



# MICHIGAN

OFFICE OF THE AUDITOR GENERAL

## AUDIT REPORT



THOMAS H. McTAVISH, C.P.A.  
AUDITOR GENERAL

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

Audit report information can be accessed at:

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Michigan  
Office of the Auditor General  
**REPORT SUMMARY**

*Financial Audit  
Including the Provisions of the Single Audit Act*

Report Number:  
313-0100-10

*Michigan Department of Education*

*October 1, 2007 through September 30, 2009*

Released:  
June 2010

*A Single Audit is designed to meet the needs of all financial report users, including an entity's federal grantor agencies. The audit determines if the financial schedules and/or financial statements are fairly presented; considers internal control over financial reporting and internal control over federal program compliance; determines compliance with requirements material to the financial schedules and/or financial statements; and assesses compliance with direct and material requirements of the major federal programs.*

**Financial Schedules and Financial Statements:**

**Auditor's Reports Issued**

We issued unqualified opinions on the Michigan Department of Education's (MDE's) financial schedules and on the School Aid Fund's financial statements.

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**Internal Control Over Financial Reporting**

We identified significant deficiencies in internal control over financial reporting (Findings 1 through 3). We consider Finding 1 to be a material weakness.

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**Noncompliance and Other Matters  
Material to the Financial Schedules and/or  
Financial Statements**

We did not identify any instances of noncompliance or other matters applicable to the financial schedules and/or financial statements that are required to be reported under *Government Auditing Standards*.

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**Federal Awards:**

**Auditor's Reports Issued on Compliance**

We audited 18 programs as major programs and identified known questioned costs of \$12.1 million. MDE expended and distributed a total of \$3.7 billion in federal awards during the two-year period ended September 30, 2009. We issued 18 unqualified opinions. The federal programs audited as major programs are identified on the back of this summary.

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**Internal Control Over Major Programs**

We identified significant deficiencies related to internal control over federal program compliance (Findings 4 through 8 and 10 through 17). We do not consider these significant deficiencies to be material weaknesses.

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**Required Reporting of Noncompliance**

We identified instances of noncompliance that are required to be reported in accordance with the U.S. Office of Management and Budget (OMB) Circular A-133 (Findings 4 through 17).

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**Systems of Accounting and Internal Control:**

We determined that MDE was in substantial compliance with Sections 18.1483 - 18.1487 of the *Michigan Compiled Laws*.

We audited the following programs as major programs:

<u>CFDA Number</u>	<u>Program or Cluster Title</u>	<u>Compliance Opinion</u>
10.550	Food Donation	Unqualified
10.558	Child and Adult Care Food Program	Unqualified
10.565	Commodity Supplemental Food Program	Unqualified
	<u>Emergency Food Assistance Cluster:</u>	Unqualified
10.568	• Emergency Food Assistance Program (Administrative Costs)	
10.568	• ARRA - Emergency Food Assistance Program (Administrative Costs)	
10.569	• Emergency Food Assistance Program (Food Commodities)	
10.569	• ARRA - Emergency Food Assistance Program (Food Commodities)	
	<u>Title I, Part A Cluster:</u>	Unqualified
84.010	• Title I Grants to Local Educational Agencies	
84.389	• ARRA - Title I Grants to Local Educational Agencies, Recovery Act	
	<u>Special Education Cluster (IDEA):</u>	Unqualified
84.027	• Special Education - Grants to States	
84.173	• Special Education - Preschool Grants	
84.391	• ARRA - Special Education Grants to States, Recovery Act	
84.392	• ARRA - Special Education - Preschool Grants, Recovery Act	
84.048	Career and Technical Education - Basic Grants to States	Unqualified
	<u>Early Intervention Services (IDEA) Cluster:</u>	Unqualified
84.181	• Special Education - Grants for Infants and Families	
84.393	• ARRA - Special Education - Grants for Infants and Families, Recovery Act	
84.186	Safe and Drug-Free Schools and Communities - State Grants	Unqualified
84.282	Charter Schools	Unqualified
84.298	State Grants for Innovative Programs	Unqualified
84.318	Education Technology State Grants	Unqualified
84.357	Reading First State Grants	Unqualified
84.365	English Language Acquisition Grants	Unqualified
84.366	Mathematics and Science Partnerships	Unqualified
84.367	Improving Teacher Quality State Grants	Unqualified
84.369	Grants for State Assessments and Related Activities	Unqualified
	<u>State Fiscal Stabilization Fund Cluster:</u>	Unqualified
84.394	• ARRA - State Fiscal Stabilization Fund (SFSF) - Education State Grants, Recovery Act	

A copy of the full report can be obtained by calling 517.334.8050 or by visiting our Web site at: <http://audgen.michigan.gov>



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**Thomas H. McTavish, C.P.A.**  
Auditor General

**Scott M. Strong, C.P.A., C.I.A.**  
Deputy Auditor General



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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

June 30, 2010

Mr. Michael P. Flanagan  
Superintendent of Public Instruction  
Michigan Department of Education  
John A. Hannah Building  
Lansing, Michigan

Dear Mr. Flanagan:

This is our report on the financial audit, including the provisions of the Single Audit Act, of the Michigan Department of Education (MDE) for the period October 1, 2007 through September 30, 2009.

This report contains our report summary; our independent auditor's reports on the financial schedules and statements; and MDE financial schedules, School Aid Fund financial statements, required supplementary information, and schedule of expenditures of federal awards. This report also contains our independent auditor's report on internal control over financial reporting and on compliance and other matters, our independent auditor's report on compliance with requirements applicable to each major program and on internal control over compliance in accordance with U.S. Office of Management and Budget Circular A-133, and our schedule of findings and questioned costs. In addition, this report contains MDE's summary schedule of prior audit findings, its corrective action plan, and a glossary of acronyms and terms.

Our findings and recommendations are contained in Section II and Section III of the schedule of findings and questioned costs. The agency preliminary responses are contained in the corrective action plan. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL



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INDEPENDENT AUDITOR'S REPORTS,  
FINANCIAL SCHEDULES, AND  
FINANCIAL STATEMENTS



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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

## Independent Auditor's Report on the Financial Schedules

Mr. Michael P. Flanagan  
Superintendent of Public Instruction  
Michigan Department of Education  
John A. Hannah Building  
Lansing, Michigan

Dear Mr. Flanagan:

We have audited the accompanying financial schedules of the Michigan Department of Education for the fiscal years ended September 30, 2009 and September 30, 2008, as identified in the table of contents. These financial schedules are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the financial schedules present only the revenues and the sources and disposition of authorizations for the Michigan Department of Education's General Fund accounts, presented using the current financial resources measurement focus and the modified accrual basis of accounting. Accordingly, these financial schedules do not purport to, and do not, constitute a complete financial presentation of either the Department or the State's General Fund in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial schedules referred to in the first paragraph present fairly, in all material respects, the revenues and the sources and disposition of authorizations of the Michigan Department of Education for the fiscal years ended September 30, 2009 and September 30, 2008 on the basis of accounting described in Note 1.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 25, 2010 on our consideration of the Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The schedule of expenditures of federal awards, required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the Department's financial schedules referred to in the first paragraph. Such information has been subjected to the auditing procedures applied in the audit of the financial schedules and, in our opinion, is fairly stated, in all material respects, in relation to the financial schedules taken as a whole.

AUDITOR GENERAL

June 25, 2010



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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

## Independent Auditor's Report on the Financial Statements

Mr. Michael P. Flanagan  
Superintendent of Public Instruction  
Michigan Department of Education  
John A. Hannah Building  
Lansing, Michigan

Dear Mr. Flanagan:

We have audited the accompanying financial statements of the School Aid Fund, Michigan Department of Education, as of and for the fiscal years ended September 30, 2009 and September 30, 2008, as identified in the table of contents. These financial statements are the responsibility of the Department's and Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the financial statements present only the School Aid Fund and do not purport to, and do not, present fairly the financial position of the State of Michigan or its governmental funds as of September 30, 2009 and September 30, 2008 and the changes in financial position thereof for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the School Aid Fund as of September 30, 2009 and September 30, 2008 and the changes in financial position for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 25, 2010 on our consideration of the Fund's and Department's internal control over financial reporting and on our tests of their compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The budgetary comparison schedules and corresponding notes on pages 32 through 35 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The schedule of expenditures of federal awards, required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the Fund's financial statements referred to in the first paragraph. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

AUDITOR GENERAL

June 25, 2010

MICHIGAN DEPARTMENT OF EDUCATION  
Schedule of General Fund Revenues  
Fiscal Years Ended September 30

	<u>2009</u>	<u>2008</u>
REVENUES		
From federal agencies (Note 1)	\$ 46,824,380	\$ 44,732,786
From local agencies	38,588	34,142
From licenses and permits	5,377,154	4,756,597
Miscellaneous	<u>523,259</u>	<u>1,280,028</u>
Total revenues	<u>\$ 52,763,381</u>	<u>\$ 50,803,553</u>

The accompanying notes are an integral part of the financial schedules.

MICHIGAN DEPARTMENT OF EDUCATION  
Schedule of Sources and Disposition of General Fund Authorizations  
Fiscal Years Ended September 30

	<u>2009</u>	<u>2008</u>
<b>SOURCES OF AUTHORIZATIONS (Note 2)</b>		
General purpose appropriations	\$ 85,075,457	\$ 41,985,000
Balances carried forward	1,918,060	2,089,845
Restricted financing sources	57,884,388	54,793,919
Less: Intrafund expenditure reimbursements	<u>(5,174,736)</u>	<u>(5,035,218)</u>
 Total	 <u>\$ 139,703,169</u>	 <u>\$ 93,833,546</u>
 <b>DISPOSITION OF AUTHORIZATIONS (Note 2)</b>		
Gross expenditures and transfers	\$ 141,076,804	\$ 91,054,567
Less: Intrafund expenditure reimbursements	<u>(5,174,736)</u>	<u>(5,035,218)</u>
Net expenditures and transfers	<u>\$ 135,902,068</u>	<u>\$ 86,019,348</u>
Balances carried forward:		
Encumbrances	\$ 24,844	\$
Multi-year projects		180,000
Restricted revenues - not authorized or used	<u>2,216,326</u>	<u>1,738,060</u>
Total balances carried forward	<u>\$ 2,241,170</u>	<u>\$ 1,918,060</u>
Balances lapsed	<u>\$ 1,559,931</u>	<u>\$ 5,896,138</u>
 Total	 <u>\$ 139,703,169</u>	 <u>\$ 93,833,546</u>

The accompanying notes are an integral part of the financial schedules.

## Notes to the Financial Schedules

### Note 1 Significant Accounting Policies

#### a. Reporting Entity

The accompanying financial schedules report the results of the financial transactions of the Michigan Department of Education (MDE) for the fiscal years ended September 30, 2009 and September 30, 2008. The financial transactions of MDE are accounted for in the State's General Fund and in the School Aid Fund. Both the General Fund and the School Aid Fund are reported on in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

The notes accompanying these financial schedules relate directly to MDE. The *SOMCAFR* provides more extensive disclosures regarding the State's significant accounting policies; budgeting, budgetary control, and legal compliance; pension benefits; and other postemployment benefits.

#### b. Measurement Focus, Basis of Accounting, and Presentation

The financial schedules contained in this report are presented using the current financial resources measurement focus and the modified accrual basis of accounting, as provided by accounting principles generally accepted in the United States of America. Under the modified accrual basis of accounting, revenues are recognized as they become susceptible to actual, generally when they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred; however, certain expenditures related to long-term obligations are recorded only when payment is due and payable.

The accompanying financial schedules present only the revenues and sources and disposition of authorizations for MDE's General Fund accounts. Accordingly, these financial schedules do not purport to, and do not, constitute a complete financial presentation of either MDE or the State's General Fund in conformity with accounting principles generally accepted in the United States of America.

c. Revenue From Federal Agencies

Federal reimbursement for MDE administration costs were recorded in the State's General Fund. For most federally funded programs, revenue is accrued in the same period as related obligations are recorded. In certain programs, financed entirely by the federal government, expenditures and related revenues are recognized only to the extent of billings received by fiscal year-end. This treatment understates assets and liabilities and expenditures and revenues; however, there is no impact on the fund balance of the State's General Fund.

Note 2 Schedule of Sources and Disposition of General Fund Authorizations

The various elements of the schedule of sources and disposition of General Fund authorizations are defined as follows:

- a. General purpose appropriations: Original appropriations and any supplemental appropriations that are financed by General Fund/general purpose revenues. The \$43.1 million increase in general purpose appropriations between fiscal years 2007-08 and 2008-09 is primarily due to the increase in the appropriated transfer from the General Fund to the School Aid Fund.
- b. Balances carried forward: Authorizations for multi-year projects, encumbrances, restricted revenues - authorized, and restricted revenues - not authorized or used that were not spent as of the end of the prior fiscal year. These authorizations are available for expenditure in the current fiscal year for the purpose of the carry-forward without additional legislative authorization, except for the restricted revenues - not authorized or used.
- c. Restricted financing sources: Collections of restricted revenues, restricted transfers, and restricted intrafund expenditure reimbursements used to finance programs as detailed in the appropriations act. These financing sources are authorized for expenditure up to the amount appropriated. Depending upon program statute, any amounts received in excess of the appropriation are, at year-end, either converted to general purpose financing sources and made available for general appropriation in the next fiscal year or carried forward to the next fiscal year as either restricted revenues - authorized or restricted revenues - not authorized or used.

- d. Intrafund expenditure reimbursements: Funding from other General Fund departments to finance a program or a portion of a program that is the responsibility of the receiving department.
- e. Encumbrances: Authorizations carried forward to finance payments for goods and services ordered during the fiscal year but not received by fiscal year-end. These authorizations are generally limited to obligations funded by general purpose appropriations.
- f. Multi-year projects: Unexpended authorizations for work projects and capital outlay projects that are carried forward to subsequent fiscal years for the completion of the projects.
- g. Restricted revenues - not authorized or used: Revenues that, by statute, are restricted for use to a particular program or activity. Generally, the expenditure of the restricted revenues is subject to annual legislative appropriation. Significant fiscal year 2008-09 and 2007-08 carry-forwards of this type were certification fees of \$2,216,326 and \$1,738,060, respectively.
- h. Balances lapsed: Authorizations that were unexpended and unobligated at the end of the fiscal year. These amounts are available for legislative appropriation in the subsequent fiscal year.



SCHOOL AID FUND  
Michigan Department of Education  
Balance Sheet  
As of September 30  
(In Thousands)

	2009	2008
<b>ASSETS</b>		
Current assets:		
Taxes, interest, and penalties receivable (Note 6)	\$ 2,020,786	\$ 2,214,040
Amounts due from other funds		11,735
Amounts due from federal agencies	53,942	48,881
Amounts due from local units	57,248	47,613
Other current assets	179	97
Total current assets	\$ 2,132,155	\$ 2,322,366
Noncurrent assets:		
Taxes, interest, and penalties receivable	61,492	66,730
Amounts due from local units	1,650	4,208
Total assets	\$ 2,195,296	\$ 2,393,305
<b>LIABILITIES AND FUND BALANCE</b>		
Current liabilities:		
Warrants outstanding	\$ 940	\$ 695
Accounts payable and other liabilities	156,648	155,948
Amounts due to other funds (Note 5)	1,297,267	1,444,626
Deferred revenue (Note 6)	427,829	470,711
Total current liabilities	\$ 1,882,685	\$ 2,071,979
Long-term liabilities:		
Deferred revenue (Note 6)	61,492	66,730
Total liabilities	\$ 1,944,176	\$ 2,138,710
Fund balance:		
Reserved fund balance (Note 7)	\$ 251,119	\$ 254,595
Total fund balance	\$ 251,119	\$ 254,595
Total liabilities and fund balance	\$ 2,195,296	\$ 2,393,305

The accompanying notes are an integral part of the financial statements.

**SCHOOL AID FUND**  
Michigan Department of Education  
Statement of Revenues, Expenditures, and Changes in Fund Balance  
Fiscal Years Ended September 30  
(In Thousands)

	2009	2008
<b>REVENUES</b>		
Taxes (Notes 2 and 6):		
Sales	\$ 4,424,669	\$ 4,928,092
Personal income	1,895,402	2,117,698
Property	2,040,647	2,079,703
Use	428,119	459,277
Cigarette	410,429	424,728
Industrial facilities	41,810	86,129
Liquor	37,616	36,915
Commercial facilities (forest tax)	2,977	4,026
Casino gaming wagering	108,080	112,067
Real estate transfer	125,294	169,835
Michigan Business Tax	669,341	341,000
Other	13,276	12,816
Total taxes	\$ 10,197,659	\$ 10,772,286
From federal agencies	2,101,053	1,377,664
Miscellaneous	32,595	30,864
Total revenues	\$ 12,331,307	\$ 12,180,814
<b>EXPENDITURES</b>		
Proposal A (Note 2)	\$ 6,010,253	\$ 5,976,970
Discretionary payment	3,188,645	3,669,210
Special education	981,452	974,858
At risk students	310,457	310,450
Declining enrollment	20,000	19,999
Vision and hearing	5,150	5,150
Intermediate school districts	81,721	80,912
Adult education	24,000	23,996
District grants	850	1,950
School readiness grants	117,312	107,309
Vocational education	38,912	38,994
School lunch	22,495	21,087
Mathematics and science	4,225	3,500
Health and science middle college	2,000	2,000
Pre-college engineering	980	680
Court-placed children	8,000	8,000
Juvenile detention facilities	2,829	2,822
Cultural access grants	200	
Challenge Program	1,285	1,284
School bus inspections and driver safety	2,932	2,776
Out-of-formula districts	1,052	
Gifted and talented	281	285
Bilingual education	2,800	2,800
Renaissance zone	25,975	36,084
Non-Durant district settlements (Note 4)	38,794	31,687
Borrowing costs	32,135	22,800
Teen health centers	4,743	3,743
PILT (payment in lieu of taxes) reimbursement	3,367	3,351
State assessments	32,113	32,066
School breakfast	8,218	9,044
Federal non-special education	1,136,220	1,036,592
Federal special education	351,985	336,115
American Recovery and Reinvestment Act (ARRA) (Note 2)	608,979	
Other	26,403	19,837
Total expenditures	\$ 13,096,763	\$ 12,786,351
Excess of revenues over (under) expenditures	\$ (765,456)	\$ (605,537)
<b>OTHER FINANCING SOURCES (USES)</b>		
Transfers from other funds	\$ 800,980	\$ 769,969
Transfers to other funds	(39,000)	(3,833)
Total other financing sources (uses)	\$ 761,980	\$ 766,136
Net change in fund balances	\$ (3,476)	\$ 160,599
Fund balance - Beginning of fiscal year	254,595	93,996
Fund balance - End of fiscal year	\$ 251,119	\$ 254,595

The accompanying notes are an integral part of the financial statements

## Notes to the Financial Statements

### Note 1 Significant Accounting Policies

#### a. Reporting Entity

The accompanying financial statements report the financial position and the changes in financial position of the School Aid Fund, Michigan Department of Education (MDE), as of and for the fiscal years ended September 30, 2009 and September 30, 2008. The School Aid Fund is a part of the State of Michigan's reporting entity and is reported as a governmental fund in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

The notes accompanying these financial statements relate directly to the School Aid Fund. The *SOMCAFR* provides more extensive disclosures regarding the State's significant accounting policies; budgeting, budgetary control, and legal compliance; and Treasurer's common cash.

#### b. Measurement Focus, Basis of Accounting, and Presentation

The financial statements contained in this report are presented using the current financial resources measurement focus and the modified accrual basis of accounting as provided by accounting principles generally accepted in the United States of America. Under the modified accrual basis of accounting, revenues are recognized as they become susceptible to accrual, generally when they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred; however, certain expenditures related to long-term obligations are recorded only when payment is due and payable.

The accompanying financial statements present only the School Aid Fund. Accordingly, they do not purport to, and do not, present fairly the financial position and the changes in financial position of the State of Michigan or its governmental funds in conformity with accounting principles generally accepted in the United States of America.

c. Revenue and Amounts Due From Federal Agencies

For most federally funded programs, revenue is accrued in the same period as related obligations are recorded. In certain programs, financed entirely by the federal government, expenditures and related revenues are recognized only to the extent of billings received by fiscal year-end. This treatment understates assets and liabilities and expenditures and revenues; however, there is an immaterial impact on the fund balance of the School Aid Fund.

Note 2 Description of Fund

The School Aid Fund was created in 1955 by an amendment to the 1908 Michigan Constitution, and its continued existence was provided for by the 1963 Michigan Constitution. The School Aid Fund's purpose is to furnish aid to school districts of the State. Payments to school districts are based on statutory formulas.

The School Aid Fund receives State revenues restricted to school programs, including the constitutional dedication of 60% of the collections of sales tax imposed at a rate of 4% and all of the collections of sales tax imposed at the additional rate of 2%; State Lottery net revenue; approximately 33% of total State use tax revenue; and portions of the personal income, cigarette, liquor, industrial and commercial facilities, and casino gaming wagering taxes. In addition, in fiscal years 2008-09 and 2007-08, MDE received and expended the majority of federal grants through the School Aid Fund.

