



# Implementation of State Auditor's Recommendations

Audits Released in January 2006 Through December 2007

Special Report to  
*Assembly Budget Subcommittee #2—Education Finance*

February 2008 Report 2008-406 A2



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February 21, 2008

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The Governor of California  
Members of the Legislature  
State Capitol  
Sacramento, California 95814

Dear Governor and Legislative Leaders:

The Bureau of State Audits presents its special report for the Assembly Budget Subcommittee No. 2—Education Finance. This report summarizes the audits and investigations we issued during the previous two years that are within this subcommittee's purview. This report includes the major findings and recommendations, along with the corrective actions auditees reportedly have taken to implement our recommendations.

This information is also available in a special report that is organized by policy areas that generally correspond to the Assembly and Senate standing committees. This special policy area report includes an appendix that identifies monetary benefits that auditees could realize if they implemented our recommendations, and is available on our Web site at [www.bsa.ca.gov](http://www.bsa.ca.gov). Finally, we notify auditees of the release of these special reports.

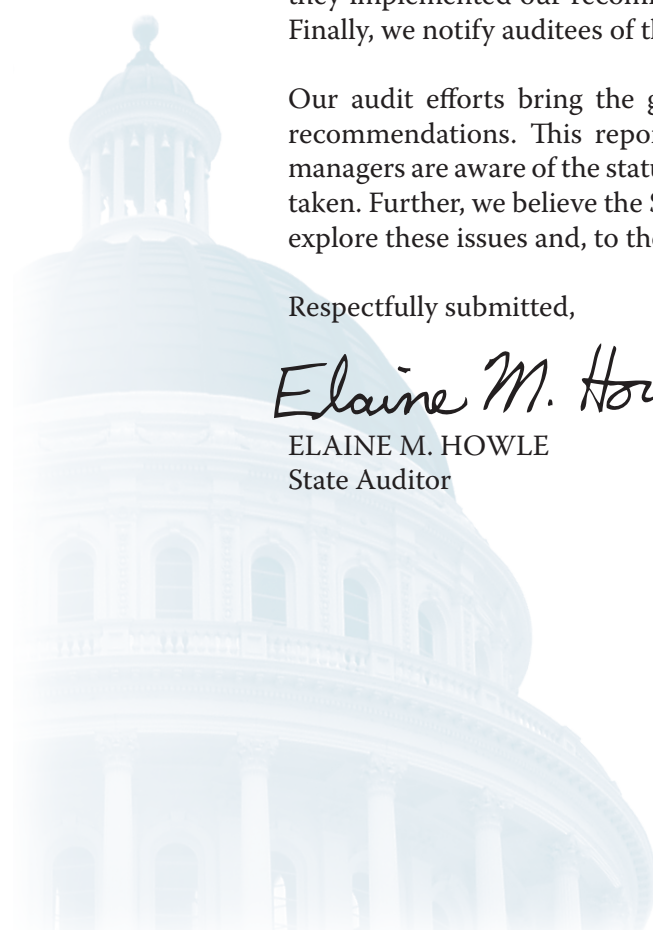
Our audit efforts bring the greatest returns when the auditee acts upon our findings and recommendations. This report is one vehicle to ensure that the State's policy makers and managers are aware of the status of corrective action agencies and departments report they have taken. Further, we believe the State's budget process is a good opportunity for the Legislature to explore these issues and, to the extent necessary, reinforce the need for corrective action.

Respectfully submitted,



*Elaine M. Howle*

ELAINE M. HOWLE  
State Auditor



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## Introduction

This report summarizes the major findings and recommendations from audit and investigative reports we issued from January 2006 through December 2007, that relate to agencies and departments under the purview of the Assembly Budget Subcommittee No. 2—Education Finance. The purpose of this report is to identify what actions, if any, these auditees have taken in response to our findings and recommendations. We have placed this symbol ➡ in the margin of the auditee action to identify areas of concern or issues that we believe an auditee has not adequately addressed.

For this report, we have relied upon periodic written responses prepared by auditees to determine whether corrective action has been taken. The Bureau of State Audits' (bureau) policy requests that the auditee provides a written response to the audit findings and recommendations before the audit report is initially issued publicly. As a follow-up, we request the auditee to respond at least three times subsequently: at 60 days, six months, and one year after the public release of the audit report. However, we may request an auditee to provide a response beyond one year or we may initiate a follow-up audit if deemed necessary.

We report all instances of substantiated improper governmental activities resulting from our investigative activities to the cognizant state department for corrective action. These departments are required to report the status of their corrective actions every 30 days until all such actions are complete.

Unless otherwise noted, we have not performed any type of review or validation of the corrective actions reported by the auditees. All corrective actions noted in this report were based on responses received by our office as of January 2008.

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# California State University

## It Is Inconsistent in Considering Diversity When Hiring Professors, Management Personnel, Presidents, and System Executives

REPORT NUMBER 2007-102.2, DECEMBER 2007

### *California State University's response as of November 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits review the California State University's (university) practices for hiring to determine how it ensures that faculty and executives reflect the gender and ethnicity of the university they serve, the State, and the academic marketplace.<sup>1</sup> As part of our audit, we were asked to determine how the university develops hiring goals and how it monitors progress in meeting those goals. In addition, we were to gather and review the university's statistics on its hiring practices and results over the last five years and, to the extent possible, present the data collected by gender, ethnicity, position, and salary level.

### **Finding #1: Campuses are inconsistent in their approaches to considering diversity in their hiring processes.**

The chancellor's office and the board of trustees (board) of the university, who delegate the hiring authority of assistant, associate and full professors (professors) to the campuses, have not adopted systemwide guidance to aid in standardizing the hiring process. As a result, the five campuses we reviewed use different methods to consider gender and ethnicity in the hiring of professors. Although California's Proposition 209 specifically prohibits the university from giving preferences to women or minorities during the hiring process, these requirements coexist with federal affirmative action regulations and thus are not intended to limit employment opportunities for women or minorities.

During the position allocation phase of the hiring process for professors, the campuses we reviewed do little, if anything, in considering gender and ethnicity. For instance, just one of the five campuses we reviewed encourages departments to consider faculty diversity at this stage. We acknowledge that departments can choose to hire professors in a specialized field of study in which proportionately fewer women and minorities exist to meet reasonable academic needs. However, when flexibility exists, they should be open to the idea of recruiting new professors from those disciplines or areas of specialization that will not decrease the likelihood of hiring female or minority professors.

Further, the California Faculty Association recommends that search committees review their campuses' affirmative action plans so they are aware of underrepresentation and the actions that administrators have recommended to improve recruitment efforts to reach women

<sup>1</sup> The audit committee also requested that we review the university's compensation practices. The results of our review of those practices were the subject of a separate report (2007-102.1) issued November 6, 2007.

### **Audit Highlights . . .**

*Our review of California State University's (university) hiring processes and employment discrimination lawsuits revealed the following:*

- » *The university has issued little systemwide guidance to the campuses regarding the hiring process.*
- » *Campuses are inconsistent in their consideration of gender and ethnicity when hiring assistant, associate, and full professors.*
- » *Campuses use differing levels of detail when estimating the percentage of qualified women and minorities available for employment, decreasing the university's ability to effectively compare data among campuses.*
- » *Campuses have hiring policies that vary in terms of the amount of guidance they provide search committees for Management Personnel Plan employees, and one campus has developed no policies for these positions that relate to nonacademic areas.*
- » *While the hiring process for presidents requires input from many stakeholders, the hiring of system executives is largely at the discretion of the chancellor in consultation with the board of trustees.*
- » *As of June 30, 2007, the university spent \$2.3 million on settlements resulting from employment discrimination lawsuits filed during the five-year period we reviewed, and \$5.3 million for outside counsel in defending itself against such lawsuits.*



and minorities. Nevertheless, the campuses we reviewed generally did not share information from the affirmative action plans with search committees. Additionally, although women and minority professors can provide search committees with different perspectives when evaluating candidates, the campuses we reviewed generally did not have written policies that address gender and ethnic representation on such committees. Further, the chancellor's office has not issued guidance on this matter. As a result, some campuses consider the gender and ethnic composition of search committees, while others forbid it.

Additionally, to analyze their employment processes in accordance with federal regulations, campuses distribute surveys to all job applicants to determine their gender and ethnicity. The University of California has issued guidelines that state that if women and minority applicants are not present in the applicant pool at about the rate of their estimated availability in the corresponding labor pool, campuses should review recruitment and outreach efforts and can consider reopening the search with expanded inclusive recruitment efforts. However, the chancellor's office has not issued guidance in this area. Not performing such comparisons increases the risk that departments are unaware of the need to perform more inclusive outreach.

Because applicants are not required to submit the surveys containing their gender and ethnicity, it is not unexpected that response rates can be low. During our review of the hiring processes at five campuses, we noted that one campus sent out a reminder e-mail to applicants requesting that they complete and submit the forms containing their gender and ethnicity, even if they decline to disclose their gender and ethnicity. The campus notes that while it does not typically send reminders to applicants, it does so when response rates are unreasonably low. This practice seems a promising measure to increase the low response rates cited by campuses as a reason why comparing applicant pool data with labor pool data often is not meaningful.

We recommended that the university issue systemwide guidance on the hiring process for professors to ensure it employs hiring practices that are consistent with laws and regulations and among campuses. This guidance should include the development of position descriptions that are as broad as possible, the use of affirmative action plans to familiarize search committees with estimated availability for women and minorities, the development of alternatives for including women and minorities on search committees, a requirement to compare the proportion of women and minorities in the total applicant pool to the proportion in the labor pool to help assess the success of their outreach efforts, and the distribution of reminders to applicants requesting them to submit information regarding their gender and ethnicity.

***University's Action: Pending.***

The university stated that the chancellor's office will include guidance in its faculty hiring guidelines to campuses on developing position descriptions as broadly as possible consistent with academic needs and the university's commitment to inclusiveness, having search committees review information in the affirmative action plans, devising alternatives to broaden the perspective of search committees and increase the reach of the search, and using applicant pool response data as one means of assessing the effectiveness of recruitment efforts. The university also stated that it will notify campus officials that they may send reminders to applicants regarding the submission of their gender and ethnicity, but that such reminders should clearly explain the use of the data collected and the applicants' rights to decline to submit such information. The university stated that it will give careful consideration to whether any action or guidance could be viewed as an illegal "preference" in violation of Proposition 209.

**Finding #2: Campuses are inconsistent in how they conduct their availability analyses.**

Because the chancellor's office does not provide campuses with a uniform method for determining availability, campuses have some latitude in deciding the factors they will consider. Availability is an estimate of the number of qualified women or minorities available for employment in a given job classification expressed as a percentage of all qualified persons available for employment in the

comparable labor pool. Because, according to the university, campuses have different recruitment areas, specialties, and positions, the campuses each determine their own availability. However, our review of the availability analyses for various university campuses revealed that the reasonable recruitment area for professors is nationwide. Therefore, we believe that a uniform method of determining availability for professors in the reasonable recruitment area is possible, appropriate, and necessary.

We also noted differing levels of detail in campus availability analyses in their affirmative action plans. For instance, three of the five campuses we reviewed presented an aggregate analysis for professors campuswide rather than comparing the gender and ethnicity of their current professors in each department to those available in the labor pool. The differing levels of detail decrease the university's ability to effectively compare data among campuses.

We recommended that the university devise and implement a uniform method for calculating availability data to better enable it to identify and compare availability and goals systemwide and among campuses. Further, it should direct campuses to compare and report the gender and ethnicity of their current workforce to the labor pool by individual department to ensure that goals are meaningful and useful to those involved in the hiring process.

***University's Action: Pending.***

The university asserted that it will establish a task force comprised of campus officials in order to identify a workable method for uniform calculating of availability data. The university also indicated that it will identify the appropriate levels for data comparisons, stating that in some cases this may be at the department level, school, or other division level.

**Finding #3: The hiring process lacks consistent training.**

Some campuses have more detailed procedures than others to maintain the integrity of the hiring process and to ensure that search committee members are aware of applicable laws and regulations. For instance, some campuses require search committee members to attend training regarding the hiring process while others do not. As a result, not all of the departments we reviewed were aware of campus hiring protocols. For example, although the collective bargaining agreement between the board and the California Faculty Association requires that search committees be elected and consist of tenured professors, some departments do not elect their search committee members. Further, this lack of guidance may have contributed to one campus developing a policy that requires the consideration of gender or ethnicity in hiring decisions. This policy is inconsistent with what other campuses are doing: the remaining four campuses we reviewed indicated that gender or ethnicity would never play a role in their hiring decisions because Proposition 209 prohibits preferences based on these factors.

We recommended that the university issue systemwide guidance that instructs campuses to require search committee members to receive training offered at the campus level regarding the hiring process, federal regulations, Proposition 209, and other relevant state and federal laws. Additionally, we recommended that the university take action to ensure that campuses have departments elect faculty to serve on search committees to help ensure that searches are conducted in accordance with the collective bargaining agreement and campus policies.

***University's Action: Pending.***

The university indicated that it will provide guidance to the campuses on the need to require training and will explore the possibility of utilizing online training to assist in meeting this requirement. Additionally, the university stated that it will remind the campuses of the requirement to elect faculty members to search committees and will ensure that the requirement is a part of campus faculty hiring procedures.

**Finding #4: Campuses' hiring processes for management personnel vary and they are inconsistent in considering diversity in recruiting for these positions.**

Similar to the hiring authority the university has delegated to campuses for professors, it has also delegated authority to the campuses to develop policies for hiring Management Personnel Plan employees (management personnel). Also, as with the hiring of professors, the university has not adopted systemwide guidance to aid in standardizing the hiring process for management personnel. Thus, it is not surprising that campuses we reviewed have developed hiring policies that vary in the amount of guidance they provide search committees on how to conduct the search process. For instance, only one of the five campuses we reviewed has developed policies that address each of the key steps in the hiring process for both academic and nonacademic management personnel, while some of the remaining campuses allow search committees for management personnel positions discretion in conducting the hiring process. In fact, one campus has not developed any formal written policies to govern the hiring of nonacademic positions.

Search committee members can be appointed or elected to serve depending on their position or campus and are generally responsible for conducting the search process for management personnel. Because these responsibilities are crucial to a hiring process that is fair and equitable, composition of the search committee is an important consideration. For instance, women and minorities can provide search committees with different perspectives when evaluating candidates. However, assessment of the gender and ethnic composition of search committees is not specifically required.

We have similar concerns regarding inconsistencies in campuses' approaches to considering gender and ethnicity at various stages in the hiring process for academic management personnel to those we express for hiring professors. Campuses we reviewed generally did not share information in their affirmative action plans with search committees when planning the search process for academic management personnel in order to make progress in achieving equal employment opportunity for underrepresented groups. Further, although federal regulations require contractors, such as the university's 23 campuses, to perform in-depth analyses of their total employment processes to determine whether and where impediments to equal opportunity exist, most campuses we reviewed do not require an assessment of applicant pool data to evaluate their success in recruiting women and minorities. Moreover, because applicants are not required to submit the surveys containing their gender and ethnicity, response rates can be low, thus inhibiting the meaningfulness of comparing the diversity of the applicant pool to the estimated availability in the labor pool. As discussed in Finding 1, we noted a promising measure at one campus as it states that it sends reminders to applicants when response rates are unreasonably low requesting that they complete and submit the forms containing their gender and ethnicity.

We have some additional concerns about the hiring of nonacademic management personnel. The campuses we reviewed generally lack a requirement that search committees review information in campus affirmative action plans when planning the hiring process and performing an analysis of applicant pool data to assess their success in recruiting women and minorities for nonacademic management personnel positions. We also noted inconsistent hiring practices between academic and nonacademic management personnel positions at one campus. This inconsistency further highlights the need for the chancellor's office to issue systemwide guidance on the hiring process for all management personnel.

Finally, we have concerns about the manner in which the campuses conduct their availability analyses for these positions. The campuses we reviewed consider management personnel at the administrator IV level as one group for purposes of their availability analysis. Because they do not separate the analysis for management personnel based on the functions of the positions, the analysis is not as meaningful as it could be. For instance, campuses could present the analysis separately based on position duties, such as those having responsibility for academic affairs or finance, because these positions typically draw from separate labor pools. Devising a meaningful analysis may assist campuses in better planning their search and recruitment efforts for management personnel.

We recommended that the university issue systemwide guidance on the hiring process for management personnel and in developing this guidance it should direct campuses to develop hiring policies for management personnel that address the key steps in the hiring process. Further, this guidance should include the development of alternatives for including women and minorities on search committees, the use of affirmative action plans so search committees are aware of the underrepresentation of women and minorities, a requirement to compare the proportion of women and minorities in the total applicant pool to the proportion in the labor pool to help assess the success of their outreach efforts, and the distribution of reminders to applicants requesting them to submit information regarding their gender and ethnicity. Additionally, we recommended that the university advise campuses to compare and report the gender and ethnicity of their current workforce to the labor pool by separating management personnel positions into groups based on the function of their positions to ensure goals are meaningful and useful to those involved in the hiring process.

***University's Action: Pending.***

The university indicated that chancellor's office staff will develop guidance indicating the basic principles that should be included in campus hiring policies for management personnel. Further, the university stated that it will include guidance to campuses on developing alternatives to broaden the perspective of search committees and increase the reach of the search for management personnel, having search committees review information in the affirmative action plans, using applicant pool data to assess the effectiveness of recruitment efforts, and identifying the appropriate levels for availability analyses. The university also stated that it will notify campus officials that they may send reminders to applicants regarding the submission of their gender and ethnicity, but that such reminders should clearly explain the use of the data collected and the applicants' rights to decline to submit such information. The university indicated that it will give careful consideration to whether any action or guidance could be viewed as an illegal "preference" in violation of Proposition 209.

**Finding #5: Policies for hiring system executives are minimal and the consideration of diversity when hiring presidents and system executives is limited.**

The chancellor alone is responsible for the search process for system executives; the policy governing this hiring process gives the chancellor discretion on how to conduct the search. According to the university's chief of staff, the board's policy provides the chancellor with this responsibility because the board believes the chancellor should have the ability to select his or her executive team. The search process for system executives must include representation from the board and advice from one or more presidents, faculty, and students chosen at the chancellor's discretion. For the one system executive hired during our audit period, the chancellor appointed a search committee whose responsibilities included screening and selecting applicants. However, without establishing more complete policies to guide the recruitment process for system executives, the university cannot ensure that the process for each search is fair, equitable, and consistent.

Further, the university policies for hiring presidents and system executives do not require consideration of gender and ethnicity during the hiring process. For instance, although professor positions are generally advertised in a variety of sources, including the Women in Higher Education and Hispanic Outlook, these same publications are not routinely used when advertising for presidential and system executive positions. According to the university's chief of staff, advertising is just one aspect of recruiting and that, in the experience of the chancellor's office, the best means to attract women and minority applicants is through direct personal contact, including that made by the chancellor, the chief of staff, or a third party such as a campus president. Nevertheless, the university could enhance the effectiveness of its current recruitment efforts by having a more broad-based and consistent advertising requirement for presidential and system executive positions. Further, the university's policies that govern the formation of the search committees involved in the search and selection process for presidential positions do not address gender and ethnic representation on such committees.

We recommended that the university establish more complete policies to guide the recruitment process for system executives to ensure that the process for each search is fair, equitable, and consistent. Further, to ensure it is conducting inclusive and consistent advertising to obtain as diverse an applicant pool as possible, the university should require broad-based advertising, including publications primarily with women or minority audiences, for all presidential and system executive positions. Finally, to broaden the perspective of the committees involved in the search for presidential positions, the university should develop policies regarding the diversity of these committees and consider alternatives to increase their diversity.

***University's Action: Pending.***

The university asserted that some improvement can be made in the existing system executive recruitment policies and procedures and stated that it will review them with the board and determine if specific changes should be made in light of our recommendations. Further, the university stated that while it is committed to improving its hiring process, it would give careful consideration to whether any changes could be viewed as an "illegal" preference in violation of Proposition 209.

# California State University

## It Needs to Strengthen Its Oversight and Establish Stricter Policies for Compensating Current and Former Employees

REPORT NUMBER 2007-102.1, NOVEMBER 2007

### *California State University's response as of October 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits review the compensation practices of the California State University (university).<sup>1</sup> Specifically, the audit committee asked us to identify systemwide compensation by type and funding source, to the extent data are centrally maintained and reasonably consistent among campuses. The audit committee also asked us, subject to the same limitations, to categorize by type and funding source the compensation of highly paid individuals receiving funds from state appropriations and student tuition and fees. In addition, for the most highly paid individuals, the audit committee asked us to identify any additional compensation or employment inducements not appearing in the university's centrally maintained records, such as those recorded in any employment agreements with the university. Further, the audit committee asked us to review any postemployment compensation packages and identify the terms and conditions of transitional special assignments for highly paid individuals, including top executives and campus presidents, who left the university in the last five years. Finally, the audit committee asked us to determine the extent to which the university's compensation programs and special assignments are disclosed to the board of trustees (board) and to the public, including the types of programs that exist, the size and cost of each, and the benefits that participants receive. To the extent that this information is available and is not publicly disclosed, the audit committee asked us to include these items in our report.

### **Finding #1: The university has not developed a central system sufficient for monitoring compliance with its compensation policies.**

The chancellor's office establishes systemwide compensation policies but does not have a system in place that allows it to adequately monitor adherence to those policies and to measure their impact on university finances. Specifically, the chancellor's office does not maintain systemwide compensation data by type and funding source, either by individual or in total. The lack of this data impairs the ability of the chancellor's office to provide effective oversight of the university's compensation programs. The executive vice chancellor and chief financial officer (executive vice chancellor) indicated that it was never the intent of the chancellor's office to have detailed systems in place to monitor employee payments and to ensure that payments are consistent with policy, as it believes that is a campus responsibility. Accordingly, the financial tools available to the chancellor's office for payroll purposes reflect its view that campuses are delegated the authority and responsibility to monitor compliance with university

<sup>1</sup> The audit committee also requested that we review the university's hiring practices and employment discrimination lawsuits. The results of our review of these areas were included in a separate report (2007-102.2), which we issued in December 2007.

