

California State Auditor

B U R E A U O F S T A T E A U D I T S

California Community Colleges:

While the Chancellor's Office Has Improved Its Administration of the Economic Development Program, It Has Failed To Fully Address All State Auditor Recommendations



November 1997
97500

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November 12, 1997

97500

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

The Bureau of State Audits presents its audit report concerning the California community colleges titled "California Community Colleges: While the Chancellor's Office Has Improved Its Administration of the Economic Development Program, It Has Failed To Fully Address All State Auditor Recommendations." This audit was performed as a follow-up to our January 1996 audit. We reviewed the actions taken by the Chancellor's Office and the Department of Education (department) in response to the recommendations we made in our January 1996 report.

This report concludes that the Chancellor's Office has significantly improved in awarding new grants competitively, has improved its monitoring efforts to ensure that community colleges submit all required reports, and is reviewing the reports it receives. In addition, it imposed stricter subcontracting requirements. However, according to its current plan, the Chancellor's Office will have delayed the use of a competitive process to award seven grants for continuing program initiatives by one year and will allow nine grants to be awarded noncompetitively for periods up to nine years. In addition, according to the Chancellor's Office, because of staffing limits, it cannot implement our recommendation to perform periodic site visits to monitor grantees. As a result, the Chancellor's Office cannot ensure that community colleges report accurate expenditures supported by their accounting records, provide sufficient matching funds as required, or comply with other grant requirements.

Both the Chancellor's Office and the department disagreed with our 1996 recommendation to determine the reasonableness of the payment the Chancellor's Office and the department made to a contractor for the preparation of a Needs Assessment and the State Plan for Vocational Education and have not taken the action we requested. Finally, the Chancellor's Office has not addressed other state auditor's recommendations, while the department is making progress at implementation.

Respectfully submitted,

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Summary



Audit Highlights...

In January 1996, we reported that the Chancellor's Office inadequately controlled its Economic Development Program. In this follow-up audit we found that the Chancellor's Office:

- ***Significantly improved in awarding new grants competitively;***
- ***Completed a plan to award renewal grants competitively; however, the phase-in plan results in an excessively long transition, up to nine years for some grants;***
- ***Improved its monitoring efforts and imposed stricter subcontracting requirements; and,***
- ***Still does not perform periodic site visits to ensure community colleges report accurate expenditures and provide sufficient matching funds as required.***

Results in Brief

In January 1996, the Bureau of State Audits (bureau) issued an audit report on the Economic Development Program, which is administered by the Board of Governors of the California Community Colleges (board) through the Chancellor's Office. Because of the significance of the recommendations made to the Chancellor's Office and the Department of Education (department) in that report, the bureau determined a follow-up audit was warranted.

Our follow-up audit found that the Chancellor's Office has implemented several of our recommendations. It has significantly improved in awarding new grants competitively, has improved its monitoring to ensure that community colleges submit all required reports, and is reviewing the reports it receives. In addition, the Chancellor's Office imposed stricter subcontracting requirements. Finally, we did not see any evidence indicating that the Chancellor's Office is using fiscal agents as contract intermediaries.

The Chancellor's Office has improved some aspects of its administration of the Economic Development Program; nevertheless, potential problems remain. According to its current plan, the Chancellor's Office will have delayed the use of a competitive process to award seven grants for continuing program initiatives by one year and will have awarded nine grants noncompetitively for periods up to nine years. In addition, according to the Chancellor's Office, because of limited staffing, it cannot implement our recommendation to perform periodic site visits to monitor grantees. As a result, the Chancellor's Office cannot ensure that community colleges report accurate expenditures supported by their accounting records, provide sufficient matching funds as required, or comply with other grant requirements.

Further, while the department has improved its controls over contracts and grants, we found two instances where it used California state universities as fiscal agents. Additionally, because it disagreed with our recommendation to determine the

reasonableness of the payments made to a contractor to prepare a Needs Assessment and State Plan for Vocational Education, the department has not taken the action we requested.

Finally, the Chancellor's Office has not implemented the remainder of our recommendations from the original audit, including the recommendation to reduce the grant funds it awards to community colleges by the amount of funds they have remaining from prior grant awards.

Recommendations

We believe the recommendations made in our January 1996 report are critical to the Chancellor's Office's administration of the Economic Development Program and its control of program funds, as well as to the department's contracting practices. Based on previous and current findings, we recommend that the Chancellor's Office do the following:

- Continue its efforts to award new grants on a competitive basis to community colleges with the highest scoring applications.
- Re-examine its plan for competitively awarding renewal grants and review the delays in using a competitive process for some grants.
- Seek avenues to ensure that community colleges report accurate expenditures, provide sufficient matching funds as required, and comply with grant requirements.
- Include in its audit guidelines a requirement for district auditors to determine each district's compliance with the local competitive bidding process regarding subcontracts.
- Consider reducing the grant funds awarded to community colleges by the amount of unspent funds remaining from prior grants.
- Establish limits on travel expenditures and require community colleges to comply with those limits.
- Ensure proper use of grants and contracts.
- Reimburse the State for costs incurred from its inappropriate use of an interjurisdictional exchange contract.

We also recommend that both the Chancellor's Office and the department review the appropriateness of payments made to the contractor for the Needs Assessment and State Plan for Vocational Education.

Finally, we recommend that the department continue its efforts to eliminate the use of fiscal agents.

Agency Comments

The Chancellor's Office agrees with most of our recommendations. However, it does not agree that it should set limits on travel expenditures for community colleges, or reimburse the State for the unnecessary costs incurred from improper use of an interjurisdictional exchange contract. Finally, the Chancellor's Office stated that it believes the amount paid for the Needs Assessment and the State Plan were appropriate; therefore, it does not intend to review payments made to the contractor. The Department of Education stated that it will continue its efforts to improve contract procedures.

