



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

William G. Holland, Auditor General

SUMMARY REPORT DIGEST

REGIONAL OFFICE OF EDUCATION #25
HAMILTON AND JEFFERSON COUNTIES

FINANCIAL AUDIT
For the Year Ended: June 30, 2013

Release Date: May 29, 2014

Summary of Findings:

Total this audit:	6
Total last audit:	10
Repeated from last audit:	6

SYNOPSIS

The Regional Office of Education #25:

- did not have sufficient internal controls over the financial reporting process;
- did not have adequate controls over cash;
- did not have adequate internal controls over payroll;
- did not have adequate internal control over grant compliance;
- did not have adequate internal controls over cash disbursements; and
- had excess working cash in an internal service fund.

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

REGIONAL OFFICE OF EDUCATION #25
HAMILTON AND JEFFERSON COUNTIES

FINANCIAL AUDIT
For The Year Ended June 30, 2013

	FY 2013	FY 2012
TOTAL REVENUES	\$2,302,031	\$2,244,769
Local Sources	\$773,511	\$734,613
% of Total Revenues	33.60%	32.73%
State Sources	\$1,428,061	\$1,361,647
% of Total Revenues	62.03%	60.66%
Federal Sources	\$100,459	\$148,509
% of Total Revenues	4.36%	6.62%
TOTAL EXPENDITURES	\$2,596,137	\$2,246,106
Salaries and Benefits	\$1,763,483	\$1,553,993
% of Total Expenditures	67.93%	69.19%
Purchased Services	\$604,693	\$554,178
% of Total Expenditures	23.29%	24.67%
All Other Expenditures	\$227,961	\$137,935
% of Total Expenditures	8.78%	6.14%
TOTAL NET POSITION	\$399,161	\$693,267
INVESTMENT IN CAPITAL ASSETS	\$710,151 ¹	\$734,439 ¹
¹ Capital asset amounts are not net of related debt which is associated with assets of the Hamilton-Jefferson Educational Services Cooperative. Percentages may not add due to rounding.		

REGIONAL SUPERINTENDENT
During Audit Period: Honorable Ron Daniels Currently: Honorable Ron Daniels

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

CONTROLS OVER FINANCIAL STATEMENT PREPARATION

The Regional Office of Education #25 did not have sufficient internal controls over the financial reporting process.

The Regional Office of Education #25 is required to maintain a system of controls over the preparation of financial statements in accordance with generally accepted accounting principles (GAAP). Regional Office internal controls over GAAP financial reporting should include adequately trained personnel with the knowledge, skills and experience to prepare GAAP based financial statements and include all disclosures as required by the Governmental Accounting Standards Board (GASB).

The Regional Office of Education #25 did not have sufficient internal controls over the financial reporting process. The Regional Office maintains its accounting records on the cash basis of accounting and posts year-end accrual entries for financial statement purposes. The Regional Office did not have sufficient internal controls over the processing of some accounting transactions. There are not sufficient controls over the preparation/review of GAAP based financial statements for management or employees in the normal course of performing their assigned functions to prevent or detect financial statement misstatements and disclosure errors and omissions in a timely manner. Auditors, in their review of the Regional Office's accounting records, noted the following:

- The Regional Office did not have adequate controls over the maintenance of complete records of cash by fund, accounts receivable, capital assets, or deferred revenue.
- The Regional Office did not post prior year audit adjusting entries correctly. This resulted in the Regional Office's ending fund balance from fiscal year 2012 rolling forward to fiscal year 2013 incorrectly.
- Numerous adjustments were required to present financial statements in accordance with generally accepted accounting principles.

According to Regional Office management, the office staff was still learning the policies and procedures and needs additional training in internal controls and GAAP based financial reporting. (Finding 2013-001, pages 11-12) **This finding was first reported in 2007.**

The auditors recommended that, as a part of its internal control over the preparation of financial statements, including disclosures, the Regional Office of Education #25 should implement comprehensive preparation and/or review procedures to ensure 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's activities and operations. Additionally, the Regional Office of Education #25 should design and implement a system of processes and controls that will ensure complete records are maintained and all transactions are properly recorded in the general ledger.

The Regional Office of Education #25 responded that it understands the nature of this finding with the reduced financial support from the state and a small staff. The Regional Office stated that it will continue to provide necessary training of GAAP accounting procedures. With available funding, the Regional Superintendent will attempt to hire an individual or firm to prepare and review the ROE's financial statements. (For previous Regional Office response, see Digest Footnote #1.)

INADEQUATE CONTROLS OVER CASH

The Regional Office of Education #25 did not have adequate controls over cash.