### **Audit Highlights . . .**

*Our review of the California State University's (university) compensation practices revealed the following:*

- » *The university has not developed a central system enabling it to adequately monitor adherence to its compensation policies or measure their impact on university finances.*
- » *Average executive compensation increased by 25.1 percent from July 1, 2002, through June 30, 2007, with salary increases contributing the most to the growth.*
- » *The board of trustees (board) has justified increasing executive salaries on the basis that its executives' cash compensation, excluding benefits and perquisites, lags those of comparable institutions, but concerns have been raised about the methodology used.*
- » *The university has three executive transition programs that provide postemployment compensation packages to departing executives, in addition to the standard retirement benefits available to eligible executives.*
- » *Some Management Personnel Plan employees received questionable compensation after they were no longer providing services to the university or while they were transitioning to faculty positions.*
- » *The discretionary nature of the university's relocation policy can result in questionable reimbursements of costs for moving household goods and closing costs associated with selling and purchasing residences.*

policy. The executive vice chancellor cited the standing orders of the board and the board's statement of general principles as the general policy basis for this delegation. Although we recognize that campuses have primary responsibility for implementing compensation policies, it is important for the chancellor's office to have sufficient data to ensure that the campuses appropriately carry out their responsibilities.

To provide effective oversight of its systemwide compensation policies, the university needs accurate, detailed, and timely compensation data. The university should create a centralized information structure to catalog university compensation by individual, payment type, and funding source. The chancellor's office should then use the data to monitor the campuses' implementation of systemwide policies and to measure the impact of systemwide policies on university finances.

***University's Action: Pending.***

The university reports that it will explore the best way to address these issues including making appropriate coding changes to improve the accuracy and detail provided by the existing systems. Its central administration will also develop and implement training to improve the consistency in coding and reporting of compensation matters by campus personnel. Finally, the university states that it will enhance monitoring at the system level through more frequent reviews of campus practices and will discuss with its board the degree to which it wants centralized monitoring to occur.

**Finding #2: The board has continually justified increasing executive salaries on the basis that its executives' cash compensation lags that of comparable institutions.**

Average executive compensation increased by 25.1 percent from July 1, 2002, through June 30, 2007. Because this increase was greater than that of other employee classifications, we examined the growth in the various components that make up executive compensation—salaries, housing allowances, and automobile allowances—over the five-year period. We found that salary increases contributed the most to this growth, with the board approving salary increases on three separate occasions. The salary increases for executives ranged from an average of 1.68 percent to 13.7 percent. The board has continually justified increasing executive salaries on the basis that its executives' cash, or salary, compensation lags behind that of comparable institutions. However, as early as October 2004, the California Postsecondary Education Commission (commission), the entity that was involved with executive compensation studies until that time, raised concerns that the methodology used in making such comparisons did not present a complete picture of the value of individual compensation packages because it did not consider benefits and perquisites provided to executives, which can be substantial. Despite these concerns and the absence of further commission involvement in surveys of executive compensation, the university proceeded to use a consulting firm to perform surveys of the comparison institutions using the questioned methodology. Further, documents indicate that the board approved executive salary increases in October 2005 and January 2007 based only on the lag in cash compensation.

The commission and the Legislative Analyst's Office (legislative analyst) expressed further concerns in 2007 about the existing methodology used in these types of comparisons. Nevertheless, in September 2007 the board granted its executives another raise averaging 11.8 percent. Further, the chancellor recommended that the board adopt a new formal executive compensation policy and that the board continue to have a salary target focused on the average cash compensation for similar positions at comparable institutions. In response to these recommendations, the board adopted a new executive compensation policy and resolved that it aims to attain parity for its executives and faculty by fiscal year 2010–11.

We asked the chancellor's office why the university continued to justify increases in compensation for its executives based on a methodology that has been questioned by the commission and the legislative analyst. The chancellor's office responded that the university did not believe it appropriate to deviate from a methodology that was agreed upon years ago by the various interested parties, including the

commission and the legislative analyst. However, as these are now the same parties that are raising concerns, we believe it is time for the university to work with the interested parties to develop a more appropriate methodology that considers total compensation.

We recommended that the board consider total compensation received by comparable institutions, rather than just cash compensation, when deciding on future salary increases for executives, faculty, and other employees. The university should work with interested parties, such as the commission and the legislative analyst, to develop a methodology for comparing itself to other institutions that considers total compensation. If the university believes it needs a statutory change to facilitate its efforts, it should seek it.

***University's Action: Pending.***

The university reports that it will continue to work with interested parties in an effort to develop a methodology for use of total compensation analysis for executives, faculty, and other employees. The university states that it is committed to using the best tools available as long as lag comparisons for executives, faculty, and other employees are all based on the same compensation elements.

**Finding #3: The university has generous postemployment compensation packages for departing executives.**

The university typically offers its departing executives a transition program that often provides a generous postemployment compensation package. This program is in addition to the standard retirement benefits the university provides to eligible executives, including retirement income, medical and dental coverage, and voluntary retirement savings plans. Although the original transition program has been overhauled a few times, leaving the university with three transition programs currently in use, each departing executive is eligible for the program that was in place at his or her time of appointment. The terms of the transition agreement offered to a departing executive vary with the transition program the executive is eligible for but can include one year of paid leave, lifetime tenure as a trustee professor at a campus, or an alternative agreement negotiated by the chancellor.

In November 2006, after media criticism of existing postemployment compensation packages, the board passed a resolution requiring the chancellor to provide every board member with a copy of each final transition agreement and to submit an annual report summarizing all existing transition agreements. However, the annual report contains no information on the status of accomplishments or deliverables that former executives may have agreed to provide the university as part of their transition agreements, and disclosure does not occur until after the chancellor has reached a final agreement with a departing executive. Although the board has decided not to participate in negotiating transition agreements, it is important that the board continue to monitor the chancellor's administration of the executive transition program to ensure that the agreements departing employees receive are prudent and that intended cost savings are achieved for the university.

We recommended that the board continue to monitor the executive transition programs to ensure that the chancellor administers them prudently and that intended cost savings are achieved for the university. In addition, the board should require the chancellor to include in the transition agreements clear expectations of specific duties to be performed, as well as procedures for the former executives to report on their accomplishments and status of deliverables. Further, the board should require the chancellor to include information in his annual report on the status of accomplishments and deliverables associated with transition agreements.

***University's Action: Partial corrective action taken.***

The university reports that the chancellor already has begun to include in transition agreements clear expectations regarding specific duties to be performed by executives. In addition, the university states that a report of accomplishments and deliverables will be added to the annual report. Finally, the board will consider whether it wishes to take specific action on this matter.



**Finding #4: The university paid questionable compensation to management personnel no longer performing services for the university.**

The paid leaves of absence the university provides as part of transition programs are intended only for departing executives. However, the university operates under a very broad policy for granting paid leaves of absence for Management Personnel Plan employees (management personnel). Title 5, Section 42727, of the California Code of Regulations, which addresses professional development, specifies that management personnel may participate in programs and activities that develop, update, or improve their management or supervisory skills. The programs and activities may include “professional leaves, administrative exchanges, academic coursework, and seminars.” Management personnel may participate in such programs and activities only after the chancellor or campus president grants approval and only to the extent that funds are available. The regulations do not sufficiently define the criteria that must be met before a paid leave will be granted, and it does not establish time restrictions for a paid leave.

Our review confirms the need for the university to strengthen its regulations and policies in this area. In reviewing a sample of personnel files at the chancellor’s office and various campuses, we found instances in which management personnel received questionable compensation after they were no longer providing services to the university or while they were transitioning to faculty positions. For example, we found that one individual, who received compensation totaling \$102,000 during a seven-year leave on the premise that he was gaining experience that would benefit the university on his return, never returned to university employment. We also noted that one individual was granted a future leave of absence with pay to transition from an administrative position to a faculty position.

We recommended that the university work through the regulatory process to develop stronger regulations governing paid leaves of absence for management personnel. The improved regulations should include specific eligibility criteria, time restrictions, and provisions designed to protect the university from financial loss if an employee fails to render service to the university following a leave. Further, the board should establish a policy defining the extent to which it wants to be informed of such leaves of absence for management personnel.

***University’s Action: Pending.***

The university reports that while balancing the need for consistency with the need for some administrative flexibility the board will consider actions that can strengthen the process for granting leave of absences for management personnel. The board will also consider development of criteria regarding eligibility, time limitations, and fiscal protective measures.

**Finding #5: The university exercises considerable discretion in paying relocation costs for new employees.**

The university has established a broad policy for paying costs related to moving and relocation (collectively referred to here as relocation) for its employees. The policy provides that incoming employees may receive reimbursement for actual, necessary, and reasonable expenses but includes few monetary limits for reimbursable expenses. Further, although the policy identifies the types of expenses that can be reimbursed, it contains clauses permitting the chancellor or campus presidents to grant exceptions. The chancellor determines the amounts of relocation reimbursements for executives, campus presidents, and management personnel in the chancellor’s office, and the campus presidents determine the amounts for management personnel and faculty at their respective campuses. Neither the chancellor nor the campus presidents are required to obtain the approval of the board for relocation reimbursements, and they typically do not disclose these payments to the board. The discretionary nature of the university’s policy can result in questionable reimbursements for costs, such as those for moving household goods and closing costs associated with selling and purchasing residences. These costs can be considerable. For example, we noted that the university reimbursed one individual for \$65,000 in closing costs and \$19,000 in moving expenses.

We recommended that the university strengthen its policy governing the reimbursement of relocation expenses. For example, the policy should include comprehensive monetary thresholds above which board approval is required. In addition, the policy should prohibit reimbursements for any tax liabilities resulting from relocation payments. Finally, the board should require the chancellor to disclose the amounts of relocation reimbursements to be offered to incoming executives.

***University's Action: Pending.***

The university reports that the board will consider means of strengthening the controls related to reimbursement of relocation expenses. The board will also review the amount of discretion given to system executives and determine the extent to which it wishes to review or approve any such expenses. Finally, the university states that the chancellor will disclose the amounts of reimbursements offered to incoming executives.

**Finding #6: The university's policy on dual employment is limited.**

The university has established a dual-employment policy that allows its employees to have jobs outside the university system as long as no conflicts of interest exist. However, the policy does not require employees to obtain prior approval for outside employment, nor does it require them to disclose that they have such employment. Thus, the university is unable to adequately determine whether employees have outside employment in conflict with their university employment.

The university should work to strengthen its dual-employment policy by imposing disclosure and approval requirements for faculty and other employees, including management personnel. If the university believes it needs a statutory change to facilitate its efforts, it should seek it.

***University's Action: Pending.***

The university reports that it will continue to work through the collective bargaining and regulatory processes to strengthen the outside employment policy for faculty. It strongly favors an information process that will allow for the identification of any conflict of commitment prior to the start of any outside employment. The university states that it will adopt for management personnel similar requirements to those adopted for faculty.





# California State Polytechnic University, Pomona

## Investigations of Improper Activities by State Employees, February 2007 Through June 2007

### INVESTIGATION I2007-0671 (REPORT I2007-2), SEPTEMBER 2007

#### *California State Polytechnic University, Pomona's response as of September 2007*

We investigated and substantiated an allegation that an employee with the California State Polytechnic University, Pomona (Pomona), inappropriately used university computers to view pornographic Web sites.

#### **Finding: The employee misused state resources to engage in improper activities.**

We asked Pomona to assist us in the investigation, and we substantiated the allegation. Pomona found that the official repeatedly used university computers to view Web sites containing pornographic material. State laws prohibit employees from using public resources, such as time and equipment, for personal purposes. In addition, these laws require employees to devote their full time and attention to their duties, and prohibit individuals employed by the State from using a state-issued computer to access, view, download, or otherwise obtain obscene matter. Specifically, Pomona found that the official viewed approximately 1,400 pornographic images on two university computers during several weeks in 2006 and also from February to May 2007. Pomona was unable to review the official's complete Internet usage because the settings on the official's main computer only allowed for a two-month retention period of Internet activity. When interviewed, the official admitted to viewing pornographic Web sites regularly using university computers.

#### *Pomona's Action: None.*

- Pomona indicated that as of the issue date of our report, the official is no longer working on campus. Pomona negotiated a resignation with the official and permitted the official to exhaust all earned leave credits and other paid leave.

Pomona indicated that it has an Appropriate Use Policy for Information Technology and that it is committed to taking appropriate action when notified of employees who access pornographic materials on the Internet. However, Pomona did not indicate that it implemented any new controls or software filters that would prevent any future access to pornographic Web sites by employees.

#### *Updated information as of January 2008: None.*

- The department failed to provide a response.

#### **Investigative Highlight . . .**

*An employee at the California State Polytechnic University, Pomona, admitted, when interviewed, to viewing pornographic Web sites regularly using university computers.*



# Home-To-School Transportation Program

## The Funding Formula Should Be Modified to Be More Equitable

REPORT NUMBER 2006-109, MARCH 2007

### *California Department of Education's response as of September 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits (bureau) review the California Department of Education's (Education) disbursement of Home-to-School Transportation (Home-to-School) program funds to identify any inequities. Specifically, we were asked to review the funding formula that Education uses to determine Home-to-School program payments to school districts. The audit committee also asked us to determine how the program is funded and what roles Education and school districts have in determining the funding levels. In addition, we were asked to compare data related to the number and percentage of students receiving transportation services, the amount paid for the Home-to-School program in total and per student, the actual cost of transporting students in total and per student, and the excess cost over Home-to-School program payments by school district and region for both regular and special education students to determine if and why variances exist. Further, the audit committee asked that we determine how school districts fund the difference between what is paid to them by Education and their actual cost, and evaluate, to the extent possible, whether this practice affects other programs. Additionally, the audit committee asked us to determine, to the extent possible, whether any correlations exist between higher transportation costs and staffing levels.

### **Finding: The prescribed funding formula does not allow some school districts to receive transportation funding.**

Home-to-School program funding is contingent upon receiving funds for this program in the immediately preceding fiscal year. Consequently, some school districts and county offices of education (school districts) are not eligible to receive these funds. Current laws require that Education allocate Home-to-School program funds to each school district based on the lesser of its prior year's allocation or approved cost of providing transportation services, increased by the amount specified in the budget act. School districts that did not previously receive Home-to-School program allocations for special education transportation, regular education transportation, or both, are not eligible to receive these allocations under the current laws. Furthermore, some school districts have experienced dramatic increases in student population over the years. Although the funding method provides for some adjustments for the increase in statewide average daily attendance, the allocations have not always increased at the same rate as the increase in student population at individual school districts.

To determine the fiscal impact on school districts that do not receive the Home-to-School program funds, we recommended that Education identify all school districts that provide transportation services to their students but are not eligible to receive Home-to-School program

### **Audit Highlights . . .**

*Our review of the Home-to-School Transportation (Home-to-School) program administered by the California Department of Education found that:*

- » *The current legally prescribed funding mechanism prevents some school districts from receiving Home-to-School program funds because of the basis of allocation.*
- » *Although the annual budget act increases the Home-to-School program funds to account for the increases in the statewide average daily attendance, these increases are less than the student population growth some school districts have experienced over the years.*
- » *Urban school districts received less overall Home-to-School program payments per student transported than rural school districts (\$559 versus \$609) and paid for more overall costs per student transported from non-Home-to-School program funds (\$828 versus \$299).*
- » *While all school districts typically incurred higher costs to transport a special education student, such costs were higher in rural school districts (\$5,315) than in urban school districts (\$4,728).*
- » *Staffing levels and student test scores bear no relationship to the amount of transportation expenditures the school districts paid per student from non-Home-to-School program funds during fiscal year 2004–05.*

funds for regular education transportation, special education transportation, or both. In addition, we recommended that Education determine the actual costs these school districts incur and the funding sources they use to pay them. Further, we recommended that Education seek legislation to revise the current laws to ensure that all school districts that provide transportation services to regular education, special education, or both, are eligible for funding. To ensure that school districts are funded equitably for the Home-to-School program, we also recommended that Education seek legislation to revise the law to ensure that funding is flexible enough to account for changes that affect school districts' transportation programs, such as large increases in enrollment.

***Education's Action: Partial corrective action taken.***

Education noted that it does not have the resources to identify all the school districts that provide transportation services to their students but are not eligible to receive Home-to-School program funds for regular education transportation, special education transportation, or both; and determine the actual costs these school districts incur and the funding sources they use to pay them. However, Education stated that it submitted a Budget Change Proposal for the fiscal year 2008–09 budget for a new consultant position to, among other things, develop a pupil transportation funding reform proposal aimed at ensuring that all eligible school districts receive state funds for the Home-to-School program.

# Department of Education

## Its Mathematics and Reading Professional Development Program Has Trained Fewer Teachers Than Originally Expected

REPORT NUMBER 2005-133, NOVEMBER 2006

*The Department of Education's and State Board of Education's responses as of October 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits review the Mathematics and Reading Professional Development Program (program). Approved in 2001 (Chapter 737, Statutes of 2001), the program provides incentive grants to local education agencies that choose to send their teachers through standards-based instructional training. Under state law, the State Board of Education (board) adopts educational content standards and is responsible for approving the curriculum of providers wishing to train teachers under the program.

The audit committee asked us to review the board's and the Department of Education's (Education) policies and management practices to determine if they are consistent with the legislative intent of the program. Specifically, the audit committee asked us to assess the method used to track teachers' access to and participation in the program and the extent of any outreach efforts. The audit committee also asked us to identify the number of training providers that offer teacher development services and whether the board's approval process allows for a sufficient pool of training providers. Finally, the audit committee asked us to assess whether Education had adequate internal controls to track program expenditures and to identify any organizational, statutory, or regulatory impediments to the program.

**Finding #1: Only a small percentage of teachers have completed the program for their current assignments, while limited data at Education and the school districts makes assessing the program's success difficult.**

When the Legislature adopted the program in 2001, it envisioned that 176,000 teachers would receive training on the State's academic content standards over a four-year period. This target represented the majority of the 252,000 teachers statewide who were eligible for program-funded training at that time. Our survey of 100 school districts that participated in the program through fiscal year 2004–05, which represented 46 percent of the State's 398,000 eligible teachers as of January 2006, indicates that data exists at school districts to substantiate that only 7,230 teachers have been fully trained. This amount represents roughly 3 percent of the 240,987 eligible teachers in school districts that had received program funds through fiscal year 2004–05. Further, 41 school districts from our survey, representing 105,764 teachers, could not readily tell us how many had completed the entire 120 hours of training. More than half of these 41 school districts indicated that they did not have enough information to report specifics about the number of teachers that had completed the training. We acknowledge that some of the teachers in these 41 districts may have completed part or all of the program. We also

**Audit Highlights . . .**

*Our review of the Mathematics and Reading Professional Development Program (program) revealed that:*

- » *Only a small percentage of mathematics and reading teachers have completed the full 120 hours of training for their current assignments.*
- » *School districts we surveyed cited several barriers to increased participation in the program, including teacher apathy toward attending training, concerns about funding, and a lack of training providers in close proximity. Nevertheless, school districts in counties with relatively large or small numbers of eligible teachers in various geographic regions throughout the State appear equally capable of accessing program services.*
- » *The Department of Education (Education) has done little to actively promote the program and currently relies on school districts to navigate its Web site to learn about and apply for the program.*
- » *Education has not ensured that program compliance audits are conducted in accordance with program statutes.*
- » *Education's July 2005 report to the Legislature was of limited value because it lacked relevant and accurate data for gauging program outcomes.*
- » *Education's ability to adequately track teacher participation in mathematics and reading training is complicated by the multiple funding sources involved and by reduced program-specific funding.*

*continued on next page . . .*



» *The State Board of Education relied on the Sacramento County Office of Education to advertise and implement the program.*

acknowledge that school districts have not likely been asked to provide complete information about the number of their teachers that have completed the program for their current teaching assignments.

Finally, we noted that Education's July 2005 report to the Legislature was of limited value because it lacks relevant and accurate data regarding the number of trained teachers that are currently using the training in the classroom and provides no correlation between teacher training and student achievement. Education's data collection process resulted in duplicated counts of teachers that had received, but not necessarily completed, program training. As a result, decision makers cannot gauge the progress being made toward accomplishing the program's goals and are ill-prepared to make future funding decisions. Education acknowledged that its report has limitations, stating as much in its report to the Legislature.

Given that only a small percentage of teachers have completed the full 120 hours of program training, and that teacher participation is voluntary, the Legislature should consider redefining its expectations for the program, clearly stating the number of teachers to be fully trained as well as any gains in student achievement expected. Based on how it defines the program's goals, the Legislature should consider making statutory changes to ensure that Education provides meaningful data with which to evaluate program success. Examples of meaningful program data include the following:

- Unduplicated counts of teachers who have completed the training with the aid of program and non-program funding, with a comparison of these figures to the total number of teachers who are eligible to participate in the program.
- Measures of the resulting gains in student achievement for teachers who have completed the program's training, such as higher student scores on standardized tests.

***Legislative Action: None.***

The statutory provisions for the program remain substantially the same since the conclusion of the audit. The Legislature has not redefined its expectations for the program in terms of the number of teachers to receive the full 120 hours of training, or how it expects such training will translate into greater student achievement. Lacking such expectations, assessing the program's effectiveness towards achieving its ultimate goal of improving student learning remains problematic. Although the Legislature continues to require that Education report statistics on the numbers of teachers trained under the program, we continue to question the value of these reports. Specifically, Education's reporting process continues to utilize the same data collection forms reviewed during the audit, which results in duplicate counts of teachers trained under the program.

**Finding #2: School districts responding to our surveys cited a variety of reasons for low teacher participation rates.**

During the audit we conducted two surveys, each comprised of 100 school districts, that either had or had not received program funding through fiscal year 2004–05. School district responses to both surveys indicated that participant districts and nonparticipant districts alike perceived similar barriers to increased teacher participation in the program. The barriers most frequently cited by school districts were teacher apathy towards the training, concerns about funding, and a lack of training providers nearby. The similarities in these results suggest an opportunity for Education and the board to take steps to improve the program.

