STATE OF ILLINOIS
OFFICE OF THE
AUDITOR GENERAL
William G. Holland, Auditor General

SUMMARY REPORT DIGEST

REGIONAL OFFICE OF EDUCATION #25
HAMILTON AND JEFFERSON COUNTIES

FINANCIAL AUDIT (In accordance with the Single Audit Act and OMB Circular A-133)
For the Year Ended: June 30, 2010

Release Date: March 30, 2011

Summary of Findings:

Total this audit:	**7**
Total last audit:	**3**
Repeated from last audit:	**3**

SYNOPSIS

- The Regional Office of Education #25 did not have sufficient internal controls over the financial reporting process.
- The Regional Superintendent did not sign off his approval of all journal entries.
- The Regional Office of Education #25 had excess working capital reserves in its Internal Service Funds.
- The Regional Office of Education #25 did not have sufficient collateral to cover deposits over the FDIC insured limit.
- The Regional Office of Education #25 did not fully comply with State law when establishing or renewing its line of credit.
- The Regional Office of Education #25 did not properly record internal activity with its blended component unit, the Hamilton-Jefferson Educational Services Cooperative.
- The Regional Office of Education #25 did not have sufficient internal controls over its federal awards.

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

REGIONAL OFFICE OF EDUCATION #25
HAMILTON AND JEFFERSON COUNTIES

FINANCIAL AUDIT
(In Accordance with the Single Audit Act and OMB Circular A-133)
For The Year Ended June 30, 2010

	FY 2010	FY 2009
TOTAL REVENUES	$3,721,152	$3,665,900
Local Sources	$708,547	$885,888
% of Total Revenues	19.04%	24.17%
State Sources	$2,676,435	$2,356,864
% of Total Revenues	71.92%	64.29%
Federal Sources	$336,170	$423,148
% of Total Revenues	9.03%	11.54%
TOTAL EXPENDITURES	$3,607,431	$3,790,776
Salaries and Benefits	$2,419,608	$2,254,711
% of Total Expenditures	67.07%	59.48%
Purchased Services	$954,114	$1,251,151
% of Total Expenditures	26.45%	33.01%
All Other Expenditures	$233,709	$284,914
% of Total Expenditures	6.48%	7.52%
TOTAL NET ASSETS	$829,844	$716,123
INVESTMENT IN CAPITAL ASSETS	$813,522[1]	$826,553[1]

[1] Capital asset amounts are not net of related debt which is associated with assets of the Hamilton-Jefferson Educational Services Cooperative. This debt was approximately $555,000 and $609,000 for FY 10 and FY 09 respectively.
Percentages may not add due to rounding.

REGIONAL SUPERINTENDENT
During Audit Period: Honorable Bryan Cross Currently: Honorable Bryan Cross

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

CONTROLS OVER FINANCIAL STATEMENT PREPARATION

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

The Regional Office of Education #25 is required to maintain a system of controls over the preparation of financial statements in accordance with generally accepted accounting principles (GAAP). Regional Office internal controls over GAAP financial reporting should include adequately trained personnel with the knowledge and expertise to prepare and/or thoroughly review GAAP based financial statements to ensure that they are free of material misstatements and include all disclosures as required by the Governmental Accounting Standards Board (GASB).

The Regional Office of Education #25 did not have sufficient internal controls over the financial reporting process. While the Regional Office maintains controls over the processing of most accounting transactions, there are not sufficient controls over the preparation of the GAAP based financial statements for management or employees in the normal course of performing their assigned functions to prevent or detect financial statement misstatements and disclosure omissions in a timely manner. Auditors, in their review of the Regional Office's accounting records, noted the following:

- Numerous material adjustments were required to present financial statements in accordance with generally accepted accounting principles.
- The Regional Office did not have adequate controls over the maintenance of complete records of capital assets and did not calculate depreciation expense.

According to Regional Office officials, they did not have adequate funding to hire and/or train their accounting personnel in order to comply with these requirements (Finding 10-01, pages 13-14) **This finding was first reported in 2007.**

The auditors recommended that, as part of its internal control over the preparation of its financial statements, including disclosures, the Regional Office of Education #25 should implement a comprehensive preparation and/or review procedure to ensure that the financial statements, including disclosures, are complete and accurate. Such procedures should be performed by a properly trained individual(s) possessing a thorough understanding of applicable generally accepted accounting principles, GASB pronouncements, and knowledge of the Regional Office of Education's activities and operations.

