

Detroit Public Schools
Office of the Auditor General

ACCOUNTABILITY



TRANSPARENCY

Review of the Corrective Action Plans
For the Fiscal Year Ended
June 30, 2013

School Year 2012-13

REPORT NO: OP-13-121

Report Date: June 16, 2014

Background

The Comprehensive Annual Financial Report (CAFR) and Single Audit Act Compliance Report (Single Audit) for Detroit Public Schools' (DPS) was prepared by the REHMANN ROBSON Accounting/Auditing firm, for the Fiscal Year (FY) ended June 30, 2013. The audit identified nine findings. There were 3 financial statement findings and 6 Single Audit Findings. Single Audit findings relate to compliance with federal grant award requirements, allowable cost and cost principal requirements. The Emergency Manager charged the Office of the Auditor General (OAG) with the responsibility of working with appropriate District personnel to facilitate the process for developing sustainable corrective action plans that address and mitigate the audit findings. In addition, the OAG was responsible for reviewing and testing the corrective action plans and reporting any exceptions to the responsible members of management for clarity, resolution and to schedule additional testing when failures occurred.

The types of audit findings disclosed in the CAFR and Single Audit included the following:

- Material weakness (Financial Reporting) - is a significant deficiency, or combination of significant deficiencies, that result in a material noncompliance issue that will not be prevented or detected by the entity's internal control structure.
- Significant deficiency (Financial Reporting) - is a deficiency, or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charges with governance.
- Material weakness in internal control over compliance (Grant Reporting) - is a deficiency, or a combinations of deficiencies in internal control over compliance such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected , on a timely basis.
- Significant deficiency in internal control over compliance (Grant Reporting) - is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in the internal control over compliance, yet important enough to merit attention by those charged with governance.
- Noncompliant - is noncompliant with certain provisions of laws, regulations, contracts, or grant agreements which could have a direct and material effect on the determination of financial statement amounts.

Of the 9 audit findings, 7 were repeat and 2 were new. In addition, 4 of the findings were classified as a material weakness, 3 were classified as a significant deficiency and 2 were classified as noncompliant.

Objective(s)

The objectives of this audit were to determine whether the corrective action plans:

- Fully addressed the audit finding.
- Are practical – Does the corrective action plan make sense to implement.
- Are sustainable – Policy and procedures established, revised, added review or self-testing.

Scope

The OAG auditors reviewed, tested and/or verified corrective actions that were completed by responsible department personnel. The audit review period was from December 10, 2012 through June 15, 2014.

The number of audit findings and respective corrective actions by the responsible department is shown below:

Responsible Department	Quantity of Findings
Accounting and Finance	4
Academics	2
State and Federal Programs	2
Office of Management & Budget (OMB)	1
Total	9

Methodology

We reviewed the audit findings from the external audit for the year ended June 30, 2013 and requested documentation from the auditors to support their findings. Next, we met with responsible District personnel to review and discuss the conditions and recommendations made by the external auditors for each audit finding. We held numerous meetings with District personnel to gain a complete and accurate understanding of the conditions that led to the audit findings and to determine the root cause. The responsible District personnel were charged with developing the corrective action plans.

The Office of Auditor General (OAG) team reviewed the plans and suggested revisions where appropriate to the corrective action plans to ensure they met the established objectives and fully mitigated the risk being addressed. We also reviewed revised policies and procedures and any process changes that were developed to address the audit findings. The team verified or tested the corrective actions to determine if they were designed and operating as intended. All test failures were reported to the applicable department head and department personnel responsible for the activity under review.

EXECUTIVE SUMMARY

The number of audit findings reported for the Year Ended June 30, 2013 declined from 18 to 9 for a 50 percent reduction compared to the prior year. The decline in the number of audit findings from the prior year represents an improvement in the level of compliance throughout the District. The improvement is attributable to a number of factors including training on best practices for the financial managers and staff, working with external auditors throughout the year and the ongoing review and testing of corrective actions put in place to mitigate audit risks.