The Regional Office of Education #25 is responsible for the safeguarding of assets and maintaining an adequate system of internal controls over accounting transactions to prevent error or fraud. In addition, bank reconciliations should be performed on a regular basis and all differences between the bank balance and the general ledger balance should be investigated and resolved.

During the audit of the Regional Office of Education #25, auditors noted the following deficiencies related to its internal control over cash:

- The Regional Office of Education did not have an accurate general ledger cash balance for their pooled cash account or an accurate bank reconciliation as of June 30, 2013.
- While it is the policy of the Regional Office that disbursement checks contain dual signatures, this control was not adequate because the bookkeeper maintained custody of a stamp of the Regional Superintendent's signature. The bookkeeper also maintained the books, custody of blank checks, and reconciled the bank accounts.

- The Regional Office used bank debit cards through April 2013. The holders of the debit cards were able to use the debit cards anywhere they were accepted. Because cash is immediately removed from the Regional Office bank account in debit purchases, these transactions were not subject to the Regional Office internal control procedures and unauthorized purchases could be made without recourse by the Regional Office.
- The Regional Office held blank checks at the end of each period in order to maintain the check sequence if a prior period liability was identified after the fact.

According to Regional Office of Education #25 officials:

- When revenue was deposited, an entry was made to credit revenue in one account and debit revenue in another account causing both assets and revenue to be understated by approximately \$6,000.
- By having dual signatures on their checks they were implementing a better internal control system than a single authorized check system provides. They did not consider the lack of segregation of duties or the signature stamp as weaknesses in the control.
- The use of debit cards made purchasing items for the programs it administers easier and they did not consider that the cards could be misused.
- The bookkeeper believed keeping checks in sequence order would make record keeping easier. (Finding 2013-002, pages 13-15)

The auditors recommended that the Regional Office of Education #25 should implement proper controls for the safeguarding of assets and maintain an adequate system of internal controls over accounting transactions to prevent error or fraud.

- Bank reconciliations should be prepared monthly and all differences between the bank balance and the general ledger balance should be investigated and resolved.
- If a signature stamp is considered necessary, it should be secured and maintained by individuals who do not have check signing authority or maintain the books and records of the Regional Office.
- Debit cards should not be used for Regional Office purchases.

- The Regional Office of Education #25 should not hold blank checks and should write checks in number sequence as payments are disbursed.

The Regional Office of Education #25 responded that the signature stamp is now maintained by an individual without signing authority. The signature stamp is rarely used to sign checks. It is used for certification documents. Although all debit card purchases were pre-approved by the Regional Superintendent, a debit card is no longer used and necessary purchases are made using a credit card. The bookkeeper has been directed not to hold checks at the end of a fiscal year.

INTERNAL CONTROLS OVER PAYROLL

The Regional Office of Education #25 did not have adequate internal controls over payroll.

The *Regional Office of Education (ROE) Accounting Manual* (Section XIV) general policies concerning payroll procedures states that a master record should be maintained on each employee or contractor for federal and State reporting purposes. The master payroll record should contain at least the following: employee name, social security number, address, date of hire, rate of pay, and terms of contract/agreement.

In addition, the *ROE Accounting Manual* (Section XIV) states all payroll costs should be supported by time and effort attendance records (prepared at least monthly and signed by the employee) that account for the total activity for which each employee is compensated. Only actual payroll costs supported by time sheets should be charged to each Source of Funds.

During the course of the audit, auditors noted that certain employees' assigned functions included tasks for various programs, but their salaries and benefits were not allocated based on actual time and effort spent on those programs.

Auditors tested thirty-six (36) employees and forty (40) payroll transactions, covering nineteen (19) payroll periods, and noted the following exceptions:

- In three (3) of the forty (40) (8%) transactions tested, there was no pay rate schedule information maintained by the bookkeeper.
- In sixteen (16) of the forty (40) (40%) transactions tested, adequate time and effort sheets were not maintained.
- In two (2) of the thirty-six (36) (5.5%) employees tested, the amount paid to the employee differed from the approved contract amount. No indication of extra work was documented.

- In four (4) of the nineteen (19) (21%) direct deposit payroll periods tested, a final direct deposit transmittal was not approved by either the Regional Superintendent or Assistant Regional Superintendent.