The Regional Office of Education #25 responded that it accepts the degree of risk associated with this condition because the added expense of seeking additional accounting expertise to prepare and/or review financial statements would take away from the funds available to provide educational services for the schools in the region.

The Regional Office noted that in an attempt to correct this finding, they sent the Controller to various trainings to better understand accrual accounting and reporting under generally accepted accounting principles (GAAP). (For previous Regional Office response, see Digest Footnote #1.)

INADEQUATE REVIEW OF JOURNAL ENTRIES

The Regional Superintendent for Regional Office of Education #25 did not sign off his approval of all journal entries.

The Regional Superintendent for Regional Office of Education #25 did not sign off his approval of all journal entries. The Regional Office of Education #25 is responsible for establishing and maintaining an internal control system over journal entries to prevent errors or fraud. In addition, adequate controls over compliance with laws, regulations, and grant agreements require supervisory review of expenditures charged to grant programs.

Without appropriate review, unallowable costs could be charged to grant program expenditures or errors in calculating allocations could be made and not be detected in a reasonable period of time. While the Regional Superintendent stated that he discussed journal entries with the Controller and verbally approved them, there was no documentation of such approval. (Finding 10-02, page 15)

The auditors recommended that the Regional Superintendent should review and approve all journal entries along with supporting information documenting the allocations before the entries are posted to the accounting records.

The Regional Superintendent agreed with this finding.

EXCESS WORKING CASH IN INTERNAL SERVICE FUNDS

The Regional Office of Education #25 had excess working capital reserves in its Internal Service Funds.

The Regional Office of Education #25 had excess working capital reserves in its Internal Service Funds. Internal Service Funds are used to account for the administrative services which are provided to many Regional Office of Education #25's funds. Revenue is generated through charges to other funds using interfund billings. Regulations set forth by OMB Circular A-87 (revised 5/14/04) require charges by an internal service activity to provide for the establishment and maintenance of a reasonable level of working capital reserve. In addition, the full recovery of costs is allowable. A working capital reserve of up to 60 days cash expenses for normal operating purposes is considered reasonable. A working capital reserve exceeding 60 days may be maintained for exceptional cases; however, it requires approval of the cognizant federal agency.

Over the last two years, average expenses within the administrative Internal Service Funds were $316,188. Cash on hand in the administrative Internal Service Funds at June 30, 2010 totaled $151,008, representing approximately 174 days of average expenses.

Additionally, the Regional Office paid $21,812 for playground equipment with excess cash from the Internal Service Fund, which is not a prescribed method of reducing the excess balance in the funds, as defined above.

All programs with expenditures paid from the Internal Services Funds' indirect cost rate included a surcharge in addition to the cost of the actual expenditure. The surcharge varied based upon the type of expenditure being paid. The amount of each grant was overcharged is not readily determinable. It is also not readily determinable which program funds were used to purchase the playground equipment.

The Regional Office of Education #25's prior year indirect cost rate was too high, as the calculation included funding for future expenditures. The Regional Office was not aware of the issue until late in fiscal year 2010 and did not have time to make the necessary adjustments before the end of the year. (Finding 10-03, pages 16-18)

The auditors recommended that the Regional Office of Education #25 should lower the indirect cost rate and provide credits to the individual programs overcharged in prior years. Funds for future equipment purchases should be accumulated in the general fund or in a special revenue fund designated for that purpose. The Regional Office should not charge grants for this expenditure, unless it is specifically allowed by the grant. Purchases made out of Internal Service Funds for playground equipment should be reclassified to a fund that would allow such expenditures.

The Regional Superintendent agreed with this finding.

UNINSURED DEPOSITS IN BANK

The Regional Office of Education #25 did not have sufficient collateral to cover deposits over the FDIC insured limit.

At June 30, 2010, the Regional Office of Education #25 did not have sufficient collateral to cover deposits over the Federal Deposit Insurance Corporation (FDIC) insured limit. There were $54,971 of deposits in a bank that were uncollateralized and uninsured.

The Public Funds Deposit Act (30 ILCS 225/1) gives the authorization for deposits in excess of the federally insured limit to be covered by pledged collateral held by the financial institution's trust department in the Regional Office of Education #25's name. In addition, prudent business practice requires that all deposits held by financial institutions for the Regional Office be adequately covered by depository insurance or collateral.

