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Office of Management and Budget  
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July 12, 2017

Mr. Ken Wagner, Ph.D.  
Commissioner of Education  
Department of Elementary and Secondary Education  
295 Westminster Street  
Providence, RI, 02903

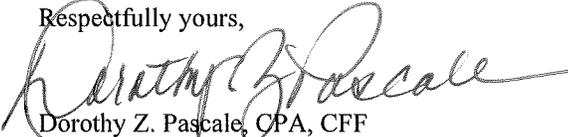
Dear Commissioner Wagner:

The Office of Internal Audit has completed its limited scope audit of the Department of Elementary and Secondary Education (RIDE). The audit was conducted in conformance with the Institute of Internal Auditors (IIA) International Standards for the Professional Practice of Internal Auditing and by the authority given to the unit as stated in accordance with Rhode Island General Laws (RIGL) §35-7.1-1 – Establishment of office of internal audit. The recommendations included herein have been discussed with members of management, and we considered their comments in the preparation of this report.

RIGL §35-7.1-10 (d), entitled Annual and interim reports, states that, “Within twenty (20) calendar days following the date of issuance of the management response copy of the draft audit report, the head of the department, agency, public body or private entity audited shall respond in writing to each recommendation made in the audit report.” Accordingly, management submitted its response to the audit findings and recommendations on July 11, 2017, and such response is included in this report. Pursuant to this statute, the Office may follow up regarding recommendations included in this report within one year following the date of issuance.

We would like to express our sincere appreciation to the staff of RIDE for the cooperation and courtesy extended to the members of our team during the course of this audit.

Respectfully yours,

  
Dorothy Z. Pascale, CPA, CFF  
Chief

c—Jonathan Womer, Director, Office of Management and Budget  
Honorable William J. Conley, Jr., Chairperson, Senate Committee on Finance  
Honorable Marvin Abney, Chairperson, House Finance Committee  
Peter Keenan, State Controller, Office of Accounts and Control

## AUDIT Executive Summary

### Why the OIA Did This Review

This audit was performed as a result of our annual risk assessment process. The purpose of this engagement was to determine if RIDE operations are being administered efficiently and effectively in accordance with requirements, statutes and state procedures, and with adequate controls to ensure safeguarding of assets and accurate reporting. The primary focus was the operations of the School Building Authority (SBA), an entity within RIDE.

### Background Information

The Rhode Island Department of Education is the administrative body which oversees statewide public education. Responsibilities of RIDE include:

- To carry out the policies and program formulated by the Council on elementary and secondary education.
- To approve the distribution of state school funds in accordance with law and the regulations of the Council.
- To verify that school sites and school building plans are in accordance with laws and regulations.
- To require the observance of all laws relating to schools and education.
- To interpret school law and to decide such controversies as may be appealed to the commissioner from decisions of local school committees.

### To Strengthen Controls and Improve Operational Efficiency, the Rhode Island Department of Education Should:

For the Rhode Island Department of Education—

- Improve reconciliation procedures of cash disbursements.
- Document Bond Refinancing Monitoring Responsibilities for RIDE and the Rhode Island Health and Educational Building Corporation to ensure adequate oversight.
- Document procedures to verify eligibility of bonus awards.
- Update Standard Operating Policies and Procedures.
- Obtain Software to assign, track and categorize legal casework to improve efficiency and consistency.

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## Introduction

The Rhode Island Department of Education (RIDE) is the administrative body which oversees statewide public education. Currently the public education system in Rhode Island enrolls over 140,000 students in elementary, middle and high schools alone. Responsibilities of RIDE include:

- To carry out the policies and program formulated by the Council on elementary and secondary education.
- To evaluate credentials of applicants for certificates, to verify that the certification of teachers is in accordance with law and established standards and to issue certificates at the direction of the board.
- To certify the approval of accredited schools.
- To recommend to the Council an outline of the subjects and courses of study and the instructional standards for elementary and secondary schools.
- To approve the distribution of State school funds in accordance with law and the regulations of the Council.
- To verify that school sites and school building plans are in accordance with law and regulations.
- To require the observance of all laws relating to schools and education.
- To interpret school law and to decide such controversies as may be appealed to the commissioner from decisions of local school committees.

## Control Environment

### *School Construction*

The Department of Elementary and Secondary Education calculates and disburses funding for school housing aid<sup>1</sup> in accordance with the formula dictated in RIGL §16-7-39. This guarantees adequate school housing for all public school children by providing State funding to communities for the construction and maintenance of school buildings. Reimbursement is linked to district wealth, with poorer communities receiving a higher reimbursement than wealthy districts.