A constitutional amendment (known as Proposal A\*) approved by voters in 1994 made significant structural changes in the method of financing school districts. This amendment authorized the levy of a Statewide education property tax and a real estate transfer tax, all of which are deposited in the School Aid Fund. Annual appropriated transfers also are made from the State's General Fund.

School Aid Fund appropriations are established annually by the Legislature. If total appropriations are less than the payments to be made based on the State School Aid Act of 1979, as amended, then total payments are to be prorated so that they equal the appropriated funding available. In accordance with Act 73,

\* See glossary at end of report for definition.

P.A. 2009, proration was avoided in fiscal year 2008-09 by using federal grant funds (State Fiscal Stabilization Fund) from the American Recovery and Reinvestment Act of 2009 (ARRA) in lieu of payments (\$600 million) under Section 22b of the State School Aid Act.

Note 3 Contingencies

a. *Adair et al. v State of Michigan et al.*

*Adair et al. v State of Michigan et al.* (Adair) asserts that the State, by operation of law, has increased the level of various specified activities and services beyond that which was required by State law as of December 23, 1978 and, after December 23, 1978, added various specified new activities or services by State law, including mandatory increases in student instruction time, without providing funding for these new activities and services, all in violation of the Headlee Amendment.

The Adair plaintiffs are seeking a declaratory judgment that the State has failed to meet its funding responsibility under the Headlee Amendment to provide the plaintiff school districts with revenues sufficient to pay for the necessary increased costs of activities and services first required by State law after December 23, 1978 and to pay for increases in the level of required activities and services beyond that which was required by State law as of December 23, 1978.

On April 23, 2002, the Court of Appeals dismissed the plaintiffs' complaint in Adair in its entirety and with prejudice. The Court held that all of the Adair plaintiffs were barred from prosecuting all but one of their claims by either the doctrine of res judicata or the principle of release. With regard to the remaining recordkeeping claim, the Court held that this is not a new activity or an increase in the level of a State-mandated activity within the meaning of the Headlee Amendment. The Adair plaintiffs filed an application for leave to appeal and a motion for immediate consideration of the application for leave to appeal with the Michigan Supreme Court on May 14, 2002.

The Michigan Supreme Court granted the Adair plaintiffs' application for leave to appeal and an oral argument was held. On June 9, 2004, the Michigan Supreme Court issued an opinion affirming the Court of Appeals' decision that the majority of the Adair plaintiffs' claims were barred by

res judicata or release. Regarding the recordkeeping claim, the Michigan Supreme Court reversed the Court of Appeals and remanded the issue to that Court. On August 4, 2005, the Court of Appeals granted the State's motion for summary disposition and dismissed the plaintiffs' remaining claim with prejudice. On September 14, 2005, the Adair plaintiffs filed an application for leave to appeal with the Michigan Supreme Court. On March 8, 2006, the Michigan Supreme Court, in lieu of granting leave to appeal, vacated the August 4, 2005 judgment of the Court of Appeals and remanded the case to the Court of Appeals for reevaluation of plaintiffs' recordkeeping claim. By Order of April 18, 2006, the Court of Appeals referred this case to Special Master Pamela R. Harwood, retired Wayne Circuit Court Judge. The Special Master was directed to determine:

[W]hether the record-keeping obligations imposed on Plaintiff school districts by MCL 388.1752 and Executive Order No. 2000-9 constitute either a new activity or service or an increase in the level of a state-mandated activity or service within the meaning of Mich Const of 1963, art 9, § 29's prohibition of unfunded mandates.

The Special Master conducted hearings throughout the summer of 2007, and the parties filed posthearing briefs during the fall of 2007. On January 27, 2008, the Special Master issued her Opinion. She found that the increased recordkeeping and reporting requirements imposed upon the school districts by the State was an attempt by the State to shift the burden to comply with additional requirements to the districts without appropriating the necessary costs to comply. She concluded that this was a shifting of the recordkeeping and reporting requirement burden from the State to the local units of government in violation of the Headlee Amendment.

The State filed objections to the Special Master's Opinion in the Court of Appeals. The school district sought attorney fees in the Court of Appeals. On July 3, 2008, the Court of Appeals issued its Opinion On Second Remand, essentially adopting the conclusions of law and factual findings of the Special Master. The Court entered a declaratory judgment in favor of the Adair plaintiffs requiring that the State fund the "necessary costs

associated with the data collection reporting mandates" associated with the Center for Educational Performance and Information (CEPI). The Court denied Adair plaintiffs' request for attorney fees.

The State moved for reconsideration as to the merits of the Court of Appeals' Opinion. The school districts moved for reconsideration as to the portion of the Opinion denying attorney fees. On August 27, 2008, the Court of Appeals denied both parties' motions for reconsideration.

On October 6, 2008, the Adair plaintiffs filed an application for leave to appeal the attorney fees aspect of the Court of Appeals' decision in the Michigan Supreme Court. On October 8, 2008, the State filed its own application for leave to appeal in the Michigan Supreme Court, raising several issues. The State claims that the Court of Appeals erred in not requiring the Adair plaintiffs to prove that they have actually incurred necessary increased costs. The State also challenged the Court of Appeals' Opinion, claiming that the recordkeeping requirement is an optional activity that school districts perform in order to receive school funding and that the adoption of Proposal A by voters in 1994, amending Article IX of the Michigan Constitution of 1963, provides the necessary State funding to school districts to perform the recordkeeping requirements.

The parties are awaiting a decision as to whether the Michigan Supreme Court will consider their respective applications for leave to appeal. The ultimate outcome of the case is not presently determinable. (If the Court of Appeals' decision is upheld, the financial outcome for either party is speculative and not possible to predict.)

b. State Education Tax - Personal Property Assessments

In December 2005, Detroit Edison, Michigan Consolidated Gas Company, the Department of Treasury, and governmental representatives from Wayne, Oakland, Macomb, and Kent counties agreed to the terms of a global settlement related to personal property tax table depreciation schedule of utility companies. The settlement was presented to and approved by the Michigan Tax Tribunal in 2006. As of September 30, 2009, \$28.2 million remains to be paid in school aid payments for prior fiscal years because school districts and other taxing units will be required

to refund utility companies. These additional payments will be paid from the School Aid Fund as follows:

<u>Fiscal Year</u>	<u>Amount Scheduled To Be Paid</u>
2009-10	\$16.3 million
2010-11	\$11.9 million

These amounts will be reflected in the School Aid Fund financial statements as they become due and payable.

Note 4 Commitments

Donald Durant, et al. v State of Michigan, et al.: In an order dated June 10, 1997 and a decision rendered July 31, 1997, the Michigan Supreme Court decided, in the consolidated cases of *Durant v State of Michigan* and *Schmidt v State of Michigan*, that the special education, special education transportation, bilingual education, driver training, and school lunch programs provided by local school districts are State-mandated programs within the meaning of Article IX, Section 29 of the Michigan Constitution (part of the Headlee Amendment); therefore, the State is obligated to fund these programs at the levels established by the Headlee Amendment. In fashioning a remedy in this case of first impression under the Headlee Amendment, the Court concluded that, in future cases, the correct remedy will typically be limited to a declaratory judgment. However, because of the protracted nature of the *Durant* and *Schmidt* litigation, the Court ruled that the 84 plaintiff school districts should be compensated for the full amount of the underfunding without interest for the State-mandated programs during school years 1991-92, 1992-93, and 1993-94.

On November 19, 1997, the Governor signed legislation providing \$212.0 million to the 84 plaintiff school districts to cover the underfunding for those three years. Most of the \$212.0 million was paid to the plaintiff school districts on April 15, 1998, through the State School Aid Act of 1979, using funds transferred from the State's Counter-Cyclical Budget and Economic Stabilization Fund to the School Aid Fund. The board of education of each plaintiff school district determined the appropriate distribution of the award between taxpayer relief and/or use by the district for other public purposes.

The Court affirmed the award to the plaintiffs of their costs, including attorney fees. Over 400 other school districts asserted claims similar to those asserted by the Durant plaintiffs.

In companion legislation signed by the Governor on November 19, 1997, the State will pay each "non-Durant" school district for its underfunded State-mandated program costs for those same three years if the district agreed by March 2, 1998 to waive any claim against the State of the same nature made by the 84 Durant plaintiffs through September 30, 1997. All of the non-Durant school districts signed waivers on or before March 2, 1998. The payments have been and will continue to be paid through the State School Aid Act of 1979, using funds transferred to the School Aid Fund from the Counter-Cyclical Budget and Economic Stabilization Fund and the General Fund. The payments were paid half in annual payments over 10 years that ended in November 2007. The other half is being paid over 15 years. Eligible non-Durant school districts were allowed to borrow and issue bonds for the amount they were to receive over 15 years. Although the School Aid Fund has no legal liability to pay the debt service costs for school districts issuing bonds, the School Aid Fund has paid and will continue to pay an additional amount for the related debt service costs as long as sufficient funds are appropriated. As a result of a refinancing of these bonds, there were no debt service payments for fiscal years 2006-07 and 2007-08. The estimated aggregate payments to the non-Durant school districts will total approximately \$780.4 million. As of September 30, 2009, the remaining expected amount to be paid on behalf of the non-Durant school districts totaled approximately \$233.1 million.

Note 5 Treasurer's Common Cash

The State Treasurer manages the State's common cash pool, which is used by most State funds. The pooling of cash allows the State Treasurer to invest money not needed to pay immediate obligations so that investment earnings on available cash are maximized. Investments of the pool are not segregated by fund. Each contributing fund's balance is treated as equity in the pool, which is recorded in separate accounts within the General Fund. Many funds, including retirement funds, use their equity in the pool as a short-term investment vehicle. In the *SOMCAFR*, the pooled cash is not reported as a separate fund. Each fund's balance in the pool is reported on the line "Equity in common cash." All negative balances in the pool are reclassified at

year-end as interfund liabilities, with the appropriate fund recording the receivable. Due to the timing of the collection of tax revenues, the School Aid Fund borrows cash at year-end to make school aid payments. This reclassification resulted in a School Aid Fund liability of approximately \$1.3 billion for fiscal year 2008-09 and \$1.4 billion for fiscal year 2007-08.

Note 6 Tax Revenue, Deferred Revenue, and Receivables

Revenues of the School Aid Fund consist primarily of sales, personal income, property, Michigan Business Tax, use, cigarette, liquor, industrial and commercial facilities, real estate transfer, and casino gaming wagering taxes. Collections of these taxes are the responsibility of other State departments. Delinquent taxes are recognized as revenue to the extent that they will be collected within 12 months.

Deferred revenues (\$489.3 million and \$537.4 million as of September 30, 2009 and September 30, 2008, respectively) are recognized if the tax revenue is not considered "available," e.g., received within 60 days of the fiscal year-end.

In general, taxes receivable represent amounts due to the State at September 30 and the underlying economic event occurred on or before September 30. For example, sales and use taxes are accrued to the extent that the related sales occurred prior to October 1 and the State receives tax payments prior to December 1. Annual tax payments (those paid with an annual return, such as personal income taxes) have not been accrued because they are neither reasonably estimable nor available.

The following taxes were due to the School Aid Fund:

Schedule of Taxes Receivable  
As of September 30  
(In Thousands)

	2009	2008
Gross taxes receivable	\$ 2,459,319	\$ 2,644,825
Less allowance for uncollectible receivables	(377,041)	(364,055)
Net taxes receivable	\$ 2,082,278	\$ 2,280,770
Current taxes receivable	\$ 2,020,786	\$ 2,214,040
Noncurrent taxes receivable	\$ 61,492	\$ 66,730

Note 7 Reserved Fund Balance

The reserved fund balance at September 30 consists of the following (in millions):

	2009	2008
Work projects	\$	\$ 2,915
Encumbrances	3,172	382
Noncurrent assets	1,650	4,208
Restricted revenues	246,298	247,089
Total reserved	\$ 251,119	\$ 254,595

The restricted revenues in the School Aid Fund fund balance represent the balance in the School Aid Stabilization Fund. Act 158, P.A. 2003, effective October 1, 2003, created the School Aid Stabilization Fund as a separate account within the School Aid Fund. Pursuant to this Act, any remaining fund balance in the School Aid Fund at year-end is transferred to this account and is restricted for future appropriations of the School Aid Fund.

## REQUIRED SUPPLEMENTARY INFORMATION

SCHOOL AID FUND  
Michigan Department of Education  
Budgetary Comparison Schedule  
Fiscal Years Ended September 30  
(In Thousands)

Statutory/Budgetary Basis	2009			Variance With Final Budget
	Original Budget	Final Budget	Actual	
Beginning budgetary fund balance	\$ 250,005	\$ 250,005	\$ 250,005	\$ 0
Resources (inflows)				
Taxes	\$ 11,028,498	\$ 10,197,659	\$ 10,197,659	\$ 0
From federal agencies	1,562,009	2,101,053	2,101,053	0
Miscellaneous		32,594	32,594	0
Transfers in	788,400	800,980	800,980	0
Total revenue inflows	\$ 13,378,907	\$ 13,132,287	\$ 13,132,287	\$ 0
Amount available for appropriation	\$ 13,628,911	\$ 13,382,292	\$ 13,382,292	\$ 0
Charges to appropriations (outflows)				
Education	\$ 13,378,907	\$ 13,213,495	\$ 13,138,553	\$ 74,942
Total charges to appropriations	\$ 13,378,907	\$ 13,213,495	\$ 13,138,553	\$ 74,942
Reconciling items:				
Change in noncurrent assets	\$	\$ 2,559	\$ 2,559	\$ 0
Net reconciling items	\$ 0	\$ 2,559	\$ 2,559	\$ 0
Ending budgetary fund balance	\$ 250,005	\$ 171,356	\$ 246,298	\$ 74,942

See accompanying notes to required supplementary information.

2008

Original Budget	Final Budget	Actual	Variance With Final Budget
\$ 83,925	\$ 83,925	\$ 83,925	\$ 0
\$ 984,858	\$ 10,772,286	\$ 10,772,286	\$ 0
1,479,326	1,377,664	1,377,664	0
	30,864	30,864	0
67,448	769,969	769,969	0
<u>\$ 2,531,632</u>	<u>\$ 12,950,783</u>	<u>\$ 12,950,783</u>	<u>\$ 0</u>
<u>\$ 2,615,557</u>	<u>\$ 13,034,708</u>	<u>\$ 13,034,708</u>	<u>\$ 0</u>
<u>\$ 2,531,632</u>	<u>\$ 12,812,387</u>	<u>\$ 12,788,952</u>	<u>\$ 23,435</u>
<u>\$ 2,531,632</u>	<u>\$ 12,812,387</u>	<u>\$ 12,788,952</u>	<u>\$ 23,435</u>
<u>\$</u>	<u>\$ 4,249</u>	<u>\$ 4,249</u>	<u>\$ 0</u>
<u>\$ 0</u>	<u>\$ 4,249</u>	<u>\$ 4,249</u>	<u>\$ 0</u>
<u><u>\$ 83,925</u></u>	<u><u>\$ 226,569</u></u>	<u><u>\$ 250,005</u></u>	<u><u>\$ 23,435</u></u>

SCHOOL AID FUND  
Michigan Department of Education  
Budgetary Comparison Schedule  
Budget-to-GAAP Reconciliation  
Fiscal Years Ended September 30  
(In Thousands)

	2009	2008
<b>Sources/inflows of resources</b>		
Actual amount (budgetary basis) available for appropriation from the budgetary comparison schedule	\$ 13,382,292	\$ 13,034,708
Differences - Budget to GAAP:		
Budgetary fund balance at the beginning of the year is a budgetary resource but is not a current year revenue for financial reporting purposes	(250,005)	(83,925)
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes	(800,980)	(769,969)
Total revenues as reported on the Statement of Revenues, Expenditures, and Changes in Fund Balance	\$ 12,331,307	\$ 12,180,814
<b>Uses/outflows of resources</b>		
Actual amounts (budgetary basis) total charges to appropriations from the budgetary comparison schedule	\$ 13,138,553	\$ 12,788,952
Differences - Budget to GAAP:		
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes, but in the year the supplies are received for financial reporting purposes	(2,790)	1,232
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	(39,000)	(3,833)
Total expenditures as reported on the Statement of Revenues, Expenditures, and Changes in Fund Balance	\$ 13,096,763	\$ 12,786,351

## Notes to Required Supplementary Information

### Note 1 Statutory/Budgetary Presentation

School Aid Fund appropriations are established annually by the Legislature.

The budgetary comparison schedule presents the original and final appropriated budgets for fiscal years 2008-09 and 2007-08, as well as the actual revenues and other sources (inflows), expenditures and encumbrances (outflows), and fund balance stated on the budgetary basis.

The original budget and related estimated revenues represent the spending authority enacted into law by the appropriation bills as of October 1, 2008 and October 1, 2007, respectively, and the original budget includes multi-year projects budgetary carry-forwards from the prior fiscal year.

Accounting principles generally accepted in the United States of America (GAAP) require that the final legal budget be reflected in the "Final Budget" column. Therefore, updated revenue estimates available for appropriations as of November 30, rather than the amounts shown in the original budget, are reported. The November 30 date is used because Act 431, P.A. 1984, as amended, permits budget adjustments by the Legislature through 60 days after year-end.

### Note 2 Statutory/Budgetary Reconciliation

The statutory/budgetary basis presentation differs from GAAP in ways that do not affect the ending fund balance.

For budgetary reporting purposes, encumbrances are included with expenditures in the "Actual" columns because they are considered uses of spending authority in the year the State incurs an obligation. Therefore, the "Original Budget" and "Final Budget" columns do not include encumbrance authorization balances carried over from the prior year. In financial statements prepared in accordance with GAAP, encumbrances are not included as expenditures. The effect of this difference is reflected as a reconciling item on the budgetary comparison schedule.



SUPPLEMENTAL  
FINANCIAL SCHEDULE

**MICHIGAN DEPARTMENT OF EDUCATION**  
Schedule of Expenditures of Federal Awards (Note 1)  
For the Period October 1, 2007 through September 30, 2009

Federal Agency/Program or Cluster	CFDA * Number	For the Fiscal Year Ended September 30, 2008		
		Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
<b>Financial Assistance</b>				
<b>U.S. Department of Agriculture</b>				
Child Nutrition Cluster:				
Direct Programs:				
School Breakfast Program	10.553	\$	\$ 55,455,967	\$ 55,455,967
National School Lunch Program	10.555		212,219,435	212,219,435
Special Milk Program for Children	10.556		722,354	722,354
Summer Food Service Program for Children	10.559		6,042,927	6,190,334
Total Child Nutrition Cluster		\$ 147,407	\$ 274,440,683	\$ 274,588,090
Emergency Food Assistance Cluster:				
Direct Program:				
Emergency Food Assistance Program (Administrative Costs)	10.568	\$ 31,764	\$ 2,221,097	\$ 2,252,861
ARRA - Emergency Food Assistance Program (Administrative Costs)	10.568			0
Total Emergency Food Assistance Cluster (Note 2)		\$ 31,764	\$ 2,221,097	\$ 2,252,861
Direct Programs:				
Child and Adult Care Food Program	10.558	765,791	60,519,978	61,285,769
State Administrative Expenses for Child Nutrition	10.560	3,932,558		3,932,558
Commodity Supplemental Food Program (Note 3)	10.565	113,956	4,768,990	4,882,946
Team Nutrition Grants	10.574	67,894	98,828	166,722
Child Nutrition Discretionary Grants Limited Availability	10.579	\$ 159,523	\$	\$ 159,523
ARRA - Child Nutrition Discretionary Grants Limited Availability	10.579			0
Total Child Nutrition Discretionary Grants Limited Availability		\$ 159,523	\$ 0	\$ 159,523
Fresh Fruit and Vegetable Program	10.582	9,205	701,771	710,976
Total Direct Programs		\$ 5,048,927	\$ 66,089,567	\$ 71,138,494
<b>Total U.S. Department of Agriculture</b>		<b>\$ 5,228,098</b>	<b>\$ 342,751,347</b>	<b>\$ 347,979,445</b>
<b>U.S. Department of Defense</b>				
Direct Program:				
Contract for Defense Activity for Non-Traditional Education Support	12.N3569703MDTM **	\$ 138,957	\$	\$ 138,957
<b>Total U.S. Department of Defense</b>		<b>\$ 138,957</b>	<b>\$ 0</b>	<b>\$ 138,957</b>
<b>U.S. Department of Education</b>				
Title I, Part A Cluster:				
Direct Programs:				
Title I Grants to Local Educational Agencies	84.010	\$ 5,724,238	\$ 422,282,235	\$ 428,006,473
ARRA - Title I Grants to Local Educational Agencies, Recovery Act	84.389			
Total Title I, Part A Cluster		\$ 5,724,238	\$ 422,282,235	\$ 428,006,473
Special Education Cluster (IDEA):				
Direct Programs:				
Special Education - Grants to States	84.027	\$ 15,017,037	\$ 359,200,887	\$ 374,217,924
Special Education - Preschool Grants	84.173	553,547	12,219,621	12,773,168
ARRA - Special Education Grants to States, Recovery Act	84.391			0
ARRA - Special Education - Preschool Grants, Recovery Act	84.392			0
Total Special Education Cluster (IDEA)		\$ 15,570,584	\$ 371,420,508	\$ 386,991,092
Early Intervention Services (IDEA) Cluster:				
Direct Programs:				
Special Education - Grants for Infants and Families	84.181	\$ 544,064	\$ 12,329,893	\$ 12,873,957
ARRA - Special Education - Grants for Infants and Families, Recovery Act	84.393			0
Total Early Intervention Services (IDEA) Cluster		\$ 544,064	\$ 12,329,893	\$ 12,873,957

This schedule continued on next page.