We received 169 responses to our surveys of 200 school districts. Responses from 51 of the 169 school districts indicated that a lack of teacher interest was a barrier to greater teacher participation. Some districts indicated that their teachers felt the training program was too long or too closely tied to textbooks, as opposed to a broader focus on understanding state standards. In addition, 42 of the 169 school districts cited funding concerns, primarily related to the timeliness of payment or the amount of funding. Some school districts stressed that they must initially pay for program training with their own funds and then seek program payment from Education, which can take many months. We noted that the program's payment process can be as long as four to six months for any single year's first payment. Some of this delay is caused by Education's need to wait for the board to approve annual certifications from school districts before making program payments.

The remaining barrier cited most frequently by school districts was the lack of training providers in close proximity to the school district. In particular, 33 of the 169 survey respondents cited this as a concern. Some respondents stated that rural school districts are placed at a disadvantage in obtaining training for their teachers because they have more difficulty accessing training providers. However, our review of program payments through fiscal year 2005–06 revealed that counties with relatively large and small numbers of eligible teachers in various geographic regions throughout the State appear equally capable of accessing program services.

To remove a barrier to increased teacher participation in the program, Education should explore opportunities to expedite its payment process to school districts. One such opportunity would be to seek legislation authorizing Education to approve the annual certifications submitted by school districts instead of waiting for board approval, thus removing any payment delay caused by the need to wait for the next board meeting.

***Education's Action: Pending.***

Education indicated that it continues to work with the board on expediting the program's reimbursement approval process. Although this process has remained the same since the audit took place in 2006, Education has reported its future plans to expedite reimbursement payments. Specifically, in fiscal year 2008–09, Education expects to change its program guidelines by requiring school districts to obtain SBE's approval to participate in the program at the beginning of the fiscal year. Given that program payments cannot occur until the board has approved a school district's participation in the program, Education expects this upfront approval by the board will eliminate some of the delays noted in the audit report. Further, Education also plans to implement an on-line payment request system that it expects will further reduce Education's reimbursement processing times.

**Finding #3: Education does little to encourage districts to participate in the program.**

Education's role in administering the program has essentially been limited to forwarding school districts' annual application to the board for approval and to processing program payments. Although not specifically required to do so under the program's statutes, Education has done little to actively promote the program. This lack of ongoing outreach may contribute to the low percentage of school

districts that have participated in the program, and may explain why nine of the districts that responded to our nonparticipant survey indicated that they were unaware of the program's existence or were confused about the eligibility or funding aspects of the program.

To ensure that school districts are aware of the program and that as many teachers participate in the program as possible, Education should conduct annual outreach activities to all school districts. A component of such an outreach program should include directly informing each school district of the amount of funding for which it is eligible each year.

***Education's Action: Pending.***

Education reports that it continues to disseminate program information to school districts through its annual notifications and its program's Web site. In addition, Education anticipates that its new on-line system, expected in fiscal year 2008–09, will provide school districts with additional program information, such as their specific funding cap amounts for the year.

**Finding #4: Education has not taken the necessary steps to ensure that program compliance audits occur at school districts.**

Education has not ensured that program compliance audits are conducted in accordance with program statute. Specifically, Section 99237 of the Education Code requires that annual financial and compliance audits of school districts include steps to ensure that teachers for whose training districts received program funding were, in fact, trained and that the training met program requirements. In addition, this section requires Education to withhold monthly apportionment payments to school districts to the extent that the results of audits reveal noncompliance with these requirements. Given this responsibility, we would have expected Education to take the necessary steps to ensure that these audits are actually taking place. However, discussion with Education staff revealed that such audits have likely never taken place because the compliance requirements have never been included in audit guides.

According to program statute, the compliance audits are to be performed by licensed local auditors, as opposed to Education's audit division, with the assistance of an audit guide specifying state compliance requirements. The Education Code, Section 14502.1, requires the State Controller's Office (controller), in consultation with the Department of Finance, Education, and representatives of specified organizations to propose the content of the audit guide and submit it to the Education Audit Appeals Panel for review, possible amendment, and eventual adoption. To Education's knowledge, the program's compliance requirements have never been included in the audit guide, and a controller representative confirmed that Education never informed that office of the program and its compliance requirements. As a result, Education has disbursed about \$113 million through fiscal year 2005–06 without ensuring the level of oversight required by statute.

To ensure that required compliance audits are occurring, Education should take steps to ensure that the program's compliance requirements are included in audit guides related to the annual audits of school districts.

***Education's Action: Corrective action taken.***

Education reported that the program's compliance requirements are continuing to be updated in the audit guides related to the annual audits of school districts. Our independent review of the audit guide published by the Education Audit Appeals Panel for fiscal year 2007–08 shows that the program is now included in the guide. Auditors of local school districts can now refer to Section 19838 of the guide for audit procedures aimed at assessing compliance with the program.

**Finding #5: The board did not obtain approval from the Department of General Services for program-related contracts with two county offices of education.**

Our audit noted that the board relied on two county offices of education for various program functions, including the development of criteria for evaluating training providers and the facilitation of the evaluation of curricula submitted by potential training providers. To provide these services, the board, acting through Education, entered into various contracts with the Sacramento County Office of Education and Orange County Department of Education. According to state law, all contracts entered into by state agencies, except those meeting certain exemptions, are not in effect unless and until approved by the Department of General Services. The board did not obtain the required approvals before the beginning of the contract term for all three program-related contracts and related amendments requiring approval. As a result, the board exposed the State to potential liability for work performed before the contract was approved.

To ensure that it does not expose the State to potential liability for work performed before the contract is approved, the board should ensure that it obtains the Department of General Services' approval of its contracts and amendments before the start of the contract period and before contractors begin work.

***Education's Action: Corrective action taken.***

In its response to the audit report, the board indicated that Education's procedural revisions to its contracting process, which it had implemented since the time of the program-related contracts referenced in the audit report, has had a profound effect on eliminating late contracts. Specifically, Education's Contracts and Purchasing Unit requires staff to submit contract request forms 60 days prior to the start of the contract. The board also cited an administrative order by the Department of General Services, clarifying the general policy on the timely submission of contracts and the circumstances under which contracts can be approved after the start date.



# California Children and Families Commission

## Its Poor Contracting Practices Resulted in Questionable and Inappropriate Payments to Contractors and Violations of State Law and Policies

REPORT NUMBER 2006-114, OCTOBER 2006

### *California Children and Families Commission's response as of October 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits (bureau) review the California Children and Families Commission's (state commission) spending practices, planning efforts, and contracting procedures.

#### **Finding #1: The state commission did not enforce contract terms for one contractor, resulting in overpayments totaling more than \$673,000.**

The state commission, in paying invoices totaling \$623,000 in fees and expenses submitted by one of its media contractors, allowed the contractor to circumvent the payment provisions of a contract. The contractor claimed the expenses by representing some of its employees as subcontractors. In addition, the state commission paid the media contractor an added \$50,000 fee that was unallowable per the contract. These payments violated the terms of the contract, which allowed for payments based only on the contractor's own services, in the form of commissions applied to the cost of the advertising it placed; no other services or fees were to be charged.

We recommended that the state commission ensure that both it and its contractors comply with all contract terms.

#### ***State Commission's Action: Corrective action taken.***

The state commission stated in its 90-day response to our audit that its most concerted efforts have been on staff training to ensure that all staff with any contract management responsibility understand the state's contracting procedures. In its one-year response, the state commission provided a schedule of the training courses that its staff attended between December 2006 and September 2007. It also stated that now that it has completed the Procurement Policy and Procedure Manual (manual), key staff will attend formal, internal training courses during November and December 2007 on topics such as contract concepts and timeline development, contract monitoring, invoice review and approval, and conducting and documenting solicitations. In its 90-day response, the state commission also had indicated that it appointed a specific staff member to track the training status of staff with contract responsibility. Finally, in its one-year response, the state commission pointed to a specific section of the new manual that discusses procedures its staff should follow when contractors do not appear to be complying with contract terms.

#### ***Audit Highlights . . .***

*Our review of the California Children and Families Commission's spending practices and contracting procedures revealed that it:*

- » *Allowed one of its media contractors to circumvent the payment provisions of a contract by paying invoices totaling \$673,000 for fees and expenses of some of the contractor's employees that were prohibited under the terms of the contract.*
- » *Did not fully use the tools available to it to ensure its contractors provided appropriate services.*
- » *Could not always demonstrate it had reviewed and approved final written subcontracts and subcontractors' conflict-of-interest certificates.*
- » *Did not always follow state policy when it used a competitive process to award three contracts valued at more than \$47.7 million and failed to provide sufficient justification for awarding one \$3 million contract and six amendments totaling \$27.6 million using the noncompetitive process.*

**Finding #2: The state commission did not fully use the tools available to it to ensure that its contractors promptly provided appropriate services.**

The state commission did not always include certain important elements when developing some of the contracts we reviewed. Specifically, the state commission's contracts did not always include a clear description of work to be performed, schedules for the progress and completion of the work, and a reasonably detailed cost proposal. Further, it did not always ensure that its contractors submitted adequate work plans, that it received all required work plans, and that it promptly approved them. As a result, the state commission cannot ensure that the resulting contracts clearly established what was expected from the contractor, that the contracts provided the best value, and that its contractors provided the agreed-upon services within established timelines and budgets.

We recommended that the state commission ensure that it fully develops its contracts by including clear descriptions of work, schedules for progress and completion of work, reasonably detailed cost proposals, a requirement for adequate supporting documentation for expenses, and clearly defined types of allowable expenses. We also recommended that it consistently enforce contract provisions requiring contractors to submit complete and detailed work plans before they perform services and incur expenses and to ensure that it promptly reviews and approves work plans.

***State Commission's Action: Corrective action taken.***

Again, the state commission referred to its 90-day response, which stated that it was sending all staff with any contract management responsibility to various training courses. In that same response, it also indicated that it had developed standard language for all new contracts, which addresses allowable out-of-pocket expenses and requires the contractor to obtain clarification from the state commission in advance of incurring an expense when it is unclear under the terms of the contract whether the expense is authorized. The state commission also stated that it redesigned the work plans it requires its public relations contractors to provide to include a detailed description of services and to identify the deliverables, target audience, and proposed completion timeline, as well as other information. Finally, in its one-year response, the state commission pointed to various sections of its new manual that describes the processes and procedures staff must follow related to the scope of work for a contract, schedules for progress and completion of work, contract budgets, and work plans.

**Finding #3: The state commission did not document its oversight of subcontractor agreements and conflict-of-interest certificates.**

The state commission could not demonstrate that it had reviewed and approved the final written subcontracts and subcontractors' conflict-of-interest certificates as required. Specifically, our review of a sample of nine contracts and 28 invoices associated with those contracts found that under each contract, the contractors charged for services provided by at least one and sometimes as many as six subcontractors. When we requested these subcontracts and conflict-of-interest certificates, the state commission had to forward our request to its contractors because it did not maintain copies of these documents in its files. Ultimately, it was only able to obtain 19 of a total of 22 requested subcontract agreements. Furthermore, the state commission was only able to obtain either the conflict-of-interest certificate or the conflict-of-interest language embedded within the subcontract for 14 of the 19 subcontracts it obtained. However, it was unable to locate the remaining five certificates. Because the state commission did not maintain these documents in its files, we question whether it reviewed and approved these documents as required before authorizing the use of subcontractors.

Additionally, subcontractors may be unaware of their obligation to preserve records that could be the subject of future audits. The state contracting manual requires contractors to include a provision in subcontracts indicating that the State has the right to audit records and interview staff in any subcontract related to the performance of the agreement. Our review of 19 subcontractor agreements found that five did not contain this language.

We recommended that the state commission establish a process to ensure that it obtains and reviews final written subcontracts and conflict-of-interest certificates before it authorizes the use of subcontractors. Additionally, it should ensure that its contractors include in all their subcontracts a provision indicating that the State has the right to audit records and interview staff in any subcontract related to the performance of the agreement.

***State Commission's Action: Corrective action taken.***

The state commission's 90-day response indicated that it is ensuring all staff with any contract management responsibility understand contracting procedures by requiring them to attend various training courses. Moreover, in its one-year response, it also pointed out a section in its new manual, which clearly indicates that the state commission must approve in advance final written subcontracts and conflict-of-interest certificates before the subcontractor performs any work. Further, in its 90-day response, the state commission indicated that it uses a Department of General Services' (General Services) form that contains general terms and conditions as a standard part of its contracts. One of the clauses in that document indicates the State's right to audit records and interview staff in any subcontract related to the performance of the agreement.

**Finding #4: The state commission sometimes paid unsupported and inappropriate contractor expenses.**

Although prudent business practices and some of its contracts include provisions requiring its contractors to include documentation necessary to support the expenses claimed, our review found that the state commission did not always enforce these provisions. Although generally the state commission received documentation to support the expenses claimed in our sample of 62 payments made to its contractors, we found both significant and minor instances in which this was not the case. Even when contractors included supporting documentation, the state commission did not always adequately review it before approving payment.

We recommended that the state commission consistently enforce contract provisions requiring contractors to submit supporting documentation for expenses claimed. Further, it should ensure that it performs an adequate review of such documentation before approving expenses for payment.

***State Commission's Action: Corrective action taken.***

The state commission's 90-day response indicated that it is ensuring all staff with any contract management responsibility understand contracting procedures by requiring them to attend training courses. In its one-year response, it also referred to a section in its new manual that discusses its invoice review and approval process, including a process for comparing the invoice to various documents, such as the contract and work plans, before approving them for payment.

**Finding #5: The state commission inappropriately advanced funds to three contractors.**

The state commission provided advance payments to three contractors even though it does not have the authority to do so. According to the state contracting manual, the State is permitted to make advance payments only when specifically authorized by statute, and such payments are to be made only when necessary. In addition, state laws are designed to ensure that public money is invested in and accounted for in the state treasury. Further, other state laws prohibit making a payment until services have been provided under a contract.

However, the state commission inappropriately advanced \$2.5 million to a public relations contractor for the administration of the state commission's regional community-based organization program. The public relations contractor then took between 30 days and six months to disburse the funds to the selected community-based organizations. Our review of 13 other invoices from the same public relations contractor showed that the state commission advanced it funds for the regional community-based organization program totaling \$6.8 million on three other occasions—invoices dated



July 2003, February 2004, and September 2004. Further, the state commission made advance payments in December 2005 and March 2006 to two county commissions totaling more than \$91,500 under memorandums of understanding. When the state commission makes advance payments without the proper authority, it loses the interest it would otherwise earn on these public funds.

We recommended that the state commission ensure it does not make advance payments to its contractors unless it has authority to do so.

***State Commission's Action: Corrective action taken.***

According to the state commission's 90-day response, the community-based organization program for which it made advances was completed before the bureau raised its concern about these advances. Additionally, the state commission indicated that based on the bureau's recommendation, it cancelled a similar program that was in the pre-disbursement phase. It further stated that it has no current plans to pursue other programs requiring advance payments absent sufficient legal authority to do so. Finally, in its one-year response, it pointed to the section of its new manual that prohibits advance payments unless specifically authorized by statute.

**Finding #6: Although it held strategic planning sessions annually, the state commission has not updated its written strategic plan since 2004.**

The state commission poorly managed its process for updating its strategic plan, which outlines the current progress of its initiatives and future plans to advance its vision of school readiness. According to the executive director, the state commission annually either develops a draft plan or updates the prior year's plan, and presents it to the commissioners for their review and approval. However, it last updated its strategic plan in 2004. According to the executive director, although the strategic plan was presented and discussed with the commissioners in January 2004 and January 2005, the state commission did not request their formal approval.

In October 2006 the executive director provided us with a draft copy of a commission proceedings manual. The manual includes an annual commission calendar that lists recurring issues the commissioners are required to consider, such as adopting the strategic plan. The executive director hopes to begin using the manual in January 2007 if the commissioners adopt it.

We recommended that the state commission ensure that it updates its strategic plan annually and presents it to the commissioners for review and approval.

***State Commission's Action: Corrective action taken.***

In its 90-day response, the state commission indicated that the commissioners reviewed and approved the strategic plan in October 2006, which was effective until June 30, 2007. Additionally, in its one-year response, the state commission stated that it had developed and the commissioners adopted the most recent plan in September 2007.

**Findings #7: The state commission did not always follow state requirements when awarding competitive contracts and it provided insufficient justification for awarding two contracts and six amendments using the noncompetitive process.**

The state commission did not always follow state policies during its process of competitively awarding contracts. For instance, it did not fully justify its reason for awarding three contracts, totaling more than \$47.7 million, when it received fewer than the minimum required number of three bids. Also, the state commission was unable to demonstrate that it had advertised a \$90 million contract in the state contracts register as required by state policy.

Moreover, when awarding some of its contracts and amendments using the State's noncompetitively bid (noncompetitive) contract process, the state commission did not provide reasonable and complete justifications for using the process or for the costs of the contracts awarded. Two of the five noncompetitive contracts we reviewed had insufficient justification of the costs of the contract. For one of these contracts, as well as for six of eight amendments to contracts originally awarded using either a competitive bid or the noncompetitive process, the state commission cited insufficient staff resources or time limitations as its reason for using the noncompetitive process. We do not believe that these circumstances are compelling reasons for avoiding a competitive bidding process.

To ensure that it protects the State's interests and receives the best products and services at the most competitive prices, we recommended that the state commission follow the State's competitive bid process for all contracts it awards, unless it can provide reasonable and complete justification for not doing so. Further, it should plan its contracting activities to allow adequate time to use the competitive bid process.

We also recommended that the state commission fully justify the reasonableness of its contract costs when it receives fewer than three bids or when it chooses to follow a noncompetitive bid process. It should also advertise all nonexempted contracts in the state contracts register.

***State Commission's Action: Corrective action taken.***

The state commission's 90-day response indicated that it is ensuring all staff with any contract management responsibility understand contracting procedures by requiring them to attend training courses. The state commission also referred to several sections of its new manual—acquisition planning, ensuring a full and open competitive process for formal competitive procurements, noncompetitively bid contracts, and competitive contracts receiving less than three bids, as well as others—where it has addressed some of the issues related to these recommendations. For example, the manual specifically identifies the documentation that staff must prepare when three bids are not received. It also provides guidance to staff related to noncompetitively bid contracts and justification as to the reasonableness of the contract costs.

**Finding #8: Documentation for the scoring of competitive proposals was inconsistent.**

Inconsistencies in its documentation of the scoring process for contract bids may leave the state commission open to criticism and challenges to its decisions. It uses a consensus method to score proposals it receives on competitively bid contracts. For the nine competitively bid contracts we reviewed, the state commission retained only the consensus score sheet for each proposal submitted in six of the competitive contracts. Without all the individual scoring materials used in discussing and selecting a winning proposal, it is not possible for us or others to independently replicate the results.

To ensure that it promotes fair and open competition when it awards contracts using a competitive bid process, we recommended that the state commission ensure that it fully documents its process for scoring proposals, and that it retains the documentation.

***State Commission's Action: Corrective action taken.***

The state commission's 90-day response indicated that it is ensuring all staff with any contract management responsibility understand contracting procedures by requiring them to attend training courses. In its one-year response, the state commission also referred to several sections of its new manual that outline its competitive bid process including requirements that all RFPs include the evaluation criteria and selection process and all evaluation and scoring sheets be available for public inspection at the conclusion of the scoring process.

**Finding #9: The state commission did not always follow state policies when allowing subcontractors under its interagency agreements and contracts with government agencies.**

Of the 24 interagency agreements and four contracts with other government agencies we reviewed, 25 included the services of subcontractors, for a total of at least \$64.6 million. This represents 53.6 percent of the total of \$120.6 million for these agreements and contracts. For 17 of 25 interagency agreements and contracts with other government agencies, the state commission did not always comply with state policies when justifying the use of subcontractors. Three of the 17 appear to have included subcontractors, but the amount of funds subcontractors are to receive is not clear. We also question the justification for the remaining 14 subcontracts totaling \$38.3 million.

To ensure that it follows state policies and protects the State's interest when using interagency agreements and contracts with government agencies, we recommended that the state commission obtain full justification for the use of subcontractors when required and, if unable to do so, deny the use of subcontractors.

***State Commission's Action: Corrective action taken.***

The state commission indicated that its new manual addresses this recommendation. Our review of the new manual found that it provides guidance related to interagency agreements and contracts with governmental agencies, but more specifically, it states that work performed under a government contract generally must be performed by the contractor agency, not subcontractors. However, it also provides staff the specific provisions that apply if subcontractors are used under these types of contracts.

**Finding #10: The state commission agreed to reimburse contractors for indirect costs at higher rates than state policy allows.**

The state commission did not always comply with state policies limiting the amount of administrative overhead fees paid to contractors for each subcontract. In fact, the state commission, in its interagency agreements, approved budgets to reimburse its contractors for over \$1.2 million more than the state contracting manual allows.

To ensure that it follows state policies and protects the State's interests when using interagency agreements and contracts with government agencies, we recommended that the state commission limit the amount that it will reimburse its contractors for overhead costs to the rates established in the state contracting manual.

***State Commission's Action: Corrective action taken.***

The state commission indicated that its new manual addresses this recommendation. Our review of the new manual found that it contains a section that appears to provide appropriate guidance to staff on overhead fees and indirect costs, including establishing limits.

**Finding #11: The state commission circumvented contracting law when it used memorandums of understanding to obtain services.**

In fiscal years 2004–05 and 2005–06, the state commission awarded five memorandums of understanding (MOUs) and two amendments totaling more than \$595,000. It appears to have intentionally used some of these to avoid having to comply with state contracting requirements, and for at least two MOUs and one amendment the intention was explicit. Although state contracting law allows agencies to enter into contracts with local government entities without competitive bidding, it strictly prohibits agencies from using these contracts to circumvent competitive bidding requirements.

