeted or pre-determined allocation rates on a regular basis. Payroll charges by program should be based on the time devoted and identified specifically to the performance of those programs.

The Regional Office of Education #34 responded that it agrees with the finding. While the ROE had begun implementation of corrective action regarding this repeat finding, the corrective actions did not encompass all the requirements of OMB Circular A-87. The Regional Office has developed and implemented time and effort accounting policies and procedures to ensure compliance with the Allowable Costs/Cost Principles of the OMB Circular A-133 Compliance Supplement and Cost Principles of OMB Circular A-87 for Compensation for Personnel Services. These policies and

procedures require staff involved in multiple programs to submit time sheets by program or time and effort reports by program. The ROE will also establish a payroll cost allocation procedure that allows for computation and comparison of actual time charged with budgeted or pre-determined allocation rates on a regular basis. Payroll charges by program will be reviewed based on the time devoted and will be identified specifically to the performance of the applicable programs. Additionally, semi-annual certifications for employees who work solely on federal grant programs stating that they had worked full time on those programs are now being prepared.

INADEQUATE DOCUMENTATION FOR EXPENDITURE REPORTS

The Regional Office of Education #34 did not have adequate documentation for expenditure reports.

Amounts submitted on grant expenditure reports to the Illinois State Board of Education and to Will County Regional Office of Education #56 should be in agreement with the general ledger.

The Regional Office of Education #34 did not report expenditures in agreement with the general ledger. The total amount reported was overstated on the ARRA Title I-School Improvement & Accountability grant program final expenditure report by \$21,545. The total amount reported was overstated on the Title I-School Improvement & Accountability grant program final expenditure report by \$51,932.

Of the six expenditure reports selected for testing, the Regional Office of Education #34 was unable to provide supporting documentation or reconciliation of amounts reported to the general ledger for four of those reports. The Regional Office of Education #34 has inadequate controls over the reporting process. The Regional Office did not have supporting documents that reconciled the amounts incurred to the amounts reported. (Finding 11-7, pages 28-29)

The auditors recommended that the Regional Office of Education #34's management should review expenditure reports and supporting documentation prior to submission to granting agencies to ensure that expenditures were actually incurred, allowable, and properly classified. Supporting expenditure documentation and indication of management's review should be included with a copy of the report and available for subsequent internal and external review and analysis. In addition, the Regional Office of Education #34 should contact the Illinois State Board of Education and Will County Regional Office of Education #56 to determine the need to amend its expenditure reports.

The Regional Office of Education #34 responded that it agrees with the finding. Year-end errors in expenditure reports were due to loss of critical expertise in expenditure report preparation, inexperience in both preparing and reviewing staff members regarding expenditure reports, and failures to reconcile (with documentation) expenditures to budgeted categories and amounts. As a result, management controls have been put in place to ensure full supporting documentation is available for all expenditure reports and that expenditures align with budgeted categories. In addition, procedures now include comparisons of obligations (where payment has been received) to subsequent expenditures claimed to avoid double payment of an obligation when it becomes an actual expenditure. The ROE will contact the Illinois State Board of Education and the Will County Regional Office of Education (area grant manager) to determine whether the need exists to amend the expenditure reports, return over-payments, or adjust current year/future grant awards to offset the overpayments.

AUDITORS' OPINION

Our auditors state the Regional Office of Education #34's financial statements as of June 30, 2011 are fairly presented in all material respects.



WILLIAM G. HOLLAND
Auditor General

WGH:KJM

AUDITORS ASSIGNED: Winkel, Parker & Foster, CPA PC were our special assistant auditors.

DIGEST FOOTNOTE

#1: Inadequate Controls Over Purchased Services Expenditures

In its prior response in 2010, the Regional Office of Education #34 responded that it agrees with the finding. The Regional Office noted that corrective documents were created in June 2010 for FY2009, FY2010 and FY 2011 contracts. The Regional Office noted that it will continue to follow established procedures to ensure program costs are sufficiently documented and adequately supported. The ROE also noted that all consultant agreements will be supported by a current written contract with detailed scope of services and rates of compensation.