The School Building Authority (SBA) is a statutory entity within RIDE that, with assistance from the School Building Authority Advisory Board and Council on Elementary and Secondary Education, manages the school construction aid program consisting of the:

- School housing aid program – These funds are used to reimburse school districts for approved school construction projects once they have been completed. It is designed to guarantee adequate school housing for all public school children in the State, and to prevent the cost of school housing from interfering with the effective operation of the schools. Schools can elect to use reserve funds to finance a project upfront and then receive State reimbursement at the

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<sup>1</sup>Housing Aid is State funds designated for community school systems to construct, improve and maintain school buildings.

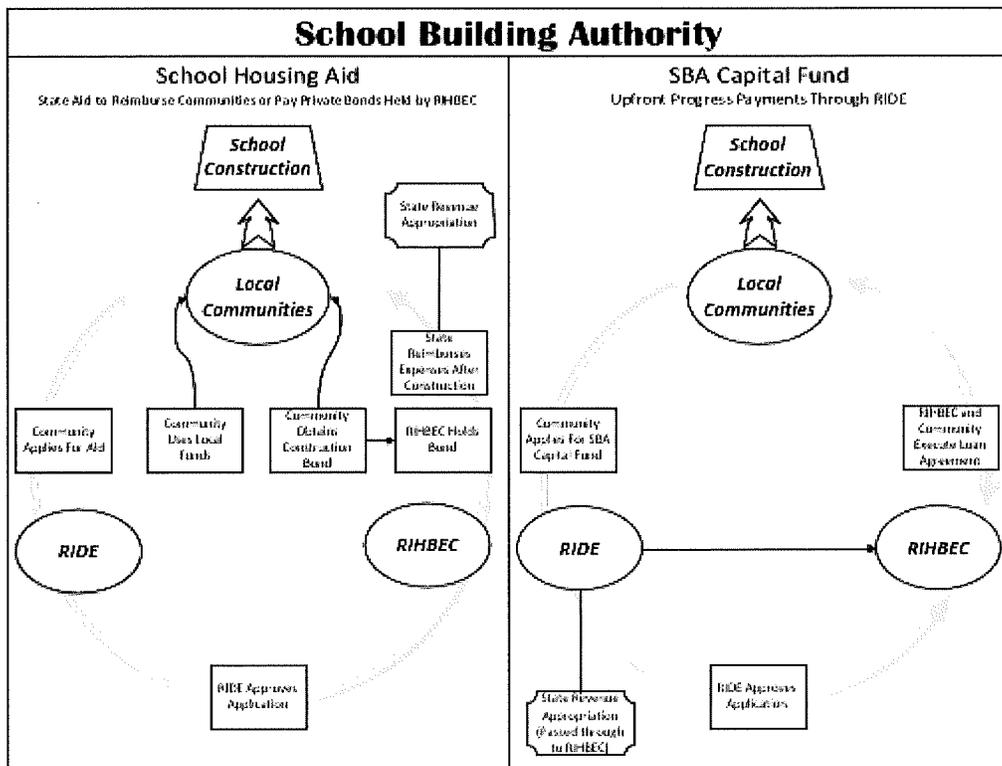
conclusion of the project, or they can finance the project through a private bond and receive State reimbursement in accordance with the bond payments.

- SBA capital fund - A funding mechanism designed to provide upfront funding for projects. The fund may be used to repair public school facilities and be distributed on a priority basis to ensure that funding has the greatest impact.

The School Building Authority works in conjunction with the Rhode Island Health and Educational Building Corporation (RIHEBC) and an SBA Capital Fund Manager to administer these programs. The SBA performs the administrative functions for these programs, including processing applications, obtaining recommendation from the SBA Advisory Board and approval from the Council on Elementary and Secondary Education, reviewing building plans and coordinating State funding with communities and RIHBEBC.

RIHBEBC is a quasi-governmental organization incorporated for the purpose of assisting health and education entities gain access to capital. For the purposes of securing school housing aid through the State, RIHBEBC plays two major roles: holding private bonds for school construction to be paid with State and local funds and disbursing the SBA capital fund by using State appropriations for grants and loans with communities.

A depiction of the interaction between the local communities, RIDE and RIHBEBC is presented below.



While the SBA operates the two programs in an effective manner based on requirements of the Rhode Island General Laws and internal operating practices, we identified areas at RIDE where controls could be strengthened to further improve efficiency in the sections to follow.