To ensure that MOUs it awards allow for fair and competitive contracting and protect the State's best interests, we recommended that the state commission follow laws and policies applying to contracts when awarding and administering MOUs.

***State Commission's Action: Corrective action taken.***

Although in its 90-day response the state commission indicated that it had suspended its MOU program pending further review, its new manual provides specific guidance as to those few instances when an MOU can be used.

**Finding #12: The state commission consistently failed to obtain approvals for its contracts and amendments on time.**

According to state law, all contracts entered into by agencies, except those meeting criteria for exemptions, are not in effect unless and until approved by General Services. The state commission failed to obtain the required approvals before the beginning of the contract term for 43 of 45 of the contracts we reviewed. Similarly, it did not obtain the required approvals for 22 of the 44 amendments we reviewed until after the related contract or prior amendment had ended. Although we did not review all of the contracts to determine whether work began before approval, we noted three instances in which the contractor provided services totaling more than \$7 million before the state commission obtained final approval of the contracts. The state commission also failed to obtain the required approvals altogether on three amendments.

To ensure that it does not expose the State to potential financial liability for work performed before the contract is approved, we recommended that the state commission ensure that it obtains General Services' approval of its contracts and amendments before the start of the contract period and before contractors begin work.

***State Commission's Action: Corrective action taken.***

The state commission's 90-day response stated that it is ensuring all staff with any contract management responsibility attend training courses related to contracting procedures. In its one-year response, it also referred to several sections in its new manual, one of which clearly states that staff are not authorized to instruct contractors to begin work before a signed copy of the contract is received.

**Finding #13: The commissioners may have improperly delegated authority to award contracts.**

State law authorizes the state commissioners to enter into contracts on behalf of the state commission. The commissioners adopted a formal resolution in May 2001 delegating their contracting authority to enter into and amend contracts to state commission staff. In this same resolution, the commissioners took action to ratify all prior contracts. It is our understanding that although the commissioners meet in public session to authorize expenditure authority and specify amounts of money for particular purposes, the ultimate decision to enter into contracts and the selection of providers of goods and services is performed by state commission staff. Our legal counsel advised us that it is a well-accepted principle of law that a power given to a public official that involves the exercise of judgment or discretion may not be delegated to others without statutory authority. In this case, no statute authorizes the commissioners to delegate their contracting authority.

To ensure that the state commission staff may lawfully enter into or amend contracts on behalf of the commissioners, we recommended that the state commission seek appropriate legal counsel.

*State Commission's Action: Corrective action taken.*

The state commission has hired a chief counsel. In its one-year response, the state commission did not address whether the chief counsel had reviewed the bureau's recommendation and advised commission staff regarding the legality of delegating the authority for taking certain actions regarding contracts. However, in a separate letter dated December 5, 2007, the state commission indicated that its chief counsel reviewed this issue beginning in May 2007 and continuing through July 2007, when she rendered her legal opinion to the commission and its staff. However, when we requested a copy of the legal opinion, the chief counsel told us that it was an oral opinion and that she could not provide us any information related to her opinion, asserting attorney-client privilege.

She did, however, provide us with the state commission's current policy related to the approval of contracts and it remains as it was during our audit. Accordingly, it is the continued practice of the state commission to authorize all expenditures in excess of \$150,000, and to delegate to the executive director and his or her designee the authority to award and enter into any contracts that expend those funds.

# California Public Schools

## Compliance With Translation Requirements Is High for Spanish but Significantly Lower for Some Other Languages

REPORT NUMBER 2005-137, OCTOBER 2006

### *California Department of Education's response as of October 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits determine whether the California Department of Education (department) and California public schools are in compliance with California Education Code, Section 48985 (state translation requirements). This code section requires that when 15 percent or more of students enrolled in a public school speak a single primary language other than English, all materials sent to the parent by the school or school district must be provided in that language as well as in English. Specifically, the audit committee requested that we identify and evaluate the department's role, if any, in informing local education agencies of the state translation requirements and in monitoring and ensuring their compliance with these requirements. The audit committee also asked us, to the extent possible, to determine how pending legislation would affect the department's distribution of information and oversight of local education agencies' compliance with state translation requirements. Finally, the audit committee asked that we select a sample of districts or schools and identify and evaluate measures taken to include parents in their children's education, the process through which schools meet the state translation requirements, and the extent to which schools comply with these requirements. We found that:

### **Finding #1: Some districts do not perceive a demand for translations and the home language survey may overstate the need for translations.**

About half of California's 10,100 public schools had at least one primary language that required translations in fiscal year 2004–05, and we found that compliance for fiscal year 2005–06 was high for Spanish. Specifically, a survey requesting information about certain notices schools send to parents that we sent to 359 schools, to which 292 schools responded, indicated that schools are providing required Spanish translations for 4,136 of 4,534, or 91 percent of the notices for which we received responses, while for 1,134 notices we did not receive a response. However, compliance rates drop significantly for some of the languages other than Spanish. For example, our survey indicates that schools are providing Mandarin and Hmong translations for only 54 percent and 48 percent, respectively, of the notices for which we received a response. We did not receive responses regarding the translations of 36 and 18 notices in Mandarin and Hmong, respectively. We found a variety of reasons for these lower compliance rates. For example, 16 percent of the survey respondents were not aware of the state translation requirements. In addition, some schools may not be meeting state translation requirements because their districts may use incorrect methods to identify the languages requiring translations.

### **Audit Highlights . . .**

*Our review of the California Department of Education's (department) and California public schools' compliance with California Education Code, Section 48985 (state translation requirements) revealed the following:*

- » *Compliance with the state translation requirements is high for Spanish, but significantly lower for some other languages.*
- » *Some schools are unaware of this state law or may use incorrect methods to identify languages that require translations. In addition, some schools believe there is little demand for translated notices.*
- » *Although the department has a process that may assist schools in meeting these requirements, recently enacted legislation requires it to take a larger role in ensuring that schools comply with the state translation requirements.*
- » *The department created an electronic clearinghouse for multilingual documents, but it has not achieved much participation from school districts.*

As indicated by the results of our site visits, some school districts do not comply with state translation requirements because they believe there is little demand for translated notices. For example, San Diego Unified School District (San Diego) asserted that the main reason it stopped translating documents into Tagalog was a lack of requests for Tagalog translations from schools. Furthermore, although Tagalog was the primary language spoken at home by nearly 40 percent of the students enrolled at San Diego's Mary McLeod Bethune Elementary School during fiscal year 2004–05, a survey initiated by the principal in June 2006 resulted in only 5.6 percent of parents requesting that notices be sent home in Tagalog. Similarly, Cupertino Union Elementary School District generally does not provide Mandarin translations, even though this primary language is spoken by at least 15 percent of the students at several of its schools, because it perceives little demand for these translations. Finally, two districts indicated that in addition to low demand, some parents actually resented receiving translated documents. For example, both San Diego and Fountain Valley School District recalled instances in which parents had called the district to complain that they did not want to be sent translated documents in Tagalog and Vietnamese, respectively.

School districts should use a home language survey developed by the department to determine each student's primary language. Specifically, when parents enroll their children in a new school, the school district should administer the home language survey, which contains a series of questions to assist the school district in identifying the primary language spoken at home. However, the home language survey may overstate the need for translations because it does not account for parents who are fluent in English. The survey was designed to identify the primary language that a student speaks at home and to determine whether the district must assess the student's English proficiency using the California English Language Development Test. It was not designed to identify those parents who are bilingual. Consequently, this tool may overstate the need for translations for those parents whose primary language is not English but who are also fluent in English. Nevertheless, it is inappropriate for districts to assume that there are no parents who need documents translated into the languages that meet the 15 percent threshold under state law. Without asking parents whether they require translations, districts and schools have no way of knowing what the actual demand is and therefore cannot justify sending documents home in English only.

To ensure that translated notices are sent only to parents who need them, the department should modify the home language survey to include a question asking parents to indicate the language in which they would like to receive correspondence. To ensure that this modification does not conflict with current law, the department should seek legislation to amend state law to allow parents to waive the requirement that they receive translated materials in their primary language when they do not need such translations.

*Department's Action: None.*

- ➔ The department agrees that translated notices should be sent only to parents who need them. However, the department reports that after considering the expected benefits and related costs of making and supporting such determinations, it deems it more cost-effective to continue the existing processes of providing translated notices to parents.

**Finding #2: Although not extensively utilized, the clearinghouse for multilingual documents could become a useful tool.**

Pursuant to state law, the department created an Internet-based electronic clearinghouse for multilingual documents (clearinghouse) on which local education agencies and the department can post links to translated parental notices. The purpose of the clearinghouse is to provide increased access to translated documents, to assist local education agencies in meeting legal requirements for parental notification, and to reduce redundancy in document translation work. Launched in September 2005, the clearinghouse is an online resource designed to help local education agencies locate, access, and share parental notification documents that have been translated into languages other than English.

Through the clearinghouse, local education agencies voluntarily provide information regarding translations they have made and are willing to make available to others. The department hosts the clearinghouse on its Web site.

Despite the department's efforts to promote the clearinghouse, it has not achieved much participation from school districts. Specifically, 12 school districts and the department had posted links to translated notices on the clearinghouse as of mid-September 2006. In addition, 80 percent of the 230 translated documents available through the clearinghouse were available only in Spanish as of mid-September 2006. The value of the clearinghouse as a resource cannot truly be achieved without greater participation from school districts.

To increase the value of the clearinghouse as a resource for translated parental notices, the department should encourage school districts to form coalitions for the purpose of leveraging their combined resources to translate standard parental notices into the languages they have in common. In addition, the department should consider using its available funding to encourage districts to upload links to their translated documents, especially in languages that are currently underrepresented in the clearinghouse.

***Department's Action: Corrective action taken.***

In February 2007 the department sent a letter to county and district superintendents encouraging them to form translation consortia. The department also continues to promote the idea of translation consortia on its Web site and in presentations to professional and field organizations. Further, the department posted new data reports in the clearinghouse making it possible for districts to identify other districts with common translation needs. Finally, the department states that it is not authorized to use funds appropriated for the clearinghouse to pay districts as an incentive to enter translated documents into the clearinghouse. However, the department reports that it continues to use these funds to promote the clearinghouse at meetings and conferences to encourage districts to increase direct participation in the clearinghouse, and to provide promotional mailings to districts.





# Los Angeles Unified School District

## It Has Increased Administrative Positions for Various Reasons and Although Making Progress, Its Performance Evaluation and Salary-Setting Procedures for Managers Still Need Improvement

REPORT NUMBER 2005-132, SEPTEMBER 2006

*Los Angeles Unified School District's response as of October 2007*

The Joint Legislative Audit Committee (audit committee) asked the Bureau of State Audits (bureau) to evaluate the cost and position reductions resulting from the Los Angeles Unified School District's (LAUSD) 2000 and 2004 reorganizations. Also, the audit committee asked us to determine if community and parent access and participation had increased as a result of the 2000 reorganization. Further, we were asked to determine whether LAUSD periodically evaluates its administrative organization and whether it uses performance measures to evaluate staff. In addition, we were asked to analyze its salary-setting practices and determine whether high-level executive and administrative salaries continue to differ from similar positions in other school districts. Finally, the audit committee asked us to determine the extent to which LAUSD implemented recommendations from our July 2001 audit. In doing so, we noted the following findings:

### **Finding #1: LAUSD did not achieve lasting reductions in support services positions proposed in its 2000 and 2004 reorganizations, and has not adequately tracked their impact.**

Support services employees are those that do not interact directly with students but rather provide administrative and operational support for LAUSD. In 2000 LAUSD proposed to cut 835 support services positions at its central office, including shifting 501 of these positions to regional offices and schools. However, it cut only 664 positions, almost all of which were shifted to regional offices. In contrast, the 2004 reorganization plan proposed cutting 205 support positions but LAUSD actually cut 231 such positions. These staffing reductions were temporary because by December 2005 support services staffing had increased to levels that exceeded those existing prior to the 2000 reorganization. LAUSD indicates that many of these additional employees were needed to manage its school construction and information services efforts. We also noted that the salaries and benefits costs of LAUSD's support services positions increased at a faster rate than those same costs for the school services group—employees that are located at school sites—between fiscal years 1999–2000 and 2004–05.

When the LAUSD Board of Education (board of education) adopted the 2000 reorganization plan, it required the district to perform some follow-up studies. Although LAUSD has updated the board of education on changes to its administrative structure since the reorganization, it has not reported the financial changes resulting from the reorganization as the board has requested.

### **Audit Highlights . . .**

*Our review of the Los Angeles Unified School District's (LAUSD) reorganizations and its procedures for evaluating performance and setting salaries for managers found that:*

- » *Both the 2000 and 2004 reorganizations achieved staffing reductions, but by December 2005 support services staffing levels had increased to levels that exceed those existing before the 2000 reorganization, which LAUSD attributed to the need for additional employees to manage school construction and information services efforts.*
- » *Only four of the eight local district Parent/Community Advisory Councils (advisory councils) created by the 2000 reorganization plan are still operating, and LAUSD has not attempted to measure parent satisfaction with the remaining advisory councils.*
- » *Although LAUSD has established measurable benchmarks and goals for the superintendent, it has not replicated this practice with other managers responsible for improving student achievement.*
- » *LAUSD has addressed many of the concerns over the salary-setting practices that we noted in a July 2001 audit, but its Personnel Commission still does not have written procedures for determining salaries or appropriate documentation to support salary-setting recommendations for classified managers and executives.*

*continued on next page . . .*

» *Based on our survey of four of the nation's largest school districts, LAUSD's salaries are higher than those of comparable positions for more than half of the 27 high-level positions surveyed, but there may be factors that justify such differences.*

We recommended that when LAUSD makes major changes in its organizational structure with the intent of improving its operations, it consider ways to track the impact of these organizational changes on such factors as staffing and cost.

***LAUSD's Action: Partial corrective action taken.***

LAUSD previously indicated that its ability to more closely monitor organizational staffing changes would be greatly enhanced with the implementation of a new enterprise resource planning system called Business Tools for Schools. This system was to be implemented in three phases starting in July 2006. LAUSD states that implementation of the first phase had few problems, but that the second phase, which included human resources functions, has suffered many challenges after it was rolled out in January 2007. These challenges included payroll errors ranging from employees receiving no pay to receiving large overpayments. As a result, LAUSD decided to delay implementing the third phase until it resolves these problems.

LAUSD reports taking other steps to improve its ability to track the impact of organizational changes on its operations. In February 2007 the school board adopted a resolution requiring each division to use program effectiveness data to make decisions on resources allocations for the 2007–08 school year. Further, starting with the 2008–09 school year, LAUSD began preparing the budget earlier so that it could use data demonstrating program effectiveness in its budget decisions. Finally, LAUSD indicates the school board adopted a resolution in July 2007 requiring LAUSD to deliver a performance measurement plan to the board in late 2007. This plan is to provide measures to determine program and system effectiveness in both instructional and non-instructional areas. LAUSD reports creating a new division that will be responsible for establishing a system-wide performance measurement and accountability system.

**Finding #2: LAUSD did not fully develop the six performance metrics it had proposed when expanding its legal staff in 2001.**

LAUSD expanded its legal services staff in 2001 to improve the quality of legal services it receives. It proposed to evaluate this expansion through six performance metrics. Although LAUSD tracks data related to the metrics, it did not fully develop them by setting quantifiable goals and measuring itself against those goals. Without establishing such goals and targets, LAUSD lacks an objective way to determine which goals it is meeting and which ones it is not, which will aid in reevaluating its operations.

We recommended that LAUSD develop performance metrics with goals and quantifiable benchmarks to evaluate itself on its progress in achieving planned improvements.

***LAUSD's Action: Corrective action taken.***

LAUSD states that beginning in fiscal year 2006–07 it developed performance objectives relating to each of the six performance measures included in its legal reorganization plan. Each of the performance objectives establishes specific and measurable goals, which, if properly monitored, should allow LAUSD to measure whether it is making progress against the six performance measures.

**Finding #3: Parent/Community Advisory Councils (advisory councils) are not serving the purpose that the 2000 reorganization plan intended.**

The 2000 reorganization plan created advisory councils at each local district to provide parents and community members with access to local district administrators and the ability to provide feedback on district policy. However, only four of the eight local districts currently have active advisory councils and only two are functioning as the plan intended. The remaining two serve to receive information from district administrators. Additionally, LAUSD has not attempted to measure the impact that the advisory councils may have on access to district administrators and the policy-making process.

If LAUSD decides to continue with the advisory councils, we recommended that it evaluate why advisory councils have not met the objectives in the 2000 reorganization plan, develop more specific guidelines on what they should accomplish, define the local districts' roles, and develop a mechanism to monitor and oversee them.

***LAUSD's Action: Pending.***

LAUSD indicates it has decided to continue using advisory councils. It is reviewing and developing, as needed, additional guidance on the composition and purpose of the councils and the local districts' role in assisting and monitoring the councils.

**Finding #4: LAUSD has not established performance benchmarks or maintained performance evaluations for the majority of its executive managers.**

The board of education has established specific, easily measurable goals for the superintendent, but the superintendent has not replicated this practice with LAUSD's local district superintendents or other executive managers. A January 2006 review of LAUSD by a peer group of other school administrators—the Council of the Great City Schools—also found little evidence that district staff were evaluated explicitly on their ability to attain specific goals and benchmarks or faced consequences for failing to meet performance goals. As a result, LAUSD may not be able to assess the performance of certain executive managers effectively because it has not established specific and measurable performance standards.

Further, of the 28 evaluations for executive managers we requested, LAUSD was able to provide performance measures only for the superintendent, and evaluations for two key administrators. LAUSD indicates that some performance evaluations were not available because the superintendent does not perform written evaluations and others were unavailable because the records could not be located or had been destroyed. Performance evaluations can be useful tools to measure and direct the progress of LAUSD's efforts to improve student outcomes. Without copies of evaluations to draw on, LAUSD may limit its ability to track and hold executive managers accountable for their performance over time.

To measure the effectiveness of executive managers, we recommended that LAUSD establish specific, measurable, and reasonable goals for these administrators that are aligned with the district's goals and hold them accountable for their performance. When establishing these goals, LAUSD should do so in conjunction with implementing the January 2006 peer group's recommendations. We also recommended that LAUSD evaluate key administrators in writing based on their ability to meet their goals, and ensure that it retains these written evaluations for a reasonable time period.

***LAUSD's Action: Partial corrective action taken.***

In line with the peer group's recommendations, LAUSD reports developing draft performance objectives and measures aligned with its mission and the superintendent's goals for eight central office senior instructional managers and senior-level instructional positions at each of the local districts. In addition, LAUSD indicates that in January 2007 it began placing interim performance measures into each senior management contract submitted to the school board for ratification. As part of the process to establish a performance measurement system, LAUSD anticipates that job descriptions with measurable goals for these positions will be implemented in the 2008–09 school year and that the district's evaluation process will be updated during the 2009–10 school year.

**Finding #5: LAUSD's Personnel Commission does not have written procedures for setting classified employee salaries and it does not maintain complete records of its salary determination process.**

Classified employees are those whose positions do not require an education-related certification. The Personnel Commission relies on several methods to set salaries for LAUSD classified employees, but it lacks written procedures for determining salaries to ensure that its staff applies these methods consistently. Further, the written guidelines it does have are vague and are not policy that staff must follow. It also lacked documentation to support the salary recommendations for 11 of the 15 salary-setting decisions we reviewed for classified administrators. The lack of comprehensive written procedures and insufficient documentation leaves the Personnel Commission vulnerable to criticism that the process it uses to set salaries lacks objectivity, thoroughness, and consistency.

We recommended that to avoid the appearance of subjectivity and lack of thoroughness, LAUSD's Personnel Commission should establish written guidelines for setting salaries and ensure that it consistently follows these processes for determining administrative compensation. It should also maintain complete records of its salary determination process, including methods and information used to support its decisions.

***LAUSD's Action: Corrective action taken.***

As part of an overall plan to standardize and consolidate the salary assignment process, LAUSD indicates that the Superintendent's Compensation Advisory Council, which began meeting in March 2007, now reviews salary-setting decisions for both classified and certificated positions to make recommendations to the superintendent and the Personnel Commission. It notes that all reports presented to the council and the Personnel Commission use a standard format. Also, LAUSD indicates that the Personnel Commission has updated its guidelines for conducting salary surveys, including augmenting the criteria used for salary recommendations and documenting its methodology.

**Finding #6: LAUSD has only limited documentation to support the salary levels of executive-level administrators that the superintendent and board of education determine.**

The superintendent determines salaries for executive-level certificated positions hired on employment contracts, and the board of education determines salaries for executive-level positions that report to it. However, both the superintendent and the board of education lack written procedures for determining these salaries and did not maintain detailed documentation to support salary levels set for the 12 positions we reviewed. However, based on our interviews and review of the limited documentation that existed, they appear to use reasonable practices in their salary-setting decisions.

We recommended that LAUSD maintain complete records to support salary determinations for executive-level administrators to show that these determinations are based on reasonable and objective criteria.

***LAUSD's Action: Corrective action taken.***

LAUSD indicates that it has implemented procedures to ensure that appropriate documentation is retained to support the salary levels of executive-level administrators that the superintendent and board of education establish. These steps include integrating those salary levels into a new master salary schedule, developing a new point-factor system for evaluating these positions' salary levels, and creating file storage protocols for these salary-setting procedures.

**Finding #7: LAUSD has taken steps to implement most of the recommendations from our July 2001 audit.**

In July 2001 we issued a report titled *Los Angeles Unified School District: It Has Made Some Progress in Its Reorganization but Has Not Ensured That Every Salary Level It Awards Is Appropriate* (2000-125). The report concluded that LAUSD had made some progress in implementing its 2000 reorganization plan (plan); however, it has not shifted to local districts the level of authority over financial resources or instructional programs described in its plan. Also, we found that some administrative management positions earned substantially more in comparison to positions at other school districts, while a few positions earned less. Because it lacked formal guidance for determining what salaries to award, we concluded that the propriety of some of these compensation levels was questionable. Furthermore, we found that LAUSD lacked updated job descriptions for these positions and was unable to provide adequate documentation detailing how it set compensation levels for some positions.