Despite these efforts, the District's ability to fully address the risks that led to this year's audit findings was challenged in two areas; the District's budget process and income verification and in-kind support for the Head Start Program. The District was cited for violations in multiple areas of the budget process. Due to the District's deficit financial position, it will be in violation of the State Uniform Budgeting and Accounting Act until the deficit is eliminated. With the implementation of PeopleSoft 9.2 the OAG believes other budget violations can be adequately addressed. However, the PeopleSoft 9.2 financial module will be implemented after the 2013-2014 fiscal year, therefore, the budget audit finding pertaining to actual expenditures exceeding budgeted expenditures will not be addressed until after the 2014-2015 fiscal year.

Despite added training for administrative staff and managers on acceptable documentation for income verification and input from the OAG team on appropriate in-kind documentation for the Head Start program, the corrective actions for these two findings failed our testing. Management officials for the program believe that their decision based on the grantee's input to accept homelessness and child support as eligible forms of income verification is appropriate. However, we discussed this with the external auditors and were told they were not eligible items in accordance with OMB Circular A-133.

Overall, 6 of the 9 corrective action plans passed our review and testing resulting in a 67 percent pass rate, while 3 corrective action plans failed for a 33 percent fail rate. The pass rate percentage for corrective actions plans that were tested was lower than the previous year's percentage; however, one of the findings is a result of a systemic issue that cannot be addressed until the deficit is eliminated and the other two audit findings related to the Head Start Program represent areas that have been a challenge for the District over the last few years.

Notwithstanding the lower pass rate of corrective actions, the District has made progress by offering financial training to staff and managers and reaching out to external auditors for guidance on accounting treatment for complex transactions. Moreover, the practice of testing corrective actions and holding process owners and department heads accountable has also made them more aware of the importance of strong internal controls. Officials from the U.S. Department of Education and state of Michigan have applauded efforts by the OAG to drive the corrective action process citing it as an effective method in helping to mitigate risks and ensure compliance.

The District is in the process of upgrading PeopleSoft from version 8.4 to 9.2. The upgrade to PeopleSoft 9.2 for Financials and Supply Chain Management (FIN/SCM) is scheduled to be deployed in July 2014. The timing of the deployment of the upgrade for financials, however, represents a major challenge for the year-end closing process.

Finally, reforms to grant administrative requirements, cost principles and audit requirements will change effective December 26, 2014. The purpose of these reforms is to reduce waste, fraud and abuse by limiting allowable costs and strengthening oversight requirements. Any new grants awarded after December 26, 2014 will be governed by the new requirements.

Summary of Results
2013 Audit Findings and Corrective Action Testing

Finding	Department	Audit Finding Title	Test			Finding Type	Financial or Compliance	Repeat	Questioned Costs
			Status						
FS-01	Finance	Payroll Benefits	T	T	T	Material Weakness	F	Yes	
FS-02	Finance	Unearned Revenue	D			Material Weakness	F	New	
FS-03	Finance	Budget	D			Material Weakness	F	Yes	
SA-01	Finance	Payroll Documentation	D	T	T	Material Weakness	F	Yes	\$ 409,093
SA-02	Academics	In-Kind Contributions (Head Start)	T			Significant Deficiency	F	Yes	\$ 81,267
SA-03	Finance	26 Pay Accrual Calculation	D			Noncompliance	F	New	\$ 4,595
SA-04	Academics	Eligibility - Income Verification (Head Start)	T			Noncompliance; Significant Deficiency	C	Yes	
SA-05	State and Federal	1512 Reports	T			Noncompliance; Significant Deficiency	C	Yes	
SA-06	State and Federal	Schools in Need of Improvement	T			Noncompliance	C	Yes	
						Total Questioned Costs			\$ 494,955
6		67%	Passed – complete for the 2013 Fiscal year						
3		33%	Failed testing						
9		100%							
Passed or failed based on Design		D							
Passed or failed based on Testing		T							

Our audit was performed in accordance with U.S. Government Accountability Office, Government Auditing Standards and Institute of Internal Auditors, International Standards for the Professional Practice of Internal Auditing, except as it relates to an external peer review. This report is intended solely for management and should not be used for any other purpose. This restriction is not intended to limit the distribution of the report which is a matter of public record.

A handwritten signature in blue ink, appearing to read 'Odell W. Bailey', is positioned above the printed name.

Odell W. Bailey, CIA
Auditor General
Detroit Public Schools