The Regional Office did not document when terms or pay amount changes were made to employee contracts or update the pay schedules to reflect those changes. The Regional Office believed that by documenting that an employee worked on various programs each day, rather than the number of hours worked, there was sufficient support to allocate time and effort across funds. The bookkeeper indicated that she sometimes did not print the final direct deposit transmittal for review and approval. (Finding 2013-003, pages 16-17) **This finding was first reported in 2011.**

The auditors recommended that the Regional Office of Education #25 should implement proper controls over payroll, including properly documenting any changes to salary, job title and/or job duties and responsibilities. Each change should be clearly described and approved by the Regional Superintendent on an employee contract and updated on the bookkeeper's pay schedule. Auditors also recommended that time and effort sheets should be completed and maintained and the Regional Superintendent should approve payroll only after proper fund allocation has been determined. The Regional Superintendent should also review and approve direct deposit confirmation reports to ensure that accurate payroll has been disbursed.

The Regional Office of Education #25 responded that the Regional Superintendent always approves any salary or job changes. Extra duties or responsibilities assigned and paid will be more clearly documented in the employee's personnel file and on the bookkeeper's pay schedule. The Regional Office will work with auditors to understand the exact style and type of time and effort sheet that should be kept for employees paid out of multiple accounts. (For previous Regional Office response, see Digest Footnote #2.)

INTERNAL CONTROL OVER GRANT COMPLIANCE

The Regional Office of Education #25 did not have adequate internal control over grant compliance.

As a recipient of federal, State, and local funds from various grantor agencies, the Regional Office must incorporate certain procedures into their operations in order to comply with the grant agreements with these entities. The Regional Office is responsible for establishing and maintaining an internal control system over the completion of timely quarterly expenditure reports required for grants administered by the Illinois State Board of Education.

In addition, grant agreements require the Regional Office to report actual expenditures incurred rather than reporting expenditures based on the amount budgeted in the grant

agreement. The Regional Office is required to spend funding in accordance with budgets submitted to grantors.

Auditors noted the following related to the controls over grant compliance:

- The Regional Office did not document the time and effort of employees that work for or were paid from multiple grants (Finding 2013-003) so that salary can be allocated to the grants based on actual costs.
- The final expenditure reports for the Truants Alternative/Optional Education and Regional Safe Schools grant were both submitted to the Illinois State Board of Education 12 days late.

The Regional Office of Education #25 believed that by documenting that an employee worked on various programs each day, rather than the number of hours worked, there was sufficient support to allocate time and effort across funds. The Regional Office did not have an internal control system in place to ensure timely expenditure reports were filed to the Illinois State Board of Education. (Findings 2013-004, pages 18-19)

The auditors recommended that the Regional Office of Education #25 should formally document time and effort spent on each grant for employees paid from multiple grant sources and allocate actual costs to each grant accordingly. The Regional Office should implement an internal control system to ensure that timely expenditure reports are filed with the Illinois State Board of Education.

The Regional Office of Education #25 responded that time and effort sheets are kept for all employees. The Regional Office stated that salary allotted from each grant is based on funds available and cannot always be determined by the hours worked on a particular grant since needs fluctuate each school year. The ROE noted that the bookkeeper will file final expenditure reports in a timely manner.

INTERNAL CONTROLS OVER CASH DISBURSEMENTS

The *Regional Office of Education (ROE) Accounting Manual* (Foreword) establishes that the Regional Superintendent of Schools is responsible for establishing and maintaining an internal control system that provides reasonable assurance about the reliability of its GAAP financial statements, operational compliance with legal and contractual provisions, safeguarding of assets, and effectiveness and efficiency of ROE operations.

The Regional Office of Education #25 did not have adequate internal controls over cash disbursements.

Regional Office of Education #25 policies and procedures indicate that all cash disbursements, other than those for payment on regular monthly utilities, would be initiated through the preparation of a purchase order. The purchase order would be later matched to the invoice and then subsequently entered into the general ledger for payment.

During detail testing of cash disbursements, auditors selected sixty-four (64) individual check disbursements, and twenty-five (25) debit card and twenty-two (22) credit card transactions, and noted the following exceptions:

- In 1 of the sixty-four (64) (2%) check disbursements tested, the payment was greater than the amount approved by the purchase order.
- In twelve (12) of twenty-three (23) (52%) disbursements requiring purchase orders, no purchase order was prepared.
- In five (5) of the twenty-five (25) (20%) debit card disbursements tested, the purchase order and/or invoice did not contain a general ledger account number.
- In all of the twenty-two (22) (100%) credit card transactions tested, no purchase order was present.

The Regional Office of Education #25 did not have adequate procedures for internal control over cash disbursements. (Finding 2013-005, pages 20-21) **This finding was first reported in 2011.**

The auditors recommended that the Regional Office of Education #25's management should ensure the Regional Office designs and implements an adequate system of internal controls over cash disbursements to prevent errors and fraud. All disbursements made by the Regional Office should be supported by sufficient documentation and should be recorded in the correct fund.