For the Fiscal Year Ended September 30, 2009			Total Expended and Distributed for the Two-Year Period
Directly Expended	Distributed to Subrecipients	Total Expended and Distributed	
\$	\$ 64,401,962	\$ 64,401,962	\$ 119,857,929
	236,582,516	236,582,516	448,801,951
	641,681	641,681	1,364,035
164,765	6,581,934	6,746,699	12,937,033
<b>\$ 164,765</b>	<b>\$ 308,208,093</b>	<b>\$ 308,372,858</b>	<b>\$ 582,960,948</b>
\$ 28,063	\$ 2,816,011	\$ 2,844,074	\$ 5,096,935
	995,933	995,933	995,933
<b>\$ 28,063</b>	<b>\$ 3,811,944</b>	<b>\$ 3,840,007</b>	<b>\$ 6,092,868</b>
753,317	61,016,827	61,770,144	123,055,913
4,109,048		4,109,048	8,041,606
108,359	5,035,383	5,143,742	10,026,688
244,319	64,343	308,662	475,384
\$ 521,495	\$	\$ 521,495	\$ 681,018
	246,170	246,170	246,170
<b>\$ 521,495</b>	<b>\$ 246,170</b>	<b>\$ 767,665</b>	<b>\$ 927,188</b>
21,243	941,045	962,288	1,673,264
<b>\$ 5,757,781</b>	<b>\$ 67,303,768</b>	<b>\$ 73,061,549</b>	<b>\$ 144,200,043</b>
<b>\$ 5,950,609</b>	<b>\$ 379,323,805</b>	<b>\$ 385,274,414</b>	<b>\$ 733,253,859</b>
\$ 52,951	\$	\$ 52,951	\$ 191,908
<b>\$ 52,951</b>	<b>\$ 0</b>	<b>\$ 52,951</b>	<b>\$ 191,908</b>
\$ 6,179,920	\$ 488,060,153	\$ 494,240,073	\$ 922,246,546
	2,361,991	2,361,991	2,361,991
<b>\$ 6,179,920</b>	<b>\$ 490,422,144</b>	<b>\$ 496,602,064</b>	<b>\$ 924,608,537</b>
\$ 11,986,721	\$ 377,422,860	\$ 389,409,581	\$ 763,627,505
571,089	11,959,598	12,530,687	25,303,855
	7,589,085	7,589,085	7,589,085
	86,676	86,676	86,676
<b>\$ 12,557,810</b>	<b>\$ 397,058,219</b>	<b>\$ 409,616,029</b>	<b>\$ 796,607,121</b>
\$ 551,553	\$ 11,629,984	\$ 12,181,537	\$ 25,055,494
	226,938	226,938	226,938
<b>\$ 551,553</b>	<b>\$ 11,856,922</b>	<b>\$ 12,408,475</b>	<b>\$ 25,282,432</b>

**MICHIGAN DEPARTMENT OF EDUCATION**  
Schedule of Expenditures of Federal Awards (Note 1)  
For the Period October 1, 2007 through September 30, 2009  
Continued

Federal Agency/Program or Cluster	CFDA * Number	For the Fiscal Year Ended September 30, 2008		
		Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
<b>State Fiscal Stabilization Fund Cluster:</b>				
Direct Program:				
ARRA - State Fiscal Stabilization Fund (SFSF) - Education State Grants, Recovery Act	84.394	\$	\$	\$ 0
Total - State Fiscal Stabilization Fund Cluster		\$ 0	\$ 0	\$ 0
<b>Direct Programs:</b>				
Migrant Education - State Grant Program	84.011	\$ 539,410	\$ 7,973,439	\$ 8,512,849
Title I Program for Neglected and Delinquent Children	84.013	5,620	758,049	763,669
Career and Technical Education - Basic Grants to States (Note 4)	84.048	2,375,702	37,008,972	39,384,674
Migrant Education - Coordination Program	84.144			0
Safe and Drug-Free Schools and Communities - National Programs	84.184	502,073		502,073
Safe and Drug-Free Schools and Communities - State Grants	84.186	283,044	7,866,400	8,149,444
Education for Homeless Children and Youth	84.196	185,613	1,689,663	1,875,276
Even Start - State Educational Agencies	84.213	72,172	2,861,048	2,933,220
Fund for the Improvement of Education	84.215	137,863		137,863
Tech-Prep Education	84.243	180,391	3,415,191	3,595,582
Charter Schools	84.282	405,825	5,013,614	5,419,439
Twenty-First Century Community Learning Centers	84.287	790,148	32,074,844	32,864,992
State Grants for Innovative Programs	84.298	757,201	2,326,831	3,084,032
Education Technology State Grants	84.318	487,993	6,906,434	7,394,427
Special Education - State Personnel Development	84.323		886,359	886,359
Advance Placement Program (Advanced Placement Test Fee; Advanced Placement Incentive Program Grants)	84.330	260,955		260,955
Comprehensive School Reform Demonstration	84.332	477	720,534	721,011
Teacher Quality Enhancement Grants	84.336		(558)	(558)
Reading First State Grants	84.357	3,344,203	29,835,464	33,179,667
Rural Education	84.358	29,711	811,190	840,901
English Language Acquisition Grants	84.365	331,538	8,401,107	8,732,645
Mathematics and Science Partnerships	84.366	406,491	3,962,316	4,368,807
Improving Teacher Quality State Grants	84.367	1,690,087	88,597,512	90,287,599
Grants for State Assessments and Related Activities	84.369	9,663,002		9,663,002
Statewide Data Systems	84.372	408,918		408,918
Special Education - Technical Assistance on State Data Collection	84.373	173,187		173,187
School Improvement Grants	84.377			0
Contract with National Center for Education Statistics	84.ED03CO0074 **	162,747		162,747
<b>Total Direct Programs</b>		<b>\$ 23,194,371</b>	<b>\$ 241,108,409</b>	<b>\$ 264,302,780</b>
<b>Total U.S. Department of Education</b>		<b>\$ 45,033,257</b>	<b>\$ 1,047,141,045</b>	<b>\$ 1,092,174,302</b>
<b><u>U.S. Department of Health and Human Services</u></b>				
Direct Programs:				
Substance Abuse and Mental Health Services - Projects of Regional and National Significance	93.243	\$	\$	\$ 0
Cooperative Agreements to Support Comprehensive School Health Programs to Prevent the Spread of HIV and Other Important Health Problems	93.938	529,204	256,510	785,714
<b>Total U.S. Department of Health and Human Services</b>		<b>\$ 529,204</b>	<b>\$ 256,510</b>	<b>\$ 785,714</b>
<b><u>Corporation for National and Community Service</u></b>				
Direct Program:				
Learn and Serve America - School and Community Based Programs	94.004	\$ 0	\$ 646,878	\$ 646,878
<b>Total Corporation for National and Community Service</b>		<b>\$ 0</b>	<b>\$ 646,878</b>	<b>\$ 646,878</b>
<b>Total Financial Assistance</b>		<b>\$ 50,929,516</b>	<b>\$ 1,390,795,780</b>	<b>\$ 1,441,725,296</b>

This schedule continued on next page.

For the Fiscal Year Ended September 30, 2009			Total Expended and Distributed for the Two-Year Period
Directly Expended	Distributed to Subrecipients	Total Expended and Distributed	
\$	\$ 597,471,883	\$ 597,471,883	\$ 597,471,883
\$ 0	\$ 597,471,883	\$ 597,471,883	\$ 597,471,883
\$ 682,576	\$ 7,250,795	\$ 7,933,371	\$ 16,446,220
10,966	873,999	884,965	1,648,634
2,595,745	37,936,543	40,532,288	79,916,962
43,547		43,547	43,547
2,312		2,312	504,385
302,855	7,039,080	7,341,935	15,491,379
321,510	1,792,290	2,113,800	3,989,076
72,935	2,334,113	2,407,048	5,340,268
204,653		204,653	342,516
182,017	3,330,274	3,512,291	7,107,873
346,972	3,822,544	4,169,516	9,588,955
886,071	35,444,529	36,330,600	69,195,592
80,341	1,500,123	1,580,464	4,664,496
413,356	10,256,809	10,670,165	18,064,592
	1,299,304	1,299,304	2,185,663
365,411		365,411	626,366
		0	721,011
		0	(558)
2,688,883	12,244,496	14,933,379	48,113,046
38,740	1,339,529	1,378,269	2,219,170
329,096	9,095,292	9,424,388	18,157,033
343,983	5,169,456	5,513,439	9,882,246
1,918,818	96,151,469	98,070,287	188,357,886
12,414,786		12,414,786	22,077,788
1,921,753		1,921,753	2,330,671
111,097		111,097	284,284
379,817	1,036,317	1,416,134	1,416,134
164,761		164,761	327,508
\$ 26,823,001	\$ 237,916,962	\$ 264,739,963	\$ 529,042,743
<b>\$ 46,112,284</b>	<b>\$ 1,734,726,130</b>	<b>\$ 1,780,838,414</b>	<b>\$ 2,873,012,716</b>
\$ 54,959	\$	\$ 54,959	\$ 54,959
680,679	245,173	925,852	1,711,566
<b>\$ 735,638</b>	<b>\$ 245,173</b>	<b>\$ 980,811</b>	<b>\$ 1,766,525</b>
\$ 0	\$ 601,317	\$ 601,317	\$ 1,248,195
<b>\$ 0</b>	<b>\$ 601,317</b>	<b>\$ 601,317</b>	<b>\$ 1,248,195</b>
\$ 52,851,482	\$ 2,114,896,425	\$ 2,167,747,907	\$ 3,609,473,203

MICHIGAN DEPARTMENT OF EDUCATION  
Schedule of Expenditures of Federal Awards (Note 1)  
For the Period October 1, 2007 through September 30, 2009  
Continued

Federal Agency/Program or Cluster	CFDA *	For the Fiscal Year Ended September 30, 2008		
		Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
<u>Nonfinancial Assistance</u>				
<b>U.S. Department of Agriculture</b>				
Emergency Food Assistance Cluster:				
Direct Program:				
Emergency Food Assistance Program (Food Commodities)	10.569	\$	\$ 8,210,529	\$ 8,210,529
ARRA - Emergency Food Assistance Program (Food Commodities)	10.569			0
Total Emergency Food Assistance Cluster (Note 2)		\$ 0	\$ 8,210,529	\$ 8,210,529
Direct Programs:				
Food Donation (Note 5)	10.550	\$	\$ 26,119,662	\$ 26,119,662
Commodity Supplemental Food Program (Note 3)	10.565		16,155,586	16,155,586
Total Direct Programs		\$ 0	\$ 42,275,248	\$ 42,275,248
<b>Total U.S. Department of Agriculture</b>		<b>\$ 0</b>	<b>\$ 50,485,777</b>	<b>\$ 50,485,777</b>
Total Nonfinancial Assistance		\$ 0	\$ 50,485,777	\$ 50,485,777
Total Expenditures of Federal Awards		\$ 50,929,516	\$ 1,441,281,557	\$ 1,492,211,073

\* CFDA is defined as *Catalog of Federal Domestic Assistance*.

\*\* CFDA number not available. Number derived from federal agency number and contract number.

The accompanying notes are an integral part of this schedule.

For the Fiscal Year Ended September 30, 2009			Total Expended and Distributed for the Two-Year Period
Directly Expended	Distributed to Subrecipients	Total Expended and Distributed	
\$	\$ 20,901,696	\$ 20,901,696	\$ 29,112,225
	2,272,779	2,272,779	2,272,779
<u>\$ 0</u>	<u>\$ 23,174,475</u>	<u>\$ 23,174,475</u>	<u>\$ 31,385,004</u>
\$	\$ 32,584,972	\$ 32,584,972	\$ 58,704,634
	18,632,397	18,632,397	34,787,983
<u>\$ 0</u>	<u>\$ 51,217,369</u>	<u>\$ 51,217,369</u>	<u>\$ 93,492,617</u>
<b>\$ 0</b>	<b>\$ 74,391,844</b>	<b>\$ 74,391,844</b>	<b>\$ 124,877,621</b>
\$ 0	\$ 74,391,844	\$ 74,391,844	\$ 124,877,621
<u>\$ 52,851,482</u>	<u>\$ 2,189,288,269</u>	<u>\$ 2,242,139,751</u>	<u>\$ 3,734,350,824</u>

## Notes to the Schedule of Expenditures of Federal Awards

### Note 1 Basis of Presentation

This schedule presents the federal grant activity of the Michigan Department of Education (MDE) on the modified accrual basis of accounting and in accordance with the requirements of U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. In certain programs, financed entirely by the federal government, expenditures and related revenue are recognized only to the extent of billings received by fiscal year-end. This treatment understates assets and liabilities and expenditures and revenues; however, there is no impact on the fund balance of the State's General Fund.

### Note 2 Emergency Food Assistance Cluster

The Emergency Food Assistance Cluster is made up of financial assistance (CFDA 10.568) totaling \$2.3 million and \$3.8 million and nonfinancial assistance (CFDA 10.569) valued at \$8.2 million and \$20.9 million as of September 30, 2008 and September 30, 2009, respectively.

### Note 3 Commodity Supplemental Food Program

The Commodity Supplemental Food Program is made up of financial assistance (CFDA 10.565) totaling \$4.9 million and \$5.1 million, as well as nonfinancial assistance (CFDA 10.565) distributed to subrecipients valued at \$16.2 million and \$18.6 million as of September 30, 2008 and September 30, 2009, respectively.

### Note 4 Program Transfers

This schedule presents the federal grant activity for Career and Technical Education - Basic Grants to States (CFDA 84.048) for the fiscal years ended September 30, 2008 and September 30, 2009. On May 1, 2007, the Governor issued Executive Order No. 2007-4, which transferred career and technical education programs, pursuant to the Carl D. Perkins Vocational and Technical Education Act of 1998, as amended, to the State Board of Education within MDE. The State Board of Education then delegated the responsibilities regarding postsecondary career and technical education back to the Department of Labor and Economic Growth (DLEG), while the responsibility for secondary students remained with MDE. Pursuant to an interagency

agreement between DLEG and MDE, these transfers took effect for administrative purposes on October 1, 2007.

Note 5 Food Donation

*CFDA* 10.550 pertains to food commodities distributed by the U.S. Department of Agriculture (USDA) under the following categorical programs: National School Lunch Program (*CFDA* 10.555) and Summer Food Service Program for Children (*CFDA* 10.559). The USDA deleted this number from the *CFDA* on May 6, 2008. The audit covering MDE's fiscal year beginning October 1, 2009, and future audits, will therefore identify commodity assistance by the *CFDA* numbers of the programs under which the USDA donated the commodities.

Note 6 Reporting Entity

In fiscal years 2007-08 and 2008-09, the majority of federal grants were reported in the School Aid Fund. Administrative federal expenses and transfers to other State agencies were recorded in the State's General Fund.



# INDEPENDENT AUDITOR'S REPORTS ON INTERNAL CONTROL AND COMPLIANCE



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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

## Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters

Mr. Michael P. Flanagan  
Superintendent of Public Instruction  
Michigan Department of Education  
John A. Hannah Building  
Lansing, Michigan

Dear Mr. Flanagan:

We have audited the financial schedules and financial statements of the Michigan Department of Education as of and for the fiscal years ended September 30, 2009 and September 30, 2008, as identified in the table of contents, and have issued our reports thereon dated June 25, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

### Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial schedules and financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed in the next paragraph, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control

deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial schedules and financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in Findings 1 through 3 in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial schedules and financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described in the third paragraph of this section, we consider Finding 1 to be a material weakness.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial schedules and financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial schedule and financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The Department's responses to the findings identified in our audit are described in the accompanying corrective action plan. We did not audit the Department's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Governor, the Legislature, the State Board of Education, the Department's management, others within the Department, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

June 25, 2010



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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

Independent Auditor's Report on Compliance With  
Requirements Applicable to Each Major Program  
and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133

Mr. Michael P. Flanagan  
Superintendent of Public Instruction  
Michigan Department of Education  
John A. Hannah Building  
Lansing, Michigan

Dear Mr. Flanagan:

Compliance

We have audited the compliance of the Michigan Department of Education with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each major federal program for the two-year period ended September 30, 2009. The Department's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each major federal program is the responsibility of the Department's management. Our responsibility is to express an opinion on the Department's compliance based on our audit.

We conducted our audit of compliance in accordance with 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 OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to in the preceding paragraph that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Department's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Department's compliance with those requirements.

In our opinion, the Michigan Department of Education complied, in all material respects, with the requirements referred to in the first paragraph that are applicable to each of its major federal programs for the two-year period ended September 30, 2009. However, the results of our auditing

procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as Findings 4 through 17.

#### Internal Control Over Compliance

The management of the Department is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Department's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, 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 the Department's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the Department's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as Findings 4 through 8 and 10 through 17 to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We did not consider any of the deficiencies described in the preceding paragraph to be material weaknesses.

The Department's responses to the findings identified in our audit are described in the accompanying corrective action plan. We did not audit the Department's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Governor, the Legislature, the State Board of Education, the Department's management, others within the Department, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

June 25, 2010

# SCHEDULE OF FINDINGS AND QUESTIONED COSTS

## Section I: Summary of Auditor's Results

### Financial Schedules and Financial Statements

Type of auditor's report issued: Unqualified\*

Internal control\* over financial reporting:

Material weaknesses\* identified? Yes

Significant deficiencies\* identified that are not considered to be material weaknesses? Yes

Noncompliance or other matters material to the financial schedules and/or financial statements? No

### Federal Awards

Internal control over major programs:

Material weaknesses\* identified? No

Significant deficiencies\* identified that are not considered to be material weaknesses? Yes

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133, Section 510(a)? Yes

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster*</u>
10.550	Food Donation
10.558	Child and Adult Care Food Program
10.565	Commodity Supplemental Food Program

\* See glossary at end of report for definition.

Emergency Food Assistance Cluster:

- 10.568 • Emergency Food Assistance Program (Administrative Costs)
- 10.568 • ARRA - Emergency Food Assistance Program (Administrative Costs)
- 10.569 • Emergency Food Assistance Program (Food Commodities)
- 10.569 • ARRA - Emergency Food Assistance Program (Food Commodities)

Title I, Part A Cluster:

- 84.010 • Title I Grants to Local Educational Agencies
- 84.389 • ARRA - Title I Grants to Local Educational Agencies, Recovery Act

Special Education Cluster (IDEA):

- 84.027 • Special Education - Grants to States
- 84.173 • Special Education - Preschool Grants
- 84.391 • ARRA - Special Education Grants to States, Recovery Act
- 84.392 • ARRA - Special Education - Preschool Grants, Recovery Act

84.048 Career and Technical Education - Basic Grants to States

Early Intervention Services (IDEA) Cluster:

- 84.181 • Special Education - Grants for Infants and Families
- 84.393 • ARRA - Special Education - Grants for Infants and Families, Recovery Act

84.186 Safe and Drug-Free Schools and Communities - State Grants

84.282 Charter Schools

84.298 State Grants for Innovative Programs

84.318 Education Technology State Grants

84.357	Reading First State Grants
84.365	English Language Acquisition Grants
84.366	Mathematics and Science Partnerships
84.367	Improving Teacher Quality State Grants
84.369	Grants for State Assessments and Related Activities
84.394	<u>State Fiscal Stabilization Fund Cluster:</u> <ul style="list-style-type: none"> <li>• ARRA - State Fiscal Stabilization Fund (SFSF) - Education State Grants, Recovery Act</li> </ul>

Dollar threshold used to distinguish between type A and type B programs: \$11,203,052

Auditee qualified as a low-risk auditee\*? No

## **Section II: Findings Related to the Financial Schedules and Financial Statements**

### **FINDING (3131001)**

#### **1. Security and Application Controls**

The Michigan Department of Education (MDE), in conjunction with the Michigan Department of Information Technology (MDIT), did not implement a comprehensive security program to protect its application systems and data.

Without a comprehensive security program, management cannot ensure that MDE's internal control is operating as intended and that the integrity of its data is safeguarded. We noted:

- a. MDE did not restrict the system developers and project management personnel from administrative access privileges for MDE's information systems database. As a result, unauthorized changes to MDE's systems and data could be made and go undetected. System developers and project management personnel possess a detailed knowledge about the systems and

\* See glossary at end of report for definition.

their controls. Granting these individuals administrative access privileges gives them the ability to bypass established system controls and make changes to the data. In addition, it increases the risk that an individual could process unauthorized transactions.