Introduction

Background

The Board of Governors of the California Community Colleges (board) was established to provide statewide direction, coordination, and leadership to the community college segment of California higher education. The Legislature appropriates funds to the board for the support of the Chancellor's Office and for various local assistance programs, such as the Economic Development Program. The mission of the Economic Development Program is to advance California's economic growth and competitiveness through quality education and services. To accomplish this, the Chancellor's Office awards grants to various community colleges throughout the State to support their efforts to provide education, training, and technical services to California business and industry.

The Bureau of State Audits (bureau) audited the Chancellor's Office's administration of the Economic Development Program and in January 1996 issued a report titled *"California Community Colleges: The Chancellor's Office Inadequately Controlled Its Economic Development Program and, Along With the Department of Education, Circumvented State Contracting Procedures."* The report concluded that the Chancellor's Office lacks adequate control over this program. Specifically, the Chancellor's Office did not comply with its own procedures for awarding Economic Development grants, and did not ensure that community colleges complied with grant requirements. The report also concluded that the Chancellor's Office and the Department of Education (department) inappropriately circumvented state controls by using fiscal agents to obtain the services of a specific contractor to prepare the Needs Assessment and State Plan for Vocational Education for the years 1994 through 1996.

Furthermore, the Chancellor's Office and the department submitted erroneous and misleading information to the Department of General Services to support requests for approval of contracts and amendments. Finally, by using fiscal agents to pay the contractor, neither the Chancellor's Office nor the department could verify the appropriateness of amounts paid to the contractor.

Our 1996 report included seven recommendations for the Chancellor's Office to improve its administration of the Economic Development Program and its control of the program funds. In addition, the report included four recommendations for the Chancellor's Office and the department to improve their compliance with state contracting procedures.

Scope and Methodology

The purpose of this follow-up audit was to determine the extent to which the Chancellor's Office and the Department of Education (department) have implemented the recommendations included in our January 1996 report. We reviewed the 60-day, 6-month, and 1-year responses prepared by the Chancellor's Office and the department to determine if they have established appropriate policies and procedures to address our recommendations. We also met with the Chancellor's Office and the department staff to update the status of the implementation.

In addition, we reviewed newly established policies and procedures to determine if they resolve the issues raised in our January 1996 audit report. Further, we reviewed the Chancellor's Office's grant selection process for new grants and its implementation plan for awarding renewal grants initially awarded prior to January 1, 1996, to determine whether the Chancellor's Office complies consistently with established procedures. We also reviewed a sample of grant files to determine if the Chancellor's Office is monitoring the receipt of the required reports from community colleges and reviewing the reports it receives. In addition, we reviewed the list of unspent funds for fiscal year 1995-96 grants.

Finally, as part of a state contracting audit completed in July 1997, the bureau reviewed the department's administration of consultant contracts.

Analysis of Recommendations

While the Chancellor's Office Has Improved Its Administration of the Economic Development Program, It Has Failed To Fully Address All State Auditor Recommendations


The Chancellor's Office Is Awarding New Grants Competitively

Our January 1996 report indicated that the Chancellor's Office had not always complied with its own procedures when awarding new grants for the Economic Development Program. Our original report showed that the Chancellor's Office could not prove it had competitively awarded 33 of the 40 new grants. In response to concerns raised during that audit, the Board of Governors of the California Community Colleges (board) in November 1995 adopted a new policy requiring all grants awarded on or after January 1, 1996, to undergo a competitive bidding process, or be assigned through allocation formulas approved by the board. In addition, the new policy requires the Chancellor's Office to seek board approval for any grants that exceed either \$100,000 or three years in duration.


Our follow-up review confirms that the Chancellor's Office has generally complied with the board's current policy for awarding new Economic Development grants. Of 110 grants awarded for fiscal year 1996-97, 47 new grants should have been competitively awarded. Our review revealed that the Chancellor's Office did use a competitive process to award all 47 of these grants.

The remaining 63 are renewal grants for continuing program initiatives. Under the board's new policy, the Chancellor's Office has the discretion to award these grants through a competitive process or continue using a noncompetitive process for an additional three fiscal years. For fiscal year 1996-97, the Chancellor's Office awarded 3 grants through a competitive

process and continued to use a noncompetitive process for the remaining 60. Therefore, it awarded 50 out of 110 grants competitively.



For nine of ten grants tested, the Chancellor's Office followed the board's new policy for evaluating grant applications.



We reviewed the grant selection process for 10 of the 50 competitively awarded grants to determine if the Chancellor's Office followed the board's new policy. In addition to using a competitive process to award grants, the new policy also requires that panels evaluating or scoring grant proposals be selected from more than one division in the Chancellor's Office. These panels may include outside readers, as appropriate, to assure objectivity and prevent conflicts of interest. Of the ten grant applications reviewed, nine had been read and scored by at least two readers from more than one division, including outside readers, and only the highest scoring applications were awarded grants. In addition, proper board approval was obtained for the two grants that exceeded \$100,000.



However, for one grant, the Chancellor's Office could not produce a copy of each reader's scoring sheet or a summary listing of scores. According to the Chancellor's Office, the scoring sheet was probably misfiled. As a result, we verified that a competitive process did take place, but could not verify that only districts with the highest scoring applications received the grant funds.

Some Grants Will Have Been Awarded Noncompetitively for Nine Years

Although the Chancellor's Office has shown significant improvement in complying with its own procedures to award new Economic Development grants through a competitive process, it may not be complying with the board's new policy related to grants that have originally been awarded on a noncompetitive basis prior to January 1, 1996.

As mentioned earlier, the Chancellor's Office has the discretion to award grants for continuing program initiatives on a noncompetitive basis for an additional three fiscal years. These grants must have been initially awarded prior to January 1, 1996, the district's performance must be satisfactory, and funding must be available each year. The new policy also allows the chancellor, in consultation with the board president, to award grants noncompetitively when certain conditions beyond the chancellor's control exist, such as matching fund requirements or the involvement of other agencies in the selection of grantees.

