

STATE OF NORTH CAROLINA

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

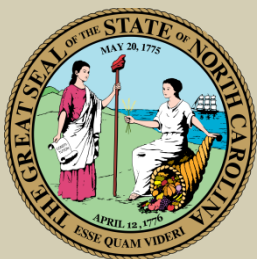


NORTH CAROLINA DEPARTMENT OF PUBLIC INSTRUCTION

RALEIGH, NORTH CAROLINA

STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2018



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Beth A. Wood, CPA
State Auditor

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Article V, Chapter 147 of the *North Carolina General Statutes*, gives the Auditor broad powers to examine all books, records, files, papers, documents, and financial affairs of every state agency and any organization that receives public funding. The Auditor also has the power to summon people to produce records and to answer questions under oath.

STATE OF NORTH CAROLINA
Office of the State Auditor



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AUDITOR'S TRANSMITTAL

The Honorable Roy Cooper, Governor
Members of the North Carolina General Assembly
Mr. Mark Johnson, State Superintendent
North Carolina Department of Public Instruction

As part of our audit of the State of North Carolina's compliance with the types of requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of its major federal programs, we have completed certain audit procedures at the North Carolina Department of Public Instruction for the year ended June 30, 2018.

Our responsibility is to express an opinion on compliance for each of the State of North Carolina's major federal programs based on our audit of the types of compliance requirements referred to above. However, the results included herein are in relation to our audit scope at the Department and not to the State of North Carolina as a whole. The State Auditor expresses an opinion on the State's compliance with requirements applicable to its major federal programs in the State's *Single Audit Report*.

Our federal compliance audit scope at the North Carolina Department of Public Instruction included the following:

- Child Nutrition Cluster
 - CFDA 10.553: School Breakfast Program
 - CFDA 10.555: National School Lunch Program
 - CFDA 10.556: Special Milk Program for Children
 - CFDA 10.559: Summer Food Service Program for Children
- CFDA 84.365: English Language Acquisition State Grants

Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

We conducted our audit of compliance in accordance with the auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform*

Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with types of compliance requirements referred to above that could have a direct and material effect on major federal programs occurred. An audit includes examining, on a test basis, evidence about compliance with those requirements and performing such other procedures as we consider necessary in the circumstances.

Other Matters

Compliance

The results of our audit procedures at the North Carolina Department of Public Instruction disclosed an instance of noncompliance that is required to be reported in accordance with the Uniform Guidance and which is described in finding 2 in the Findings, Recommendations, and Responses section.

Internal Controls

Management is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered internal control over compliance with the types of requirements that could have a direct and material effect on a major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses and significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control that we consider to be material weaknesses. However, we consider the deficiencies described in both findings in the Findings, Recommendations, and Responses section to be significant deficiencies in internal control over compliance.

North Carolina Department of Public Instruction's Response to Findings

The Department's responses to the findings identified in our audit are included in the Findings, Recommendations, and Responses section of this transmittal. The Department's responses were not subjected to the auditing procedures applied in the audit of compliance, and accordingly, we express no opinion on the responses.

Purpose of This Transmittal

The purpose of this transmittal is solely to describe the scope of our testing of internal control over compliance and testing of compliance and the results of that testing at the North Carolina Department of Public Instruction based on the requirements of the Uniform Guidance. Accordingly, this transmittal is not suitable for any other purpose.

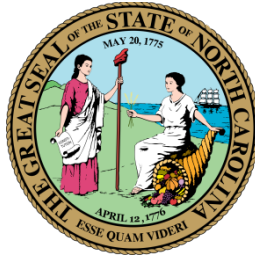
North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this transmittal.



Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

March 19, 2019



FINDINGS, RECOMMENDATIONS, AND RESPONSES

Matters Related to Federal Compliance Audit Objectives

The following audit findings were identified during the current audit and describe conditions that represent deficiencies in internal control or noncompliance with laws, regulations, contracts, grant agreements, or other matters.

CHILD NUTRITION CLUSTER

1. INADEQUATE SUBRECIPIENT MONITORING

The Department did not timely obtain subrecipients'¹ audit reports, review for problems, and communicate expected corrective actions to subrecipients of the Child Nutrition Cluster (Cluster). During the audit period, the Department passed \$524.5 million to these subrecipients.

Auditors reviewed the monitoring process for all 44 subrecipients that were both required to have an audit in accordance with the Uniform Guidance² and had audit findings. There were 12 reports that had findings specifically related to the Cluster.³ The Department did not issue timely management decisions⁴ for four of the subrecipients that had findings related to the Cluster. Management decisions in these instances were two to 43 days past the six-month deadline.