Uninsured deposits could cause a loss to the Regional Office of Education #25 if the bank failed. The Regional Office had an agreement with the bank to monitor the cash balance and make sure that collateral was sufficient to cover any balance that exceeded the amount insured by FDIC. On June 29, 2010, deposits totaling $305,809 were made to the checking account from the State of Illinois. The deposits resulted in uncollateralized deposits of $54,971. (Finding 10-04, page 19)

Auditors recommended that the amount of pledged collateral should be monitored periodically by the Regional Office personnel to ensure that an adequate level is maintained. The Regional Office should work with the bank to determine that collateral is sufficient to cover large deposits.

The Regional Superintendent agreed with this finding.

CONTROLS OVER COMPLIANCE WITH LAWS AND REGULATIONS

The Regional Office of Education #25 did not fully comply with State law when establishing or renewing its line of credit.

The Regional Office of Education #25 did not fully comply with the statutes when establishing a line of credit or renewing its line of credit. The Illinois School Code in section 105 ILCS 5/18-20 allows a Regional Superintendent to borrow an amount up to 50 percent of the State payments that are due and payable, as certified by the State Superintendent. Funds borrowed under this section are to be repaid immediately upon receipt of payments.

In a section added June 26, 2009, the Illinois School Code 105 ILCS 5/17-19 also allows a Regional Superintendent to take out a line of credit in anticipation of revenues. However, the Regional Superintendent is only allowed to take out 85 percent of current year anticipated grant revenue or 50 percent of next fiscal year anticipated grant revenue, as certified by the State Superintendent. The Regional Superintendent shall authorize this line of credit by executive order or resolution. The executive order or resolution shall set forth facts demonstrating the need for the line of credit, the amount to be borrowed, the maximum interest rate allowed, and the date by which the funds will be repaid. Funds borrowed under this section are to be repaid within 60 days after the revenues have been received.

The Regional Office did not fully comply with the statutes when establishing the line of credit or renewing its line of credit on December 31, 2009 and on February 10, 2010. The Regional Office could not produce certification documentation required by sections 5/18-20 or 5/17-19 of the School Code regarding the revenue that was being borrowed upon and did not authorize the line of credit by executive order or resolution.

The Regional Office of Education #25 originally took out a line of credit on May 15, 2009, following the provision of the Illinois School Code 105 ILCS 5/18-20 borrowing authority. On June 26, 2009, the Illinois School Code 105 ILCS 5/17-19 establishment of lines of credit by Regional Superintendents became effective. This new law had additional requirements for Regional Superintendents to follow.

When the line of credit matured on December 31, 2009, it was renewed through February 15, 2010. On February 10, 2010, the line of credit was again renewed and the credit line available was increased. The Regional Superintendent could not document compliance with the certification requirements of either of the statutory provisions. Section 5/18-20 required that the grant payments to be borrowed against be certified by the State Superintendent. In addition, the new section 5/17-19 requires the Regional Superintendent to authorize the line of credit by executive order or resolution. (Finding 10-05, pages 20-21)

The auditors recommended that the Regional Office of Education #25 should comply with the requirements of 105 ILCS 5/18-20 or 105 ILCS 5/17-19, as applicable, when borrowing against anticipated revenues.

The Regional Superintendent agreed with this finding.

RECORDING OF TRANSACTIONS IN THE REGIONAL COOPERATIVE FUND

The Regional Office of Education #25 did not properly record internal activity with its blended component unit, the Hamilton-Jefferson Educational Services Cooperative.

The Regional Office of Education #25 did not properly record internal activity with its blended component unit, the Hamilton-Jefferson Educational Services Cooperative (Coop Board). GASB No. 34 states that the interfund activity, including activity with a government's blended component units, can be reported as interfund reimbursements. This interfund activity should be reported as a reduction of the expenditure or expense by the provider/recipient fund and an expenditure of the benefactor/paying fund. Additionally, the expenditures used to reimburse the provider fund should be carefully monitored to make sure they are classified in the correct expenditure category.

The Coop Board purchases supplies that it in turn resells to the Regional Office. The Coop Board also pays bills which it then allocates to the Regional Office's funds. Rather than reporting the payments for these purchases from the Regional Office's funds as reduction of related expenditures in the Coop Board's accounting records, the Coop Board shows these reimbursements as local revenue. As a result, the expenditures are reported twice, once by the Regional Office's funds and once by the Coop Board. In addition, the Coop Board is incorrectly reporting local revenue.