The Chancellor's Office developed a plan to award 60 grants for continuing program initiatives. According to its plan, 21 of the 60 grants are exempt from competitive processes. We consider the exempt status for these grants reasonable because the districts receiving the grants provide for the State's match for federal funds.


The Chancellor's plan to phase in the competitive process results in an excessively long transition for some grants.


The Chancellor's Office plans to award the remaining 39 grants on a competitive basis over a four-year bid cycle because it must balance its staff workload, and allow a transition year for the current grant recipient to close down while the newly awarded district prepares for implementation. While we agree with the Chancellor's Office's plan to award these grants using a competitive process over a period of time, we consider the resulting transition period for some grants excessive. For example, the Chancellor's Office will not competitively award nine grants that it initially awarded as early as fiscal year 1988-89 until fiscal year 1998-99 or later. As a result, the Chancellor's Office will have awarded each of these nine grants to certain districts on a noncompetitive basis for up to nine years. Moreover, because the Chancellor's Office allows an additional transition year, those districts will have received grant funds noncompetitively for ten years.

In addition, the Chancellor's Office will have delayed the use of a competitive process by one year to award seven grants. The board's new policy requires these grants to be awarded on a competitive basis by fiscal year 1999-2000; however, the Chancellor's Office will not do so until fiscal year 2000-01.


The Chancellor's Office Still Does Not Properly Monitor the Economic Development Program Expenditures

The Chancellor's Office has improved its monitoring efforts to ensure that community colleges submit all required quarterly and final reports, and it is reviewing the reports it receives. However, according to the Chancellor's Office, because of limited staffing, it cannot implement our recommendation to perform periodic site visits. As a result, the Chancellor's Office cannot ensure that community colleges report accurate expenditures, provide sufficient matching funds, or comply with other grant requirements.


Our 1996 audit revealed that four of the five community colleges tested did not provide a sufficient amount of matching funds, and for 5 of 12 final reports we reviewed, expenditures reported to the Chancellor's Office did not agree with the respective community college's accounting records. Further,

we found that all five community colleges had exceeded certain budget category limits without obtaining required approval from the Chancellor's Office.

The Chancellor's Office Improved Its Monitoring Efforts



With the creation of a grant and contracts processing unit, the Chancellor now tracks, verifies, and follows up on reports submitted by community colleges.



We noted in our 1996 report that the Chancellor's Office had created a grants and contracts processing unit as part of its fiscal division to process grant awards, and to verify and log quarterly and final fiscal reports submitted by community colleges. The Chancellor's Office has established formal procedures for the unit to track the receipt of reports and to follow up on late reports. In addition, the unit reviews expenditure reports for arithmetical accuracy as well as consistency with the budgeted expenditures. We found that the Chancellor's Office staff are currently following these new procedures.


When applying for an Economic Development grant, each community college must submit a budget summary estimating project expenditures by categories such as instructional salaries, capital outlay, and supplies. In addition, this budget summary identifies the funding source for each category of expenditures. Under the new procedures, when the grants and contracts unit receives an expenditure report, it recalculates the total expenditure and the balance of funds for arithmetic accuracy. If the expenditure report contains mathematical errors, does not identify funding sources, or shows an incorrect amount of grant funds, a unit coordinator contacts the community college to resolve the problem.

The Chancellor's Office has also established procedures for its program specialists in the Vocational Education and Economic Development Division to review the expenditure reports and other program reports, and to contact community colleges to resolve questions and problems identified by their support staff or the grants and contracts coordinators.

However, because these expenditure reports do not include any supporting documentation for the reported expenditures or matching information, these reviews are not sufficient to provide assurance that amounts reported by community colleges are accurate and supported by respective accounting records, or to verify that the community colleges are providing sufficient matching funds, as required.


The Chancellor's Office Still Does Not Perform Periodic Site Visits

The Chancellor's Office has not implemented our recommendation to perform periodic site visits at the districts to review supporting documentation for expenditures and matching information, stating that it does not have sufficient staff. In its initial response to our January 1996 report, the Chancellor's Office noted that it had lost 40 percent of its state-funded staff (over 60 full-time positions) and 47 percent of its state-funded operations budget during the four-year period prior to January 1996. The Chancellor's Office also stated, however, that it would seek additional resources to enable it to monitor and review grant expenditures.




The Chancellor's Office has not requested additional resources to monitor grants despite statements that it had done so.

In its 60-day response, the Chancellor's Office stated that it had prepared a Budget Change Proposal (BCP) for the 1996-97 fiscal year requesting resources to monitor districts' handling of state funds and compliance with grant requirements. In its 6-month response, the Chancellor's Office indicated that the BCP was vetoed by the governor. However, we reviewed all of the 11 BCPs the Chancellor's Office prepared for fiscal year 1996-97 and none specifically address additional resources to monitor the community colleges.



We also reviewed a budget augmentation request prepared by the Chancellor's Office in April 1996 to increase its fiscal year 1996-97 budget. As part of the request, the Chancellor's Office requested an additional \$200,000 to fill three or four positions in areas determined most critical by the board and the chancellor. Again, the request does not specifically address the need to monitor the community colleges for compliance with grant requirements. Instead, it mentioned that, while the agency has been forced to reduce staff, the State has enacted more laws requiring the Chancellor's Office to perform additional functions. The Chancellor's Office cited two examples in the request. Chapter 493, Statutes of 1995, requires the Chancellor's Office to absorb the costs of developing and maintaining a common course numbering system within its existing resources and Chapter 1188, Statutes of 1991, requires the Chancellor's Office to participate in the maintenance of a healthy transfer system that ensures successful transfers of community college students to the University of California or the California State University if academic performances are satisfactory.



If funding to conduct periodic site visits is unavailable, the Chancellor's Office should incorporate tests of expenditure reporting into its guidelines for Economic Development grant audits.