Additionally, the audit report of a non-profit organization which received \$997,218 from the Department was not reviewed nor was a management decision issued regarding an audit finding pertaining to the Cluster.

Lack of timely monitoring increased the risk that federal funds would not be used in accordance with the federal requirements. For example, audit reports that lacked evidence of timely communication of corrective action reported deficiencies such as:

- Noncompliance with Child Nutrition eligibility requirements;
- Untimely filing of required financial reports.

According to the Department, management oversight focused on subrecipients deemed critical and delayed oversight of the full subrecipient audit resolution process. Additionally, management did not correct deficiencies in the process including:

- Measurement of the due dates for the Department's decisions on audit findings by the Federal Audit Clearinghouse dates⁵
- Omission of non-profit organizations that met the audit requirement threshold

¹ Subrecipients are local public school districts, non-profits, and other organizations that use Child Nutrition Cluster funds to administer School Breakfast, National School Lunch, Special Milk, and/or Summer Food Service programs.

² 2 CFR section 200.331(f) & 2 CFR section 200.501

³ The other 32 reports contained findings related to financial reporting or other grant programs.

⁴ 2 CFR section 200.521(a) – Management decisions must clearly state whether or not the finding is sustained, the reasons for the decision, and the expected auditee actions. (i.e., repay disallowed costs, make financial adjustments, or take other actions).

⁵ The Federal Audit Clearinghouse is a public database of completed audits for distribution to federal agencies and support of audit requirement oversight.

Federal regulations⁶ require the Department to monitor the activities of its subrecipients by reviewing audit reports. Specifically, the Department is required to:

- Review financial and programmatic reports
- Follow-up to ensure that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the federal awards
- Issue management decisions⁷ for audit findings that relate to federal awards it makes to subrecipients within six months of acceptance of the audit report by the Federal Audit Clearinghouse.

Federal Award Information: Child Nutrition Program – CFDA # 10.553, 10.555, 10.556, 10.559. Federal award numbers 201818N109945 and 201717N109945 for fiscal years ending September 30, 2017, and September 30, 2018, respectively.

Recommendation: Department management should provide increased and timely oversight of the audit resolution process, and should modify existing procedures to include consideration of nonprofit organizations and the Federal Audit Clearinghouse report receipt dates.

Agency Response: See pages 7-8 for the North Carolina Department of Public Instruction's response to this finding.

ENGLISH LANGUAGE ACQUISITION STATE GRANTS

2. FUNDS USED FOR ACTIVITIES PERFORMED OUTSIDE THE AWARD PERIOD

The Department improperly charged \$42,195 of expenditures to an English Language Acquisition grant award that was no longer available for obligations.⁸ For the fiscal year, the Department spent \$15.5 million to help students attain English proficiency and provide enhanced opportunities for immigrant children.

The 2015 award obligation period ended during our audit year. This award began on July 1, 2015, and ended on September 30, 2017. The Department had 90 days to liquidate obligations made during the award period.

Auditors examined all expenses related to the 2015 award in the 90 days subsequent to the award period. The following amounts were improperly charged to the award:

- \$30,387 in state aid that was reallocated between Local Education Agencies⁹ (LEAs) after September 30, 2017
- \$7,727 to reimburse travel that was taken after September 30, 2017

⁶ 2 CFR section 200.331(d)

⁷ 2 CFR section 200.521(c) and 2 CFR section 200.521(d)

⁸ When used in connection with the Department's utilization of funds under a Federal award, 'obligations' means orders placed for property and services, contracts and subawards made, and similar transactions during a given period that require payment by the non-Federal entity during the same or a future period.

⁹ Synonymous with a local school district, a Local Education Agency is a public authority, such as a board of education, with administrative control of public schools within a city or county. The Department allocates funds to the LEAs to carry out the objectives of the program.

- \$4,081 of indirect costs and miscellaneous expenditures incurred after September 30, 2017

Improper charging of expenses leads to inaccurate financial reporting. Further, the Department may be required to pay \$42,195 back to the United States Department of Education.

According to the Department, the improper charges occurred because of a lack of sufficient staff. The Department had multiple positions that were vacant during the audit period. The review of the allocations and expenditures to ensure they were obligated in the award period was delayed due to the remaining staff focusing on other priorities.

Federal regulations¹⁰ require the Department to charge the federal award for allowable costs incurred during the period of performance (award period). The U.S. Department of Education specifies this period as the 27 months extending from July 1 of the fiscal year for which the funds were appropriated through September 30 of the second following year.

Further, the federal Department of Education states that reallocating grant funds between recipients may not be done after the period of performance ends.¹¹

Federal Award Information: U.S. Department of Education; CFDA Number: 84.365 (English Language Acquisition State Grants); Federal Award Number: S365A150033 (October 1, 2015 – September 30, 2016).

Recommendation: Department management should either

- Assign adequate staff to review allocations and expenditures timely to ensure that obligations are made within the award period or
- Modify the existing procedures of review to ensure obligations are made within the award period.

Agency Response: See pages 7-8 for the North Carolina Department of Public Instruction's response to this finding.

¹⁰ 2 CFR 200.309

¹¹ United States Department of Education Cross-Cutting Section of the 2018 OMB Compliance Supplement, "Period of Performance (All Grantees)."



PUBLIC SCHOOLS OF NORTH CAROLINA

DEPARTMENT OF PUBLIC INSTRUCTION | Mark Johnson, *Superintendent of Public Instruction*

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February 8, 2019

The Honorable Beth A. Wood, State Auditor
Office of State Auditor
2 South Salisbury Street
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Raleigh, North Carolina 27699-0601

The North Carolina Department of Public Instruction (DPI) is pleased to submit our response to your findings in connection with the 2018 federal compliance audit. We agree with the findings and recommendations contained in the report and appreciate the assistance provided by the Office of State Auditor (OSA) to identify areas for improvement.

Finding 1: Inadequate Subrecipient Monitoring

OSA Recommendation: Department Management should provide increased and timely oversight of the audit resolution process and should modify existing procedures to include consideration of nonprofit organizations and the Federal Audit Clearinghouse report receipt dates.

The Department of Public Instruction (DPI) concurs with the Auditor's finding and recommendation related to nonprofit organizations and the Federal Audit Clearinghouse (FAC) report receipt dates. DPI did obtain, review and verify implementation of corrective action for the four Local Education Agencies; however, the management decision letters were issued using a timeline initiated by the date the audit was provided from the Local Government Commission (LGC) pursuant to GS 159 and GS 115C, instead of the FAC acceptance date. This difference resulted in issuance of the management decision letters outside the timeline initiated by the FAC acceptance date.

Effective July 1, 2018, the Division of School Business within DPI revised audit tracking tools to incorporate both the LGC and FAC audit acceptance dates. The Division's internal procedure for audit resolution was revised, requiring the earlier of the two receipt dates to initiate the six-month timeframe in which management decision letters must be issued. These changes ensure DPI's compliance with the respective federal timeline.

Effective July 1, 2018, the Division of School Business developed and implemented an internal procedure for resolution of nongovernmental organization (NGO) audits as well as an NGO audit

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AN EQUAL OPPORTUNITY/AFFIRMATIVE ACTION EMPLOYER

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tracking tool. This helps to ensure DPI's compliance with federal audit requirements for nonprofit entities.

Finding 2: Funds Used for Activities Performed Outside the Award Period

OSA Recommendation: Department Management should either

- *Assign adequate staff to review allocations and expenditures timely to ensure that obligations are made within the award period or*
- *Modify the existing procedures of review to ensure obligations are made within the award period.*

The Department of Public Instruction concurs with the Auditor's finding and recommendation. The Division of School Business will develop internal procedures for reallocation of federal grant funds designed to ensure funds are not reallocated between subrecipients after the period of performance. The Division of Financial Services will develop and communicate internal procedures designed to ensure that only obligations made within the award period are paid through grant funds. The Division of Financial Services also has plans to hire for a Grant Accountant position during the current fiscal year to assist with tracking and monitoring of grant related spending.

We believe implementation of these corrective actions will address the deficiencies noted. Please feel free to contact Jeani Rousseau or me if you have any questions about our response. As always, we appreciate the effort and professionalism of your staff in conducting audits of the Department of Public Instruction.

Sincerely,



Mark Johnson

c: Eric Davis, State Board of Education Chairman
Alan Duncan, SBE Audit Committee Chair
Eric Hall, Deputy Superintendent of Innovation
Kathryn Johnston, Deputy Superintendent of Operations
Maria Pitre-Martin, Deputy Superintendent of District Support
Jeani Rousseau, Director of Internal Audit

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For additional information contact:
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This audit was conducted in 3,143.5 hours at an approximate cost of \$323,780.