The Regional Office of Education #25 responded that the Regional Superintendent will implement tighter control over cash disbursements by assigning a second staff member to review disbursement statements and fund allocations. Purchase orders will be prepared for all disbursements that require them. (For previous Regional Office response, see Digest Footnote #3.)

EXCESS WORKING CASH IN INTERNAL SERVICE FUND

The Regional Office of Education #25 had excess working cash in an internal service fund.

Internal Service Funds are used to account for the Regional Office of Education #25's administrative services, which are provided to many of the Regional Office's funds. Revenue is generated through charges to other funds using inter-fund billings. Regulations set forth by *OMB Circular A-87 (Revised 5/10/04)* require charges by an internal service activity to provide for the establishment and maintenance of a reasonable level of working capital reserve. In addition, the full recovery of costs is allowable. A working capital reserve of up to 60 days cash expenses for normal operating purposes is considered reasonable. A working capital reserve exceeding 60 days may be maintained for exceptional cases; however, it requires approval of the cognizant Federal agency.

Over the last two years, average annual expenses within the Workers' Compensation Fund, an Internal Service Fund, was \$7,355.64. Workers' Compensation Fund cash at June 30, 2013 totaled \$88,664.30, representing approximately 4,400 days of average expenses.

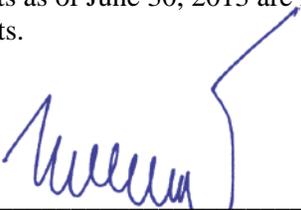
The Regional Office of Education #25's prior years' indirect cost rates were too high, as the calculations included funding for future expenditures. (Finding 2013-006, pages 22-23)
This finding was first reported in 2009.

The auditors recommended that the Regional Office of Education #25 should examine and adjust the indirect cost rate as needed and provide credits to the individual programs overcharged in prior years.

The Regional Office of Education #25 responded that the Regional Superintendent understands the finding that indirect cash charged to the Workers' Compensation Fund was not reduced enough and has since stopped paying any funds into this account until it has been reduced properly. (For previous Regional Office response, see Digest Footnote #4.)

AUDITORS' OPINION

Our auditors state the Regional Office of Education #25's financial statements as of June 30, 2013 are fairly presented in all material respects.



WILLIAM G. HOLLAND
Auditor General

WGH:KJM

AUDITORS ASSIGNED: West & Company, LLC were our special assistant auditors.

DIGEST FOOTNOTES

#1: Controls Over Financial Statement Preparation —Previous Regional Office Response

In its prior response in 2012, the Regional Office of Education #25 responded that it understands the nature of this finding and realizes that this circumstance is not unusual in an organization of this size. The transition to the office without any prior knowledge of the office practices and a part-time bookkeeper for half of the year led to several mistakes. The Regional Office stated that now that a full time trained bookkeeper has been hired, the ROE is implementing procedures and controls that ensure all records are maintained and all assets and revenues are recorded in the general ledger, which includes all transactions, deposits, expenses, assets and liabilities.

#2: Internal Controls Over Payroll —Previous Regional Office Response

In its prior response in 2012, the Regional Office of Education #25 responded that during the transition year many adjustments were made to match payroll to the actual funds available to the Regional Office. The ROE noted that it was extremely difficult to determine how much salary could be assigned to different funds when income from different programs was not known. An office policy manual with job titles, duties and responsibilities is being developed. The Regional Office stated that the Regional Superintendent is in the process of implementing proper controls over payroll and any payroll changes that occur during the fiscal year. Time and effort sheets have been implemented with certain staff, along with yearly days worked calendars. The ROE noted that the Regional Superintendent or Assistant Regional Superintendent currently checks and signs off on the payroll register report, direct deposit report and the transmittal confirmation from the bank for the direct deposits. The Regional Office also stated that salaries have been adjusted during the FY 13 year to better match available funding. Job titles, descriptions and responsibilities should all be completed by the end of the fiscal year.

#3: Internal Controls Over Cash Disbursements —Previous Regional Office Response

In its prior response in 2012, the Regional Office of Education #25 responded that the Regional Superintendent will implement closer control over the cash disbursements made and documentation provided by the bookkeeper to ensure adequate procedures are followed and that expenses are recorded in the correct fund.

#4: Excess Working Cash in Internal Service Fund —Previous Regional Office Response

In its prior response in 2012, the Regional Office of Education #25 responded that the Regional Superintendent agrees with this finding that indirect costs are too high and is working to make adjustments accordingly. The ROE stated that it will credit individual accounts and transfer some of the excess for other liabilities. Since the fund balance is extremely large and with a reduced number of employees, during the next fiscal year, the ROE will allocate zero indirect costs to individual accounts.