Because the grant monitoring issues identified in our 1996 audit are significant, and because the expenditure reports submitted by community colleges lack supporting documentation, we believe periodic site visits at the districts are warranted. If the Chancellor's Office cannot implement our recommendation without additional staff, it should seek funds specifically for periodic on-site monitoring. If funding is unavailable, the Chancellor's Office should consider incorporating requirements for accurate expenditure reporting and sufficient matching funds into its guidelines for Economic Development grant audits required by new legislation, as explained below.



New Requirements for Subcontracting, Though More Stringent, Do Not Sufficiently Ensure That Community Colleges Select the Most Qualified Vendor

Although Chapter 1057, Statutes of 1996, requires audits to ensure that proper written approval for subcontracting is obtained, it does not require confirmation that a competitive process is used for subcontracting. Additionally, requirements for fiscal year 1997-98 grants are more stringent than earlier ones, but they allow community colleges to follow the rules established by their local governing boards. Furthermore, the Chancellor's Office does not have written procedures requiring project monitors to determine if the community colleges are complying with the rules established by their governing boards.

Our 1996 audit revealed that four of the five community colleges tested failed to obtain required written approval from the Chancellor's Office before entering into subcontracts. In addition, they did not use a competitive process to award any of the 31 subcontracts we reviewed. Consequently, we recommended that the Chancellor's Office require the community colleges to use a competitive process to award subcontracts. As part of the policy it adopted in November 1995, the board now requires community colleges to disclose the intended purpose and amount of subcontracts and to follow competitive bidding processes established by the local district governing boards.


New board policy requires community college grant applications to disclose the identity of any subcontractor and the purpose and amount of the subcontract.


To implement this policy, the Chancellor's Office revised its agreement for all fiscal year 1997-98 grants. The revision requires community colleges to disclose in the grant application the intended purpose and amount of subcontracts, identify the proposed subcontractors, and certify that the subcontractors were selected according to rules established by their district governing board. In addition, the grant agreement requires community colleges to submit a written request indicating compliance with the foregoing requirements, and to obtain approval from the project monitor at the Chancellor's Office before entering into any subsequent subcontracts. Finally, it requires community colleges to include in all subcontracts or subgrants a provision prohibiting any third-tier subcontracts or subgrants without written approval from the project monitor at the Chancellor's Office.

In addition, the recently enacted legislation, requires each community college or district to agree to complete an audit of the funds received as a condition of receiving Economic Development grants and requires the Chancellor's Office to oversee the auditing for the Economic Development Program. Further, this legislation requires the audits to verify compliance with all state laws and regulations concerning subcontracting, including receiving appropriate authorization by the Chancellor's Office. The Chancellor's Office states that these audits will be conducted by private certified public accountants as part of the annual audit each community college is required to submit to the Chancellor's Office, and that it will revise its Contracted District Audit Manual in fall 1997 to include all new program requirements stipulated by this legislation. The Chancellor's Office has notified the community colleges that these requirements will apply for grants awarded after January 1, 1997.

The Chancellor's Office allows community colleges to follow the rules established by their local governing boards; however, it does not perform periodic site visits at districts, or have written procedures that require project monitors to determine if the community colleges are complying with these rules. Because the Chancellor's Office cannot confirm that community colleges are selecting the most qualified vendor at a reasonable cost, when revising its Contracted District Audit Manual, it should include a requirement for district auditors to determine each district's compliance with the local competitive bidding process.

The Chancellor's Office May Not Be Maximizing Economic Development Funds

The Chancellor's Office has still not reduced the amount of grant funds awarded to community colleges by the amount of unspent funds remaining from prior grants.

The Chancellor's Office has not implemented our recommendation to reduce the amount of grant funds it awards to community colleges by the amounts of funds those districts have remaining from prior grant awards. We reported in 1996 that the Chancellor's Office may not be maximizing its use of Economic Development funds because it allowed the grantees additional time to spend the funds rather than recover unspent moneys for other Economic Development initiatives.

The Economic Development grant agreements specify that funds remaining at the end of the grant period may revert to the State. The Chancellor's Office recovers these unspent grant funds either by billing the entity for the remaining balance or by withholding this amount from future apportionments. According to the Chancellor's Office, once these unspent funds revert to a portion of the State's general fund reserved for Proposition 98 programs, they are available for future appropriation through the Budget Act, and the Chancellor's Office can no longer use them for the Economic Development Program.

Five of the 14 grants we reviewed in 1996, had excess funds at the end of the original grant term. Rather than recover the funds, the Chancellor's Office extended the time frame for completion of project activities or allowed for new activities. However, we contend that this policy reduces the incentive for a community college to complete its projects on time and denies other community colleges the opportunity to use the unspent grant funds. We recommended that the Chancellor's Office consider reducing the amount of current-year grant funds by the amount of unspent funds remaining from prior grants.

Grant Extension Policy Reduces Incentive for Completing Projects on Time


As stated above, our follow-up audit reveals that the Chancellor's Office has not reduced the amount awarded to community colleges by the amount of unspent funds remaining from prior grants. For example, in fiscal year 1995-96, it awarded a grant totaling \$492,335 to State Center Community College District (State Center) to fund a Statewide Economic Development Coordination Network (Ed-Net) initiative. Of this amount, \$82,393 remained unspent at June 30, 1996. Rather than reduce the amount of the 1996-97 grant, the Chancellor's

Office extended the original grant term to June 30, 1997, and awarded State Center another grant of \$700,818 for fiscal year 1996-97. Moreover, according to the fourth quarter expenditure report State Center submitted to the Chancellor's Office, State Center had not used \$70,342 (85 percent) of the \$82,393 as of June 30, 1997. This illustrates our point that the policy of granting extensions reduces the incentive for a community college to complete projects on time.