During our current audit we found that LAUSD has fully implemented most of the July 2001 audit's recommendations, but it either has not implemented or only partly implemented our recommendations concerning performance measurements and salary-setting procedures as previously noted in findings 4, 5, and 6.



# Department of Education

## Its Flawed Administration of the California Indian Education Center Program Prevents It From Effectively Evaluating, Funding, and Monitoring the Program

REPORT NUMBER 2005-104, FEBRUARY 2006

### *Department of Education's response as of March 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits review the Department of Education's (department) administration of the California Indian Education Center program (program), how it determines funding for the California Indian Education Centers (centers), and how it evaluates them. Specifically, the audit committee asked us to determine the department's roles and responsibilities related to the centers and to review and evaluate the department's existing policies, procedures, and practices for administering the program and monitoring the centers. The audit committee was also interested in any written procedures the department has developed to guide program administration. In addition, it asked us to review the department's funding structure for the program and how it appropriates funds to administer the program.

Further, the audit committee requested that we assess the reasonableness of the department's uses of program funds; determine whether it has directed sufficient resources to the program in general and sufficient management attention to completing the program evaluation report that was due to the Legislature on January 1, 2006; and review the department's document retention policies and practices. Finally, the audit committee asked us to review and evaluate the department's process for allocating and disbursing funds to the centers. We found that, despite established guidance, the department has not adequately administered the program and consequently cannot ensure that the program is successfully meeting the goals established in law or the needs of the communities it serves.

### **Finding #1: The department does not know how the program is performing.**

Despite established guidance, the department has not adequately administered the program and consequently cannot ensure that the program is successfully meeting the goals established in law or the needs of the communities it serves. To address the challenges facing American Indian students enrolled in California's public schools—low academic achievement at all grade levels, high dropout rates, and few students continuing their education beyond high school—the Legislature established the program in 1974. The legislation indicated that the centers should serve as educational resources for American Indian students, their parents, and the public schools. In addition, to guide the operation of the centers, the Legislature established a set of goals, such as improving the academic achievement, self-concept, and employment opportunities of American Indian students and adults. From its initial 10 centers funded by a total of \$400,000 in grants,

### **Audit Highlights . . .**

*Our review of the management of the California Indian Education Center program (program) by the Department of Education (department) found that:*

- » *Because the department has largely ignored the existing guidance for administering the program, it cannot ensure that the program is successfully meeting the established goals or the needs of the communities it serves.*
- » *The department did not ensure that California Indian Education Centers (centers) reported all the annual data required by law to measure performance.*
- » *The department has no record of the centers' assessments of needs called for by the guidelines adopted by the State Board of Education and thus has no way of knowing whether the services the centers assert they provide are those most needed by the populations they serve.*
- » *Though submitted to the Legislature on time, the department's evaluation of the program lacks sufficient analysis to adequately support its recommendations to improve the program.*
- » *The department is unable to justify its basis either for selecting centers to receive funding or for determining the annual amount of funding it grants each center.*
- » *The department has not always promptly disbursed funds to the centers.*

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» *The department lacks a monitoring process to ensure that centers spend funds appropriately, pursue program goals, and report accurate data.*

the program has grown to comprise 30 centers that annually receive more than \$4.4 million in total funding as of fiscal year 2005–06. If not reauthorized, the program is set to end on January 1, 2007.

The department is required by state law to administer and oversee the program and receives guidance from legislation as well as internal policies. For instance, state law requires the department to collect data annually to measure the academic performance of the students the centers serve and how well the centers are meeting the goals established by law. Additionally, although no regulations govern the program, state law requires the State Board of Education (board) to adopt guidelines for selecting and administering the centers. The guidelines the board adopted in 1975 require, among other things, that centers design their programs after assessing the needs of their respective communities. Internal guidance comes from the department's 2001 Grant Administration Handbook (handbook), which guides the administration of programs funded by grants similar to those used in this program. The handbook stipulates that the department establish a competitive process to objectively select grant recipients, a monitoring plan to ensure that grant recipients appropriately implement the program, and a document retention and filing process to effect stable program administration and clear communication between the department and the centers.

However, the department has largely ignored the existing guidance for administering the program and therefore has little means of determining program effectiveness. For example, until 2005 the department did not ensure that centers reported the annual academic performance data of their students.

Another indication of the department's flawed administration of the program is its inability to fully justify its basis either for initially selecting centers to receive funding or for determining the annual amount of funding it grants each center. According to the handbook, it should select grant recipients following a competitive process, which includes an objective scoring methodology and independent raters. However, the department could not demonstrate that it used a competitive process to select the most recent centers currently funded. Further, although program staff state that the department's sole basis for computing the amount that each center receives is the amount granted in the previous fiscal year, it has not consistently followed that method.

Further, the department has not always promptly disbursed funds to the centers. Despite the department's informal policy that it would issue the first of three annual installment payments to centers with approved applications an estimated six to 10 weeks after the governor signs the state budget, in fiscal year 2003–04 the centers did not receive their first grant allocations until December—18 weeks after the budget was approved.

Finally, the department lacks a monitoring process to ensure that centers spend funds appropriately, pursue program goals, and report accurate data to the department. Without operating policies and procedures outlining how staff should consistently administer the program, the department may create confusion among the centers.

The department indicates that it is attempting to improve its administration of the program by proposing more detailed legislation to reauthorize the program and by developing a plan for monitoring the centers, but these efforts are too preliminary for us to assess.

To ensure that it administers the program clearly, consistently, and effectively, we recommended that the department develop operating policies and procedures specific to the program and train staff in their application. The policies and procedures should include the following:

- A description of the data that centers must annually report to measure program performance and a standardized format for reporting to allow the department to effectively aggregate and consolidate the data for reports to the Legislature and other interested parties. Further, the department should outline the consequences for failing to submit the data.
- An equitable process to select centers to receive grant awards and determine their respective funding amounts.
- A set time frame that it adheres to for disbursing payments to the centers once their applications are received and approved. The time frame for the first payment can be expressed as a set number of weeks after enactment of the state budget for centers with approved applications.
- A centralized filing system that contains all documents pertinent to the grant program, including documentation of the technical assistance provided to the centers.
- A monitoring process and plan to ensure that reported fiscal and program information is accurate and complete, including a process for corrective action and departmental follow-up for noncompliance.
- A set schedule indicating how long program records are to be kept.

***Department's Action: Partial corrective action taken.***

The enactment of Senate Bill 1710 (SB 1710) mandated the formation of an American Indian Education Oversight Committee (AIEOC) to provide input and approve regulations for the administration of the centers. In accordance with SB 1710, the AIEOC members were selected and the first meeting was held on January 22, 2007.

SB 1710 also mandated new reporting requirements, a competitive application process, and a process for program and fiscal monitoring. The department developed and presented draft regulations and guidelines for the AIEOC's consideration and approval at its meeting scheduled in February 2007 and, if approved, will take effect beginning in fiscal year 2007–08. For fiscal year 2006–07, the department will continue to use the following operational policies and procedures:

- Developing the fiscal year 2006–07 application packets that instruct the centers on what they are required to report. Training on the application process was provided to center directors in January and May 2006.
- Revising the end-of-year report to address all statutory reporting requirements after receiving input from the center directors. The report was designed so that the information could be aggregated and consolidated, and clear consequences were communicated for failure of the centers to report the information required.
- When SB 1710 is enacted, the department stated it would follow policies and procedures in accordance with the new statute for selecting centers to receive grant awards and determine funding amounts.

- The department indicated that it had included set time frames within which it would make periodic payments to the centers in a letter to the centers' directors. However, the letter to which the department refers to does not contain this information.
- Establishing a centralized filing system for the center grant program.
- Scheduling 10 centers for monitoring visits during fiscal year 2006–07, of which seven were completed. The department was silent concerning a process to ensure corrective actions are taken when needed and followed up for compliance.
- Approving a record retention schedule that indicates how long various records will be retained.

**Finding #2: With staff unaware of guidelines requiring needs assessments, the department does not know if centers have designed their programs to meet community needs.**

The department has no record of the centers' needs assessments on file and thus has no way of knowing whether the services the centers assert they are providing are the services most needed by the populations they serve.

To ensure that centers use program funds effectively, we recommended that the department ensure that they periodically conduct needs assessments as required by the guidelines adopted by the board.

If the Legislature decides to reauthorize the program, we recommended that it consider requiring annual or biannual reports from the department to monitor the progress of the program and supplement the report the department submitted to the Legislature by the due date of January 1, 2006. Alternatively, the Legislature might want to extend the life of the program in one- or two-year increments to augment the data available for evaluation.

***Department's Action: Pending.***

SB 1710 requires that centers conduct and submit needs assessment results as part of the 2007 through 2012 application cycle. The draft regulations submitted to the AIEOC by the department include a requirement that each center submit a needs assessment as part of its application.

***Legislative Action: None.***

SB 1710 extended the program until January 1, 2012. However, the Legislature did not choose to implement our suggestions regarding our recommendation for considering requiring the department to submit annual or biannual reports monitoring the progress of the program or, alternatively, extending the program in one- or two-year increments.

# California K-12 High-Speed Network

## The Network Architecture Is Sound, but Opportunities Exist to Increase Its Use

REPORT NUMBER 2005-116, JANUARY 2006

*The Department of Education's response as of January 2007*

The California K-12 High-Speed Network (High-Speed Network) connects the vast majority of kindergarten through 12th grade (K-12) schools, school districts, and county offices of education statewide to each other, to California's universities and community colleges, and to various Internet service providers that provide access to the commodity Internet. The Joint Legislative Audit Committee (audit committee) requested the Bureau of State Audits (bureau) to determine whether the State is efficiently using its resources by supporting the maintenance of the High-Speed Network. Specifically, the audit committee asked the bureau to determine the roles and responsibilities of the various entities involved since the inception of the High-Speed Network project, to identify the network's funding sources and determine whether there are any limitations or restrictions on the use of this funding or on the disposition of unused funds, and to review the methods used to allocate the costs of the High-Speed Network to determine if they are reasonable. In addition, the audit committee instructed the bureau to review the cost, usage, and, to the extent possible, benefits of the High-Speed Network and to determine whether these costs and benefits are comparable to those of other Internet service providers. The audit committee also directed the bureau to examine any information the State, consortium, or other entity has used to determine whether the benefits of the network outweigh its costs. Further, the bureau was asked to evaluate the reasonableness of any options or plans the State or consortium of county offices of education considered to maximize the use of the High-Speed Network. Moreover, the audit committee requested that the bureau determine the ownership rights to purchases made or services related to the High-Speed Network, including but not limited to intellectual property rights and how the State may exercise those rights. Finally, the bureau was asked to review and evaluate the laws, rules, and regulations significant to the objectives stated above.

### **Finding #1: From the beginning, state law has provided limited guidance and oversight for the High-Speed Network project.**

Between fiscal years 2000–01 and 2003–04, the budget control language that appropriated more than \$93 million to the University of California (UC) for the High-Speed Network stated only that the purpose of the funding was for “expanding the Internet connectivity and network infrastructure for K-12.” This budget control language did not impose any more specific requirements or controls on the expenditure of these funds, nor did the Legislature enact legislation to further define the parameters of this project or what was meant by “Internet connectivity and network infrastructure for K-12.” Therefore, it is difficult to determine if the Legislature got what it sought in appropriating the funds.

### **Audit Highlights . . .**

*Our review of the California K-12 High-Speed Network (High-Speed Network) found that:*

- » *The State most likely spent less on the building and operation of the High-Speed Network by expanding the existing infrastructure used by the University of California and other higher education institutions than it would have spent for a separate network with comparable services.*
- » *A study conducted by our technical consultant in 2005 found that the High-Speed Network has adequate bandwidth for potential growth but is not overbuilt. Furthermore, our technical consultant found no compelling technical or financial reason to abandon the existing High-Speed Network.*
- » *Because of the lack of specific performance measures in state law and because the Imperial County Office of Education (ICOE), which currently administers the project, is in the early stages of developing a suitable plan for measuring the success of the High-Speed Network, it is difficult to determine whether the network accomplishes the Legislature's goals.*
- » *As of June 30, 2005, the Corporation for Education Network Initiatives in California (CENIC), the nonprofit that built and currently operates the network, held \$13.6 million in High-Speed Network funds and it expects to receive an additional \$3.6 million related to telecommunication discounts in fiscal year 2005–06. These funds are being used to keep the network operating in fiscal year 2005–06 or are held for future equipment replacement.*

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» *Opportunities exist for ICOE to strengthen its agreements with CENIC to better protect the State's interests. Specifically, its agreements lack detailed service-level agreements, do not ensure that it retains ownership of tangible nonshared assets, and do not ensure that interest earned on advance payments made to CENIC or funds held by CENIC on its behalf accrue to the benefit of the High-Speed Network.*

In the Budget Act of 2004, the Legislature effectively transferred the responsibility for managing the Internet connectivity and infrastructure for K-12 educational institutions from UC to the California Department of Education (Education). Although the Legislature shifted control of this project from UC to Education and ultimately to the Imperial County Office of Education (ICOE), it still has not enacted legislation that clearly prescribes the goals to be accomplished using these funds. Until legislation is enacted, Education cannot be certain that the design and use of the High-Speed Network are achieving the Legislature's desired outcomes.

We recommended that to ensure that the High-Speed Network meets its expectations, the Legislature should consider enacting legislation that prescribes the specific goals and outcomes it wants from the High-Speed Network project.

***Legislative Action: Legislation enacted.***

Legislation (Assembly Bill 1228) was enacted on September 28, 2006, that requires the Superintendent of Public Instruction (Superintendent) to, among other things, establish a High-Speed Network advisory board. The legislation requires the advisory board to meet quarterly and to recommend policy direction and broad operational guidance to the Superintendent and the Lead Education Agency responsible for administering the High-Speed Network on behalf of the Superintendent. The advisory board, in consultation with the Lead Education Agency, shall develop recommendations for measuring the success of the network, improving network oversight and monitoring, strengthening accountability, and optimizing the use of the High-Speed Network and its ability to improve education. The advisory board shall report its recommendations to the Legislature, the governor, the Department of Finance, the Legislative Analyst's Office, and the Office of the Secretary for Education by March 1 2007. It is the Legislature's intent that the report identifies and recommends specific annual performance measures that should be established to assess the effectiveness of the network.

**Finding #2: The current agreement between ICOE and the Corporation for Education Network Initiatives in California (CENIC) could be strengthened to better protect the State's interests.**

UC contracted with CENIC to carry out the High-Speed Network project. After its selection as the lead agency in 2004, ICOE entered into agreements with CENIC under terms that were substantially similar to UC's agreement. The first was executed December 1, 2004, and the second was executed June 24, 2005, and became effective July 1, 2005, after the first agreement expired. Both agreements continue to lack service-level agreements. A service-level agreement describes the specific level of service a vendor is required to provide and typically provides a penalty if that level is not provided. The lack of a service-level agreement makes it difficult to monitor CENIC's

performance. Additionally, the agreements fail to contain provisions that fully address the issue of the State's ownership of assets and that require CENIC to limit the use of interest earned on advance payments it receives related to the High-Speed Network.

We recommended that to ensure that the High-Speed Network is appropriately managed, Education should ensure that ICOE does the following:

- Develops a comprehensive and extensive set of service-level agreements based upon applications to be delivered via the High-Speed Network project.
- Requests that CENIC provide a master service-level agreement for its review.
- Includes the appropriate service-level agreements in its ongoing contracts with CENIC and other service providers for the High-Speed Network, using industry standards.

To ensure adequate protection of the State's interest in tangible, nonshared assets, we also recommended that Education should direct ICOE to transfer ownership of those types of assets to the State, to the extent that ICOE is able to bargain for the provision.

Finally, we recommended that to ensure that the interest earned on advance payments made to CENIC are used to benefit the High-Speed Network, Education should direct ICOE to amend its agreement with CENIC to stipulate the allowable use of the interest earned.

***Education's Action: Corrective action taken.***

Legislation (Assembly Bill 1228) was enacted on September 28, 2006, that requires the Lead Education Agency to enter into appropriate contracts for the provision of high-speed, high-bandwidth Internet connectivity, provided such contracts secure the necessary terms and conditions to adequately protect the interests of the State. The terms and conditions are to include, but are not limited to, all of the following:

- (a) Development of comprehensive service level agreements.
- (b) Protection of any ownership rights of intellectual property of the State that result due to its participation in the High-Speed Network.
- (c) Appropriate protection of state assets acquired due to its participation in the High-Speed Network.
- (d) Assurance that appropriate fee structures are in place.
- (e) Assurance that any interest earned on funds of the State for this purpose are used solely to the benefit of the project.

Education stated that ICOE has not entered into any agreements with service providers, and that, if and when it does, those agreements will include the appropriate service-level agreement terms. Education also stated that ICOE and CENIC have reached agreement on both a master-service level agreement and a service-level agreement for the services CENIC delivers to the High-Speed Network. Our review of the first amendment to the master agreement executed by ICOE and CENIC on January 30, 2007, found that the amendment does contain these provisions. Additionally, the amendment contains language that will require CENIC to transfer ownership of tangible non-shared assets to the State if CENIC ceases to serve K-12 entities. Finally, Education reported that fiscal year 2006–07 budget control language requires “any interest earned on state monies is used for operating the CalREN serving the UC, CSU, CCC, and K-12 segments. Any segment-specific cash reserves held by CENIC for an individual segment shall be held separately and accrue interest to that segment.” The amended agreement between ICOE and CENIC stipulates that interest earned be used in accordance with this budget control language.

**Finding #3: CENIC's charges for commodity Internet use could have been lower.**

CENIC provides connections to Internet service providers, enabling High-Speed Network users to access the commodity Internet. Although the annual fees it charges for this access are lower than state negotiated pricing, it could further reduce the amount it charges users by consistently using funds left over from prior-year fees to offset the next year's cost of providing the service.

CENIC's commodity Internet service, which became effective during fiscal year 2002–03, has generated a surplus each year; as of June 30, 2005, this surplus was \$2.1 million. The commodity Internet service model approved by its board in June 2001 specifically states that the fixed rate charged per unit of commodity Internet usage should be set to enable CENIC to recover the entire cost of providing the services, should be reviewed semiannually, and should be adjusted downward if cost recovery is projected to be excessive. CENIC did use a portion of its fiscal year 2002–03 surplus revenues to reduce its per-unit rate in fiscal year 2003–04 by 38 percent. For fiscal year 2004–05, however, although CENIC reduced its per-unit rate by a further 25 percent compared to its fiscal year 2003–04 per-unit rate, it did not use the surplus revenues to do so. It achieved its reduction by reducing its estimated annual costs and increasing the minimum usage commitments for commodity Internet service for certain users. We believe that further reductions would have been possible if CENIC had also used a portion of the surplus.

We recommended that to ensure that CENIC's per-unit rate for access to the commodity Internet is closer to its actual cost to provide the service, Education should require ICOE to amend its agreement with CENIC to stipulate that to the extent possible, CENIC should use its surplus Internet service program revenues from each year to offset the per-unit rate that it sets the following year. ICOE should also stipulate in its agreement that if CENIC is unable to apply the surplus revenue due to a change in its financial position, that CENIC should provide ICOE with documentation to support its inability to do so.

***Education's Action: Corrective action taken.***

Education reported that ICOE is currently a participating member of CENIC's Business Advisory Council and board. Additionally, K-12 representatives are participating members of CENIC's audit and finance committees. Education believes that this participation on behalf of K-12 provides equal input (compared with other public segments participating in CENIC) into CENIC's decisions regarding rates and the use of surplus revenues. Finally, the first amendment to the master agreement executed by ICOE and CENIC indicates that for fiscal year 2006–07 CENIC now recovers the fixed portion of commodity Internet costs using a flat rate contribution by the participating entities. Consequently, CENIC was able to reduce its per-unit rate for the entities' actual usage of the commodity Internet from \$95 to \$29, a reduction of almost 70 percent.

**Finding #4: CENIC has a portion of the High-Speed Network's funds in its consolidated equipment replacement account.**

During its September 12, 2002 meeting, CENIC's board approved the following three action items related to the High-Speed Network funds held by CENIC for equipment replacement: (1) the creation of a consolidated designated equipment replacement account as part of its CalREN account, the transfer of \$5.7 million in High-Speed Network funds from an account designated solely for the High-Speed Network into this new account, and the transfer of future High-Speed Network equipment replacement funds into this new account; (2) the transfer of \$970,000 of the interest income in an account designated solely for the High-Speed Network into the consolidated designated equipment replacement account; and (3) the transfer of \$6 million from the consolidated designated equipment replacement account into a one-year certificate of deposit with a bank, the borrowing of \$6 million from the same bank, and the use of the certificate of deposit as collateral against the loan. According to CENIC's accounting records, on June 30, 2004, an additional \$1.5 million was placed into the consolidated designated equipment replacement reserve account using state appropriations for the High-Speed Network.

The board's decision to include the High-Speed Network's equipment replacement funds into a consolidated account appears inconsistent with CENIC's agreement with UC, which requires CENIC to set up and use a separate financial account for the High-Speed Network funds and to not use that account to hold or disperse any other funds. The purpose of establishing a separate financial account for the High-Speed Network funds is to ensure that these funds are being used to benefit the project. The transfer of these funds to CENIC's consolidated account makes it difficult to identify those funds belonging to the High-Speed Network.

Further, CENIC could not provide us with a technology refresh plan. An effective technology refresh plan establishes the points along the service life of a product or system at which it is optimal to change system components. Without a technology refresh plan, we do not believe CENIC can support its assertion that it needs the full \$7.2 million, or that only \$4.9 million represents funds for the replacement of equipment specific to the High-Speed Network.