The Regional Office of Education #25 also misclassified some expenditures when reporting activity with the Coop Board. Since the Regional Office's funds are reimbursing the Coop Board, the expenditures reported by both funds should be classified to the same type of expenditure categories. However, several instances were noted where the expenditures would be reported as one type of expenditure, such as purchased services, in the Regional Office's fund but would be reported as another type of expenditure, such as supplies, by the Coop Board.

The Regional Office of Education #25's Coop Board revenues and expenditures were overstated. In addition, some expenditures paid to the Coop Board were misclassified. The Regional Office's personnel were not aware of the proper reporting of internal activities between funds and its blended component unit. (Finding 10-06, pages 22-23)

Auditors recommended that the Regional Office of Education #25 should report payments between its funds and the Coop Board as internal reimbursements. The Coop Board should report a reduction in expenditures when it receives a reimbursement from the Regional Office's funds. The Regional Office also needs to make sure that expenditures are classified properly when reimbursing the Coop Board.

The Regional Superintendent agreed with this finding.

CONTROLS OVER FEDERAL AWARDS

The Regional Office of Education #25 did not have sufficient internal controls over its federal awards.

The Regional Office of Education #25 did not have sufficient internal controls over its federal awards. The A-102 Common Rule and OMB Circular A-110 require that the non-federal entities receiving federal awards establish and maintain internal control designed to reasonably ensure compliance with federal laws, regulations, and program compliance requirements. The objectives of internal control pertaining to the compliance requirements for federal programs are found in OMB Circular A-133.

Auditors, in their review of the Regional Office's federal award for Title I School Improvement and Accountability –

System of Support (Title I), Title II Teacher Quality – System of Support (Title II), State Fiscal Stabilization Fund (SFSF) – Education State Grants, Recovery Act – ARRA – General State Aid (ARRA Education), and State Fiscal Stabilization Fund (SFSF) – Government Services, Recovery Act – ARRA General State Aid (ARRA Government), noted the following:

- Some Title I and Title II expenditures had not yet been paid out by October 26, 2010. The grant period ended June 30, 2010, and all but one reimbursement had been received as of September 30, 2010.
- At least one Title II reimbursement request that had been sent to the grant administrator had not been reimbursed. The Regional Office did not realize that the amount had not been reimbursed until noted by the auditor.
- The Regional Office did not record System of Support revenue from separate revenue sources in separate accounts. Per an auditor request for the revenue information from the Regional Office of Education #2 (which passes System of Support funding to ROE #25), revenue was also received from State sources for Title I and Title II.
- The Regional Office did not entirely spend its 2009 ARRA Education grant within the grant period specified by the Illinois State Board of Education. Some 2010 ARRA Education and ARRA Government Services expenditures were also outside of the grant period.

The Regional Office of Education #25 had Title I and Title II payables at October 26, 2010 that should have been paid previously. The Regional Office did not receive all of the reimbursements it was entitled to. Revenues were misclassified between federal and State sources. The ARRA federal grants were not spent within the specified period of availability. This could result in the granting agency requesting reimbursements or adjusting any future grant awards.

The Regional Office of Education #25 did not realize that its procedures for its federal awards did not meet the objectives for internal control over compliance requirements for federal programs. (Finding 10-07, pages 24-26)

Auditors recommended that the Regional Office of Education #25 should implement internal control procedures to ensure that all transactions are properly recorded and accounted for and are executed in compliance with laws, regulations, and the provisions of contracts or grant agreements in accordance with OMB Circular A-133.

The Regional Superintendent agreed with this finding.

AUDITORS' OPINION

Our auditors state the Regional Office of Education #25's financial statements as of June 30, 2010 are fairly presented in all material respects.

WILLIAM G. HOLLAND
Auditor General

WGH:KJM

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

DIGEST FOOTNOTES

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

In its prior response in 2009, the Regional Office of Education #25 responded that it understands the nature of this finding and realizes that this circumstance is not unusual in an organization of this size. The Regional Office accepts the degree of risk associated with this condition because the added expense of seeking additional accounting expertise to prepare and/or review financial statements would take away from the funds available to provide educational services for the schools in the region.

The Regional Office noted that in an attempt to correct this finding, they contracted with a Certified Public Accountant to assist the Regional Office with its yearend closing entries and who is willing to accept responsibility for the financial statements.