Unspent Funds Appear Excessive for Some Individual Colleges

Rather than continue to grant extensions, the Chancellor's Office can monitor the projects more closely to reduce the amount of unspent funds. During this audit, we reviewed the Chancellor's Office's list of unspent funds for fiscal year 1995-96 grants to determine the amount that remained unspent at the end of the grant term. While the amount of unspent funds for the Economic Development Program as a whole does not appear to be excessive (2.7 percent of the total amount awarded for the grant term ending June 30, 1996), the amount of unspent funds for certain individual grants does. For example, by the end of the grant term, Peralta Community College District had not spent \$45,538 (36 percent) of the \$125,000 awarded for fiscal year 1995-96. According to the Chancellor's Office, the district was unable to promptly fill a director position vacated during fiscal year 1995-96, and the Chancellor's Office expected minimal, if any, unspent funds from the 1996-97 grant. Nevertheless, the district had not spent \$46,689 (37 percent) of the \$125,000 awarded for fiscal year 1996-97 by June 30, 1997.

In another instance, Ventura Community College District had not spent \$17,387 (23 percent) of the \$73,790 grant it received by the end of fiscal year 1995-96. According to the Chancellor's Office, while the district had been searching for a full-time director, the director for this initiative was only employed part-time; thus, the district did not use all of the funds it received. Rather than reduce the amount the district would receive for the next year, the Chancellor's Office awarded Ventura Community College District \$123,790 for its fiscal year 1996-97 grant. As of June 30, 1997, the district had not spent \$71,518 (57 percent) of the \$123,790 awarded. In May 1997, the district requested an extension of the grant term to December 31, 1997, to use the remaining funds for a staff development project because it had not hired a full-time director.


The Chancellor's Office is not adequately monitoring grants to identify excessive amounts of unspent funds.

As we mentioned earlier, the Chancellor's Office has established written procedures requiring its program specialists in the Vocational Education and Economic Development Division to review reports submitted by the community colleges and to contact them regarding identified problem areas. Although these procedures were put in place in 1996, it does not appear that the Chancellor's Office is maximizing the review of these reports and adequately monitoring grants for excessive unspent funds at some individual colleges.


Because the final reports for fiscal year 1996-97 grants were not due until August 31, 1997, after the completion of our fieldwork, we do not know the full amount of unspent funds at the fiscal year end. However, the Chancellor's Office does agree that monitoring unspent funds is important and claims that it will review the information for fiscal year 1996-97 when it becomes available. The Chancellor's Office further stated that if it determines certain recipients continue to have unspent funds from their fiscal year 1996-97 grants, it will consult with its legal counsel regarding the possibility of amending grant agreements for future years to reduce awards to those colleges.

The Chancellor's Office and the Department of Education Have Not Implemented All Recommendations Related to the State Plan



The Chancellor's Office and the department agree to comply with state contracting requirements, and the department has instituted more administrative controls and oversights over its contracting process; however, both entities disagree with our recommendation to determine the appropriateness of payments made to a contractor for the preparation of a Needs Assessment and State Plan for Vocational Education (state plan).

In 1996, we reported that the Chancellor's Office and the department inappropriately circumvented state controls by using fiscal agents to obtain the services of a specific contractor to prepare the 1994-96 state plan. We recommended that the Chancellor's Office and the department discontinue this practice, comply with state requirements for awarding contracts, and submit complete and accurate information to the Department of General Services when requesting contract approval. We also recommended that the Chancellor's Office

and the department determine whether the amounts paid to the contractor for the state plan were appropriate and, if necessary, recover any overpayments.

The Chancellor's Office Has Not Determined if Amounts Paid for the State Plan Were Appropriate

Since our 1996 report, the federal government approved the State's request to extend the state plan an additional two years. As a result, the Chancellor's Office has not yet issued any contracts for preparation of the plan. In its initial response to our recommendations, the Chancellor's Office stated that it would comply with state requirements for awarding contracts and submit complete and accurate information to the Department of General Services when requesting approval of contracts.


Despite our 1996 findings that it may have paid for the same services more than once, the Chancellor's Office is taking no action on this issue.




We did not see any evidence indicating that the Chancellor's Office is using fiscal agents. However, it has not taken any action to determine if the amounts paid to the contractor who prepared the state plan were appropriate. Our 1996 audit revealed that by using fiscal agents to pay the contractor, the Chancellor's Office cannot assure that payments made to the contractor were appropriate and may have paid for the same services more than once.

The Chancellor's Office disagrees with our assessment. In its initial response to our 1996 audit, it states that "[b]oth the products and the invoices were reviewed by the Chancellor's Office," and that "[t]he market survey verifies, at least under the circumstances, that the costs were reasonable." The Chancellor's Office also states that it paid for the product in increments because the contract was for professional services; therefore, neither Chaffey College nor the Chancellor's Office made duplicate payments to the contractor. However, during our 1996 audit, we found no evidence that the invoices were ever received by the Chancellor's Office. Actually, the invoices were submitted directly to the fiscal agent who simply paid the contractor but did not monitor the progress of the work. Because we found inadequate controls over payments and some invoices submitted to the fiscal agents that contained charges for the same services, we still believe the Chancellor's Office should review the payments made to the contractor to determine whether the amounts paid were appropriate.

The Department Improved Its Control Over Contract Reviews but Continues to Use Fiscal Agents

We noted in our 1996 report that the superintendent of public instruction (superintendent) had implemented new policies regarding approval and use of contracts at the department. These new policies include a review of all proposed contracts by the superintendent, requirements for a full explanation and a summary of the work completed to date for contract extensions, and a closer review by the superintendent of sole-source contracts and delayed contracts.

The department has implemented these new policies except that the deputy superintendent of the Department Management Services Branch, who oversees the department's contracts unit, is currently reviewing all the contracts in place of the superintendent. In addition, according to the department, it has further identified and implemented more administrative controls within its High School Division, which administers some vocational education programs, to further support the objectives of administrative oversight, fiscal integrity, and programmatic accountability. These controls include requiring all contracts and grants to be reviewed by both the unit manager and the division director before they are sent to the department's contract office for review, and requiring all invoices to be reviewed by the project monitor, the contracts and grants administrative analyst, and the division director before they are sent to accounting for payment. Our follow-up review determined that the division is performing these reviews for both contracts and invoices.