Finally, although CENIC is holding \$7.2 million in High-Speed Network funds for equipment replacement, any interest earned on this money does not accrue to the benefit of the High-Speed Network. Specifically, its agreement with ICOE does not contain a provision that limits the use of any interest earned on state appropriations to the High-Speed Network. By including this provision in its agreement, ICOE can ensure that the project benefits directly from any interest earnings.

To ensure that High-Speed Network equipment replacement funds are used to benefit the K-12 education community, we recommended that Education should direct ICOE to request that CENIC reestablish a reserve for equipment replacement that is in an account solely for the High-Speed Network. Further, CENIC should consult with ICOE on the development of a technology refresh plan, which ICOE should use to establish its own equipment replacement funds for the High-Speed Network. Finally, ICOE should amend its agreement with CENIC to stipulate that interest earned on the funds held in the High-Speed Network's equipment replacement account accrues to the benefit of the High-Speed Network.

***Education's Action: Corrective action taken.***

Our review of ICOE's amended master agreement with CENIC found that it requires K-12 equipment replacement funds to be segregated into a separate account. Additionally, ICOE and CENIC developed a 2006–2009 technology refresh plan in January 2007 to address the appropriate use of the funds for the replacement of equipment specific to the High-Speed Network. Education stated that upon the advisory board's approval, and contingent upon available funding, the implementation of the plan will occur over two years and modifications will be made as necessary in response to industry changes. Finally, Education reported that the fiscal year 2006–07 budget control language requires that "any interest earned on state monies is used for operating the CalREN serving the UC, CSU, CCC, and K-12 segments. Any segment-specific cash reserves held by CENIC for an individual segment shall be held separately and accrue interest to that segment." The amended agreement between ICOE and CENIC stipulates the use of interest earned, including interest earned on funds held in an equipment replacement account, in accordance with this budget control language.

**Finding #5: ICOE's agreement does not require CENIC to increase the amount that it holds on behalf of ICOE by any interest earned on funds related to E-rate or California Teleconnect Fund discounts.**

In accordance with their contract executed on December 6, 2004, ICOE and CENIC plan to use unspent E-rate and California Teleconnect Fund discounts to continue the operation of the High-Speed Network in fiscal year 2005–06. The contract states, "To the extent that program revenue balances generated by E-rate and California Teleconnect fund discounts from fiscal year 2002–03, or prior fiscal years exist, such balances will be held by CENIC to help meet cash flow needs." The contract further stipulates, "Such funds will be held in trust by CENIC for the benefit of the High-Speed Network and



will not be expended without advance consultation with ICOE.” Finally, ICOE and CENIC agreed that any E-rate and California Teleconnect Fund discounts for fiscal year 2004–05 circuit expenditures received in that year shall be held by CENIC and applied against the network circuits, backbone fees, and related costs in fiscal year 2005–06.

E-rate—or, more precisely, the Schools and Libraries Universal Service Support Mechanism—is a federal program that provides discounts to assist most schools and libraries in the United States to obtain affordable telecommunications and Internet access. Eligible schools can receive discounts ranging from 20 percent to 90 percent. All customers eligible to receive E-rate discounts for telecommunication services can also receive discounts from the California Public Utilities Commission, via the California Teleconnect Fund program. The discounts are 50 percent and must be applied after deducting the E-rate discount.

As of December 2005, according to CENIC’s estimate, a total of \$10 million was available for use toward the fiscal year 2005–06 High-Speed Network operational costs. However, ICOE’s agreement does not require CENIC to increase the amount that it holds on behalf of ICOE by any interest earned on the funds. Until ICOE modifies its agreement with CENIC, the State will continue to lose the ability to use interest earnings to reduce High-Speed Network costs.

We recommended that to ensure that any interest earnings received for E-rate and California Teleconnect Fund discounts accrue to the benefit of the High-Speed Network, Education should direct ICOE to amend its agreement and require CENIC to credit any interest earnings to the High-Speed Network project. Additionally, ICOE should require CENIC to provide a detailed accounting of E-rate and California Teleconnect Fund discounts so that it can verify that it received the appropriate amount of interest.

***Education’s Action: Corrective action taken.***

Education reported that the fiscal year 2006–07 budget control language requires that “any interest earned on state monies be used for operating the CalREN serving the UC, CSU, CCC, and K-12 segments. Any segment-specific cash reserves held by CENIC for an individual segment shall be held separately and accrue interest to that segment.” The amended agreement between ICOE and CENIC stipulates the use of interest earned, including interest earned on E-rate and California Teleconnect Fund discounts, in accordance with this budget control language.

The amended master agreement requires CENIC to keep detailed records and to work closely with ICOE to monitor and track revenues and interest related to E-rate and California Teleconnect Fund discounts. Further, Education stated that if CENIC holds E-rate and California Teleconnect Fund discounts on behalf of K-12 in the future, periodic audits will be conducted to ensure the appropriate amounts of revenue are received and that, if such funds are retained by CENIC instead of paid over immediately to ICOE, appropriate interest is credited to K-12.

**Finding #6: Although ICOE has worked to increase awareness of content it postponed awarding grant funds to develop content hosted on the High-Speed Network.**

As lead education agency for the High-Speed Network, ICOE is responsible for technical oversight of the project, financial and administrative services, collaboration and coordination with other agencies and projects, and the advancement of network uses.

ICOE currently provides certain videoconferencing services at no cost to schools in California that are connected to the High-Speed Network. Videoconferencing is a tool that connects two or more locations with interactive voice and video. Additionally, in November 2004, ICOE began operating its own High-Speed Network Web site that includes links and information related to learning resources, such as the UC College Preparatory Initiative, and the California Digital Library. Moreover, ICOE’s application coordination committee (application committee) is evaluating some methods related to

linking with academic content, from various sources, that are aligned with the California content standards for placement on the High-Speed Network. For example, ICOE plans to identify and work with academic content providers to develop strategies for placing their content on the network.

ICOE created the Advancing Network Uses Grant program to support the development and sharing of applications and learning resources that meet the critical needs of California's schools and that make good use of the benefits of the High-Speed Network. However, ICOE did not award the grant funds of roughly \$650,000 in fiscal year 2005–06 as planned because it was uncertain as to whether the High-Speed Network would receive state funding in fiscal year 2005–06. According to ICOE, should state funds be appropriated in the future, and provided enough funding exists, it will award funds to the winners of that previous grant competition.

Finally, both CENIC and ICOE have made an effort to increase the usage of the High-Speed Network by assisting schools and school districts in connecting their LANs to existing node sites, which is commonly referred to as the last mile connection. However, in June 2005, given the uncertainty of the fiscal year 2005–06 budget, ICOE decided to table the awarding of \$1.1 million in last mile grants. ICOE estimated that it would cost roughly \$10 million to connect the remaining roughly 500 schools and school districts without any connection. It further stated that when funds become available, it would determine how best to proceed with the last mile grant program.

We recommended that to maximize the benefits of the High-Speed Network, Education should ensure that ICOE does the following:

- Continue its efforts to implement statewide videoconferencing.
- Continue the efforts of its application committee to identify academic content and application uses to place on the High-Speed Network.
- Continue with its plans to fund the Advancing Network Uses Grant applicants.
- Proceed with its last mile grant program.

***Education's Action: Partial corrective action taken.***

Education stated that ICOE has implemented a fully functional statewide videoconferencing system. Education also stated that the application committee continues to assist the High-Speed Network project staff in identifying applications and Web-based resources to support teaching and learning.

Finally, Education stated that the Budget Act of 2006 did not include funding for the Advancing Network Uses Grant and last mile grant program, but it will continue to work with resource providers and to seek ways to cost-effectively connect schools and districts across the State. During fiscal year 2006–07, the High-Speed Network project staff collected up-to-date information on the state of connectivity in California. If resources are available, the project staff will be able to prioritize location for the last mile grant program.

**Finding #7: ICOE is in the early stages of developing a suitable plan for evaluating the success of the High-Speed Network.**

Although Education requires administrators of certain education technology projects to work with ICOE on the High-Speed Network project, ICOE is in the early stages of developing a method to evaluate the statewide success of the High-Speed Network. According to ICOE, it is working closely with Education to obtain existing data from certain education technology projects and is evaluating

these data to determine if they will assist it in tracking the types of applications the K-12 education community is using. Establishing a method to track K-12 network use is key to measuring the success of the High-Speed Network project.

Until ICOE establishes a process to measure the success of the High-Speed Network that includes tracking the type of applications the K-12 education community is using, and the Legislature establishes clear goals for the program, it is difficult to determine whether the network has achieved such goals.

We recommended that Education should ensure that ICOE develops a process to measure the success of the High-Speed Network.

***Education's Action: Partial corrective action taken.***

Education stated that it and ICOE are collaborating with various stakeholders to assess the impact technology has on education. Specifically, they are coordinating the use of information collected from certain education technology projects and will continue to work toward developing analyses and reports as well as modifying data collection tools as appropriate. Additionally, ICOE contracted with an evaluator who will assist it with the development of an evaluation framework with specific goals and objectives for the program. Education expects to finalize the framework and present it to the advisory board in February 2007.

# California Student Aid Commission

## Changes in the Federal Family Education Loan Program, Questionable Decisions, and Inadequate Oversight Raise Doubts About the Financial Stability of the Student Loan Program

REPORT NUMBER 2005-120, APRIL 2006

### *California Student Aid Commission's response as of April 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits (bureau) review California Student Aid Commission's (Student Aid) governance and oversight of its auxiliary organization, known as EDFUND, including EDFUND's financial management and business practices. The audit committee was interested in ensuring the proper use of state assets in maximizing support for financial aid purposes.

### **Finding #1: Federal changes will affect Student Aid's ability to earn surplus funds from the Federal Family Education Loan (FFEL) Program.**

Student Aid's ability to generate an operating surplus from the FFEL Program will be affected significantly by a change required under the Federal Higher Education Reconciliation Act of 2005 (Reconciliation Act) contained in the Federal Deficit Reduction Omnibus Reconciliation Act of 2005. How Student Aid and its competitors choose to implement one change in particular ultimately could determine whether the State should continue to participate as a guaranty agency in the FFEL Program. The change requires guaranty agencies to charge borrowers a 1 percent federal default fee on the principal amount of all FFEL Program loans issued after July 1, 2006, and deposit the proceeds into the Federal Student Loan Reserve Fund (Federal Fund) or transfer an equal amount from nonfederal sources into the Federal Fund. Guaranty agencies with sufficient resources can elect to pay the fee on behalf of borrowers, while agencies with limited resources, such as Student Aid, will have to charge borrowers the fee. These guaranty agencies will be at a distinct competitive disadvantage and may experience a reduction in their market share.

EDFUND staff performed two analyses to determine the impact on FFEL Program operations depending on whether or not other guaranty agencies elect to pay the federal default fee on behalf of borrowers. However, EDFUND's legal counsel asserts that these analyses are confidential and proprietary. Thus, we cannot discuss the specific details of the analyses. Nevertheless, recent announcements by some of the other guaranty agencies indicate that they will not charge borrowers the fee. Conversely, Student Aid has announced it would charge borrowers the fee.

Because of the recent announcements by other guarantors, it will be necessary for EDFUND to revise its forecasts for federal fiscal years 2006 and 2007. It is our belief that FFEL Program revenues could be reduced to the point where EDFUND's role as an auxiliary organization assisting Student Aid in administering the program is

### **Audit Highlights . . .**

*Our review of the California Student Aid Commission (Student Aid) and EDFUND's administration of the Federal Family Education Loan (FFEL) Program revealed the following:*

- » *Changes in federal laws governing the FFEL Program raise doubts that the State will be able to sustain the program.*
- » *Ongoing tensions between Student Aid and EDFUND have hampered Student Aid's ability to renegotiate a revenue agreement with the U.S. Department of Education, which may have cost the State at least \$24 million in federal fiscal year 2005. These tensions also have delayed attempts to expand and diversify EDFUND's financial services.*
- » *Student Aid approved sizeable bonuses for EDFUND executive staff even when the FFEL Program had an operating deficit.*
- » *Student Aid has maintained poor oversight over EDFUND. For example, Student Aid has not ensured that EDFUND travel and business policies are fiscally conservative, which results in less funding available to Student Aid to fulfill its mission.*

no longer warranted. EDFUND states that it has many tactics to minimize the impact of any changes in its competitive position. These tactics include strategies it and other guarantors in the industry use to maintain effective relations with and competitive services for schools, and to work with lenders to strike new relationships that include payment of the default fee. However, EDFUND cannot determine what, if any, impact these tactics will have on its ability to remain competitive in the student loan guaranty market.

The Reconciliation Act imposes other changes that likely will reduce Student Aid's FFEL Program revenues. Specifically, on or after October 1, 2006, the Reconciliation Act prohibits guaranty agencies from charging borrowers collection costs that exceed 18.5 percent of the outstanding principal and interest of a defaulted loan that is paid off through consolidation by the borrower. It also requires the agencies to remit to the U. S. Department of Education (Education) 8.5 percent of the collection charge. Effective October 1, 2009, the Reconciliation Act will require guaranty agencies to remit to Education the entire amount of collection costs for each defaulted loan that is paid off with excess consolidation proceeds, which are the proceeds of consolidated defaulted loans that exceed 45 percent of the guaranty agency's total collections on defaulted loans in each federal fiscal year. Because it has relied so heavily in the past on using consolidations to collect on defaulted loans, these changes will almost certainly result in a decrease to the portion of Student Aid's net recoveries on loan defaults that result from this collection method. Although these changes in federal law do not become operative until federal fiscal year 2010, according to EDFUND it is aggressively reducing its use of consolidations to collect on defaulted loans.

To manage the FFEL Program in a manner that benefits the State, we recommended that Student Aid continue to reassess the financial impact on the FFEL Program caused by changes in the federal Higher Education Act and the recent announcements made by some large guaranty agencies that they will pay the federal default fee for borrowers. Additionally, Student Aid should monitor EDFUND's progress toward reducing its reliance on defaulted loan consolidations.

To determine if it remains beneficial for the State to participate in the FFEL Program as a guaranty agency, we recommended that the Legislature closely monitor Student Aid and EDFUND to ensure that they are able to remain competitive with other FFEL Program guaranty agencies.

Additionally, we recommended that the Legislature closely monitor the Student Loan Operating Fund (Operating Fund) to ensure that the FFEL Program is generating a sufficient operating surplus so that it can supplement funding for Student Aid's other services and programs. If it is unable to generate a sufficient operating surplus, the Legislature should require Student Aid to dissolve EDFUND and contract with another guaranty agency to administer the FFEL Program. The contract should include, among other things, a provision that allows Student Aid to receive a share of the revenues generated by the guaranty agency, which then could be used to supplement funding for Student Aid's other financial aid programs. In addition, the contract should include a provision for Student Aid to hire external auditors to ensure that the guaranty agency is complying with federal laws and regulations. Alternatively, the Legislature could reconsider the need for a state-designated guaranty agency.

***Student Aid's Action: Partial corrective action taken.***

Student Aid and EDFUND staff continue to inform and discuss with the commission and EDFUND board members the fiscal impact caused by changes in the federal Higher Education Act. Additionally, Student Aid paid the federal default fee on behalf of borrowers on loans issued from July 1, 2006, through September 30, 2006, which, according to Student Aid, accounts for the bulk of the fee incurred during the entire academic year. According to Student Aid, it determined that it would not be able to pay the fee on behalf of all borrowers for loans guaranteed on or after October 1, 2006. To remain competitive in the market, private lenders—those who provide the funds for the loans made to the FFEL Program, such as banks and other financial institutions—decided to pay the fee for loans guaranteed from October 1, 2006, through June 30, 2007. Beginning July 1, 2007, EDFUND implemented an annual default fee strategy in which EDFUND and lenders will form

partnerships beginning with the 2007–08 academic year to pay the federal default fee through nonfederal sources. This cost sharing policy was designed to pay 100 percent of the federal default fee on behalf of borrowers and be open to any lender who voluntarily agreed to participate.

Furthermore, EDFUND has successfully shifted its collection strategy and has seen an increase in loan rehabilitations, wage garnishments, and voluntary borrower payments while moving away from a focus on consolidations.

However, new proposed federal changes could again affect FFEL Program revenues. As of September 7, 2007, both houses of Congress approved House of Representatives Bill 2669 (H.R. 2669), which will reduce the guaranty agency collection retention rate on borrower payments from 23 percent to 16 percent beginning October 1, 2007. H.R. 2669 also contains provisions that will reduce the account maintenance fee paid to FFEL Program guarantors from 0.10 percent to 0.06 percent of the original principal amount of outstanding loans issued by the guaranty agency. These changes are likely to significantly impact the revenues earned by FFEL Program guarantors throughout the student loan industry. The President signed H.R. 2669 on September 27, 2007.

***Legislative Action: Legislation enacted.***

Senate Bill 89 (SB 89), an urgency measure enacted as Chapter 182, Statutes of 2007, which took effect immediately, may affect the ownership of EDFUND. This bill authorizes the director of Finance to act as an agent for the State in the sale and transfer of the student loan guarantee portfolio and certain related assets and liabilities of the FFEL Program held by EDFUND. Alternatively, this bill authorizes the director of Finance to enter into an arrangement other than the sale and transfer of EDFUND's assets if the director, in consultation with the state treasurer, determines that arrangement will meet the goals specified in SB 89. SB 89 also prohibits the commission from authorizing EDFUND to perform any new or additional services unless they are deemed necessary or convenient by the Finance director for the operation of the loan program or for maximizing the value of the state student loan guarantee program. Similarly, the director must approve any expenditure by EDFUND. Moreover, SB 89 provides that all actions, approvals, and directions of the commission affecting the state student loan guarantee program are effective only upon approval of the director. Thus, the Finance director now has significant authority over the commission and EDFUND. Finally, the bill requires the Finance director to conduct the activities authorized by SB 89 no later than January 10, 2009.

**Finding #2: Tensions between Student Aid and EDFUND have delayed critical activities, resulting in lost revenue.**

The inability of Student Aid and EDFUND to agree on the role of each organization and the general lack of cooperation between the two has hampered efforts to renegotiate an important agreement with Education that may have resulted in a lost opportunity to receive at least \$24 million in federal fiscal year 2005. Further, these same problems have hindered attempts to expand the financial aid services provided by EDFUND, thereby preventing it from generating additional revenues that could have been used for students. Finally, Student Aid and EDFUND have yet to clarify the roles and responsibilities of each organization despite several attempts to do so.

Student Aid failed to renegotiate its voluntary flexible agreement (VFA) with Education in a timely manner. Disputes between Student Aid and EDFUND, along with turnover in EDFUND's executive management team, have contributed to delays in Student Aid's submission of a VFA proposal to Education. In federal fiscal year 2005, EDFUND budgeted \$30 million in VFA revenues. However, it received only \$6 million. According to Education's state agency liaison, he informed Student Aid and EDFUND in June 2004 that they would not receive any VFA funding beyond federal fiscal year 2004 until the agreement was renegotiated to obtain cost neutrality. Thus, Student Aid may not be able to receive the additional \$24 million that EDFUND budgeted for federal fiscal year 2005 or any other funds it may have been eligible to receive. If Education and Student Aid are unable to complete their renegotiations and comply with the VFA requirements before September 30, 2006, Student Aid also risks losing the opportunity to receive the \$31.4 million that EDFUND budgeted for federal fiscal year 2006.

As discussed previously, federal changes will affect Student Aid's ability to earn surplus funds from the FFEL Program. Thus, the State's ability to continue to generate sufficient FFEL Program revenue to support its other programs and services may rely upon Student Aid's and EDFUND's ability to obtain additional sources of revenue from a diverse set of student loan-related business activities. Currently, neither Student Aid nor EDFUND has a formal plan that specifically identifies the business diversification opportunities they will target.

Student Aid and EDFUND also do not agree on the appropriate role each should have in the administration of the FFEL Program. Despite attempting to craft a roles and responsibilities document (document) since at least May 2005, they have yet to finalize one. Furthermore, based on our review of the ninth version of the two-page draft document, Student Aid may be inappropriately ceding some of its responsibilities to EDFUND. For example, it states that EDFUND has the primary role in operating all aspects of the FFEL Program. However, federal law requires the guaranty agency that chooses to delegate the performance of the FFEL Program function to another entity to ensure that the other entity complies with the program requirements and to monitor its activities. In addition, federal regulations require the state agency to maintain full responsibility for the operation of the FFEL Program when the program is administered by a nonprofit organization.

We recommended that Student Aid ensure that critical tasks, including the renegotiation of its VFA with Education and the development of a diversification plan, are completed. Student Aid should also ensure that the roles and responsibilities it delineates for itself and EDFUND do not inappropriately cede its statutory responsibilities to EDFUND. We also recommended that the Legislature closely monitor Student Aid's progress toward completing critical tasks, including the renegotiation of its VFA with Education and the development of a business diversification plan.

***Student Aid's Action: Partial corrective action taken.***

Student Aid's original VFA remains in place and it was successful in collecting \$28 million for federal fiscal year 2005. Student Aid and EDFUND staff met with Education to discuss Student Aid's participation in the FFEL Program. However, Education has not renegotiated Student Aid's VFA or the VFAs of the other four guaranty agencies that currently have one. Student Aid officials believe that the president's proposed national budget, which would eliminate all VFAs, may have contributed to Education's not moving forward in renegotiations.

Student Aid states that when it received legislative approval to diversify its operations, the Operating Fund had sufficient cash balances to diversify. Since then, the State had redirected approximately \$300 million in operating funds to pay for non-FFEL Program general fund obligations. The commissioners and board members believe that insufficient cash reserves preclude any major initiatives to diversify in the near term.

Finally, Student Aid reported that it has been working closely with a consultant and staff to delineate the roles and responsibilities of the commission, the EDFUND board, and the staff of both organizations. As a result of these efforts, the commission and EDFUND board members approved a new operating agreement and submitted it to the Department of Finance (Finance) and the Joint Legislative Budget Committee for their comment in May 2007. Furthermore, Student Aid and EDFUND finalized a roles and responsibilities document that was approved by the commission on May 1, 2007.