## **Recommendations and Management's Responses**

### **Document Reconciliations between RIDE and RIHEBC pertaining to SBA Capital Fund**

Reconciliation is an important detection control to determine whether the money leaving an account matches the invoiced amount, ensuring the two values are balanced at the end of the reporting period. In addition, reconciliation helps to ensure the accuracy and validity of financial information and that unauthorized changes due to errors or irregularities have not occurred to transactions during processing.

While the SBA is responsible for processing the applications, overseeing school construction and monitoring expenditures, the cash disbursements to municipalities from the capital fund are performed by RIHEBC. In order to ensure that these disbursements were made accurately in accordance with the project expenditures, RIDE compares its project records to the SBA Capital Fund Manager's master spreadsheet to detect errors and irregularities.

However, the process used by the SBA to compare the disbursement of capital funds between SBA and RIHEBC records was not adequately documented. The worksheets provided by RIDE did not contain sufficient documentation to prove that records were fully reconciled. Additionally, there are no formally documented policies or procedures for the process.

#### *Recommendation:*

1. Perform and document timely reconciliations of SBA Capital Fund disbursements.

#### *Management's Response:*

The School Building Authority currently has a Housing Aid procedures document. This document will be updated to include reconciliation processes and procedures, as part of a broader SBA Capital Fund & Housing Aid Operating Policies and Procedures manual.

#### *Responsible Party:*

Director of Statewide Efficiencies  
Rhode Island Department of Education

#### *Anticipated Completion Date:*

12/31/17

### **Improve the Monitoring Procedures for Bond Refinancing**

RIGL §16-7-41(e) *Computation of school housing aid* authorizes the Commissioner of Elementary and Secondary Education to monitor the potential for refunding bonds of local communities. The Commissioner may, but is not required to, inform the community to refinance any bond if the net present

value of savings achieved by refunding is at least \$100,000. These functions are performed primarily by RIHEBC through an informal arrangement with RIDE.

The statute also requires the finance director or the chief financial officer of the community to certify the net interest savings to the Commissioner and to timely refinance in accordance with the Commissioner's directive, if such directive is issued. Failure to timely refund such bond shall result in reduction of State aid in subsequent fiscal years in an amount proportionate to the lost savings from the refinancing opportunity.

We were informed that RIDE works closely with RIHEBC to monitor bond refinancing; however, we did not find evidence that RIDE collected and used information from RIHEBC to pursue refinancing opportunities. The OIA found that RIDE does not have a formalized process to notify towns of their refinancing requirement. Since bond markets are volatile, it is critical that action be taken to refinance immediately. As a result of this informal notification process, bond refinancing opportunities may be foregone or delayed.

*Recommendation:*

2. Document the responsibilities of RIDE and RIHEBC through a formal Memorandum of Understanding. Ensure procedures therein provide adequate oversight and compliance with the bond refinancing monitoring responsibilities.

*Management's Response:*

RIDE will define responsibilities through a formal Memorandum of Understanding with RIHEBC. These procedures will also be documented in the SBA Capital Fund and Housing Aid Operating Policies and Procedures document. Please note, as previously documented, every cost savings bond has refinanced since FY 2012 for a total savings of \$33M.

*Responsible Party:*

Director of Statewide Efficiencies  
Rhode Island Department of Education

*Anticipated Completion Date:*

12/31/17

## **Improve Controls over Housing Aid Bonuses**

In addition to housing aid provided through the State housing aid ratio, RIGL §16-7-40 provides 4 percent bonus funding for certain types of projects, including energy savings, ADA improvements and asbestos removal. In order to qualify for these incentives, the project must meet specific criteria including that at least 75 percent of project costs must be related to those objectives.

In the course of our audit we reviewed two applications which were awarded a bonus for energy efficiency. For these applications, the SBA did not perform verification procedures to ensure that the project met the eligibility requirements mandated by State law. Instead, they relied upon the assertions of the applicant that the project met all of the eligibility requirements. Without a process to verify

eligibility requirements, there is a risk that the SBA could make improper payments to communities for ineligible projects.

For the projects reviewed, we were unable to determine whether the projects met all of the eligibility requirements based upon the documentation provided by RIDE.

*Recommendations:*

3. Implement a formal process to validate the eligibility of projects for the bonus funding incentives.

*Management's Response:*

A formal process to validate the eligibility of projects for the bonus funding incentives will be included in the SBA Capital Fund and Housing Aid Operating Policies and Procedures document.