The High School Division that administers some vocational education programs has improved its process for reviewing and approving contracts and invoices.


Finally, according to the department, it has commissioned a contracts and grants work group and is developing a handbook of contract and grant policies and procedures. In fall 1996, the work group, through training classes and discussion with co-workers, began to disseminate some guidelines to department staff. Further, as of May 1997, the department has completed a section of the handbook on invoicing guidelines. According to the department, it expects to complete the remaining sections in 1998.

In its 60-day, 6-month, and 1-year responses to the bureau, the department did not specifically address our recommendation to discontinue the use of fiscal agents. As part of an audit the bureau recently conducted at five state departments, including the Department of Education, to evaluate compliance with state laws and regulations for fiscal year 1995-96 consultant contracts, we found two instances where the department used

California state universities as fiscal agents. These instances are reported in our July 1997 report titled *“State Contracting: Improvements Are Still Needed To Ensure the Effective Use of Public Resources,”* which concluded that the department misused interagency agreements with the California state universities to circumvent the usual competitive bidding process.

In its initial response to our July 1997 audit report, the department stated that at no time did it intend to circumvent competitive bidding procedures; instead, it intended to take advantage of the valuable source of knowledge at the universities.


The department has taken some actions to discourage the use of fiscal agents.


The department has taken some actions to discourage the use of fiscal agents. For example, in March 1996, the superintendent expressed her concerns about the use of fiscal agents at a department wide meeting. Further, the department’s contracts office, through training classes and in response to staff requests, has recommended avoiding the use of fiscal agents to department staff. In addition, as of October 1997, the department has drafted guidelines on fiscal agents, stating that the use of fiscal agents circumvents the competitive bidding process and violates laws.

The department disagrees with our 1996 recommendation requesting it to verify the amounts paid to the contractor for the state plan and, if necessary, to recover any overpayments. In its initial response to our audit report, the department stated that it had worked closely with the Chancellor’s Office and the contractor throughout the project. As a result, the department felt that it did receive the services it paid for and, absent evidence to the contrary, it believed a new review would not be cost-effective.

The Chancellor’s Office Has Not Addressed Other Recommendations

As shown in the Appendix, the Chancellor’s Office has not acted on the remaining recommendations in our original audit. Specifically, it has not restricted travel costs to state per diem rates, improved its control over proper use of grants, or reimbursed the State for costs of an interjurisdictional exchange contract.

Recommendations

We believe the recommendations made in our January 1996 report are critical to the Chancellor's Office's administration of the Economic Development Program, its control of the program funds, and the department's contracting practices.

Based on previous and current findings, we recommend that the Chancellor's Office continue its effort to comply with its own policy when awarding new Economic Development grants. It should document its grant selection process and re-examine its plan for competitively awarding grants for continuing program initiatives.

In addition, the Chancellor's Office should seek state funds to monitor grants, including funds for performing periodic site visits to review supporting documentation for expenditures and matching information. If funding is unavailable, the Chancellor's Office should consider incorporating grant requirements into its guidelines for audits of Economic Development Program grants.

The Chancellor's Office should also ensure that community colleges award subcontracts to the most qualified vendors at a reasonable cost. It should continue its efforts to monitor community colleges more closely to ensure they complete the projects on time and have minimum, if any, unspent funds by the end of the grant term. For those districts with unspent funds, the Chancellor's Office should consider reducing their future awards by the amount remaining from prior grants.

Finally, it should establish limits on travel expenditures and require community colleges to comply with these limits, ensure proper use of grants and contracts, and reimburse the State for the additional costs tied to an interjurisdictional exchange contract.

We recommend that both the Chancellor's Office and the department review the payments made to the contractor for the state plan to assure that they were appropriate. Finally, we recommend that the department continue its efforts to eliminate the use of fiscal agents.

We conducted this review under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in this report. The information in this report was shared with the Chancellor's Office and the Department of Education, and we considered their comments.

Respectfully submitted,

A handwritten signature in cursive script that reads "Kurt R. Sjoberg".

KURT R. SJOBERG
State Auditor

Date: November 12, 1997

Staff: Elaine M. Howle, CPA, Audit Principal
Young H. Hamilton, CPA
Olivia M. Haug

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Appendix

The Chancellor's Office Has Not Taken Corrective Action on Three State Auditor Recommendations

The Chancellor's Office Should Set Limits on Travel Costs and Ensure That Districts Comply With Those Limits

We found during our prior audit that the Chancellor's Office allowed community colleges to reimburse staff for travel expenditures in accordance with policies adopted by each college's governing board. In some cases, reimbursement was well in excess of the State's rate. We recommended that the Chancellor's Office modify the terms and conditions of the grants to restrict travel costs to state per diem rates and ensure that districts comply with those restrictions.

The Chancellor's Office disagreed with our recommendation and continued to allow community colleges to reimburse travel expenditures in accordance with individual governing board policies. It stated in its initial response to our 1996 report that, because the grants are in the form of local assistance funds to the colleges, it allows districts the same freedom with those funds that they have with other local assistance funds. The Chancellor's Office further stated that since district employees are not state employees, the state reimbursement rates are not legally applicable.

In response to our January 1996 report, the Legislature added Section 15379.28 to the Government Code, which requires, as a condition of receiving Economic Development funds, that each community college district agree to complete an audit of funds received. Although the new law requires the audits to include activities that would ensure compliance with all state laws and regulations concerning travel authorization, it does not require compliance with state travel reimbursement rates.

While we agree that Economic Development grant funds are classified as local assistance funds, because the program utilizes state funds that should be prudently spent, the Chancellor's Office should set limits on travel expenditures and require

community colleges to comply with those limits. In addition, the Chancellor's Office should require each district's auditor to determine compliance.