- b. MDE, in conjunction with MDIT, did not have effective controls to identify unauthorized changes to application systems. While both MDE and MDIT used numbering systems for requesting and processing change requests, respectively, the two numbering systems were not linked. As a result, neither MDE nor MDIT could trace a change request from initial request through to production. An effective change control process would ensure that all program modifications are properly initiated, authorized, and tracked.
- c. MDE had not developed policies for monitoring access to all MDE data or applications. Periodic monitoring of access ensures that only authorized users have access to data and applications. For example, MDE policies may include identifying and monitoring high-risk transactions.

We first reported this issue in our performance audit\* of Technology Services and the Automated Information Systems, Department of Education (31-594-00), issued May 2001. We again noted this issue in our two prior MDE Single Audits\* issued in 2006 and 2008. MDE agreed with our recommendation and informed us that improvements to security were implemented. However, we found that MDE and MDIT had not allocated the resources to complete all necessary system changes to establish an effective and comprehensive information security program.

### **RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE, IN CONJUNCTION WITH MDIT, IMPLEMENT A COMPREHENSIVE SECURITY PROGRAM TO PROTECT ITS APPLICATION SYSTEMS AND DATA.

\* See glossary at end of report for definition.

## **FINDING (3131002)**

### **2. Monitoring of Internal Control Over Financial Reporting**

MDE did not periodically monitor the effectiveness of its internal control over financial reporting. As a result, MDE was not assured that its internal control was sufficiently designed to ensure that its assets were safeguarded and the accounting data was accurate and properly reported.

Monitoring the effectiveness of MDE's internal control should include assessing risk related to MDE's accounting systems and processes, determining if controls have been designed to mitigate risk, and periodically evaluating the controls to determine if the controls are functioning as designed.

Section 18.1485 of the *Michigan Compiled Laws* (a section of Act 431, P.A. 1984, as amended) requires State agencies to establish and maintain an internal control system and to document the system, communicate system requirements, and ensure that the system is functioning as prescribed. In addition, this section requires State agencies to complete a biennial assessment of risks and identify controls over financial accounting and reporting.

MDE completed its biennial assessment, which included assessing risks and determining key controls that were related to the assessed risks. However, our review disclosed that MDE did not periodically evaluate and test the reliability of most of the key controls over financial reporting that it had listed in its biennial assessment.

For example, to ensure that all general ledger transactions were for valid items, were properly valued, and were correctly recorded, MDE documented that one of its key controls was that divisions had monitored their accounts for proper recording and classification. However, MDE did not test this control. MDE could have reviewed a sample of transactions to ensure that the transactions were properly recorded to determine if this control was working.

In addition, Section 18.1486(4)(b) of the *Michigan Compiled Laws* requires the internal auditor of each principal department to conduct audits relating to financial activities of the department's operations. The internal audit staff at the State Budget Office, along with MDE management, could play an important role in evaluating the effectiveness of controls by independently testing and verifying the

integrity of MDE's system of internal control. We noted that neither the internal audit staff at the State Budget Office nor MDE had audited MDE's key controls over financial reporting.

We reported on this issue in our prior Single Audit, and MDE responded that it expected the internal audit staff of the State Budget Office to periodically monitor the effectiveness of MDE's internal control over financial reporting. However, we do not believe that this sufficiently addresses the requirement in Section 18.1485 that MDE ensure that the internal control system is functioning as prescribed.

### **RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE PERIODICALLY MONITOR THE EFFECTIVENESS OF ITS INTERNAL CONTROL OVER FINANCIAL REPORTING.

### **FINDING (3131003)**

#### 3. Accounting Controls

MDE's year-end closing procedures did not ensure that all accrual transactions were properly recorded in the School Aid Fund. As a result, MDE did not detect that it had not recorded payables and receivables for school districts' special education costs and that it incorrectly recorded payables and receivables related to changes in taxable value for the Proposal A accrual. Subsequent to our review, the Office of Financial Management (OFM), State Budget Office, recorded adjusting transactions prior to the issuance of the School Aid Fund financial statements.

We identified the following errors in the School Aid Fund for fiscal year 2008-09 year-end accrual transactions:

- a. MDE did not record the accruals for changes in school districts' costs for selected special education programs. As a result, accounts payable were understated by \$24,248,099, amounts due from local units were understated by \$25,257,396, and expenditures were overstated and fund balance was understated by \$1,009,297.

- b. MDE incorrectly recorded accruals related to taxable value changes based on fiscal year 2007-08 data rather than fiscal year 2008-09 data. As a result, accounts payable and expenditures were overstated by \$14,444,393 and amounts due from local units and miscellaneous revenues were overstated by \$5,802,222. This results in a fund balance understatement of \$8,642,171.

Our review of the adjusting transactions recorded by OFM disclosed that amounts due from local units, miscellaneous revenues, and reserved fund balance were still overstated by \$442,658 as of September 30, 2009.

Section 18.1485 of the *Michigan Compiled Laws* (a section of Act 431, P.A. 1984, as amended) provides that State agencies are responsible for developing and maintaining a system of controls over the preparation of financial statements in accordance with generally accepted accounting principles.

MDE informed us that these errors occurred because the programming query used to extract the data from its payment system was not accurate. MDE performs a supervisory review of year-end closing transactions. However, MDE did not include a comparison of the amounts calculated for the current year to the amounts recorded in prior years. This review could help detect the omission of an account payable or an account receivable. In addition, MDE should compare subsequent year actual payments to the estimated Proposal A accruals for individual districts to help detect errors in the amount calculated as a payable or a receivable for taxable value changes.

### **RECOMMENDATION**

We recommend that MDE ensure that all year-end closing accrual transactions are properly recorded in the School Aid Fund.

**The status of the findings related to the financial schedules and financial statements that were reported in prior Single Audits is disclosed in the summary schedule of prior audit findings.**

## Section III: Findings and Questioned Costs\* Related to Federal Awards

### **FINDING (3131004)**

#### 4. Food Donation, CFDA 10.550

U.S. Department of Agriculture	CFDA 10.550: Food Donation
Award Number: N/A	Award Period: N/A
	Known Questioned Costs: \$0

MDE's internal control over the Food Donation Program did not ensure its compliance with federal laws and regulations regarding special tests and provisions. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions in Food Donation commodities.

The U.S. Department of Agriculture (USDA) donates food commodities to MDE, the State's distributing agency, for distribution to School Food Authorities (SFAs) that participate in the National School Lunch Program. SFAs receive commodity entitlements based on the number of eligible lunches served to school children. The value of USDA donated food commodities for the Food Donation Program totaled \$58.7 million for the two-year period ended September 30, 2009.

MDE is responsible for oversight of the Food Donation Program and for ensuring compliance with federal laws and regulations relating to USDA donated food commodities. MDE has entered into agreements with three consortiums to distribute USDA donated food commodities. The consortiums, in turn, contract directly with their own processors and distributors to process, warehouse, and distribute food commodities to SFAs.

Our audit disclosed the following internal control weaknesses over compliance with federal regulations related to special tests and provisions:

- a. MDE did not provide the necessary oversight to ensure that consortiums were in compliance with federal regulations regarding maintenance of records, storage facility standards, and annual reviews of storage facilities.

\* See glossary at end of report for definition.

Title 7, Part 250, section 16(a)(4) of the *Code of Federal Regulations (CFR)* requires MDE to ensure that distributors utilized by the program keep accurate and complete records with respect to the receipt, distribution/disposal, storage, and inventory of the USDA donated commodities. In addition, federal regulation 7 *CFR* 250.14(b) requires MDE to ensure that facilities used for the handling, storage, and distribution of donated foods meet certain standards. Finally, federal regulation 7 *CFR* 250.14(c) requires MDE to ensure that annual reviews of storage facilities are conducted. These reviews must include conducting physical inventories and a reconciliation of the inventory with inventory records.

MDE informed us that it relied on the agreements between the consortiums and their distributors to ensure that the distributors comply with federal requirements. MDE informed us that it does not conduct, nor is it required to conduct, on-site visits of the consortiums' distributors. However, because MDE did not require the consortiums to conduct on-site visits of distributors and did not require the consortiums to submit documentation or the results of any on-site visits conducted, MDE could not document its compliance with federal requirements. Failure to comply with these warehousing requirements could potentially result in improper distribution or loss of USDA donated foods.

- b. MDE did not require processors to submit written justification of excess inventories of USDA donated commodities. As a result, MDE did not maintain written approvals for all excess inventories.

Federal regulation 7 *CFR* 250.30(n) requires MDE to ensure that processor inventories do not exceed a six-month supply based on the processor's average monthly usage, unless a higher level has been specifically approved by MDE as a result of written justification submitted by the processor. USDA policy requires MDE to provide written approval of the excess inventories. Excess inventories could potentially be a result of ordering commodities in excess of demand or of SFAs failing to use up their commodity inventories. It is essential that MDE work closely with the processors to determine the cause and whether transfers of commodities are necessary.

We reviewed all 18 commodities listed on 14 monthly performance reports submitted to MDE during our audit period. The inventory levels for 13 (72%) of the 18 commodities exceeded a six-month supply. The monthly supply for

10 commodities ranged from 11 to 81 months. MDE's practice was to periodically review the monthly performance reports, identify excess inventory levels, and evaluate the reasonableness of any surpluses. However, for 11 (85%) of the 13 commodities, MDE had not obtained written justification from the processors for the excess inventories and had not provided written approval for the excess inventories. MDE informed us that the processors were not properly informed of the requirement for submitting written justification for excess inventories. As a result, the majority of processors did not submit written justification regarding excess inventory levels.

- c. MDE's methodology for conducting semiannual sales verifications was not in compliance with federal regulations.

Federal regulation 7 *CFR* 250.19(b)(2) requires distributing agencies to conduct a semiannual review of a sample of sales for the previous six-month period for selected processors utilized by the Food Donation Program. Since MDE has delegated this responsibility to processors, federal regulations require that MDE, in its role as the distributing agency, must review the processors' findings, select a random subsample of at least 10% of all sales verified by the processors, and reverify the sample items by direct confirmation with the SFA.

We reviewed MDE's process for reverifying a sample of sales verified by the processors. MDE was required to reverify all sales for the six-month period for 10% of the schools that were verified by processors. MDE program staff incorrectly computed the samples for reverification resulting in significantly undertesting the processors' sample. For example, if a processor verified sales for 200 schools, MDE should have verified sales for 20 (10%) of those schools. However, MDE selected one or two schools that combined had sales of at least 20 cases of product and only verified those 20 cases, instead of reviewing the sales for 20 schools. Sales verifications are essential for ensuring that the value of USDA commodities is properly passed through to the SFAs and that any problems are identified and corrected.

- d. MDE did not retain documentation of its sales verifications submitted by the processors for the six-month period ended June 2008, nor could it provide documentation regarding its reverifications. Program staff informed us that this documentation had been misplaced and could not be located but assured

us that the sales verifications were completed and submitted as required. However, without reviewing this documentation, we could not verify that the required verifications and reverifications were completed.

**RECOMMENDATION**

We recommend that MDE improve its internal control over the Food Donation Program to ensure its compliance with federal laws and regulations regarding special tests and provisions.

**FINDING (3131005)**

5. Child and Adult Care Food Program, CFDA 10.558

U.S. Department of Agriculture	CFDA 10.558: Child and Adult Care Food Program
Award Number: 2008CN202042 2008IN202042 2009IN202042	Award Period: 10/01/2007 - 09/30/2008 10/01/2007 - 09/30/2008 10/01/2008 - 09/30/2009
	Known Questioned Costs: \$16,228

MDE's internal control over the Child and Adult Care Food Program did not ensure its compliance with federal laws and regulations regarding eligibility and reporting. As a result, we questioned costs of \$16,228. Noncompliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Child and Adult Care Food Program awards.

Federal expenditures for Child and Adult Care Food Program totaled \$123.1 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$60.5 million and \$61.0 million to 439 and 470 subrecipients\* in fiscal years 2007-08 and 2008-09, respectively. Program subrecipients included sponsoring organizations of child day care centers and family day care homes, as well as independent child day care centers. These subrecipients are collectively known as institutions that each have one or more sites providing child day care food services.

\* See glossary at end of report for definition.

Our audit disclosed the following exceptions by compliance area:

a. Eligibility

MDE's internal control did not ensure that it reimbursed program expenditures only to eligible subrecipients.

Federal regulation 7 *CFR* 226.15(l) requires that no institution participate in both the Child and Adult Care Food Program and the Special Milk Program at the same time. Additional USDA guidance indicates that the eligibility to participate in the Child and Adult Care Food Program and the Special Milk Program can be determined on a site-by-site basis.

We performed an analytical review of Child and Adult Care Food Program and Special Milk Program expenditures. We were able to confirm that 7 sites of one subrecipient claimed the same children in both the Child and Adult Care Food Program and the Special Milk Program during fiscal years 2007-08 and 2008-09, which resulted in questioned costs of \$16,228 in the Child and Adult Care Food Program.

b. Reporting

MDE did not report accrued expenditures eligible for federal reimbursement in the fiscal year 2008-09 fourth quarter year-end report for one grant. We determined that the omission resulted in a combined understatement of \$1,464,023 for the total expenditures eligible for federal reimbursement for the grant. Federal regulation 7 *CFR* 226.7(d) requires each State agency to submit quarterly and year-end final financial status reports of the Child and Adult Care Food Program reporting obligations in the fiscal year in which they occur. Our review disclosed that although MDE reported expenditures eligible for federal reimbursement inaccurately, MDE received the full amount in the subsequent quarter.

**RECOMMENDATION**

We recommend that MDE improve its internal control over the Child and Adult Care Food Program to ensure its compliance with federal laws and regulations regarding eligibility and reporting.

## **FINDING (3131006)**

### 6. Monitoring ARRA Grants, CFDA 10.568, 10.569, 84.389, 84.391, 84.392, 84.393, and 84.394

U.S. Department of Agriculture	Emergency Food Assistance Cluster: CFDA 10.568: ARRA - Emergency Food Assistance Program (Administrative Costs) CFDA 10.569: ARRA - Emergency Food Assistance Program (Food Commodities)
Award Number: 2M1840053	Award Period: 03/01/2009 - 09/30/2009
	Known Questioned Costs: \$0

U.S. Department of Education	Title I, Part A Cluster: CFDA 84.389: ARRA - Title I Grants to Local Educational Agencies, Recovery Act
Award Number: S389A090022 S389A09022A	Award Period: 02/17/2009 - 09/30/2010 02/17/2009 - 09/30/2010
	Known Questioned Costs: \$0

U.S. Department of Education	Special Education Cluster (IDEA): CFDA 84.391: ARRA - Special Education Grants to States, Recovery Act CFDA 84.392: ARRA - Special Education - Preschool Grants, Recovery Act
Award Number: H391A090110 H391A090110A H392A090117 H392A090117A	Award Period: 02/17/2009 - 09/30/2010 02/17/2009 - 09/30/2010 02/17/2009 - 09/30/2010 02/17/2009 - 09/30/2010
	Known Questioned Costs: \$0

U.S. Department of Education	Early Intervention Services (IDEA) Cluster: CFDA 84.393: ARRA - Special Education - Grants for Infants and Families, Recovery Act
Award Number: H393A090012	Award Period: 02/17/2009 - 09/30/2010
	Known Questioned Costs: \$0

U.S. Department of Education	State Fiscal Stabilization Fund Cluster: CFDA 84.394: ARRA - State Fiscal Stabilization Fund (SFSF) - Education State Grants, Recovery Act
Award Number: S394A090023	Award Period: 05/28/2009 - 09/30/2010
	Known Questioned Costs: \$0

MDE's internal control over the American Recovery and Reinvestment Act of 2009 (ARRA) funded grant programs did not ensure its compliance with federal laws and regulations regarding subrecipient monitoring specific to ARRA grants. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of ARRA grant awards for the Emergency Food Assistance Cluster, Title I Grants to Local Educational Agencies, Special Education Cluster (IDEA), Special Education - Grants for Infants and Families Program, and State Fiscal Stabilization Fund (SFSF) - Education State Grants Program.

Expenditures funded with ARRA grants for 6 of the 7 programs totaled \$608.7 million and the value of USDA donated food commodities totaled \$2.3 million for the period ended September 30, 2009. MDE distributed 100% of these funds to subrecipients. Subrecipients of the programs receiving ARRA funds included local educational agencies (LEAs), institutions of higher education, and nonprofit organizations.

Our review of MDE's subrecipient monitoring activities specific to the 7 programs that received ARRA grant funding disclosed:

- a. MDE did not ensure that subrecipients registered with the Central Contractor Registration (CCR) prior to receiving ARRA funds.

Federal regulation 2 *CFR* 176.50 requires subrecipients to maintain current registrations in the CCR if they have active federal awards funded with ARRA funds. The CCR is the primary registrant database for the U.S. federal government. The CCR collects, validates, stores, and disseminates data in support of agency acquisition missions. MDE informed us that it did not verify CCR registration before providing ARRA funding.

Using the CCR Web site, we tested a sample of subrecipients from the 6 ARRA programs to determine whether subrecipients were registered prior to receiving funds. MDE could not provide documentation that 2 (6%) of 31 subrecipients from the ARRA - State Fiscal Stabilization Fund (SFSF) - Education State Grants Program were registered with the CCR before receiving grant funds. We located documentation to verify that the subrecipients tested for the remaining 5 programs were registered with the CCR.

- b. MDE did not ensure that subrecipients receiving commodities funded by the ARRA - Emergency Food Assistance Program (Food Commodities) (TEFAP) were informed of all of the federal identifying information. As a result, 28 fiscal year 2008-09 TEFAP subrecipients may not have been aware that the funding for certain commodities was from the ARRA and could result in the subrecipients not properly identifying the ARRA commodities on their schedules of expenditures of federal awards.

Federal regulation 2 *CFR* 176.210 requires the recipients to separately identify to each subrecipient the federal award number, *CFDA* number, and amount of ARRA funds. When a recipient awards ARRA funds for an existing program, the information furnished to subrecipients shall distinguish the subawards of incremental ARRA funds from regular subawards under the existing program.

**RECOMMENDATION**

We recommend that MDE improve its internal control over ARRA funded grant programs to ensure its compliance with federal laws and regulations regarding subrecipient monitoring specific to ARRA grants.

**FINDING (3131007)**

7. Title I, Part A Cluster, *CFDA* 84.010 and 84.389

U.S. Department of Education	Title I, Part A Cluster: <i>CFDA</i> 84.010: Title I Grants to Local Educational Agencies <i>CFDA</i> 84.389: ARRA - Title I Grants to Local Educational Agencies, Recovery Act
Award Number: S010A070022 S010A070022A S010A080022 S010A080022A S010A090022 S010A090022A S389A090022 S389A090022A	Award Period: 07/01/2007 - 09/30/2008 07/01/2007 - 09/30/2008 07/01/2008 - 09/30/2009 07/01/2008 - 09/30/2009 07/01/2009 - 09/30/2010 07/01/2009 - 09/30/2010 02/17/2009 - 09/30/2010 02/17/2009 - 09/30/2010
	Known Questioned Costs: \$11,515,472

MDE's internal control over the Title I, Part A Cluster did not ensure its compliance with federal laws and regulations regarding allowable costs/costs principles, subrecipient monitoring, and special tests and provisions. As a result, we questioned costs of \$11,515,472. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Title I, Part A Cluster awards.

Federal expenditures for the Title I, Part A Cluster totaled \$924.6 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$422.3 million and \$490.4 million to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the Title I, Part A Cluster were LEAs.

In addition to the testing of Title I, Part A Cluster grant expenditures in this audit, our audit report on the performance audit of Assistance to High Priority Schools, Office of School Improvement, Michigan Department of Education (313-0201-08), issued in May 2010, disclosed internal control weaknesses and questioned costs related to the Title I Grants to LEAs Program, which is part of the Title I, Part A Cluster. The exceptions, by compliance area, from both audits are as follows:

a. Allowable Costs/Cost Principles

MDE's internal control did not ensure that subrecipients met allowable costs/cost principles for Title I Grants to LEAs Program grant expenditures. Our review disclosed:

- (1) One of MDE's subrecipients incorrectly charged the Title I Grants to LEAs Program \$48,700 for services not related to Title I Grants to LEAs Program high priority schools. OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments* (federal regulation 2 CFR 225), provides that any cost allocable to a particular federal award may not be charged to other federal awards. Neither MDE nor its subrecipient documented that these services were for Title I Grants to LEAs Program high priority schools. Our review of supporting documentation indicates that the services were for two other federal grants.
- (2) Neither MDE nor its subrecipient could demonstrate that \$11.1 million in professional and information technology services expenditures had met the reasonable cost criteria in accordance with federal regulations. OMB

Circular A-87 (federal regulation 2 *CFR* 225) indicates that, in determining reasonableness of a given cost, consideration shall be given to market prices for comparable good or services. Three contracts for professional and information technology services totaling \$11.1 million were not competitively bid. Neither MDE nor the subrecipient documented how the contract amounts were determined to be reasonable. We questioned the \$11,151,302 in costs MDE paid over three years from October 1, 2006 through September 30, 2009 for the professional and information technology services.

b. Subrecipient Monitoring

MDE's internal control did not ensure that it monitored subrecipients' submission of compliance plans, cash draws, completion of required performance reports, and compliance with Education Department General Administrative Regulations and Title I Grants to LEAs Program set-aside requirements. If MDE does not sufficiently monitor subrecipient activities, MDE cannot be assured that subrecipients used federal awards in compliance with laws, regulations, and provisions of contracts or grant agreements and that performance goals were achieved.

MDE reviewed subrecipients' program budgets for allowable activities and costs, provided training, appropriately identified federal award information to subrecipients, and performed on-site monitoring and desk reviews for selected subrecipients. However, our review of MDE's subrecipient monitoring activities disclosed:

- (1) MDE did not ensure that 27 subrecipients submitted compliance plans based on deficiencies identified during MDE's on-site visits.

MDE's Field Services Unit conducted 70 comprehensive on-site visits during fiscal years 2007-08 and 2008-09. The Field Services Unit is responsible for the on-site visits of several federal programs, including the Title I Program. MDE's on-site reports included recommendations requiring corrective action for all 70 subrecipients. MDE had not received required compliance plans from 27 (39%) of the 70 subrecipients. All of the 27 on-site visit files requiring compliance plans identified deficiencies related to the Title I Program.

MDE procedures require that when the on-site monitoring review identifies recommendations requiring corrective action, the subrecipient must submit a compliance plan to MDE within 30 days after receipt of the on-site review report.

In our prior Single Audit, we reported this issue and MDE informed us that it was unable to fully implement procedures because of staffing limitations.

- (2) MDE did not monitor subrecipient cash draws to ensure that the draws were only for reimbursement needs. We noted that 1 of 26 subrecipients had requested a cash draw that may have been in excess of its expenditure needs. The cash draw was for 100% of the subrecipient's total grant award, yet the percentage of the grant award period that had expired was 42%. Because MDE allows subrecipients to draw funds electronically without providing supporting documentation, monitoring unusually large subrecipient cash draws would help to ensure that subrecipients are in compliance with cash management requirements.
- (3) MDE did not ensure that its subrecipient had received audit services prior to paying for the services and had contracts with consultants. We noted that MDE's subrecipient paid for audit services prior to receiving the audit reports it had contracted for. In addition, the subrecipient paid a total of \$315,470 to 7 consultants for which it did not have supporting contracts. Federal Education Department General Administrative Regulations require grantees and subgrantees to maintain a contract administration system to ensure that contractors perform in accordance with the terms, conditions, and specifications of their contracts or purchase orders. We questioned \$315,470 in costs.
- (4) MDE did not ensure that its subrecipients (school districts) set aside required funds from their school improvement grants to provide tutoring and transportation to schools of choice when school buildings within the districts failed to make annual yearly progress.

Federal regulations require that school districts set aside an amount equal to 20% of their grant allocation for Title I, Part A, Improving Basic Programs Operated by Local Educational Agencies, unless a lesser

amount is needed. The 20% set-aside establishes a budget for LEAs to provide tutoring and the transportation of students opting to transfer to another school. We noted that 6 of the 10 school districts we reviewed did not set aside the required amount or demonstrate a lesser amount was needed during fiscal year 2007-08. For example, in fiscal year 2007-08, the 10 local school districts were required to set aside a total of \$37.0 million, and the actual amount set aside was \$32.4 million and actual expenditures for tutoring and transportation were only \$17.2 million.

c. Special Tests and Provisions

MDE did not always document its determination that LEAs had demonstrated their compliance with comparability requirements. We reviewed a sample of 24 LEAs for which the comparability requirement was applicable. We noted that MDE had not documented its determination for 4 (17%) of the 24 LEAs that submitted documentation of their compliance with comparability requirements.

Section 1120A(c) of the Elementary and Secondary Education Act requires LEAs receiving program funds to use State and local funds in participating schools to provide services that, taken as a whole, are at least comparable to services that the LEAs are providing in schools not receiving Title I, Part A funds. MDE reviews documentation submitted by LEAs and approves it after determining that instructional staffing levels of schools that received Title I, Part A Cluster funding were comparable to schools that did not.

**RECOMMENDATIONS**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE TITLE I, PART A CLUSTER TO ENSURE ITS COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING SUBRECIPIENT MONITORING.

We also recommend that MDE improve its internal control over the Title I, Part A Cluster to ensure its compliance with federal laws and regulations regarding allowable costs/cost principles and special tests and provisions.

## **FINDING (3131008)**

### **8. Special Education Cluster (IDEA), CFDA 84.027, 84.173, 84.391 (ARRA), and 84.392 (ARRA)**

U.S. Department of Education	Special Education Cluster (IDEA): CFDA 84.027: Special Education - Grants to States CFDA 84.173: Special Education - Preschool Grants CFDA 84.391: ARRA - Special Education - Grants to States, Recovery Act CFDA 84.392: ARRA - Special Education - Preschool Grants, Recovery Act
Award Number: H027A040110 H027A050110 H027A060110 H027A070110 H027A080110 H173A050117 H173A060117 H173A070117 H173A080117 H173A090117 H391A09110 H392A09117	Award Period: 07/01/2004 - 09/30/2005 07/01/2005 - 09/30/2006 07/01/2006 - 09/30/2007 07/01/2007 - 09/30/2008 07/01/2008 - 09/30/2009 07/01/2005 - 09/30/2006 07/01/2006 - 09/30/2007 07/01/2007 - 09/30/2008 07/01/2008 - 09/30/2009 07/01/2009 - 09/30/2010 02/17/2009 - 09/30/2010 02/17/2009 - 09/30/2010
	Known Questioned Costs: Undeterminable

MDE's internal control did not ensure that the Special Education Cluster complied with federal laws and regulations regarding subrecipient monitoring and special tests and provisions. Noncompliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Special Education Cluster awards.

Federal expenditures for the Special Education Cluster totaled \$796.6 million for the two-year period ended September 30, 2009. MDE distributed \$371.4 million and \$397.1 million of the Special Education Cluster to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the Special Education Cluster included LEAs, other State departments, nonprofit organizations, and private companies.

Our audit disclosed the following exceptions by compliance area:

a. Subrecipient Monitoring

MDE's internal control did not ensure its compliance with the subrecipient monitoring requirements. If MDE does not sufficiently monitor subrecipient activities, MDE cannot be assured that subrecipients used federal awards for authorized purposes in compliance with laws, regulations, and provisions of contracts or grant agreements and that performance goals were achieved.

Our review of MDE's subrecipient monitoring activities disclosed that MDE reviewed subrecipient program budgets for allowable activities and costs, appropriately identified federal award information to its subrecipients, reconciled subrecipients' final expenditure reports (FERs) to approved budgets, and conducted on-site and programmatic monitoring for selected subrecipients.

However, our review of the subrecipient monitoring activities by MDE disclosed:

- (1) MDE did not always review the final narrative progress reports required to be submitted by subrecipients to document that project goals were met. The subrecipient grant applications state that a final narrative report is due at the end of the two-year grant period for Part B Flow-Through and Preschool Flow-Through grants and at the end of the one-year grant period for Enhancing Opportunities for Students With Disabilities grants and Transition Services grants.

For 18 of the 57 LEAs that received Flow-Through funding, Enhancing Opportunities for Students With Disabilities funding, and Transition Services funding during the two-year period ended September 30, 2009, we reviewed the LEAs' submitted progress reports. We noted that MDE did not receive 1 (6%) of the 18 final narrative progress reports from the LEA. In addition, we noted that MDE did not document its review of 9 (53%) of the 17 final narrative progress reports submitted by the 17 LEAs during our audit period.

We reported in our prior Single Audit on the review of final narrative progress reports. MDE informed us that it had not fully complied because of staff limitations and staff turnover.

- (2) MDE did not adequately document all program fiscal reviews. MDE reviews all 57 intermediate school districts (ISDs) and selected LEAs within the ISDs on a three-year rotating schedule. We reviewed documentation for 8 (24%) of the 34 program fiscal reviews completed for the ISDs during the two-year period ended September 30, 2009. Our review disclosed that, for 1 (13%) of the 8 program fiscal reviews, MDE did not document its review of the LEA selected for that ISD.
- (3) MDE did not review the federal maintenance of effort for all LEAs during fiscal years 2006-07 and 2007-08. MDE identified 63 LEAs and 74 LEAs that required additional information or follow-up to determine if the LEA met the maintenance of effort requirements in fiscal years 2006-07 and 2007-08, respectively. Our review disclosed that MDE did not follow up on 14 (22%) of 63 LEAs as of April 1, 2010 for fiscal year 2006-07 and did not follow up on 65 (88%) of 74 LEAS as of April 1, 2010 for fiscal year 2007-08.

Federal regulation 34 *CFR* 300.203 requires LEAs to expend funds for the education of children with disabilities greater than or equal to the level of those expenditures provided in the preceding fiscal year. In addition, MDE must determine that an LEA complies for the purposes of establishing the LEA's eligibility for an award.

b. Special Tests and Provisions

MDE's internal control did not ensure that Special Education Cluster funds were allocated to new or significantly expanded charter schools. MDE allocated Special Education Cluster funds to ISDs based on the prior year's student counts and did not consider new charter schools in its allocation of funds. As a result, 8 (73%) of 11 new charter schools were not included in the allocation of Special Education Cluster funds for the two-year period ended September 30, 2009.

Federal regulation 34 *CFR* 76.791 requires that the states must determine a new or expanding charter school's eligibility based on actual enrollment or

other data available on or after the date that the charter school opens or significantly expands. In addition, MDE must ensure that a charter school that opens for the first time or significantly expands its enrollment receives the funds for which it is eligible, even if eligibility and allocation amounts for other LEAs are based on prior year data.

**RECOMMENDATIONS**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE SPECIAL EDUCATION CLUSTER TO ENSURE ITS COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING SUBRECIPIENT MONITORING.

We also recommend that MDE improve its internal control over the Special Education Cluster to ensure its compliance with federal laws and regulations regarding special tests and provisions.

**FINDING (3131009)**

9. Career and Technical Education - Basic Grants to States, CFDA 84.048

U.S. Department of Education	CFDA 84.048: Career and Technical Education - Basic Grants to States
Award Number: V048A070022 V048A070022A V048A080022 V048A080022A V048A090022 V048A090022A	Award Period: 07/01/2007 - 09/30/2008 07/01/2007 - 09/30/2008 07/01/2008 - 09/30/2009 07/01/2008 - 09/30/2009 07/01/2009 - 09/30/2010 07/01/2009 - 09/30/2010
	Known Questioned Costs: Undeterminable

MDE's Career and Technical Education - Basic Grants to States Program did not comply with federal laws and regulations regarding matching, level of effort, and earmarking. Noncompliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Career and Technical Education Program awards.

Federal expenditures for the Career and Technical Education - Basic Grants to States Program totaled \$79.9 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$37.0 million and \$37.9 million to

subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the Career and Technical Education - Basic Grants to States included secondary educational institutions, postsecondary educational institutions, and two State agencies.

Section 311(b)(1)(A) of the Carl D. Perkins Vocational and Technical Education Act of 2006 requires that a State must maintain its fiscal effort for total career and technical education program expenditures for the fiscal year to equal or exceed the total program expenditures for the preceding fiscal year in aggregate. Total career and technical educational expenditures used in the level of effort calculation include both State and subrecipient funded career and technical educational expenditures funded by nonfederal sources.

We compared the eligible State and subrecipients' career and technical education expenditures for fiscal years 2005-06 through 2008-09:

	Fiscal Year			
	2008-09	2007-08	2006-07	2005-06
Total career and technical education expenditures funded with nonfederal sources	\$67.9 million	\$72.2 million	\$ 67.8 million	\$85.8 million
Increase (decrease) from previous year	\$ (4.2 million)	\$ 4.4 million	\$(18.0 million)	N/A

In fiscal year 2008-09, the level of effort calculation indicated that MDE was short \$4.2 million in eligible costs to meet its level of effort requirement. MDE indicated that it did not meet the level of effort requirement because of the decline in subrecipient program expenditures funded by local sources. We have reported an undeterminable amount of questioned costs because the federal regulations only indicated that the State would not be eligible for subsequent year awards if it fails to maintain its fiscal effort in preceding years.

We previously reported that the Career and Technical Education Program did not meet the level of effort requirement for fiscal year 2007-08 in the financial audit\*, including provisions of the Single Audit Act, of the Department of Labor and Economic Growth (641-0100-09) audit report, issued in June 2009. Effective July 1, 2007, the Governor issued Executive Order No. 2007-04, which transferred career and technical education programs from the Department of Labor

\* See glossary at end of report for definition.

and Economic Growth (DLEG) to the State Board of Education. For fiscal years 2007-08 and 2008-09, MDE delegated the responsibilities regarding postsecondary career and technical education back to DLEG, while responsibility for secondary students remained with MDE.

MDE informed us that it submitted a request to the U.S. Department of Education (USDOE) for a revised approach for its level of effort computation and the revised approach would allow MDE to meet the level of effort requirements. However, the USDOE has not yet approved this request.

**RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE's CAREER AND TECHNICAL EDUCATION – BASIC GRANTS TO STATES PROGRAM COMPLY WITH FEDERAL LAWS AND REGULATIONS REGARDING MATCHING, LEVEL OF EFFORT, AND EARMARKING.

**FINDING (3131010)**

10. Early Intervention Services (IDEA) Cluster, CFDA 84.181 and 84.393 (ARRA)

U.S. Department of Education	Early Intervention Services (IDEA) Cluster: CFDA 84.181: Special Education - Grants for Infants and Families CFDA 84.393: ARRA - Special Education - Grants for Infants and Families, Recovery Act
Award Number: H181A060012 H181A070012 H181A080012 H181A090012 H393A090012	Award Period: 07/01/2006 - 09/30/2007 07/13/2007 - 09/30/2008 07/01/2008 - 09/30/2009 07/01/2009 - 09/30/2010 02/17/2009 - 09/30/2010
	Known Questioned Costs: Undeterminable

MDE's internal control over the Early Intervention Services (IDEA) Cluster did not ensure its compliance with federal laws and regulations regarding matching, level of effort, and earmarking. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of the Early Intervention Services (IDEA) Cluster awards.

Federal expenditures for the Early Intervention Services (IDEA) Cluster totaled \$25.3 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$12.3 million and \$11.9 million to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the Early Intervention Services (IDEA) Cluster included LEAs, institutions of higher education, and nonprofit organizations.

MDE's internal control did not ensure that it complied with federal requirements related to level of effort. Our review disclosed that MDE did not have a method to identify the State and local program expenditures funded by nonfederal sources for fiscal years 2007-08 and 2008-09. Therefore, MDE could not ensure compliance with the federal regulation related to level of effort.

Federal regulation 34 *CFR* 303.124 states that the total amount of State and local funds budgeted for expenditures in the current fiscal year for early intervention services for children eligible under this part and their families must be at least equal to the total amount of State and local funds actually expended for early intervention services for these children and their families in the most recent preceding fiscal year for which the information is available. We have reported undeterminable questioned costs because the federal regulations do not provide for consequence for noncompliance with level of effort requirements.

### **RECOMMENDATION**

We recommend that MDE improve its internal control over the Early Intervention Services (IDEA) Cluster to ensure its compliance with federal laws and regulations regarding matching, level of effort, and earmarking.

## **FINDING (3131011)**

### 11. Safe and Drug-Free Schools and Communities - State Grants, CFDA 84.186

U.S. Department of Education	CFDA 84.186: Safe and Drug-Free Schools and Communities - State Grants
Award Number: S186A030023A Q186A040023 Q186A050023 Q186A060023 Q186A070023 Q186A080023 Q186A090023	Award Period: 07/01/2003 - 09/30/2004 07/01/2004 - 09/30/2005 07/01/2005 - 09/30/2006 07/01/2006 - 09/30/2007 07/01/2007 - 09/30/2008 07/01/2008 - 09/30/2009 07/01/2009 - 09/30/2010
	Known Questioned Costs: \$0

MDE's internal control over the Safe and Drug-Free Schools and Communities - State Grants (SDFSC) Program did not ensure its compliance with federal laws and regulations regarding subrecipient monitoring and special tests and provisions. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions in SDFSC Program awards.

Federal expenditures for the SDFSC Program totaled \$15.5 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$7.9 million and \$7.0 million to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the SDFSC Program were LEAs, ISDs, and regional educational service agencies.

Our audit disclosed the following exceptions by compliance area:

a. Subrecipient Monitoring

MDE's internal control over the SDFSC Program did not ensure its compliance with the subrecipient monitoring requirements. If MDE does not sufficiently monitor subrecipient activities, MDE cannot be assured that subrecipients used federal awards for authorized purposes in compliance with laws, regulations, and provisions of contracts or grant agreements and that performance goals were achieved.

MDE, in conjunction with Office of Drug Control Policy (ODCP), Department of Community Health, monitored subrecipients that received SDFSC grants. MDE and ODCP reviewed subrecipients' program budgets for allowable activities and costs and appropriately identified federal award information to subrecipients.

However, our review of the subrecipient monitoring activities by either MDE or ODCP for 33 grants disclosed:

- (1) MDE and ODCP did not perform on-site monitoring or desk reviews for any subrecipients during fiscal year 2007-08. During fiscal year 2007-08, MDE distributed \$7.9 million in grants to 138 subrecipients.
- (2) MDE and ODCP did not monitor subrecipient cash draws to ensure that the draws were only for reimbursement needs. We noted that 5 (19%) of the 26 subrecipients had requested a cash draw that may have been in excess of their accumulated expenditures. The 5 cash draws represented cumulatively from 64% to 100% of each subrecipient's total grant, yet the percentage of the grant award periods that had expired ranged from 46% to 67%. One subrecipient drew down 100% of its total grant within 67% of its grant award periods. Because MDE allows subrecipients to draw funds electronically without providing supporting documentation, monitoring unusually large subrecipient cash draws would help ensure that subrecipients are in compliance with cash management requirements.

We reported on the lack of monitoring of cash draws in the prior Single Audit, and MDE informed us that it had developed a new process to review cash draws. However, due to staff changes, it had not fully implemented this process.

b. Special Tests and Provisions

MDE's and ODCP's internal control did not ensure that SDFSC Program funds were allocated to new or significantly expanded charter schools. As a result, 4 new charter schools were not included in the allocation of SDFSC Program grant funds for fiscal year 2007-08.

Federal regulation 34 *CFR* 76.791 requires that the states must ensure that a charter school that opens for the first time or significantly expands its enrollment receives the funds for which it is eligible, even if eligibility and allocation amounts for other LEAs are based on prior year data.

ODCP allocated SDFSC Program funds based on the prior year's allocations for Title I Grants to Local Educational Agencies and did not consider new charter schools in its allocation of funds. Therefore, the 4 charter schools were not notified that the schools were eligible to apply for the SDFSC grant.

We reported on the allocation to new or expanded charter schools in our prior Single Audit, and MDE informed us that it would implement a new process. However, MDE did not implement the process because of staffing changes.

**RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE SDFSC PROGRAM TO ENSURE ITS COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING SUBRECIPIENT MONITORING AND SPECIAL TESTS AND PROVISIONS.

**FINDING (3131012)**

12. State Grants for Innovative Programs, *CFDA* 84.298

U.S. Department of Education	<i>CFDA</i> 84.298: State Grants for Innovative Programs
Award Number: S298A060022 S298A070022	Award Period: 07/01/2006 - 09/30/2007 07/01/2007 - 09/30/2008
	Known Questioned Costs: \$0

MDE's internal control over the State Grants for Innovative Programs did not ensure compliance with federal laws and regulations regarding subrecipient monitoring. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions and/or disallowances of awards.

Federal expenditures for the State Grants for Innovative Programs totaled \$4.7 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$2.3 million and \$1.5 million to subrecipients in

fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the State Grants for Innovative Programs included LEAs.

MDE's subrecipient monitoring activities include comparing final expenditure reports (FERs) to budgeted amounts and following up on all expenditures greater than budgeted amounts. MDE requires subrecipients to request a budget transfer for any line-item expenditure that exceeds the budgeted amount. MDE reviews these budget transfer requests to help ensure that the federal awards are used for authorized purposes.

Our review of MDE's subrecipient monitoring activities for 34 subrecipients disclosed:

- a. MDE did not follow up or document its follow-up of 2 (40%) of 5 FERs, where the subrecipients reported line-item expenditures that exceeded 10% of the approved budget subtotal. As a result, MDE could not be assured that those expenditures were for authorized purposes.
- b. MDE did not ensure that subrecipients submitted compliance plans based on deficiencies during MDE's on-site visits.

MDE's Field Services Unit conducted 10 on-site visits of the State Grants for Innovative Program's subrecipients during fiscal year 2007-08. Our review of the 10 on-site visit files identified 5 with deficiencies related to the State Grants for Innovative Programs. MDE had not received required compliance plans from 2 of the 5 subrecipients.