*Responsible Party:*

Director of Statewide Efficiencies  
Rhode Island Department of Education

*Anticipated Completion Date:*

12/31/17

School Building Authority

### **Establish Standard Operating Policies and Procedures for the SBA Unit**

Documented policies and procedures allow for organized operations by establishing work processes and promoting uniformity of operations among staff. Also, developing and periodically updating written policies and procedures will improve continuity of practices whenever new employees are brought into the unit.

The SBA manages and oversees the School Housing Aid Program and SBA Capital Fund based on requirements of Rhode Island General Law §16-7. This process is extremely complex and includes:

- Determining the Necessity of School Construction Projects.
- Gathering property values and population data from municipalities.
- Calculating the state housing aid ratio.
- Calculating and distributing state funding according to the formula dictated by State law.
- Receiving, processing and approving school housing aid applications.
- Reviewing school construction plans to:
  - Ensure conformance with minimum requirements for schools.
  - Approve incentive payments for projects meeting certain standards.
- Monitoring outstanding bonds and coordinating with municipalities for refinancing.

Currently, most of these complex financial calculations and processes are performed by a select group of people. While the Council on Elementary and Secondary Education has promulgated School Construction Regulations, Housing Aid Regulations, and written instructions for communities related to application, plan reviews, and invoice submission, there are limited written internal policies and operating procedures

for the financial management of the program. Turnover of any of the key individuals would lead to a great loss of institutional knowledge and pose a risk to the continuity of operations within the unit.

*Recommendation:*

4. Develop written policies and procedures and include areas identified in Appendix A of this report.

*Management's Response:*

RIDE will develop written policies and procedures to include areas identified in the Appendix A of this report. These will be included in the SBA Capital Fund and Housing Aid Operating Policies and Procedures document, which will be circulated to SBA staff upon completion in order to ensure transparency.

*Responsible Party:*

Director of Statewide Efficiencies  
Rhode Island Department of Education

*Anticipated Completion Date:*

12/31/17

## RIDE General Operations

### **Obtain Case Management Software for RIDE Legal Section**

RIGL §16-1-5 requires the commissioner of Education to:

- Require the observance of all laws relating to schools and education; and
- Interpret school law and to decide such controversies as may be appealed to the commissioner from decisions of local school committees.

This statute provides broad authority to handle a range of legal matters related to education. Legal department management staff in the legal section do not currently have a systematic means to assign casework to staff and review prior legal actions to ensure consistency of decisions. Cases are reviewed by senior legal staff before decisions are issued; however, there is currently no systematic way to identify similar cases or to ensure consistent application of State and Federal laws. Additionally, RIDE management does not have an effective system for categorizing, sorting and identifying prior decisions relevant to current case work. As a result of these weaknesses, RIDE has limited assurance that State and Federal laws are consistently applied and that the agency is being consistent in the interpretation and application of Federal and State law.

*Recommendation:*

5. Obtain software to assign, track, and categorize legal casework to improve efficiency and consistency within RIDE.

*Management's Response:*

The RIDE Legal Office is currently in the process of evaluating several software products to enable tracking and organization of casework, and will have a preferred system selected and implemented by the end of the calendar year.

*Responsible Party:*

Chief Legal Counsel  
Rhode Island Department of Education

*Anticipated Completion Date:*

12/31/17

## **Objective and Scope**

The Office of Internal Audits (OIA) conducted an audit of general management practices at RIDE. The purpose of this engagement is to review RIDE's organizational structure and processes and determine if operations are being administered efficiently and effectively in accordance with requirements, statutes and state procedures. Our primary focus was the School Building Authority (SBA).

## **Methodology**

As part of our audit work, we gained an understanding of the existing controls and management practices at RIDE. To address our audit objective, we performed the following:

- Reviewed policies, procedures, rules, regulations, and State laws.
- Met with RIDE management personnel and staff.
- Prepared flow charts of significant processes.
- Performed business process analysis based on meetings and flow charts.
- Tested a sample of refinanced bonds to determine compliance with laws and regulations.
- Tested a sample of SBA capital fund and school housing aid disbursements for accuracy and completeness of supporting documentation.
- Tested a sample of school projects to determine compliance with the approval process.

## Appendix A

# Recommended Policies and Procedures

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To improve efficiencies and strengthen controls, the RIDE should include the following topics within the Policy and Procedure Manual:

- Calculating housing aid and related ratios.
- Approving housing aid/SBA capital fund applications.
- Disbursing SBA capital funds.
- Reconciling SBA capital fund disbursements.
- Documenting bond refinancing protocols.

All policies and procedures must be transparent and adequately communicated to staff.