***Chancellor's Office Procedures
Do Not Always Assure Proper Use
of Grants and Contracts***

Our 1996 audit also disclosed that the Chancellor's Office had inappropriately awarded grants instead of contracts to prepare the Economic Development Program Evaluation and Annual Report (annual report). The Chancellor's Office had the statutory responsibility to submit this annual report to the governor and the Legislature. Its use of grants unnecessarily curtailed competition to produce the annual report, and the grantee received the grant amount at least a year before the work was required to be completed.

At the time of our 1996 audit, the Chancellor's Office had established procedures requiring its Legal Affairs and Contracts Division to review all grants and contracts to assure their proper use. However, because of the exception we noted, we recommended that the Chancellor's Office ensure that it follows those procedures by using contracts rather than grants to award funds when it has the legal or statutory responsibility to perform the activities.

While the Chancellor's Office has established written procedures to require its program staff to submit all project specifications to the Legal Affairs and Contracts Division for review to ensure proper classification of contracts and grants, these written procedures do not require program staff or the Legal Affairs and Contracts Division to maintain a log or a copy of the project specifications reviewed and approved. The Legal Affairs and Contracts Division contracts manager stated that she reviews each project specification to determine if a contract or a grant has been properly used. If yes, she initials the project specification and sends it back to the program division. If not, she forwards the project specification to legal counsel for further review. She does not maintain a log or a copy of the project specifications she has reviewed.

Although we saw evidence that the program division maintained some copies of the project specifications that had been reviewed and initialed by the contracts manager, the file the division maintains is incomplete. For example, the division did not have copies of the project specifications on file for two of the six projects we reviewed, and only one of the four specifications had the contract manager's initials on it.

Therefore, we cannot verify that the Chancellor's Office is complying with its own internal procedures. Without adequate control to ensure that its Legal Affairs and Contracts Division reviews project specifications for all grants and contracts, the Chancellor's Office cannot ensure the proper use of grants and contracts.

The Chancellor's Office Has Not Reimbursed the State for Costs of an Interjurisdictional Exchange Contract

In our 1996 audit, we found that the Chancellor's Office inappropriately used an interjurisdictional exchange contract for employment, thereby incurring additional costs to the State of approximately \$15,500. Specifically, the Chancellor's Office continued to pay its deputy chancellor through an interjurisdictional exchange contract with State Center from July 1991 through June 1994, even though he had been appointed to an exempt position in July 1991. We recommended that the Chancellor's Office reimburse the State for these unnecessary costs.

The Chancellor's Office disagreed with our finding, stating that the interjurisdictional exchange is specifically allowed by law and that it obtained all necessary control approvals for this contract. It also stated that the unnecessary costs cited in our 1996 report, if any, occurred over a period of three years; therefore, the actual additional cost each year, if any, was very small. To date, the Chancellor's Office has not repaid the additional costs, as we recommended. The deputy chancellor has since left the position, and as of September 1997, it remained vacant.

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Response to the report provided as text only

Chancellor's Office
California Community Colleges
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<http://www.cccco.edu>
(916) 445-8752

November 4, 1997

Kurt R. Sjoberg
California State Auditor
600 J Street, Suite 300
Sacramento, California 95814

Subject: Response to Draft Audit Report: California Community Colleges: While the Chancellor's Office Has Improved Its Administration of the Economic Development Program, It Has Failed To Fully Address All State Auditor Recommendations

Dear Mr. Sjoberg:

Thank you for the opportunity to respond to your draft report, "California Community Colleges: While the Chancellor's Office Has Improved Its Administration of the Economic Development Program, It Has Failed To Fully Address All State Auditor Recommendations."

We appreciate your recognition of the many good-faith efforts my office and the Board of Governors have initiated to address concerns raised in your original report of January 1996, and we remain committed to improving our leadership and oversight of this critical program. What follows is our initial response to the recommendations raised in your most recent draft report.

Recommendation:

The Chancellor's Office should continue its efforts to award new grants to community colleges with the highest scoring applications

Response:

As noted in the audit, the Chancellor's Office did award all 47 of the 1996-97 new grants on a competitive basis. This practice will continue. Additionally, readers' score sheets will be placed in the audit file for each competitively awarded grant.

Recommendation:

The Chancellor's Office should re-examine its plan for competitively awarding renewal grants and determine the propriety of delaying the use of a competitive process by one year and allowing grants to be awarded non-competitively for periods up to nine years.

Response:

The Chancellor's Office concurs that the resulting length of transition for the Centers for International Trade grants is excessive. Therefore, the four centers scheduled to be

competitively bid in 1998-99 will be moved forward and new Requests for Applications will be issued during the 1997-98 fiscal year. Likewise, the four centers scheduled to be competitively bid in 1999-2000 will be moved forward and new Requests for Applications will be issued during the 1998-99 fiscal year.

Recommendation:

The Chancellor's Office should seek avenues to ensure that community colleges report accurate expenditures, provide sufficient matching funds as required, and comply with grant requirements.

Response:

The Chancellor's Office has submitted a budget change proposal for additional staff to provide administration and oversight for Economic Development.

Recommendation:

The Chancellor's Office should include in its audit guidelines a requirement for districts' auditors to determine each respective district's compliance with the local competitive bidding process regarding subcontracts.

Response:

In response to the requirements of SB 1809 (Chapter 1057, Statutes of 1996), the Chancellor's Office is revising its Contracted District Audit manual to have the auditors who annually examine the community colleges to review the Economic Development program to ensure compliance with all state laws and regulations concerning each of the following:

- Procedures for subcontracts or grant amendments, including appropriate authorization by the Chancellor's Office,
- Procurement procedures,
- Hiring procedures, and
- Appropriate use of fiscal agents.

In addition, the Chancellor's Office will have the auditors examine expenditure reports and test the information to ensure that the information is accurately reported and properly documented.

Recommendation:

The Chancellor's Office should consider reducing the amount of grant funds awarded to community colleges by the amount of unspent funds remaining from prior grants.