MDE procedures require that when the on-site monitoring review identifies recommendations requiring corrective action, the subrecipient must submit a compliance plan to MDE within 30 days after receipt of the on-site review report.

We reported in our prior Single Audit that MDE did not obtain all required corrective action plans. MDE informed us that the grant was ending on September 30, 2009 and it would obtain compliance reports if resources were available.

## **RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE STATE GRANTS FOR INNOVATIVE PROGRAMS TO ENSURE ITS COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING SUBRECIPIENT MONITORING.

## **FINDING (3131013)**

### 13. Education Technology State Grants, CFDA 84.318

U.S. Department of Education	CFDA 84.318: Education Technology State Grants
Award Number: S318X050022A S318X060022A S318X070022 S318X080022 S318X090022	Award Period: 07/01/2005 - 09/30/2006 07/01/2006 - 09/30/2007 07/01/2007 - 09/30/2008 07/01/2008 - 09/30/2009 07/01/2009 - 09/30/2010
	Known Questioned Costs: \$566,045

MDE's internal control over the Education Technology State Grants Program did not ensure its compliance with federal laws and regulations regarding eligibility and subrecipient monitoring. As a result, we questioned costs of \$566,045. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Education Technology State Grants Program awards.

Federal expenditures for the Education Technology State Grants Program totaled \$18.1 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$6.9 million and \$10.3 million to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the Education Technology State Grants Program included LEAs.

The Education Technology State Grants Program requires that states must use at least 95% of their award amount to make subgrants to LEAs, of which up to half must be distributed to eligible LEAs on a formula basis. States may award the remaining amount to eligible LEAs on a competitive basis.

Our review disclosed the following exceptions by compliance area:

a. Eligibility

MDE's internal control did not ensure that it awarded the competitive grants to only eligible LEAs in accordance with federal laws and regulations. As a result, we questioned costs in the amount of \$198,277.

Title 20, Section 6753 of the *United States Code (USC)* provides that an eligible local entity must be a high-need LEA or an eligible local partnership that includes at least one high-need LEA. A high-need LEA is an LEA: (a) that is among the LEAs in a state with the highest numbers or percentages of children from families with incomes below the poverty line and (b) that operates one or more schools identified for improvement or corrective action or restructuring or has a substantial need for assistance in acquiring and using technology.

MDE established scoring criteria for these grants to determine if the LEA met the definition of a high-need LEA as federally required and met additional State-defined criteria. We reviewed scoring documentation for 13 LEA competitive grants and noted that 1 (8%) competitive grant was awarded to an LEA that did not document that it met the high-need definition. We questioned the total amount of \$198,277 disbursed to the ineligible subrecipient.

We reported in our prior Single Audit on ineligible LEAs, and MDE informed us that it did not agree with the finding. MDE is waiting for the USDOE to make a determination as to eligibility.

b. Subrecipient Monitoring

MDE's internal control over the Education Technology State Grants Program did not ensure that MDE complied with subrecipient monitoring requirements. If MDE does not sufficiently monitor subrecipient activities, MDE cannot be assured that subrecipients used federal awards for authorized purposes in compliance with laws, regulations, and provisions of grant agreements and that performance goals were achieved.

MDE's subrecipient monitoring activities include performing on-site monitoring, reviewing subrecipients' program budgets for allowable activities and costs,

and appropriately identifying federal award information to its subrecipients. We reviewed MDE's monitoring activities for 33 subrecipients and noted:

- (1) MDE's review of subrecipient FERs did not identify that 6 (18%) of 33 subrecipients had not met their earmarking requirement for professional development activities. As a result, we questioned costs in the amount of \$367,768 based on the difference between 25% of the final total expenditures and the total professional development expenditures reported on the subrecipients' FERs.

Federal law 20 USC 6766(a) provides that LEAs receiving awards under the program must use at least 25% of the funds to provide ongoing, sustained, and intensive high-quality professional development.

We reported in our prior Single Audit on subrecipients not meeting their professional development earmarking requirement. MDE agreed but did not implement sufficient procedures to monitor for earmarking.

- (2) MDE did not ensure that 17 subrecipients submitted compliance plans based on deficiencies related to the Education Technology State Grants Program identified during MDE's on-site visits. MDE's Field Services Unit conducted 70 on-site visits during fiscal years 2007-08 and 2008-09 that covered several federal programs, including the Education Technology State Grants Program. MDE procedures require that when the on-site monitoring review identifies recommendations requiring corrective action, the subrecipient must submit a compliance plan to MDE within 30 days after receipt of the on-site review report.
- (3) MDE did not monitor cash draws by subrecipients to ensure that the draws were only for reimbursement needs. We noted that 2 (11%) of the 19 subrecipients had requested cash draws that may have been in excess of their respective expenditure needs. The two cash draws represented cumulatively 99% and 62% of the total amount of the grants, yet the percentage of the grant award period that had expired was 82% and 30%, respectively. Because MDE allows subrecipients to draw funds electronically without providing supporting documentation, monitoring unusually large subrecipient cash draws would help to ensure that subrecipients are in compliance with cash management requirements.

## **RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE EDUCATION TECHNOLOGY STATE GRANTS PROGRAM TO ENSURE ITS COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING ELIGIBILITY AND SUBRECIPIENT MONITORING.

## **FINDING (3131014)**

### 14. Reading First State Grants, CFDA 84.357

U.S. Department of Education	CFDA 84.357: Reading First State Grants
Award Number:	Award Period:
S357A050023	07/01/2005 - 09/30/2006
S357A050023A	07/01/2005 - 09/30/2006
S357A050023B	07/01/2005 - 09/30/2006
S357A060023	07/01/2006 - 09/30/2007
S357A060023A	07/01/2006 - 09/30/2007
S357A070023	07/01/2007 - 09/30/2008
S357A070023A	07/01/2007 - 09/30/2008
S357A080023	07/01/2008 - 09/30/2009
	Known Questioned Costs: \$0

MDE's internal control did not ensure that the Reading First State Grants Program complied with federal requirements relating to subrecipient monitoring. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Reading First State Grants Program awards.

Federal expenditures for the Reading First State Grants Program totaled \$48.1 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$29.8 million and \$12.2 million to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the Reading First State Grants Program included LEAs.

MDE's subrecipient monitoring activities include comparing FERs to budgeted amounts and following up on all expenditures greater than budgeted amounts. MDE's Reading First State Grants Program staff indicated that they required subrecipients to request a budget transfer for any line-item expenditure that

exceeds the budgeted amount. Program staff review these budget transfer requests to help ensure that the federal awards are used for authorized purposes.

In our sample of 33 FERs, we noted that 5 (15%) subrecipients reported line-item expenditures that exceeded approved budgets by more than 10%. MDE could not document its follow-up of 1 (20%) of the 5 subrecipients whose line-item expenditures exceeded the budget by more than 10%. As a result, MDE could not be assured that those expenditures were for authorized purposes.

We reported on this weakness in our prior Single Audit, and MDE agreed and hired additional staff. However, MDE informed us that the Program is ending September 30, 2010 and it has lost staff resources.

**RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE READING FIRST STATE GRANTS PROGRAM TO ENSURE COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING SUBRECIPIENT MONITORING.

**FINDING (3131015)**

15. English Language Acquisition Grants, CFDA 84.365

U.S. Department of Education	CFDA 84.365: English Language Acquisition Grants
Award Number: T365A050022	Award Period: 07/01/2005 - 09/30/2006
T365A060022	07/01/2006 - 09/30/2007
T365A070022A	07/01/2007 - 09/30/2008
T365A080022A	07/01/2008 - 09/30/2009
S365A090022A	07/01/2009 - 09/30/2010
	Known Questioned Costs: \$0

MDE's internal control over the English Language Acquisition (ELA) Grants Program did not ensure its compliance with federal laws and regulations regarding subrecipient monitoring. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of ELA Grants Program awards.

Federal expenditures for the ELA Grants Program totaled \$18.2 million for the two-year period ended September 30, 2009. Of these expenditures, MDE distributed \$8.4 million and \$9.1 million to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the ELA Grants Program included LEAs and nonprofit organizations.

If MDE does not sufficiently monitor subrecipient activities, MDE cannot be assured that subrecipients used federal awards for authorized purposes in compliance with laws, regulations, and provisions of contracts or grant agreements and that performance goals were achieved. MDE's monitoring activities included reviewing subrecipients' program budgets for allowable activities and costs, providing training, appropriately identifying federal award information to subrecipients, and performing on-site monitoring and desk reviews for selected subrecipients. However, our review of MDE's subrecipient monitoring activities disclosed:

- a. MDE did not ensure that subrecipients submitted compliance plans for 6 of the 18 on-site visits requiring corrective action or follow-up with the subrecipient. MDE's Field Services Unit conducted 70 on-site visits during fiscal years 2007-08 and 2008-09 that covered several federal programs, including the ELA Grants Program. MDE requires that when the on-site monitoring review identifies the need for corrective action, the subrecipient must submit a compliance plan to MDE within 30 days after receipt of the on-site review report.
- b. MDE did follow up on discrepancies identified in its comparison of subrecipients' FERs to approved budgets during fiscal year 2007-08. MDE could not provide us with documentation indicating that it had reviewed and approved expenditures in 4 (25%) of 16 FERs where subrecipients reported line-item expenditures that varied by more than 10% from approved budgets. MDE's process for monitoring subrecipients' expenditures includes following up on those expenditures that exceed budgeted amounts by more than 10%.
- c. MDE did not monitor subrecipient cash draws to ensure that the draws were only for reimbursement needs. We noted that 3 (10%) of 30 subrecipients requested a cash draw that may have been in excess of their respective expenditure needs. The three cash draws represented cumulatively 90%, 96%, and 100% of each subrecipient's total grants, yet the percentage of the grant award period that had expired was 42%, 11%, and 27%, respectively.

Because MDE allows subrecipients to draw funds electronically without providing supporting documentation, monitoring unusually large subrecipient cash draws would help to ensure that subrecipients are in compliance with cash management requirements.

We reported in our prior Single Audit on the weaknesses in obtaining corrective action plans and comparisons of FERs to approved budgets. MDE agreed and informed us that it would implement a new process and hire additional staff. However, MDE did not fully implement changes to address these deficiencies.

**RECOMMENDATION**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE ELA GRANTS PROGRAM TO ENSURE ITS COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING SUBRECIPIENT MONITORING.

**FINDING (3131016)**

16. Improving Teacher Quality State Grants, CFDA 84.367

U.S. Department of Education	CFDA 84.367: Improving Teacher Quality State Grants
Award Number: S367A040021A, S367B040019A S367A050021A, S367B050019A S367A060021A, S367B060019A S367A070021A, S367B070019A S367A080021A, S367B080019A	Award Period: 07/01/2004 - 09/30/2005 07/01/2005 - 09/30/2006 07/01/2006 - 09/30/2007 07/01/2007 - 09/30/2008 07/01/2008 - 09/30/2009
	Known Questioned Costs: \$0

MDE's internal control over the Improving Teacher Quality State Grants (Improving Teacher Quality) Program did not ensure its compliance with federal laws and regulations regarding subrecipient monitoring and special tests and provisions. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Improving Teacher Quality Program awards.

Federal expenditures for the Improving Teacher Quality Program totaled \$188.4 million for the two-year period ended September 30, 2009. Of these

expenditures, MDE distributed \$88.6 million and \$96.2 million to subrecipients in fiscal years 2007-08 and 2008-09, respectively. Subrecipients of the Improving Teacher Quality Program included both LEAs and institutions of higher education.

Our audit disclosed the following exceptions by compliance area:

a. Subrecipient Monitoring

MDE's internal control did not ensure that subrecipients submitted compliance plans that addressed noted deficiencies and did not ensure that subrecipients' cash draws were for reimbursement needs. We noted:

- (1) MDE did not ensure that 22 subrecipients submitted compliance plans based on deficiencies related to the Improving Teacher Quality Program identified during MDE's on-site visits. MDE completed 70 on-site visits during fiscal years 2007-08 and 2008-09 that covered several federal programs, including the Improving Teacher Quality Programs.

MDE procedures require that when the on-site monitoring review identifies recommendations requiring corrective action, the subrecipient must submit a compliance plan to MDE within 30 days after receipt of the on-site review report.

We reported in our prior Single Audit on MDE not obtaining corrective action plans. MDE agreed and indicated that it would hire additional staff; however, MDE has not been able to increase staff sufficiently to ensure that all corrective action plans are obtained.

- (2) MDE did not monitor subrecipient cash draws to ensure that the draws were only for reimbursement needs. We noted that 1 of 18 subrecipients requested three cash draws and each draw may have been in excess of its expenditure needs. The cash draws represented cumulatively 33%, 50%, and 97% of the total amount of the grant, yet the percentage of the grant award period that had expired was 11%, 30%, and 54%, respectively. Because MDE allows subrecipients to draw funds electronically without providing supporting documentation, monitoring unusually large subrecipient cash draws would help to ensure that subrecipients are in compliance with cash management requirements.

b. Special Tests and Provisions

MDE did not perform sufficient monitoring of subrecipients to ensure compliance with special tests and provisions relating to participation of private school children.

Federal regulations require that LEAs receiving financial assistance under the Improving Teacher Quality Program must provide eligible private school children and their teachers or other education personnel with equitable services or other benefits under the program. Before an LEA makes any decision that affects the opportunity of eligible private school children, teachers, and other educational personnel to participate, the LEA must engage in timely and meaningful consultation with private school officials.

In our review of 18 grant applications, 1 LEA did not provide evidence that it had invited private schools within the LEA's school district to participate in the grant activities. MDE's application procedures require that the LEAs certify that private schools have been notified of the opportunity to participate in planning and implementing grant activities. As part of the grant application, MDE required the LEA to provide an example of the LEA's letter forwarded to the private school officials. This LEA did not provide MDE with an example of the letter forwarded to the private school officials, but certified in its application to MDE that it had notified private school officials. MDE approved this application without following up and requesting the letter from the LEA.

**RECOMMENDATIONS**

WE AGAIN RECOMMEND THAT MDE IMPROVE ITS INTERNAL CONTROL OVER THE IMPROVING TEACHER QUALITY PROGRAM TO ENSURE ITS COMPLIANCE WITH FEDERAL LAWS AND REGULATIONS REGARDING SUBRECIPIENT MONITORING.

We also recommend that MDE improve its internal control over the Improving Teacher Quality Program to ensure compliance with federal laws and regulations regarding special tests and provisions.

## **FINDING (3131017)**

### **17. State Fiscal Stabilization Fund Cluster, CFDA 84.394**

U.S. Department of Education	State Fiscal Stabilization Fund Cluster: CFDA 84.394: ARRA - State Fiscal Stabilization Fund (SFSF) - Education State Grants, Recovery Act
Award Number: S394A090023	Award Period: 05/28/2009 - 09/30/2010
	Known Questioned Costs: Undeterminable

MDE's internal control over the State Fiscal Stabilization Fund Cluster did not ensure its compliance with federal laws and regulations regarding subrecipient monitoring. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of State Fiscal Stabilization Fund Cluster awards.

MDE's federal expenditures for the State Fiscal Stabilization Fund Cluster totaled \$597.5 million for the period ended September 30, 2009. MDE distributed 100% of these funds to LEAs. MDE expended federal financial assistance under only the ARRA - State Fiscal Stabilization Fund (SFSF) - Education State Grants, Recovery Act Program (CFDA 84.394), one of the two programs included in the cluster.

For the State Fiscal Stabilization Fund Cluster awards, MDE provided subrecipients with training on preparing the grant application and reporting and identifying allowable activities and reviewed subrecipients' FERs to ensure that program expenditures were for allowable activities. MDE's only opportunity to review subrecipient expenditures was during its review of the FERs. If MDE does not sufficiently monitor subrecipient activities, MDE cannot be assured that subrecipients used federal awards for authorized purposes in compliance with laws, regulations, and provisions of contracts or grant agreements.

We reviewed subrecipient monitoring activities for 33 subrecipients. Each of the 33 subrecipients had expended its entire fiscal year 2008-09 award prior to September 30, 2009. Our review disclosed:

- a. MDE did not receive 31 (94%) of 33 FERs from subrecipients in a timely manner. The 31 subrecipients were between 4 and 249 days late in submitting their 2009 FERs.

MDE's instructions to the 762 awarded subrecipients may have resulted in delays in receiving FERs. MDE's grant award notification documents and Michigan Electronic Grants System (MEGS) instructions required subrecipients to submit FERs within 60 days of the expenditure of all funds or within 60 days of the grant ending date, whichever comes first. However, in another section of the grant award notification document, it also states that the due date for the FER is November 29, 2011. Subrecipients may not have submitted their FERs timely because of the contradictory instructions provided by MDE.

- b. As of April 5, 2010, MDE had not documented its review of 8 (29%) of 28 FERs received between September 24, 2009 and March 24, 2010. MDE's inability to review FERs in a timely manner may impede its ability to obtain assurance that grant awards were used for authorized purposes.

### **RECOMMENDATION**

We recommend that MDE improve its internal control over the State Fiscal Stabilization Fund Cluster to ensure its compliance with federal laws and regulations regarding subrecipient monitoring.

**The status of the findings related to federal awards that were reported in prior Single Audits is disclosed in the summary schedule of prior audit findings.**

## OTHER SCHEDULES

MICHIGAN DEPARTMENT OF EDUCATION  
Summary Schedule of Prior Audit Findings  
As of June 25, 2010

**PRIOR AUDIT FINDINGS RELATED TO THE FINANCIAL SCHEDULES AND FINANCIAL STATEMENTS**

Audit Findings Not Corrected or Partially Corrected:

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130801  
**Finding Title:** Security and Application Controls

**Finding:** The Michigan Department of Education (MDE), in conjunction with the Department of Information Technology (DIT), did not implement a comprehensive security program to protect its application systems and data. In addition, MDE and DIT's implementation of MDE's new Cash Management System (CMS) did not ensure that subrecipients received only the payments to which they were entitled.

- a. MDE's security policies and procedures over critical systems had the following control weaknesses:
  - (1) MDE did not restrict the system developers from administrative access privileges to MDE's information systems and databases.
  - (2) MDE, in conjunction with DIT, did not have effective controls to identify unauthorized changes to application systems.
  - (3) Responsibilities of MDE's security officer did not include granting and monitoring access to all MDE data or application and operating systems.

- b. MDE's internal control over the implementation of its new CMS in fiscal year 2006-07 did not ensure that grant subrecipients received only the payments to which they were entitled.

**Agency Comments:**

- a. (1) System developers have been restricted to 'read only' access as of November 1, 2008 and some developer access has also been limited; however, due to the fact that the application is written in Visual FoxPro, access cannot be further limited. This system is being upgraded to .Net, which is scheduled for deployment by October 1, 2010. Actual deployment may be delayed due to furlough days and budget constraints.
- (2) The Michigan Department of Information Technology (MDIT) staff have responsibility to identify and monitor the change control methods utilized by each MDE information technology (IT) application. MDIT has published a document that identifies the process that should be used for change control by each MDE IT application: \\Common\DIT\IT Standards\Change Management. The document identifies three allowable systems for tracking change control:
  - (a) Remedy Ticket.
  - (b) SUITE System Maintenance Template located at ([http://www.michigan.gov/documents/techtalk/SEM-0931\\_267841\\_7.dot](http://www.michigan.gov/documents/techtalk/SEM-0931_267841_7.dot)) or [www.michigan.gov/suite](http://www.michigan.gov/suite).
  - (c) Entry in an approved Change Management System (for example, the Michigan Electronic Grants System (MEGS) uses Bugzilla; OEAA Applications use Issue Tracker).

MDE staff responsible for each system are working with MDIT to ensure that proper change controls methods are implemented.

- (3) The MDE security officer, Louis Burgess, has reviewed the systems and has issued guidance for all managers of these systems to institute a security access program. The program office responsibility includes developing a process for establishing an access control procedure and monitoring of security access forms and user access.
- b. MDE monitors daily reports to ensure that all financial transactions are accounted for and accurately reported in the CMS.

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 3130802

**Finding Title:** Monitoring of Internal Control Over Financial Reporting

**Finding:** MDE did not periodically monitor the effectiveness of its internal control over financial reporting.

**Agency Comments:** Although the audit finding states that "The internal auditor could play an important role in evaluating the effectiveness of controls by independently testing and verifying the integrity of the department's system of internal control," the internal audit unit in the State Budget Office, Department of Management and Budget, clearly disagrees and will not monitor MDE's internal control. MDE has documented its oversight and review control system. Although MDE believes that its current oversight process is adequate, it will consider adding additional oversight and monitoring if resources become available.

## PRIOR AUDIT FINDINGS RELATED TO FEDERAL AWARDS

### Audit Findings That Have Been Fully Corrected:

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130803  
**Finding Title:** Title I Grants to Local Educational Agencies, *CFDA* 84.010 - Cash Management

**Finding:** MDE's internal control did not ensure that it complied with federal laws and regulations regarding cash management.

**Agency Comments:** MDE closely monitors its recoding processes and ensures that all recordkeeping transactions are recorded within the Tydings period. MDE applies first in, first out (FIFO) cost flow assumption for drawing down federal funds. This method ensures that all financial recordkeeping transactions occur within the 27 months of availability.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130807  
**Finding Title:** Charter Schools, *CFDA* 84.282

**Finding:** MDE's internal control over the Charter Schools Program did not ensure that it processes payments only for eligible charter schools in compliance with federal laws and regulations regarding eligibility.

**Agency Comments:** MDE has corrected conversion errors and updated the mail codes in the CMS. MDE corrected the incorrect payments and forwarded to the correct payee during the audit period.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130812  
**Finding Title:** Mathematics and Science Partnerships (MSP), *CFDA* 84.366

**Finding:** MDE's internal control over the MSP Program did not ensure its compliance with federal laws and regulations regarding subrecipient monitoring.

**Agency Comments:** MDE has visited 2 of the current 8 projects to look at receipts, agendas, meeting notes, workshop materials, etc. Site visits have been made to 4 projects to observe actual grant activities. Desk monitoring has increased for all projects. The state evaluator has attended workshops by all projects and ensured compliance with evaluation requirements of the grant. Year 2 funding for eligible projects is dependent on their compliance with federal and State requirements for this grant program. No project has been found noncompliant. Details and documentation from site visits by MDE and the evaluator are on file.

Audit Findings Not Corrected or Partially Corrected:

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 3130804

**Finding Title:** Title I Grants to Local Educational Agencies, *CFDA* 84.010

**Finding:** MDE internal control over the Title I Grants to Local Educational Agencies Program did not ensure its compliance with federal laws and regulations regarding allowable costs/cost principles; matching, level of effort, and earmarking; and subrecipient monitoring.

**Agency Comments:**

- a. Has been fully accepted by the U.S. Department of Education (USDOE).
- b. Has been fully resolved.
- c. The office was severely understaffed at the time, preventing us from appropriately following up on on-site review compliance plans. Staffing has now increased. New systems are in place to ensure appropriate follow-up.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130805  
**Finding Title:** Special Education Cluster (IDEA), *CFDA* 84.027 and 84.173

**Finding:** MDE's internal control over the Special Education Cluster did not ensure its compliance with federal laws and regulations regarding reporting and subrecipient monitoring.

**Agency Comments:**

- a. Reporting - Completed. Discussed with USDOE and audit closed.
- b. Subrecipient Monitoring - Partially Completed. The final narrative review is going through an improvement process that will be more comprehensive and timely.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130806  
**Finding Title:** Safe and Drug-Free Schools and Communities - State Grants (SDFSC), *CFDA* 84.186

**Finding:** MDE's internal control over the SDFSC Program did not ensure its compliance with federal laws and regulations regarding matching, level of effort, and earmarking; subrecipient monitoring; and special tests and provisions.

a. Matching, Level of Effort, and Earmarking

MDE's internal control did not ensure its compliance with federal requirements relating to earmarking of State administrative costs.

b. Subrecipient Monitoring

MDE's internal control over the SDFSC Program did not ensure its compliance with the subrecipient monitoring requirements.

(1) MDE and the Office of Drug Control Policy (ODCP) did not review the discrepancies identified during the

reconciliation of final expenditure reports (FERs) to approved budgets.

- (2) MDE and ODCP did not monitor subrecipient cash draws to ensure that the draws were only for reimbursement and/or three-day cash needs.

**Agency Comments:**

a. Matching, Level of Effort, and Earmarking

MDE has initiated a procedure of checking on the administrative expenses for this grant on a regular basis. As specified in the memorandum of understanding (MOU), MDE works closely with Department of Community Health to monitor all expenses related to this grant program. An MDE analyst reviews the grant spending plan on a monthly basis. He will coordinate directly with ODCP on any issues that arise with spending plan issues. The Grants Administration and Coordination supervisor will coordinate directly with ODCP on any issues requiring higher level action.

b. Subrecipient Monitoring

An MOU between MDE and ODCP has been signed. The MOU states that MDE is responsible for all compliance and oversight of all federal education funds, including the Title IV, Part A, Safe and Drug-Free Schools and Communities Act funds. The specific subrecipient monitoring tasks are outlined in the MOU. Subrecipient monitoring is conducted by the Education Section of ODCP. As to the specific plan of action for monitoring subrecipient draws, ODCP's Education Section has a policy to use MDE's CMS to monitor all draws, by grant year, for any grant program. A cash timing report is available that lets program offices monitor the percent draw for any grant. ODCP is reviewing all cash draws on a quarterly basis. The cash timing report was run on October 1 for the current year grant. Because there was only one approval and no draws on the system, the report was not meaningful. This monitoring will continue, with the office running the cash timing report on a quarterly basis to

review all grant cash draws. The office has developed a guide to review cash draw percentages throughout the school year.

c. Special Tests and Provisions

ODCP will follow the same procedures that MDE's Office of School Improvement uses when determining the allocations for all districts. It will work with the Charter School Office to determine estimated enrollments of any new charter schools planning to open. Based on the estimated enrollments, ODCP will ensure that funds are set aside to cover the allocations. These set aside funds will then be allocated to new charter schools when the fall enrollment counts are finalized. This process will be part of the on-going procedures for ODCP.

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 3130808

**Finding Title:** State Grants for Innovative Programs, *CFDA* 84.298

**Finding:** MDE needs to improve internal control over State Grants for Innovative Programs to ensure its compliance with federal laws and regulations regarding subrecipient monitoring.

**Agency Comments:** MDE considered the recommendation in the original report as an idea that did not demand a response. However, since this award was scheduled to end September 30, 2009, MDE did not focus its limited resources on resolving compliance requirements identified during the Title V on-site reviews. MDE's strategy was primarily to focus its resources to completing on-site reviews of subrecipients providing them with information of compliance deficiencies. As resources permitted, MDE attempted to follow up with subrecipients who had not taken steps to correct noted compliance deficiencies.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130809  
**Finding Title:** Education Technology State Grants, *CFDA* 84.318

**Finding:** MDE's internal control over the Education Technology State Grants Program did not ensure its compliance with federal laws and regulations regarding eligibility and subrecipient monitoring.

**Agency Comments:** Eligibility concerns were a part of the legislatively directed Freedom to Learn Program. This program was terminated in September 2007. The Education Technology and Data Coordination unit is now responsible for all Education Technology State Grants. This office has dedicated education consultants responsible for all aspects of the Ed Tech Programs, including determination of eligibility and subrecipient monitoring. The office has been advised of and acknowledges its responsibilities in both areas.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130810  
**Finding Title:** Reading First State Grants, *CFDA* 84.357

**Finding:** MDE's internal control over the Reading First State Grants (Reading First) Program did not ensure its compliance with federal laws and regulations relating to matching, level of effort, and earmarking and subrecipient monitoring.

**Agency Comments:** a. Matching, Level of Effort, and Earmarking  
The Reading First Program hired a financial analyst to budget, execute, and monitor Reading First Program expenditures. The analyst was hired January 14, 2008. The analyst will file a spending plan with the office director. In this spending plan the Reading First Program will ensure that the expenditures do not exceed the 20% threshold as outlined. Once the spending plan is approved, the analyst along with the Program supervisor will carry out the budget.

The analyst will monitor budget expenditures and make certain that the Program is in compliance. If the Program is not in compliance, the analyst will then inform the office director and document any findings. To date, the earmarkings are in compliance with Reading First Program legislation.

b. Subrecipient Monitoring

The Program staff reviewed all FERs in 2008. Since the program office has hired a financial analyst she will be responsible for reviewing all FERs. She will document this review and report any findings to the Program staff and the office director. The Program staff will follow up with local educational agencies (LEAs) to ensure that expenditures were authorized. The Reading First Program staff documented the follow-up with LEAs.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130811  
**Finding Title:** English Language Acquisition (ELA) Grants, *CFDA* 84.365

**Finding:** MDE's internal control over the ELA Grants Program did not ensure its compliance with federal laws and regulations regarding subrecipient monitoring and special tests and provisions.

**Agency Comments:** MDE has initiated a monitoring system for all of its subrecipients beginning with an annual self-evaluation of all programs. The federally-required self-evaluation includes all components of the Title III law I as required in statute. Following the self-evaluation and based on predetermined risk factors, selected subrecipients are monitored in one of two ways: via telephone/desk monitoring or on-site monitoring. Subrecipients selected for the telephone/desk or on-site monitoring receive a report with recommendations, suggestions for change and changes required to place the program in compliance with federal statute. Those with changes required are monitored for successful

implementation of the required changes. Additionally, when appropriate, the on-site visits of Field Services staff are combined with the Title III visit. Finally, Field Services staff routinely make inquiries in their on-site visits about Title III requirements.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 3130813  
**Finding Title:** Improving Teacher Quality State Grants, *CFDA* 84.367

**Finding:** MDE's internal control over the Improving Teacher Quality State Grants (Improving Teacher Quality) Program did not ensure its compliance with federal laws and regulations regarding allowable costs/cost principles; matching, level of effort, and earmarking; and subrecipient monitoring.

**Agency Comments:**

- a. MDE has recovered the overpayment and corrected the error.
- b. MDE improved internal control by closely monitoring spending plans and internal accounting records in order to comply with federal laws and regulations. Administrative cost overruns were not returned to the USDOE because they were not overruns and qualified to be recoded to another accounting period within the period of availability.
- c. The office was severely understaffed at the time, preventing MDE from appropriately following up on on-site review compliance plans. Staffing has now increased. New systems are in place to ensure appropriate follow-up.

**Audit Period:** October 1, 2006 through September 30, 2008  
**Finding Number:** 6410910  
**Finding Title:** Career and Technical Education - Basic Grants to States, *CFDA* 84.048

**Finding:** The Department of Labor and Economic Growth's internal control over the Career and Technical Education - Basic Grants to States Program did not ensure its compliance with federal laws and regulations regarding matching, level of effort, and earmarking and subrecipient monitoring.

- Agency Comments:**
- a. Matching, Level of Effort, and Earmarking  
MDE continues to wait for the Program Determination Letter from the USDOE regarding the use of an alternative methodology for calculating Michigan's maintenance of effort requirement.
  
  - b. Subrecipient Monitoring  
MDE's Office of Audits will review the Single Audit reports for the Departments of Corrections and Human Services for findings in the program. MDE will add these two agencies to its risk analysis process to determine the level of program risk and the possible need for additional monitoring.

MICHIGAN DEPARTMENT OF EDUCATION

Corrective Action Plan

As of June 22, 2010

**FINDINGS RELATED TO THE FINANCIAL SCHEDULES AND FINANCIAL STATEMENTS**

**Finding Number:** 3131001

**Finding Title:** Security and Application Controls

**Management Views:** The Michigan Department of Education (MDE) disagrees that this is a material weakness.

a. The development contractor for the Child Nutrition Application Program (CNAP) has read-only access to the application which is an approved level. The project manager should also have read-only access to CNAP; however, when required, and upon MDE manager approval, the CNAP project manager may be granted super-user access. This access is intended as short term to perform specific tasks. During the time of the audit, the project manager did have super-user access. This was an oversight by MDE staff and was corrected upon notification. This has been corrected. MDE will develop access control policies and procedures to ensure that access is properly monitored (see response to part c.)

b. MDE and the Department of Technology, Management & Budget (DTMB) acknowledge this finding and have worked together to improve the change management processes.

c. MDE agrees that there was no access monitoring policy for MDE applications or data.

**Planned Corrective Action:** a. Access to Food Nutrition System Fiscal Reporting System was reviewed and changed after the initial

audit findings were released. MDE will regularly monitor access to systems. Another system is currently being rewritten and the new system will be set up such that system developers will have no ability to make any unauthorized changes to the data.

- b. The DTMB application manager has reviewed change management procedures for all affected systems. Recommended changes to the approval process and change request workflows have been made to each of the individual procedures. Final approval was made by MDE project managers, MDE business owners, and the MDE security manager.
- c. MDE will have an access monitoring policy for the following information technology applications completed by September 30, 2010. The policy will include general provisions as well as application specific details on identifying and monitoring high risk transactions.

Cash Management System (CMS)  
Child Nutrition Application Program (CNAP)  
Food Nutrition System Fiscal Reporting System (FNS-FRS)  
Michigan Electronic Grants System (MEGS)  
State Aid Management System (SAMS)

- Anticipated Completion Date:**
- a. December 31, 2010
  - b. September 30, 2010
  - c. September 30, 2010

**Responsible Individuals:** Louis Burgess, Dan Hanrahan, and Craig Thurman

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**Finding Number:** 3131002  
**Finding Title:** Monitoring of Internal Control Over Financial Reporting

**Management Views:** MDE agrees with the underlying intent of the recommendation. MDE has documented its oversight and review control system. MDE uses internal controls, including management reviews, to ensure the accuracy of its transactions. MDE is unable to do more with current resources. Although MDE believes that its current oversight process is adequate, it will consider adding additional oversight and monitoring if additional resources become available. Also, MDE will work with its internal auditors to help ensure the integrity of MDE's internal control systems.

The Office of Audits has historically focused its resources on the areas of highest risk. The first and second risk priorities are to provide adequate oversight of the \$1.6 - \$2.1 billion of federal assistance and \$11.7 billion of State school aid. The first priority is processing subrecipient financial audits and Single Audits. The second priority is establishing pupil auditing standards, training, and doing quality control reviews of intermediate school district pupil audits.

**Planned Corrective Action:** If additional resources become available, MDE will more fully monitor the effectiveness of its internal control over financial reporting.

**Anticipated Completion Date:** Ongoing

**Responsible Individual:** Kathleen Weller

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**Finding Number:** 3131003  
**Finding Title:** Accounting Controls

**Management Views:** MDE agrees.

**Planned Corrective Action:** Management will more closely review accruals in the future.

**Anticipated Completion Date:** Immediate

**Responsible Individual:** Dan Hanrahan

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#### FINDINGS RELATED TO FEDERAL AWARDS

**Finding Number:** 3131004  
**Finding Title:** Food Donation, *CFDA* 10.550

**Management Views:**

- a. Each consortium is required to maintain records for a period of three (3) years after the end of the fiscal year to which they pertain, or until final resolution of outstanding audits or claims per the memorandum of understanding with MDE.
- b. MDE agrees.
- c. MDE agrees.
- d. MDE agrees.

**Planned Corrective Action:**

- a. Language will be added to future memorandums of understanding regarding the monitoring and review of records being maintained by each consortium.

As of July 1, 2010, more comprehensive monitoring duties will be added to the position description prior to filling that position in order for MDE to fulfill its monitoring requirements.

- b. MDE will inform all processors of the requirement for submitting written justification for inventories in excess of six months. Processors will be notified of this requirement in the National Processing Agreement (NPA)/State Participation Agreement (SPA) between MDE and the processor.
- c. MDE's procedure for conducting semiannual sales verification was revised and implemented in January 2010. The following are some of the highlights of the process:
  - Sales Verification Report will be reviewed for each processor conducting sales verification for NOI processed products.
  - Ten percent of the processor's required sample size will be verified by MDE.
  - Schools will be notified by e-mail to verify the pass through value (PTV) of each sale made during the previous six months.
- d. To ensure that sales verification is completed by the processor and MDE, documentation will be maintained and reviewed regularly.

- Anticipated Completion Date:**
- a. October 1, 2010
  - b. Completed
  - c. Completed
  - d. Completed

**Responsible Individual:** Mary Ann Chartrand

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**Finding Number:**

3131005

**Finding Title:**

Child and Adult Care Food Program, *CFDA 10.558*

**Management Views:**

- a. The U.S. Department of Agriculture (USDA) is okay with MDE's process. MDE's statement on the memo reads: "The two applications [Child and Adult Care Food Program (CACFP) and Milk] will be cross referenced and each site participating in both programs will be contacted to ensure the same children are not participating in both programs." To cross-check will mean that applicants in both programs will have sites matched. This does not occur too often. For those in both programs, staff will make a program contact to verify how the program works and will ensure that the same child is not counted twice. Although there was a potential for double counting, this double counting happened in only ONE district in all of MDE's programs.

The questioned costs in the amount of \$16,228 in CACFP should not be considered questioned costs. The over-claim was for the Special Milk Program (SMP) (*CFDA 10.556*) reimbursement in the amount of \$7,763, not CACFP. That balance is in the process of being fully recovered from the school that participated in both CACFP and SMP. The district in question receives approximately \$200,000 per month in reimbursements. The order to reclaim \$13,348.30 from the next claim has been placed. The date for the district to appeal this order has passed. Thus, the \$7,763 plus the additional amount going back from fiscal year 2006-07 through the current claim was recovered in March 2010.

- b. MDE agrees with this finding and will improve its internal control to ensure that CACFPs comply with

federal laws and regulations regarding reporting. MDE accidentally reported revenue instead of expenditures on the line.

**Corrective Action:**

- a. To ensure that sites do not receive reimbursement for the same children for both programs, a question will be added to each site page in the CNAP for both CACFP and SMP. The two applications will be cross-referenced and each site participating in both programs will be contacted to ensure that the same children are not participating in both programs.
- b. In the future, MDE will apply appropriate internal control to detect such an error.

**Anticipated Completion Date:** Immediate

**Responsible Individual:** Mary Ann Chartrand

**Finding Number:**

3131006

**Finding Title:**

Monitoring ARRA Grants, *CFDA* 10.568, 10.569  
84.389, 84.391, 84.392, 84.393, and 84.394

**Management Views:**

- a. MDE acknowledges that offices responsible for American Recovery and Reinvestment Act of 2009 (ARRA) grant awards did not check to ensure that subrecipients were registered with the Central Contractor Registration (CCR) prior to making ARRA grant approvals.
- b. MDE agrees with this finding.

**Corrective Action:**

- a. MDE has been working with all subrecipients since June 2009 to ensure that they have DUNS numbers and that they properly maintain current

registrations in the CCR. MDE is using the Section 1512 report to verify that all subrecipients maintain current registration. All subrecipients have been successfully validated as having DUNS numbers properly registered in the CCR. MDE will ensure that all future ARRA recipients are registered in the CCR prior to processing any awards.

- b. MDE has improved its internal controls to ensure its compliance with federal laws and regulations regarding federal identifying information for the reporting and subrecipient monitoring of program awards involving commodities.

**Anticipated Completion Date:** Completed

**Responsible Individual:** Louis Burgess

**Finding Number:** 3131007

**Finding Title:** Title I, Part A Cluster, *CFDA* 84.010 and 84.389

**Management Views:**

- a. (1) As previously described in response to the performance audit, MDE agrees with this finding. MDE has established more appropriate and detailed internal controls to verify that the appropriate grants are being charged. This program is now being managed by the Office of Education Improvement and Innovation (OEII).
  
- (2) As previously described in response to the performance audit, MDE agrees with the underlying intent of the recommendation. MDE will ensure that contracts are appropriately bid competitively, as required. MDE has recently used this bid process for at least two new

grants (OFS [Office of Field Services] Region 3 and Regional Collaboration Grant).

MDE disagrees with the questioned costs. MDE worked with its contractor and procured training for principals from high priority schools participating in the Statewide System of Support (SSoS); training for the principal coaches; building audits designed to assist SSoS schools determine strengths and areas of concern as well as pointing local educational agencies (LEAs) and MDE to systemic issues needing to be addressed; and development of an IT toolkit encompassing a comprehensive needs assessment, school improvement plan, and other components aligned to federal requirements. After a series of pilot tests, the IT toolkit is in use in all school buildings that are part of LEAs receiving federal funds. These services were procured from Michigan State University, Advanced Ed in collaboration with the North Central Association and Council on Accreditation and School Improvement (NCA CASI) as well as the Southern Association of Colleges and Schools Council on Accreditation and School Improvement, Inc (SACS CASI). Charges to the Title I program are based on the cost of these activities. The activities directly benefited the Title I program. They were necessary to implement key portions of the No Child Left Behind statute. There was no harm to the federal interest.

- b. (1) MDE does not disagree with this finding. OFS was severely understaffed at the time, preventing appropriate follow-up on on-site review compliance plans.

- (2) MDE agrees with this finding. MDE was understaffed at the time, making it difficult to follow up on discrepancies.
- (3) As previously described in the performance audit response, MDE agrees with this finding.
- (4) As previously described in the performance audit response, MDE disagrees with this finding. MDE is following the federal guidance for the 20% set-aside for Supplemental Educational Services (SES) and Choice/Transportation.

MDE will ensure that more appropriate and detailed documentation is provided in the future.

- c. MDE agrees with this finding. MDE was severely understaffed at the time and unable to follow up in all instances.

**Planned Corrective Action:**

- a. (1) MDE has changed its procedures and the director of the OEII now signs and approves invoices that clearly state the work done and its relationship to the High Priority Schools initiatives.
- (2) MDE now follows appropriate procurement procedures for contracts. This program is now being managed by the OEII.
- b. (1) Staffing has now increased. New systems are in place to ensure appropriate follow-up.
- (2) This program is being managed by OFS. OFS is awaiting approval of a lead fiscal auditor staff member position and will establish stronger fiscal monitoring in the near future. MDE plans

to contract with an appropriate number of fiscal monitors as needed to follow up on fiscal issues such as appropriate timing of three-day cash draws.

Part of the responsibility of the lead fiscal auditor staff member is to follow up on discrepancies in timing of three-day cash draws.

(3) This program is now being managed by the OEII. Careful attention and systems are being put in place to ensure that documentation of services and related contracts are appropriately in place, consistent with the terms, conditions, and specifications of contracts and purchase orders.

(4) MDE will monitor LEAs to ensure that they are setting aside 20% of their funds for SES. MDE is aware that the federal guidance allows the district to set aside a percentage of the 20% from federal funds and may indicate the balance from other funding sources, if applicable. MDE continues to work to strengthen the monitoring that occurs for SES and Choice.

c. Staffing has improved and management has developed processes to ensure that all required LEAs will complete the Title I Comparability Application, demonstrating compliance with this requirement. The OFS will monitor a large sample to ensure compliance.

**Anticipated Completion Date:** a. (1) Completed

(2) Completed

b. January 31, 2011

c. January 31, 2011

**Responsible Individual:** Michael Radke

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**Finding Number:** 3131008

**Finding Title:** Special Education Cluster (IDEA), *CFDA* 84.027, 84.173, 84.391 (ARRA), and 84.392 (ARRA)

**Management Views:** a. (1) MDE agrees with this finding.

(2) MDE agrees with this finding.

(3) MDE agrees with this finding.

b. MDE agrees with this finding.

**Planned Corrective Action:** a. (1) The review of final narrative reports has been undergoing improvement processes. Since the last audit, personnel assigned to the review have left MDE. New personnel have been assigned and the Office of Special Education and Early Intervention Services (OSE-EIS) has established a process that sets a specific time frame annually when final narrative progress reports will be reviewed and documented.

The OSE-EIS will develop a procedure to ensure timely submission of final narrative reports by LEAs.

(2) Program fiscal reviews have been implemented and maintained historically with significant paper documentation. Of the program fiscal reviews selected for review, the finding represents a missing single page with no

findings for the LEA. The page was available to create the Program Fiscal Review letter to the intermediate school district (ISD) and LEA and subsequently misfiled. The OSE-EIS currently maintains all supportive documentation and communications electronically utilizing TeamMate audit software. There are no longer paper files to be misplaced.

(3) Due to the extensive effort to implement the requirements of the Individuals with Disabilities Education Act (IDEA) American Recovery and Reinvestment Act funding, staff with federal maintenance of effort (MOE) responsibility were fully redirected from this activity. In addition, the staff member with primary responsibility for the MOE processing left the employment of the OSE-EIS. The OSE-EIS is in the process of hiring a new staff member that will have MOE responsibility, in addition to training additional existing staff to support the timely review of LEA MOE.

b. The OSE-EIS will establish procedures and ensure that all federal requirements related to new or expanding charter schools are met.

**Anticipated Completion Date:** a. (1) July 31, 2010

(2) Completed

(3) September 30, 2010

b. August 31, 2010

**Responsible Individual:** Jacque Thompson

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**Finding Number:** 3131009  
**Finding Title:** Career and Technical Education - Basic Grants to States, *CFDA* 84.048

**Management Views:** MDE finds itself in a quandary caused by back-to-back Single Audits. MDE agreed in part with the prior finding and anticipated completing the corrective action by March 31, 2010. However, a repeat finding is being made before the U.S. Department of Education (USDOE) issues a program determination letter on the first finding.

In April 2009, MDE requested and received informal approval to change the methodology used to calculate MOE. The prior audit finding stated that MDE must receive formal approval from the USDOE. In November 2009, the USDOE requested further input from MDE before it resolved the audit finding. In January 2010, MDE submitted additional information including the revised methodology for the years in question. Michigan has met the MOE requirement using the revised methodology. To date, the USDOE has been silent on both the audit resolution and the revised methodology.

**Planned Corrective Action:** To be determined in consultation with the USDOE.

**Anticipated Completion Date:** Indeterminate

**Responsible Individual:** Patricia Cantu

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**Finding Number:** 3131010  
**Finding Title:** Early Intervention Services (IDEA) Cluster, *CFDA* 84.181 and 84.393 (ARRA)

**Management Views:** MDE agrees with the finding.

**Planned Corrective Action:** The Office of Early Childhood Education and Family Services is developing a process for identifying and reporting local and state expenditures. This will be a phased development with input considered from the ISDs. Guidance is also being provided by the Michigan Office of Special Education and Early Intervention Services based on the Part B MOE collection.

**Anticipated Completion Date:** July 1, 2012

**Responsible Individual:** Gary Schafer

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**Finding Number:** 3131011

**Finding Title:** Safe and Drug-Free Schools and Communities - State Grants, *CFDA* 84.186

**Management Views:**

- a. (1) MDE acknowledges this finding. On-site monitoring/desk reviews were not conducted during 2007-08. A total of 16 on-site/desk reviews were conducted in 2008-09.
  
- (2) MDE acknowledges the finding. Because education grants are often program driven, it is not unusual to see programs run in the middle of the school year that result in large cash draws (e.g., prevention curriculum purchase for program implementation). An even draw of funds throughout the school year is not expected in all subrecipient situations. Since the previous audit finding, procedures were followed and reports were run in CMS quarterly to monitor these draws. These reports were saved, but follow-up documentation is not available regarding specific districts cited in this audit. However, this documentation is available

for other subrecipients participating in this grant program.

- b. MDE acknowledges the finding. An updated allocation procedure to ensure that grants funds were earmarked to account for new/expanded charter schools has been implemented. These set-aside funds were allocated to new/expanded charter schools when the fall enrollment counts were finalized. This procedure was followed as a result of the previous audit, which did not conclude until 2009, and it will continued to be followed in the event federal Safe and Drug-Free Schools and Communities - State Grants (SDFSC) funding is restored.

**Planned Corrective Action:**

- a. (1) Twenty on-site/desk reviews will be conducted in 2009-10.  
  
(2) MDE will continue to follow the approved procedures of running quarterly cash timing reports and will continue to document follow-up correspondence with districts with cash draws that may have been in excess of accumulated expenditures.
- b. An updated allocation procedure to ensure that grants funds were earmarked to account for new/expanded charter schools has been implemented.

**Anticipated Completion Date:**

- a. Completed
- b. Completed

**Responsible Individual:**

Kyle Guerrant

**Finding Number:**

3131012

**Finding Title:**

State Grants for Innovative Programs, *CFDA* 84.298

**Management Views:**

- a. MDE disagrees with the nature of the finding. MDE's OFS does not begin the monitoring of final expenditure reports (FERs) at the line item level. The Michigan Electronic Grants System (MEGS) initiates the process based on the reported subtotal as compared to the approved subtotal. If there is a 10% deviation, districts are required to describe the deviation and provide rationale for the reported numbers. The district explanation is forwarded to the OFS consultant to determine if the item was allowable.

MDE uses the results of Single Audits to document further follow-up and review of items against approved budgets.

- b. MDE conducted 16 subrecipient on-site visits during fiscal year 2007-08. The on-site review in one LEA was not completed. The high school did not complete the data required. The review was completed the following October.

OFS intends to strengthen the compliance requirement for the Plan by increasing the use of an electronic tracking system that will assist in notification that the Plan is past due. Immediate follow-up will be initiated by the OFS and consequences developed for failure to comply with the request.

**Corrective Action:**

- a. Ongoing  
MDE continues to work with the specific LEA. It has not completed compliance for three years. Its

funding will be held in 2010-11 until compliance is complete.

b. Completed

**Anticipated Completion Date:** June 30, 2011

**Responsible Individual:** Mike Radke

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**Finding Number:** 3131013

**Finding Title:** Education Technology State Grants, *CFDA* 84.318

**Management Views:**

a. MDE acknowledges that, at the time of application, the Eastern Upper Peninsula (EUP) ISD consortium and the Wexford-Missaukee ISD consortium did not list an eligible LEA applicant as part of their application pursuant to the qualified applicants list provided by MDE. It should be noted that **the federal government interest was not harmed**, i.e., to serve at least one high needs school. These grants were structured to have the grant partners conduct a sub-application process after the competitive award to increase the number of participating LEAs, particularly those schools designated as high needs. In the case of the EUP ISD grant, the project served **87 LEAs** in the 2007-2008 grant of which **9 LEAs** (10 percent) were high priority schools, including **Sault St. Marie Area Public Schools**. In the case of the Wexford-Missaukee grant, the project served **216 LEAs** in the 2007-2008 grant of which **38 LEAs** (17.5 percent) were high priority schools, including **Cadillac Area Public Schools**. It should be noted that the 2002 Title IID federal guidance also places a priority on servicing schools that have a

substantial need for assistance in acquiring and using technology:

F-5. What is a "high-need local educational agency"?

A "high-need local educational agency" is an LEA that -

- (1) Is among those LEAs in the State with the highest numbers or percentages of children from families with incomes below the poverty line; and
- (2) Serves one or more schools identified for improvement or corrective action under section 1116 of the ESEA, or has a substantial need for assistance in acquiring and using technology.

b. (1) OFS has consistently worked during the application process to ensure that the 25% of the funds is used for professional development related to implementing the professional development in the classroom. The guidance does allow for this amount to be paid from another source or to be contributed in kind by the vendor or trained facilitator familiar with the content.

(2) MDE acknowledges the complexity involved in completion of the compliance plan and submission to MDE within 30 days. MDE currently intends to maintain this 30-day time frame to clearly articulate the importance of addressing compliance issues immediately.

(3) MDE does not agree with this finding.

A review of the draws indicates upfront draws on grant funds that exceed the normal spending curve. The reason for this is that 62% to 63% of the grant funds are earmarked for course registration scholarships. The funds are required early in the grant period to facilitate online instruction. This funding sequence is unique to this project.

MDE believes that the nature of the project required accelerated fund draws.

**Planned Corrective Action:**

- a. N/A (not applicable). MDE is in compliance.
- b. (1) OFS plans to increase monitoring and oversight of all aspects of the federal programs within OFS. Additional staff will be added or contracted to ensure that the internal controls from application to FER comply with the intent and purpose of the legislation.
- (2) The electronic tracking system is being studied as a potential tracking system to help staff ensure that districts comply with the timely reporting requirements. This system will be used in tandem with the proposed, expanded monitoring procedures. It is anticipated that OFS will eliminate this issue through these additional internal controls.
- (3) N/A. MDE is in compliance.

- Anticipated Completion Date:**
- a. N/A. MDE is in compliance.
  - b. (1) June 30, 2011  
(2) June 30, 2011
  - c. N/A. MDE is in compliance.

**Responsible Individuals:** Bruce Umpstead, Mike Radke, and Linda Forward

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**Finding Number:** 3131014

**Finding Title:** Reading First State Grants, *CFDA* 84.357

**Management Views:** All 33 FERs were reviewed. The financial analyst confirmed that 4 FERs were outside the 10% variance between the FERs and the approved budget threshold. She documented this review and reported the findings to the program staff and the office director. The program staff followed up with LEAs to ensure that expenditures were authorized.

During the audit, it was determined that one of the FERs was changed from the original FER that the financial analyst reviewed. This was due to a programming issue between MEGS and CMS. The financial analyst did not know that the FER in CMS was not accurate. MDE will find a solution to this problem.

**Planned Corrective Action:** The program office has developed an excel document that will assist the office monitoring subrecipient FERs. This spreadsheet will improve internal controls to aid in proper subrecipient monitoring.

**Anticipated Completion Date:** Completed

**Responsible Individual:** Mark Coscarella

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**Finding Number:** 3131015  
**Finding Title:** English Language Acquisition Grants, *CFDA* 84.365

**Management Views:**

- a. MDE does not disagree. MDE was understaffed at the time and are now recruiting to fill the vacant positions.
- b. MDE does not disagree with this finding. MDE was understaffed at the time, making it difficult to follow up on discrepancies.
- c. MDE does not disagree with this finding. MDE was understaffed at the time, making it difficult to follow up on discrepancies.

**Planned Corrective Action:**

- a. Systematic processes have been put in place to follow up on compliance plans.
- b. Responsibilities for this program have been transferred to OFS. OFS is awaiting approval of a lead Fiscal Monitoring staff member position and will establish stronger fiscal monitoring in the near future.

Part of the responsibility of the lead Fiscal Monitoring staff member is to follow up on discrepancies in FERs.

- c. Responsibilities for this program have been transferred to the OFS. OFS is awaiting approval of a lead Fiscal Monitoring staff member position and will establish stronger fiscal monitoring in the near future. MDE plans to contract with an appropriate number of fiscal monitors as needed to follow up on fiscal issues such as appropriate timing of three-day cash draws.

Part of the responsibility of the lead Fiscal Monitoring staff member is to follow up on discrepancies in timing of three-day cash draws.

**Anticipated Completion Date:** June 30, 2011

**Responsible Individual:** Mike Radke

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**Finding Number:** 3131016

**Finding Title:** Improving Teacher Quality State Grants, *CFDA* 84.367

- Management Views:**
- a. (1) MDE wants to acknowledge that its on site review process monitors all programs in the district consolidated application at the same time. The repeated subrecipient monitoring findings relate to a single plan required to address all the federal changes required and are not individual plans.
  - (2) MDE does not agree with the finding. This grant is primarily for professional development. There is no carryover limit to the funds included in this grant. There is no way to determine if all funds could be legitimately and allowably expended on one comprehensive professional development activity.
  - b. MDE does not agree with this finding. While there may be one exception, OFS has extensive information and protocols in place to ensure the services of non-public schools. MDE does not believe this sample is substantial enough to document a finding in this area.

**Corrective Action:** a. June 30, 2011

b. None needed

**Anticipated Completion Date:** N/A

**Responsible Individual:** Mike Radke

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**Finding Number:** 3131017

**Finding Title:** State Fiscal Stabilization Fund Cluster,  
*CFDA 84.394*

**Management Views:**

- a. FERs are triggered in CMS based on the grant end date. The grant ending date for all the State Fiscal Stabilization Fund (SFSF) awards is September 30, 2011. This is the full period allowed by the USDOE grant award. Although FERs can be completed upon 100% draw of funds, there is no automatic method to trigger the FER. MDE has taken steps to adjust grant ending dates upon 100% draw of funds. This will force the system to generate FER e-mails and notices that the FER for the grant award must be completed within 60 days.
- b. This finding is true as of April 5, 2010. However, the SFSF grants team has subsequently reviewed all submitted FERs.

**Corrective Action:**

- a. As of May 20, 2010, all FERs in the reviewed sample had been certified, processed, and then reviewed by MDE staff. As noted, not all FERs from the 33 subrecipients had been submitted during the audit period. MDE is working to ensure that all FERs are submitted within 60 days of 100% draw of all funds. Modifications are being made to the CMS to trigger a notification indicating that a FER is available to complete upon 100% draw of all funds rather than the grant ending date.

- b. MDE has reviewed 100% of all processed FERS for both fiscal year 2008-09 and fiscal year 2009-10 Stabilization (SFSS) funds. CMS was forced to generate FER notifications for all subrecipients of both fiscal year 2008-09 and fiscal year 2009-10 Stabilization (SFSS) funds that had not yet submitted a FER but had drawn 100% of funds on June 4, 2010. MDE will continue to review all FERS submitted in a timely manner.

**Anticipated Completion Date:** a. Partially completed. Modifications to CMS to trigger a notification indicating that an FER is available to complete upon 100% draw of all funds rather than the grant ending date will be in place for the fiscal year 2010-11 awards.

- b. Completed.

**Responsible Individual:** Louis Burgess

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# GLOSSARY

## Glossary of Acronyms and Terms

ARRA	American Recovery and Reinvestment Act of 2009.
CACFP	Child and Adult Care Food Program.
CCR	Central Contractor Registration.
<i>CFDA</i>	<i>Catalog of Federal Domestic Assistance.</i>
<i>CFR</i>	<i>Code of Federal Regulations.</i>
CMS	Cash Management System.
CNAP	Child Nutrition Application Program.
cluster	A grouping of closely related federal programs that have similar compliance requirements. Although the programs within a cluster are administered as separate programs, a cluster of programs is treated as a single program for the purpose of meeting the audit requirements of OMB Circular A-133.
control deficiency in internal control over federal program compliance	The design or operation of a control that does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect on a timely basis noncompliance with a type of compliance requirement of a federal program.
control deficiency in internal control over financial reporting	The design or operation of a control that does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis.
DLEG	Department of Labor and Economic Growth (now known as Department of Energy, Labor & Economic Growth).

DIT	Department of Information Technology (now known as Department of Technology, Management & Budget).
ELA	English Language Acquisition.
FER	final expenditure report.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are presented fairly in all material respects in conformity with the disclosed basis of accounting.
GAAP	accounting principles generally accepted in the United States of America.
IDEA	Individuals with Disabilities Education Act.
internal control	A process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
ISD	intermediate school district.
LEA	local educational agency.
low-risk auditee	As provided for in OMB Circular A-133, an auditee that may qualify for reduced federal audit coverage if it receives an annual Single Audit and it meets other criteria related to prior audit results. In accordance with State statute, this Single Audit was conducted on a biennial basis; consequently, this auditee is not considered a low-risk auditee.

material misstatement	A misstatement in the financial schedules and/or financial statements that causes the schedules and/or statements to not present fairly the financial position or the changes in financial position or cash flows in conformity with the disclosed basis of accounting.
material noncompliance	Violations of laws, regulations, contracts, and grants that could have a direct and material effect on major federal programs or on financial schedule and/or financial statement amounts.
material weakness in internal control over federal program compliance	A significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected.
material weakness in internal control over financial reporting	A significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial schedules and/or financial statements will not be prevented or detected.
MDE	Michigan Department of Education.
MDIT	Michigan Department of Information Technology (now known as Department of Technology, Management & Budget).
MEGS	Michigan Electronic Grants System.
MOE	maintenance of effort.
MOU	memorandum of understanding.
MSP	Mathematics and Science Partnerships.
N/A	not applicable.

ODCP	Office of Drug Control Policy.
OEII	Office of Educational Improvement and Innovation.
OFM	Office of Financial Management.
OFS	Office of Field Services.
OMB	U.S. Office of Management and Budget.
OSE-EIS	Office of Special Education and Early Intervention Services.
pass-through entity	A nonfederal entity that provides a federal award to a subrecipient to carry out a federal program.
performance audit	An economy and efficiency audit or a program audit that is designed to provide an independent assessment of the performance of a governmental entity, program, activity, or function to improve program operations, to facilitate decision making by parties responsible for overseeing or initiating corrective action, and to improve public accountability.
Proposal A	Michigan residents approved Proposal A in March 1994. Proposal A provisions dedicated new revenue sources to the School Aid Fund (SAF) including the two percentage point increase in the sales and use tax rate and the 6-mill State Education Tax (SET). The increase in the sales and use tax rate became effective May 1, 1994. The 6-mill SET was first levied in July 1994. Proposal A also created a minimum per pupil foundation allowance, which is paid from the SAF to local schools districts from the dedicated revenues of the SAF.
Questioned cost	A cost that is questioned by the auditor because of an audit finding: (1) which resulted from a violation or possible violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document

governing the use of federal funds, including funds used to match federal funds; (2) where the costs, at the time of the audit, are not supported by adequate documentation; or (3) where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

SDFSC Safe and Drug-Free Schools and Communities - State Grants.

SES supplemental educational services.

SFA School Food Authority.

SFSF State Fiscal Stabilization Fund.

significant deficiency in internal control over federal program compliance A control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected.

significant deficiency in internal control over financial reporting A control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial schedules and/or financial statements that is more than inconsequential will not be prevented or detected.

Single Audit	A financial audit, performed in accordance with the Single Audit Act Amendments of 1996, that is designed to meet the needs of all federal grantor agencies and other financial report users. In addition to performing the audit in accordance with the requirements of auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in <i>Government Auditing Standards</i> issued by the Comptroller General of the United States, a Single Audit requires the assessment of compliance with requirements that could have a direct and material effect on a major federal program and the consideration of internal control over compliance in accordance with OMB Circular A-133.
SMP	Special Milk Program.
<i>SOMCAFR</i>	<i>State of Michigan Comprehensive Annual Financial Report.</i>
subrecipient	A nonfederal entity that expends federal awards received from another nonfederal entity to carry out a federal program.
TEFAP	the Emergency Food Assistance Program.
unqualified opinion	An auditor's opinion in which the auditor states that: <ul style="list-style-type: none"> <li>a. The financial schedules and/or financial statements presenting the basic financial information of the audited agency are fairly presented in conformity with the disclosed basis of accounting; or</li> <li>b. The financial schedules and/or financial statements presenting supplemental financial information are fairly stated in relation to the basic financial schedules and/or financial statements. In issuing an "in relation to" opinion, the auditor has applied auditing procedures to the supplemental financial schedules and/or financial</li> </ul>