***Legislative Action: Legislation enacted.***

Senate Bill 89 (SB 89), an urgency measure enacted as Chapter 182, Statutes of 2007, which took effect immediately, may affect the ownership of EDFUND. This bill authorizes the director of Finance to act as an agent for the State in the sale and transfer of the student loan guarantee portfolio and certain related assets and liabilities of the FFEL Program held by EDFUND. Alternatively, this bill authorizes the director of Finance to enter into an arrangement other than the sale and transfer of EDFUND's assets if the director, in consultation with the state treasurer, determines that arrangement will meet the goals specified in SB 89. SB 89 also prohibits the

commission from authorizing EDFUND to perform any new or additional services unless they are deemed necessary or convenient by the Finance director for the operation of the loan program or for maximizing the value of the state student loan guarantee program. Similarly, the director must approve any expenditure by EDFUND. Moreover, SB 89 provides that all actions, approvals, and directions of the commission affecting the state student loan guarantee program are effective only upon approval of the director. Thus, the Finance director now has significant authority over the commission and EDFUND. Finally, the bill requires the Finance director to conduct the activities authorized by SB 89 no later than January 10, 2009.

**Finding #3: Student Aid's process for establishing executive salaries and bonuses for EDFUND requires improvement.**

EDFUND created its current policy for setting executive salaries in response to federal regulations ensuring reasonable compensation for employees who exercise substantial control over nonprofit corporations. Under the regulations, payments under a compensation arrangement are presumed to be at fair market value if the arrangement is approved in advance by an authorized body of EDFUND composed of individuals without a conflict of interest, the authorized body obtained and relied upon appropriate comparability data, and the body adequately documented its basis for determination. Adequate documentation consists of the terms, approval date, members of the authorized body present, members who voted, comparability data and how it was obtained, and any actions taken with respect to consideration of the transaction by anyone who is a member of the body but who had a conflict of interest. However, EDFUND's policy does not address board members who have a conflict of interest. In addition, we question the manner in which EDFUND carried out its salary comparison. Specifically, although EDFUND uses surveys to assist in establishing salaries for its executives, it does not limit data to survey sources related to the financial industry. Furthermore, EDFUND cannot demonstrate that it follows its executive salary determination policy because the board and executive committee have not kept sufficient minutes of their meetings.

Student Aid's policy regarding EDFUND executive incentive compensation is also flawed. The operating agreement between Student Aid and EDFUND specifically states that EDFUND agrees to administer its executive performance payment plan in accordance with the Student Aid policy statement and guidelines memo (policy) titled *EDFUND Incentive Compensation Plans*, dated August 12, 2002.

This policy contains flaws because it allows bonuses when an operating deficit exists and excludes some FFEL Program revenues and expenses from the calculation of the Operating Fund surplus or deficit. In addition, the policy is completely discretionary and is silent on how EDFUND should determine the amount of the executive compensation pool. Finally, the policy directs the board to recommend the proposed bonus amounts, if any, for the president and the total bonus amount for the vice presidents. However, the board does not appear to use consistent criteria from one year to the next when determining the total bonus amount.

We recommended that Student Aid ensure EDFUND complies fully with federal regulations and its policy governing salary setting for its executives, including modifying its policy to address board members who have a conflict of interest and ensuring that its consultants compile comparable compensation data solely from similar financial-related organizations. Student Aid should also ensure that EDFUND determines bonuses for its president in accordance with Student Aid's policy. Further, Student Aid should modify its policy statement and guidelines memorandum titled *EDFUND Incentive Compensation Plans* to ensure that EDFUND includes all FFEL Program revenues and expenses in its calculation of the program's operating surplus or deficit and that EDFUND's executive management team does not receive a bonus if the FFEL Program or Operating Fund realizes a deficit. Finally, Student Aid should ensure that it and EDFUND's board establish guidelines to use when approving the total bonus pool amount for EDFUND's executive management team.



***Student Aid's Action: Partial corrective action taken.***

The EDFUND board adopted EDFUND's Executive Compensation Policy in April 2007. A compensation consulting firm has reviewed the policy and the EDFUND board obtained a legal opinion from an outside law firm to ensure the policy complied with federal regulations. The policy also addresses board member conflict of interests. Although the policy was presented to the commission in April 2007, the commission determined that more information was needed before taking any action on the policy.

The EDFUND board also adopted recommended revisions to the Student Aid Policy Statement and Guidelines Memorandum for the EDFUND Incentive Compensation plans. The revisions were presented to the commission at an April 20, 2007, meeting. During the meeting, the commission approved a precondition for inclusion in the document that stated that the year-end FFEL Program revenues must exceed expenses before bonuses will be considered. The commission also determined that more information and further discussion was necessary before considering any additional revisions to the Student Aid Policy Statement and Guidelines Memorandum for the EDFUND Incentive Compensation Plan.

**Finding #4: The method used to determine nonexecutive bonuses needs to be reevaluated.**

Student Aid has not fully addressed concerns raised by an assessment of EDFUND's accomplishment of performance goals. EDFUND has three bonus plans for nonexecutive employees, known as variable pay plans. Two of its three plans reward employees for both individual performance within and the overall performance of EDFUND as an organization, while the third plan is a straightforward award based on a percentage of monthly collections of defaulted loans. Organization performance goals are determined through a process outlined in the August 2002 Student Aid policy. EDFUND uses several high-level organizational metrics to measure its performance of the goals set by Student Aid.

Although its executive director has raised several concerns regarding EDFUND's method of calculating organizational performance, Student Aid has done little to fully address the issues. The executive director and president have agreed that four issues must be addressed: whether and how to recognize goals not achieved, whether and how to recognize a percentage of accomplishment above the assigned weights, whether to set a standard for acceptable variance to a goal, and how midyear budget changes may affect a goal. However, as of March 2006, little progress has been made to resolve these issues. Until these outstanding issues are resolved, EDFUND will continue to award bonuses that are not based on an accurate assessment of its organizational performance.

We recommended that Student Aid direct its executive director and EDFUND's president to resolve outstanding issues related to the methodology used to measure EDFUND's performance, which affects the bonuses for its nonexecutive employees.

***Student Aid's Action: Partial corrective action taken.***

Student Aid indicated that it and EDFUND have made progress in resolving the four issues identified in our report: (1) whether and how to recognize goals not achieved, (2) whether and how to recognize a percentage of accomplishment above the assigned weights, (3) whether to set a standard for acceptable variance to a goal, and (4) how midyear budget changes may affect a goal. Specifically, Student Aid states that agreement has been reached except for one area involving issues 1 and 3, which are interrelated. This area focused on the methodology that should be used to calculate turnover rate and recovery rate.

**Finding #5: More funds would have been available if Student Aid had required EDFUND to follow more fiscally conservative policies.**

Student Aid has not ensured that EDFUND policies are fiscally conservative. Further, EDFUND does not always comply with its business and travel expense policies. We also found a few instances in which Student Aid did not comply with the State's travel policy. Finally, EDFUND spent almost \$700,000 over five federal fiscal years from the Operating Fund for 14 events, such as holiday receptions, employee conferences, and workshops and meetings, that we reviewed. These events often included lodging and meals at upscale hotels and resorts for high-level staff, expensive guest speakers and entertainment. We also found several instances when EDFUND hosted and paid for an event and allowed family members to attend without paying their own way. We question how spending large sums of money on these types of events supports the State's mission of assisting students in achieving their educational goals.

We recommended that Student Aid amend its operating agreement to require EDFUND to establish a travel policy that is consistent with the State's policy. Additionally, it should closely monitor EDFUND expenses paid out of the Operating Fund for conferences, workshops, all-staff events, travel, and the like. Finally, it should ensure that EDFUND discontinues using Operating Fund money to pay for expenses related to nonemployees attending its company functions.

***Student Aid's Action: Corrective action taken.***

On September 7, 2006, Student Aid approved EDFUND's revised travel policy, which became effective on October 1, 2006. The travel policy adopts by reference the State's short-term travel reimbursement for all exempt, excluded, and represented employees. However, the travel policy includes certain exceptions such as EDFUND's use of the U.S. Internal Revenue Services' per diem rates for meals and incidental expenses and its allowable rate for personal vehicle mileage. According to EDFUND, these exceptions were necessary to reflect its status as a nonprofit public benefit corporation and its need to remain competitive with similar corporations in the industry.

On September 7, 2006, the commission approved EDFUND's new employee-wide events spending policy, which became effective on October 1, 2006. The spending policy requires EDFUND to prohibit the use of corporate funds for employee-wide benefits, except as approved by the board. EDFUND's spending policy also prohibits it from using corporate funds to subsidize the costs of guests participating in its employee-wide events.

Finally, the operating agreement between Student Aid and EDFUND includes a provision requiring an annual audit of internal controls by an independent certified public accountant. The operating agreement also requires the development of an annual oversight plan to monitor compliance with EDFUND policies.

**Finding #6: EDFUND did not always comply with its contracting policies.**

EDFUND's contracting policies are vague, leading to lack of guidance in contracting procedures, frequent issues of noncompliance, and questionable practices. EDFUND's policy requires its staff to procure goods and services using one of three methods—competitive bid, sole- and single-source procurement, and an urgency provision for sole-source contracts that are greater than \$100,000. In addition, the policy states that all procurements greater than \$10,000 require at least three bids unless documentation exists indicating three viable vendors decline to bid or are not available. Staff also must provide a justification memorandum or bid/cost analyses approved by an assistant vice president or someone in a higher position.

For 15 of the 16 contracts tested, we found violations ranging from lack of documentation to inadequate sole-source justification. For example, our review of 16 contracts found that EDFUND did not ensure that staff met the three bid and cost analyses requirement for 11 contracts exceeding \$10,000. Furthermore, although EDFUND's policy requires staff to submit a justification memorandum with procurements

under its competitive bid and single- and sole-source methods, it provides no guidance on what the memo or analysis should include. EDFUND's assistant general counsel acknowledges that its policy requires revision and stated that it is working toward doing so.

Finally, the operating agreement between Student Aid and EDFUND does not specifically require purchases of goods and services incurred by EDFUND to be reimbursed pursuant to a procurement and contracts policy approved by the executive director of Student Aid. Without such a provision, the State cannot ensure that EDFUND's purchases result in costs that are appropriate and reasonable.

We recommended that Student Aid ensure that EDFUND follows through on its efforts to revise its contracting policies. We also recommend that Student Aid amend its operating agreement to require purchases of goods and services incurred by EDFUND to be reimbursed pursuant to procurement and contracting policies approved by the executive director of Student Aid.

***Student Aid's Action: Corrective action taken.***

On September 7, 2006, Student Aid approved EDFUND's revised procurement/contracts policy, which became effective on October 1, 2006. The policy appears to address the concerns raised by the bureau.

**Finding #7: Student Aid needs to improve its oversight of EDFUND.**

Student Aid has not provided sufficient oversight over EDFUND to ensure the future success of Student Aid's participation in the FFEL Program. Specifically, Student Aid circumvented state law by delegating its authority related to the approval of EDFUND's budget without amending the operating agreement. Student Aid also dismissed several policy and fiscal concerns raised by its staff responsible for analyzing these issues. Moreover, Student Aid does not always independently verify reports that it receives from EDFUND. Rather, it relies on EDFUND staff to ensure their accuracy. Finally, Student Aid has not completed several key tasks identified within its mandated performance review of EDFUND, despite its staffs' recommendations to actively pursue them. For example, neither Student Aid nor EDFUND has performed an adequate assessment of the financial risks associated with EDFUND's student loan guaranty portfolio, a critical piece of information that Student Aid should have considered before approving EDFUND's annual budgets and business plans.

We recommended that Student Aid rescind its delegation of the approval authority of EDFUND's detailed operating budget to the EDFUND board and follow through on issues raised by its staff regarding EDFUND's operations. Student Aid should also require staff to independently verify the accuracy of the reports submitted by EDFUND. Finally, it should complete key tasks outlined in the June 2005 mandated performance review of EDFUND.

***Student Aid's Action: Partial corrective action taken.***

Student Aid rescinded its delegation of the approval authority of EDFUND's detailed operating budget to the EDFUND board on June 22, 2006.

Student Aid reported that it and EDFUND discussed EDFUND's 2006-07 Loan Program Business Plan and Budget with staff from both organizations to discuss policy and fiscal concerns raised by Student Aid staff. Student Aid indicated that these concerns were resolved to the satisfaction of both organizations.

Student Aid reported that it has been working closely with a consultant and its staff to delineate the roles and responsibilities of both organizations. This will include establishing the appropriate oversight responsibility of Student Aid, including procedures to verify information included in reports prepared by EDFUND.

EDFUND stated that it has completed the key tasks outlined in the June 2005 mandated performance review of EDFUND. We initially reported that six tasks had not been adequately addressed. However, during a follow-up review, we confirmed that EDFUND has completed two of six tasks. As for a third task, although Student Aid and EDFUND continued to explore business diversification options, the Student Aid commissioners and EDFUND board members agree that insufficient cash reserves precludes any major initiatives to diversify in the near term. Finally, EDFUND believes that its routine day-to-day activities address the remaining three key tasks. For example, EDFUND believes it continually reassesses its marketing strategies through the annual EDFUND Loan Program Business Plan, which includes short-term marketing goals for the upcoming year. Further, according to EDFUND, in order to assess the risk of its existing portfolio and future growth strategies, it reviews and confirms, on a quarterly basis, all financial assumptions and projections. This includes a detailed analysis of the results of operations and key business performance indicators, trends and changes that will impact the industry and EDFUND's performance in particular. Included in the review is assessing the loan volume forecasts over the various school segments and calculating the fiscal impact over a five-year period.

**Finding #8: The EDFUND board has violated state law governing closed-session meetings.**

The EDFUND board has not fully complied with certain provisions in state law related to closed-session meetings. Specifically, on August 11, 2004, the governor approved Senate Bill 1108, which amended state law to give the board the authority to hold a closed-session meeting to consider a matter of a proprietary nature, the public discussion of which would disclose a trade secret or proprietary business information that could potentially cause economic harm to EDFUND or cause it to violate an agreement with a third party to maintain the information in confidence if that agreement were made in good faith and for reasonable business purposes.

Our review of documents kept by EDFUND for open meetings held between August 19, 2004, and December 13, 2005, found that in one instance the board clearly violated its closed-session authority. The documentation indicates that the board voted to retain outside counsel to advise it on this audit, which clearly does not qualify as business proprietary information or a trade secret.

Additionally, the board did not consistently keep a confidential minutes book of the topics discussed and decisions made in these sessions, as the Bagley-Keene Open Meeting Act of 2004 (Bagley-Keene Act) requires. Consequently, we were unable to determine the extent to which the board complied with its recent statutory authority for closed sessions and the closed-session meeting provisions of the Bagley-Keene Act. When we asked EDFUND's assistant general counsel about the board's current record-keeping practices, she stated that the board recently was made aware that a closed-session minutes book should be maintained. The assistant general counsel asserted that the board now uses a confidential minutes book that will be maintained by the board secretary or general counsel.

We recommended that Student Aid ensure that EDFUND complies with the Bagley-Keene Act record-keeping requirements by maintaining a confidential minutes book of the business discussed during its closed sessions. In addition, Student Aid and EDFUND should establish policies and procedures to help ensure that closed sessions are conducted within the board's authority as required by state law. These policies and procedures should provide the board and staff with clear guidelines in defining trade secrets and business proprietary information that can be discussed during closed sessions so that no further violations of state law occur.

***Student Aid's Action: Corrective action taken.***

Student Aid reported that EDFUND is maintaining closed session minutes. In addition, Student Aid reported that a policy governing closed session meetings was adopted by the commission and the EDFUND board on April 9, and April 20, 2006, respectively.



# University of California

## Stricter Oversight and Greater Transparency Are Needed to Improve Its Compensation Practices

REPORT NUMBER 2006-103, MAY 2006

### *University of California's response as of May 2007*

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits review the compensation practices of the University of California (university) and to identify systemwide compensation by type and funding source. In addition, we were asked to categorize the compensation of highly paid individuals receiving the most funds from state appropriations and student tuition and fees, and to determine whether they receive any additional compensation or employment inducements not appearing in the university's centrally maintained records.

The audit committee also asked us to determine the extent to which university compensation programs are disclosed to the Board of Regents (regents) and to the public, including the types of programs that exist, their size and cost, and the benefits that participants receive. Finally, we were asked to survey other universities about their compensation disclosure practices and the number of participants and expenses for those programs. Our survey found that the University of California's disclosure practices were similar to those of other universities.

### **Finding #1: Lack of consistency within the Corporate Personnel System (CPS) limits its usefulness.**

The personnel information reporting system used by the university, the CPS, contains inconsistencies and overly vague categorizations. For example, we found a number of instances in which campuses included specific types of compensation, such as housing and auto allowances, in other categories not related to such allowances or in broad nondescriptive categories. Consequently, we could not determine the reliability of the amounts recorded in various compensation and funding source classifications contained within the CPS. In addition, the weaknesses of the CPS limit its usefulness as an oversight tool for the Office of the President (president's office) to monitor campuses' compliance with compensation policies. However, because the CPS is the most detailed and centrally maintained source of this information, our report presented several tables summarizing that total pay to university employees in fiscal year 2004–05 was \$9.3 billion, of which \$8.9 billion was regular pay and \$334 million was additional compensation.

To improve its ability to monitor campus compliance, we recommended that the president's office issue clear directives prescribing consistent use of the CPS and require campuses to consistently classify compensation into standard categories. We also suggested that the president's office consider developing additional automated controls and edits within the CPS to ensure that expenditures are properly charged and to help avoid the possibility of errors.

### **Audit Highlights . . .**

*Our review of the compensation practices of the University of California (university) revealed the following:*

- » *The Corporate Personnel System (CPS) used by the university's Office of the President (president's office) to track the pay activity of university campuses contains inconsistencies and overly vague categories that did not allow us to determine the reliability of various compensation and funding source classifications contained within it and that limit its usefulness as an oversight tool.*
- » *Despite these problems, the CPS is the most detailed and complete centrally maintained source of information, and in fiscal year 2004–05 it reflects that university employees earned approximately \$9.3 billion—comprised of \$8.9 billion in regular pay and \$334 million in additional compensation.*
- » *The president's office appears to regularly grant exceptions to university compensation policy. In a sample of 100 highly paid university employees, 17 benefited from an exception to compensation policy.*
- » *Some university campuses circumvented or violated university policy, resulting in a \$130,000 overpayment to an employee and improper increases to others' retirement covered compensation.*

*continued on next page . . .*

» *The university did not consistently disclose its officers' nonsalary compensation, such as housing allowances, to the Board of Regents as required by policy.*

***University's Action: Pending.***

The university states that by August 2007 it will issue guidance clarifying the proper use of transaction codes within the CPS and, in the future, will restrict the assignment of new codes to the president's office. After putting in place guidance to provide greater clarity about the intended use of CPS categories, the university indicates it will develop appropriate edits and analysis tools to screen for anomalies. Additionally, the university states it has developed an automated system to make compensation data for the senior leadership group available for querying and reporting, and is in the process of improving the accuracy and consistency of the data in this system.

**Finding #2: The president's office regularly granted exceptions to the compensation policy.**

The president's office regularly granted individuals exceptions to the university's compensation policy. University policy authorizes the president's office to approve policy exceptions that provide employees with benefits for which they otherwise would not be eligible. Seventeen of the 100 individuals in our sample benefited from an exception to policy, such as housing or moving allowances above established limits, auto allowances, or participation in the university's senior management severance pay plan.

To preserve the integrity of its compensation policies, we recommended that the president's office limit the number of exceptions to policy it allows. We suggested accomplishing this objective by the regents requiring the university to track and annually report exceptions to compensation policy that various university officers and officials grant during a fiscal year and provide justification for each exception.

***University's Action: Partial corrective action taken.***

The university states it has issued an interim policy requiring campuses to document the basis and rationale for all exceptions to existing compensation policies and to report them to a newly created position of Senior Vice President–Chief Compliance and Audit Officer. As of May 2007 the university indicated that it will soon be interviewing final candidates for this position. The new position will evaluate exceptions to policy to determine if they were made in accordance with the intent of existing policy, and report any concerns to the president and the regents. In addition, the university also states that this position will be responsible for developing additional monitoring and oversight activities.

**Finding #3: The circumvention of policy caused a significant overpayment and inappropriate increases in retirement-covered compensation.**

Some campuses circumvented or violated university policies, resulting in an overpayment to a university employee and questionable forms of compensation provided to others. These instances included an employee at the University of California at San Diego (San Diego) who received an overpayment of \$130,000 and a San Diego vice

chancellor who continued to receive a \$68,000 administrative stipend and an \$8,900 auto allowance despite being on sabbatical. Our review also revealed that some campuses violated the university's retirement plan policy by including inappropriate forms of compensation, such as housing and auto allowances, in three employees' retirement-covered compensation, a percentage of which they may receive when they retire.

We recommended that the president's office improve its oversight of campuses' compliance with university policies by developing a mechanism to annually identify unauthorized exceptions to policy. We also recommended that the president's office determine if it is appropriate to require repayment of university funds for the instances we identified and if so, develop a repayment plan with each employee. We further recommended that the president's office remove the inappropriate forms of retirement-covered compensation we identified from the employees' retirement earnings and establish a mechanism to detect such violations.

***University's Action: Partial corrective action taken.***

To address our recommendation that it annually identify unauthorized exceptions to compensation policies, the university states the president's office has identified arrangements that may be exceptional in nature by taking a more active role in the oversight of the preparation of executive compensation reports. Further, it indicates that its efforts to improve the clarity and consistency of recordkeeping will allow the university to more easily identify transactions that may be exceptional in nature. In addition, the university indicates that the newly created position of Senior Vice President–Chief Compliance and Audit Officer, will be responsible for developing additional monitoring and oversight practices for the campuses' compensation actions. The university states it has resolved most of the exceptions identified in our audit report by either obtaining the regents' approval of those exceptions or notifying the regents about them. The university indicates that a small number of matters were referred to the university's office of the General Counsel or to the appropriate campus in circumstances where the regent's approval would not be appropriate. A few of those issues are still pending. Additionally, the university asserts it corrected all inappropriate forms of retirement-covered compensation we identified and states that its efforts to clarify the use of codes within CPS and increase its audits of retirement-covered compensation should reduce the risk of similar errors occurring in the future.

**Finding #4: The university consistently violated policies the regents established to ensure adequate review of executive compensation.**

The regents' policies require them to approve all forms of compensation for officers of the university. Although the university consistently obtained approval for officers' salaries, in a sample of 10 officers we found that the university violated its policy by failing to disclose eight auto allowances, four housing allowances, two transfers of sabbatical credits, and an acceleration of health insurance contributions when the regents considered the individuals' appointment. Additionally, we found that the usefulness of the university's annual report on compensation to the regents was limited because the fiscal years 2003–04 and 2004–05 reports contained errors and were submitted late.

We recommended that the regents require the president's office to disclose all forms of compensation for university officers and for all employees whose compensation exceeds an established threshold. We further stated that this disclosure should occur when the regents approve the employees' salaries and at least annually in an accurate and timely report to the regents. Finally, the university should ensure that its annual report on compensation is accurate and timely.

***University's Action: Partial corrective action taken.***

In September 2006 the university developed two policies regarding how it will ensure better disclosure of employee compensation to the regents and the public. These practices include specifically identifying the elements of employee compensation to disclose in its annual report on senior management compensation and recent hires of executives and those earning an amount that



requires the regents' approval, and the methods it will use to disclose this information. Additionally, the university has developed a compensation checklist, which it indicates the regents receive when approving employee compensation. To ensure the accuracy of the annual report, the university states that campus internal auditors will audit the data and campus administrators must certify the data's accuracy.

# California's Postsecondary Educational Institutions

## Stricter Controls and Greater Oversight Would Increase the Accuracy of Crime Statistics Reporting

REPORT NUMBER 2006-032, JANUARY 2007

### *Responses from institutions we visited and the California Postsecondary Education Commission as of July 2007*

Chapter 804, Statutes of 2002, which added Section 67382 to the California Education Code (code section), requires us to report to the Legislature the results of our audit of not less than six California postsecondary educational institutions that receive federal student aid. We were also directed to evaluate the accuracy of the institutions' statistics and the procedures they use to identify, gather, and track data for reporting, publishing, and disseminating accurate crime statistics in compliance with the requirements of the Jeanne Clery Disclosure of Campus Security Policy and Campus Crime Statistics Act (Clery Act). We evaluated compliance with the Clery Act at American River College (American River); California State University, Long Beach (Long Beach); Leland Stanford Junior University (Stanford); University of California, Berkeley (Berkeley); University of California, Los Angeles (UCLA); and University of Southern California (USC).

The code section also requires the California Postsecondary Education Commission (commission) to provide on its Web site a link to the Web site of each California postsecondary institution that includes crime statistics information.

### **Finding #1: Failure to correctly classify specific incidents of potentially reportable crime types led institutions to incorrectly report the number of, or miscategorize, crimes.**

The Clery Act and federal regulations require eligible postsecondary educational institutions (institutions) to compile crime statistics in accordance with the definitions established by the Uniform Crime Reporting Program of the Federal Bureau of Investigation (FBI). Definitions for crimes reportable under the Clery Act can be found in both federal regulations and the FBI's *Uniform Crime Reporting Handbook* (UCR). If the U.S. Department of Education (Education) finds that an institution has violated the Clery Act by substantially misrepresenting the number, locations, or nature of reported crimes, it may impose a civil penalty of up to \$27,500 for each violation or misrepresentation. Additionally, Education may suspend or terminate the institution's eligibility status for federal student aid funding.

The Clery Act requires institutions to compile crime statistics in accordance with the definitions established in the UCR. Although state definitions of crimes often do not precisely match the crimes described in the UCR, there is no comprehensive list converting crimes defined in California law to those reportable under the Clery Act, or identifying crimes that cannot be uniformly converted. Consequently, institutions are responsible for ensuring that they include in their

### **Audit Highlights . . .**

*Our review of California's postsecondary educational institutions' compliance with the Jeanne Clery Disclosure of Campus Security Policy and Campus Crime Statistics Act (Clery Act), revealed the following:*

- » *One institution did not correctly convert crimes defined in California law to crimes the Clery Act requires to be reported in the annual security report.*
- » *Institutions did not review some potentially reportable crimes to determine if they are reportable under the Clery Act.*
- » *Institutions did not correctly identify all reportable locations.*
- » *Institutions have not established a written policy or procedure for some of the items described in their annual reports.*
- » *The California Postsecondary Education Commission does not ensure that the links that it provides lead to institutions' statistics.*

annual reports all reportable crimes and correctly classify crimes and their locations in accordance with the definitions of crimes reportable under the Clery Act. One of the six institutions we reviewed did not correctly convert crimes defined in California law to crimes the Clery Act requires institutions to report in their annual reports, and four institutions either did not review or did not correctly report some crimes in potentially reportable categories. When institutions fail to meet these requirements, they can distort the level of crime occurring on the campuses.

To improve the accuracy and completeness of their data, Berkeley, Long Beach, Stanford, UCLA, and USC should establish procedures to identify crimes defined in California law that cannot be directly converted to reportable crimes and take additional steps to determine if a crime is reportable. Berkeley should also ensure that crimes in California law are correctly converted to crimes the Clery Act requires institutions to report.

***University of California—Berkeley’s Action: Corrective action taken.***

Berkeley indicates that it has developed a procedure to ensure that the crimes identified by the audit as incorrectly included are no longer reported. In addition, Berkeley states that it has created a spreadsheet documenting the review of several types of crimes defined in California law to convert them to Clery Act defined crimes.

***California State University—Long Beach’s Action: Corrective action taken.***

Long Beach indicates that it has altered its crime reporting software to identify Clery Act reportable crimes.

***Leland Stanford Junior University’s Action: Partial corrective action taken.***

Stanford indicates that it intends to implement a process to formalize converting crimes defined in California law into the Clery Act reportable crimes defined by the uniform crime report. For crimes that do not have a clear counterpart, the Clery coordinator reviews the incident report and consults with the campus director of public safety and Education as necessary.

***University of California—Los Angeles’ Action: Corrective action taken.***

UCLA has conducted training and established a single method of coding crime reports to ensure consistency. The records manager conducts monthly audits of crime coding to ensure consistency and accuracy. In addition, the records manager reviews data entered into the records management system and conducts audits of the information on a monthly basis. The analyst and records manager determine the appropriate classification for questionable categories. The analyst reviews the actual crime report, as opposed to the information entered into the record management system, for all Clery reportable crimes, and has created a reference sheet to correctly count alcohol-related crimes. Finally, UCLA is attempting to obtain a software upgrade that will enable its record management system to automatically create its Clery report, and hopes to have a process in place to do so by 2009.

***University of Southern California’s Action: Pending.***

USC indicates that it will obtain information from the Los Angeles Police Department to properly categorize these incidents.

**Finding #2: Incomplete data led some institutions to under-report crimes.**

Each institution we reviewed used some form of an electronic system to record and track crimes. However, a lack of controls in these systems allowed inaccurate or incomplete information to be entered, and led some institutions to incorrectly report their crime statistics. For example, at Stanford we identified crimes that either were not entered into the system or were entered with an incorrect year. In addition, at UCLA we found instances when the type of crime was not entered in the crime-tracking

system for Clery Act reportable crimes, and UCLA subsequently assumed they were not criminal incidents. When institutions do not identify all reportable crimes or enter erroneous information for crimes, they risk misrepresenting the number of crimes occurring on their campuses.

To improve the accuracy and completeness of their data American River, Berkeley, Stanford, and UCLA should establish procedures to verify the integrity of data in their electronic crime-tracking systems.

***American River College's Action: Corrective action taken.***

American River indicates that it is now using an automated records management system and ensures the integrity of its data through the use of a separate backup server.

***University of California—Berkeley's Action: Corrective action taken.***

Berkeley indicates that it now conducts a quarterly "gap check" to identify any crimes that have not been entered into the system. In addition, the records unit supervisor maintains documentation regarding any missing case numbers (for example, cancelled case reports).

***Leland Stanford Junior University's Action: Corrective action taken.***

Stanford states that its records supervisor conducts periodic audits of the crime tracking systems to ensure the integrity of the data in the system.

***University of California—Los Angeles' Action: Corrective action taken.***

UCLA states that it has taken steps to label all incident reports, whether criminal or otherwise, to ensure that it accurately identifies and sorts all crimes. In addition, UCLA has taken steps to ensure that the date associated with the crime report is the date the crime was reported, and has introduced daily reviews and random monthly audits to ensure accuracy. Reports are generated to identify incidents without a classification, which are then reviewed. Further, each month the analyst randomly selects 10 percent of incident reports for review to verify the classification is correct. In addition, a monthly report identifies that all report numbers are accounted for, all reports have an incident classification, all criminal offenses have a penal code, and all penal codes correspond to the appropriate classification. Moreover, the analyst now reviews the actual crime report to ensure that the location in the record is the location where the crime occurred, rather than the location where the crime was reported.

**Finding #3: Failing to collect enough information from campus security authorities and local police agencies can affect crime statistics.**

The Clery Act requires institutions to collect crime statistics from campus security authorities and local police agencies. The six institutions we reviewed collect information from various campus security authorities throughout the institutions at least annually. Four of these institutions also request necessary details. However, three institutions did not retain complete records of their requests and responses from campus security authorities.

Because local police agencies may be responsible for responding to certain types of crimes or patrolling designated noncampus and public property areas, institutions must also request information that allows them to determine which additional crimes they should include in their annual reports. Two institutions we reviewed either did not maintain original documents provided by local police agencies or documentation of which crimes they included in their annual reports. Although all incidents reported to campus police departments and local police agencies should be considered, institutions should try to obtain detailed information on every incident reported to avoid over- or under-reporting. Without adequate information, an institution could under-report campus crime because it cannot confirm that it is already aware of the crime, or it could over-report as a result of counting an incident more than once.

To improve the accuracy and completeness of their data, we recommended that American River, Long Beach, Stanford, and USC establish procedures to obtain and retain sufficient information from campus security authorities and local police agencies to determine the nature, dates, and locations of crimes reported by these entities. We also recommended that USC establish procedures to identify all campus security authorities and collect information directly from each source, and that it develop a process to compare the dates that crimes occurred as recorded by the institution to the dates recorded by local police agencies to minimize the potential for duplicate reporting of crimes. Lastly we recommended that Long Beach and USC retain adequate documentation that specifically identifies incidents they include in their annual reports.

***American River College's Action: Corrective action taken.***

American River indicates that it now sends letters to campus security authorities that explain their role and provide instructions for submitting the requested information. In addition, campus security authorities are provided forms that identify required information and include simple definitions of crimes to help enhance accurate reporting. Further, American River makes all requests for information via e-mail to help document compliance.

***California State University—Long Beach's Action: Corrective action taken.***

Long Beach indicates that to provide a basis for verification of statistics in its annual report it has revised its process to collect and retain incident information, and has established procedures to ensure data is gathered and retained from local police agencies and campus security authorities for the proper period of time.

***Leland Stanford Junior University's Action: Corrective action taken.***

Stanford states that its Clery coordinator sent requests for information to all campus security authorities and required responses even if the authority had no crimes to report.

***University of Southern California's Action: Partial corrective action taken.***

USC states that it maintains original documentation provided by the Los Angeles Police Department. USC did not address our concern regarding a comparison of the dates in its records that crimes occurred to the dates recorded by local police agencies to minimize the potential for duplicate reporting of crimes. USC indicates that it is revising its list of campus security authorities and creating an incident report form for them to use.

**Finding #4: Institutions that lack adequate procedures for determining reportable locations risk confusion and inaccurate reporting.**

The Clery Act requires each institution to report statistics for crimes committed in certain geographic locations associated with the campus. Although Education's The Handbook for Campus Crime Reporting (Education handbook), which offers additional guidance on compliance with the Clery Act, provides specific examples of how various locations are to be classified, five of the six institutions we reviewed did not correctly identify all reportable locations. Some institutions did not properly identify public property for all years reviewed; incorrectly classified property meeting the definition of a campus location; did not differentiate in their annual reports between crimes occurring on campus and those occurring on certain public properties, such as streets adjacent to the institution; and failed to identify all noncampus locations subject to reporting. Although each campus is unique, it is important that institutions consistently apply the criteria established by Education to accurately classify reportable crimes.

To improve the accuracy and completeness of their data Berkeley, Long Beach, Stanford, UCLA, and USC should establish procedures to accurately identify all campus, noncampus, and public property locations and report all associated crimes.

***University of California—Berkeley’s Action: Corrective action taken.***

Berkeley states that as described in its response to the audit, it has already complied with this recommendation by using the Education handbook definition to compile statistics for two of the three years reported in its 2006 annual report.

***California State University—Long Beach’s Action: Corrective action taken.***

Long Beach states that it has altered its definition of reportable locations to match that of the Education handbook in its 2006 annual report.

***Leland Stanford Junior University’s Action: Partial corrective action taken.***

Stanford indicates that it will contact Education for guidance on the proper designation of certain properties. Further, Stanford will include the Stanford Hospital and the Stanford Linear Accelerator Center as campus locations; and will include the Stanford Sierra Camp and Boathouse as noncampus locations. Finally, its Clery coordinator will review a list of Stanford properties to determine if all campus and noncampus locations have been properly identified.

***University of California—Los Angeles’ Action: Corrective action taken.***

UCLA indicates that it now obtains a complete list of property from its Space Management Division annually, and a complete list of Greek housing from the fraternity and sorority relations staff. Further, it has reviewed its property and redrawn the campus boundaries for the purpose of identifying reportable locations. It also stated that the crime analyst ensures all locations are properly identified and associated crimes are accurately reported.

***University of Southern California’s Action: Partial corrective action taken.***

USC indicates that it has spent time to educate staff and review local police reports to improve reporting accuracy of the crimes reported by local police. It indicates that it is also expanding its review process to classify or reclassify new properties and those whose use changes. USC did not address our concerns regarding the correction of any incorrect property classifications where the use of the property has not changed.

**Finding #5: The statistics institutions report to Education do not always match the statistics in their annual security reports.**

In addition to disclosing crime statistics in their annual reports, institutions must submit the information to Education, using a form on Education’s Web site. Although we would expect these statistics to mirror one another, five institutions had discrepancies between the number of crimes published in their annual reports and those they submitted to Education. Among the causes of the discrepancies were institutions’ errors when completing Education’s online form, errors in the institutions’ annual reports, the discovery of misplaced information, and corrections institutions made after obtaining additional information. Errors made in reporting to Education and when preparing annual reports distort the actual levels of crime experienced by the institutions and result in unreliable resources for current and prospective students.

To improve the accuracy and completeness of their data, we recommended that Berkeley, Long Beach, Stanford, UCLA, and USC establish procedures to minimize data entry errors in their annual reports and in their annual submissions to Education.

***University of California—Berkeley’s Action: Partial corrective action taken.***

Berkeley indicates that it has created a checklist to ensure that all data submitted by campus security authorities is correctly included in both its annual report and the data it submits to Education. The annual report was not yet due as of the date of Berkeley’s response, so the new procedure had not been fully implemented.

***California State University—Long Beach's Action: Partial corrective action taken.***

Long Beach states that it has established written procedures to minimize data entry errors and has assigned responsibility for these tasks to a single position. The annual report was not yet due as of the date of Long Beach's response, so the new procedure had not been fully implemented.

***Leland Stanford Junior University's Action: Partial corrective action taken.***

Stanford states that its Clery coordinator and records supervisor will cross check data entries prior to the submission of statistics. The annual report was not yet due as of the date of Stanford's response, so the effectiveness of its corrective action could not be fully assessed.

***University of California—Los Angeles' Action: Partial corrective action taken.***

UCLA states that it is confident that by addressing and correcting data integrity issues the concerns regarding the statistics reported to Education will be corrected. In addition, both the crime analyst and information systems manager now review all reported Clery statistics for data entry errors before they are finalized. The annual report was not yet due as of the date of UCLA's response, so the effectiveness of its corrective action could not be fully assessed.

***University of Southern California's Action: Partial corrective action taken.***

USC indicates that it will continue its review of statistics to minimize the potential for the duplicate reporting of crimes. The annual report was not yet due as of the date of USC's response, so the effectiveness of its corrective action could not be fully assessed.

**Finding #6: Some Institutions did not comply with the Clery Act requirements to disclose campus security policies.**

The Clery Act requires that each institution disclose its current campus security policies. While all six institutions we reviewed made good-faith efforts to fully disclose these policies, two institutions did not fully comply in their disclosures. Although one institution disclosed information for all seven of the categories we reviewed, its sexual assault information did not include all the components required by the Clery Act. Complying with the Clery Act provides students and employees at these institutions with important information concerning their safety. In addition, California Education Code, Section 67382(c), suggests that institutions establish and publicize a policy that allows victims or witnesses to report crimes to the institutions' police agencies or to a specified campus security authority on a voluntary, confidential, or anonymous basis, and federal regulations require institutions offering confidential or anonymous reporting to disclose its availability in their annual reports. Unless institutions establish and inform students and staff of the availability of an anonymous reporting system, they may not have a clear picture of the degree of sexual violence occurring on their campus and surrounding communities.

To ensure compliance with the Clery Act, USC should enhance the disclosures regarding sexual assaults in its annual report to fully meet statutory requirements. Long Beach should establish procedures to ensure adequate disclosure of the availability of anonymous and confidential reporting to its campus community.

***University of California—Long Beach's Action: Corrective action taken.***

Long Beach states that it has developed a procedure to ensure adequate disclosure of the availability of anonymous reporting.

***University of Southern California's Action: Partial corrective action taken.***

USC stated that it reviewed and amended its sexual assault policy contained in its annual security report to meet statutory requirements. Although USC's amended policy now contains a section titled "*What To Do If You Are Sexually Assaulted*", it still lacks certain statutorily required wording, including the importance of prompt reporting of a sex offense and of preserving evidence following a sexual assault.

**Finding #7: Some institutions have not established all the policies or procedures described by their annual reports.**

A major component of Clery Act compliance is the disclosure of policy statements in the annual report. The Clery Act outlines numerous campus security policies that institutions must disclose, and the Education handbook provides guidance on the minimum requirements for specific information that the report must include. However, the policies and procedures described in the annual report must also accurately reflect the institution's unique security policies, procedures, and practices, and if the institution does not have a particular policy or procedure, it must disclose that fact. Although the institutions we reviewed generally disclosed the information required by the Clery Act in their annual reports, most campuses were unable to provide us with the policies and procedures to support some of the disclosures they had made in those reports. In addition, the Education handbook states that to keep the campus community informed about safety and security issues, an institution must alert the campus community of reportable crimes considered an ongoing threat to students and employees in a manner that is timely and will aid in the prevention of similar crimes. Because of its potential to prevent crimes, each institution is required to have a policy specifying how it will issue these warnings. Because the Clery Act does not define timely, we expected institutions to have established their own definitions. However, two institutions had not established guidelines or time frames for reporting incidents to the campus community.

To ensure compliance with the Clery Act, we recommended that American River, Long Beach, Stanford, and USC establish comprehensive departmental policies that support disclosures made in their annual reports, and establish a policy to define timely warnings and establish procedures to ensure that they provide timely warnings when threats to campus safety occur.

***American River College's Action: Pending.***

American River reported it was in the process of updating its general orders, and expected that it would complete this process by November 1, 2007.

***California State University—Long Beach's Action: Corrective action taken.***

Long Beach states that it has developed policies and procedures that support the disclosures made in the annual report and has integrated them into the campus police rules and regulations manual, including a policy to define timely warnings.

***Leland Stanford Junior University's Action: Pending.***

Stanford states that it will formalize aspects of existing written procedures regarding timely warnings, and will review and improve its written policies.

***University of Southern California's Action: Pending.***

USC states that it is updating its policy manual. In addition, USC states that it has developed a new timely warning policy, which will be published in the 2007 annual security report, and has amended its internal timely warning procedures.



**Finding #8: One institution did not notify all current and prospective students and employees of the availability of its annual report.**

Federal regulations require institutions to distribute their annual reports to all enrolled students and current employees by October 1 of each year through appropriate publications or mailings. In addition, institutions must notify prospective students and employees of the availability of their annual reports. American River did not distribute its annual report or satisfactorily notify students and employees of its availability during the period we audited. The annual report is only effective in educating students and staff about crime on campus and on the institution's security policies and procedures when students and staff are aware of its availability.

To ensure compliance with the Clery Act, American River should establish procedures to ensure that the campus community is informed of the availability of the annual report.

***American River College's Action: Corrective action taken.***

American River indicates that it now uses a variety of documents to notify students, staff, and faculty of the availability of its annual report.

**Finding #9: The commission does not ensure a link exists to institutions' crime statistics.**

State law requires the commission to provide a link to the Web site of each California institution containing crime statistics information. To fulfill this requirement, the commission provides links on its Web site to connect users to the selected institution's summary information on Education's Web site. The commission believes that this ensures uniform reporting of crime statistics, provides interested persons with a common reporting format for comparison purposes, reduces the reporting burden on institutions, and makes the best use of the commission's scarce resources. However, the commission was unaware that five institutions listed on its Web site had not submitted crime statistics to Education's Web site. Although the commission has procedures in place to verify that it includes a valid link to Education's summary information for each institution, it does not ensure that the summary page contains a link to a valid crime statistics report. The commission stated that in the future it will identify institutions whose pages on Education's Web site do not contain the required crime statistics information and will determine each institution's status.

To ensure that its Web site contains a link to all institutions' crime statistics, the commission should continue with its plan to test the validity of its links.

***California Postsecondary Education Commission's Action: Corrective action taken.***

The commission indicates that it has developed a program to accomplish this task, and conducts verification checks monthly.