Response:

The Chancellor's Office instituted new procedures during the 1996-97 fiscal year to improve its review of the grantees' expenditure reports submitted on a quarterly basis. These procedures will be strengthened for 1997-98. Additionally, final expenditure reports for 1996-97 continuing grants will be reviewed to determine if funds are not being spent in a timely manner and in accordance with the purposes of the grant agreement. Grant agreements for future years may be amended to reduce the amount of the grant award if review of the project(s) warrants such action. This procedure should prevent the release of excessive funds at the end of the original grant term.

It should be noted, however, that the amount of unspent funds as a whole does not appear to be excessive. Of the total amount awarded to districts during the 1996-97 fiscal year, only 2.7 percent was unspent.

Recommendation:

The Chancellor's Office should set limits on travel expenditures and require community colleges to comply with these limits.

Response:

The Chancellor's Office agrees that the Economic Development grants allow the community colleges to reimburse travel costs at district rates, which, in specific instances, may or may not happen to be in excess of the State rates. These grants, however, are in the form of local assistance funds to the colleges; and, the Chancellor's Office allows districts the same freedom to expend these revenues as they have with other local assistance revenues. Indeed, since district employees are not State employees, the State reimbursement rates are not automatically applicable. Statutes governing the role of the Board of Governors require us to allow for maximum local authority and control in the administration of the community colleges. Absent statutory direction that State rates must be applied with respect to these local assistance grants, we respectfully disagree with the auditor's recommendation on this issue.

①*

*The California State Auditor's comments on this response begin on page 29.

Recommendation:

The Chancellor’s Office should ensure proper use of grants and contracts.

Response:

The Chancellor’s Office requires a review of all Request for Application Specifications by the Legal Affairs/Contracts Division before these are released for competitive bid. This procedure ensures proper classification of contracts and grants.

During fiscal year 1997-98, new procedures will be instituted that will require a sign-off signature by the Legal Affairs/Contracts Division indicating their review and approval of all project specifications. The review and approval forms, before they are released, will be maintained in a file with the individual project specification.

These new procedures should ensure the proper use of grants and contracts.

Recommendation:

The Chancellor’s Office should reimburse the state for the amount of unnecessary costs incurred from its inappropriate use of an interjurisdictional exchange contract.

Response:

As stated in the response to the 1996 audit, the Chancellor’s Office disagreed with this finding. The interjurisdictional exchange is allowed by law and the Chancellor’s Office obtained all necessary control approvals in using this procedure.

Additionally, the Chancellor’s Office respectfully disputes the auditor’s calculation that the “unnecessary costs” of using this procedure were \$15,500. The agreement paid for some of the Deputy Chancellor’s travel that the State would have otherwise been required to reimburse. Finally, the “unnecessary costs” cited in the audit occurred over a period of three years -- meaning that the actual additional cost each year, if any, was much smaller than the \$15,500 total. ②

Recommendation:

We recommend that both the Chancellor’s Office and the department review the payments made to the contractor for the Needs Assessment and the State Plan to assure that they were appropriate.

We recommend that the department (Department of Education) continue its efforts to eliminate the use of fiscal agents.

Response:

As stated in the response to the 1996 audit, the Chancellor’s Office disagrees with this finding. Both the work products and the invoices were reviewed by the Chancellor’s Office. The Chancellor’s Office worked closely with the contractor and the Department ③

of Education throughout the development and completion of the needs assessment and State Plan. The Chancellor's Office believes that the amount paid for both these products were appropriate and reasonable.

My staff and I would be happy to meet with your staff to discuss further any of these issues. Please contact Gary Cook at 327-6222, if you have any questions regarding this response.

Sincerely,

Thomas J. Nussbaum
Chancellor

cc: Rita Cepeda
Patrick Lenz
Gary Cook
Elaine Howle
Barbara Whitney
Chris Willis

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Comments

California State Auditor's Comments on the Response From the Chancellor's Office of the California Community Colleges

To provide clarity and perspective, we are commenting on the Chancellor's Office of the California Community Colleges' response to our audit report. The numbers correspond to the numbers we have placed in the response.

- ① Our current recommendation did not require the Chancellor's Office to restrict travel costs to state per diem rates; however, we did state that the Chancellor's Office should set limits on travel expenditures and require the community colleges to comply with those limits. Furthermore, as stated on page 19 of the Appendix, while we agree that Economic Development grant funds are classified as local assistance funds, we believe that because the program utilizes state funds, these funds should be prudently spent.
- ② As stated in our original report, the Chancellor's Office's General Counsel indicated in a memorandum dated December 12, 1995, that the use of the interjurisdictional exchange contract did result in excess costs of \$15,000.
- ③ As stated on page 13, our 1996 audit found no evidence that the invoices were ever received by the Chancellor's Office. Actually, the invoices were submitted directly to the fiscal agent who simply paid the contractor but was not involved in monitoring the progress of the work. Consequently, we still believe the Chancellor's Office should review the payments made to the contractor to determine whether the amounts paid were appropriate.

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Response to the report provided as text only

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November 4, 1997

Kurt R. Sjoberg
California State Auditor
660 J Street, Suite 300
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97500

Dear Mr. Sjoberg:

Thank you for the opportunity to review and comment on your draft audit report titled, "California Community Colleges: While the Chancellor's Office Has Improved Its Administration of the Economic Development Program, It Has Failed To Fully Address All State Auditor Recommendations." We appreciate your recognition of the many steps we have taken in the past two-and-a-half years to strengthen procedures for approval and use of contracts, to improve controls over the vocational student organizations, and to eliminate the use of fiscal agents.

The California Department of Education (CDE) will continue our efforts to improve contract procedures. We look forward to the completion of the contracts and grants handbook next year.

If you have questions about the CDE's response, please contact our Audit Response Coordinator, Peggy Peters, at (916) 657-4440.

Sincerely,

Delaine Eastin
State Superintendent of Public Instruction

DE:map

cc: Members of the Legislature
Office of the Lieutenant Governor
Attorney General
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps