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United States Government Accountability Office
Washington, DC 20548

July 9, 2010

June St. Clair Atkinson, Ed.D.
State Superintendent
North Carolina Department of Public Instruction

Subject: *GAO Review of LEA Controls over and Uses of Recovery Act Education Funds (Winston-Salem/Forsyth County Schools)*

Dear Dr. Atkinson:

The American Recovery and Reinvestment Act of 2009 (Recovery Act)¹ mandates GAO to review states' and localities' use of funds made available under the act.² Since April 2009, GAO has published bimonthly reports on our findings related to federal, state, and local implementation of the Recovery Act.³ Currently, we are examining the efforts of selected states and local educational agencies (LEA) to ensure appropriate uses of Recovery Act funds. In North Carolina, we have been reviewing efforts undertaken by the North Carolina Department of Public Instruction (DPI) and selected LEAs to administer and oversee the use of Recovery Act funds under the State Fiscal Stabilization Fund (SFSF) education stabilization funds; Title I of the Elementary and Secondary Education Act of 1965 (ESEA Title I), as amended; and Part B of the Individuals with Disabilities Education Act (IDEA), as amended. As part of this effort, we met with various DPI staff and, from February 23 through 25, 2010, we visited Winston-Salem/Forsyth County Schools (WSFCS) to review and test the adequacy of controls and procedures in place pertaining to Recovery Act funds for these three federal programs. During our visit, we interviewed finance and program officials regarding internal controls, procurement procedures, and use of Recovery Act education funds. We also reviewed a nonstatistical sample of 63 expenditures of Recovery Act funds for goods, services, and salaries under these three programs. As of February 12, 2010, WFSFCS had expended about \$17.6 million in Recovery Act

¹Pub. L. No. 111-5, 123 Stat. 115 (Feb. 17, 2009).

²Recovery Act, div. A, title IX, § 901.

³For GAO bimonthly reports providing a national overview and selected state reviews of Recovery Act spending, see <http://www.gao.gov/recovery>.

funds. Expenditures in our sample totaled \$618,814.84, of which \$185,256.83 represented nonsalary expenses. We conducted our work from February 9, 2010, to April 20, 2010, in accordance with generally accepted government auditing standards. The purpose of this report is to bring to your attention our findings related to WSFCS.

Internal control helps managers better achieve an entity's mission and accountability for results through more effective stewardship of public resources. Internal control includes management and program policies, procedures, and guidance that help ensure effective and efficient use of resources; compliance with laws and regulations; prevention and detection of fraud, waste, and abuse; and the reliability of financial reporting. According to the Office of Management and Budget (OMB) Circular No. A-133, nonfederal entities expending federal awards are required to maintain "internal control over federal programs that provides reasonable assurance that the auditee is managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its federal programs."⁴ U.S. Department of Education (Education) regulations also require grantees and subgrantees (other than states) to maintain effective internal control over "all grant and subgrant cash, real and personal property, and other assets,"⁵ in addition to other controls.⁶

According to Education regulations, grant funds may only be used for allowable costs and reasonable fees or profit to cost-type contractors, and state and local governments must follow the cost principles set out in OMB Circular No. A-87 for determining allowable costs.⁷ For example, OMB Circular No. A-87 states that costs for entertainment, promotional materials (such as souvenirs), alcoholic beverages, certain lobbying, and organized fund-raising and campaigns to raise capital are unallowable. States and LEAs that receive federal funds must ensure that the funds are spent on allowable costs as described in OMB Circular No. A-87, agency program regulations, and the terms of grant and subgrant agreements.⁸

Education's regulations state that grantees and subgrantees will use their own procurement procedures that reflect applicable state and local laws and regulations, provided that the procurements conform to applicable federal law and the standards identified in 34 C.F.R. § 80.36.⁹ In May 2009, according to state officials, North

⁴OMB Circular No. A-133 § __.300(b). 34 C.F.R. § 80.26 requires Education's state and local government grantees and subgrantees to obtain audits in accordance with OMB Circular No. A-133.

⁵34 C.F.R. § 80.20(b)(3).

⁶See e.g., 34 C.F.R. §§ 80.26 (audit) and 80.40 (monitoring).

⁷34 C.F.R. § 80.22.

⁸34 C.F.R. § 80.20(b)(5).

⁹34 C.F.R. § 80.36(b)(1).

Carolina's Office of Economic Recovery & Investment (OERI) issued management directives regarding the use of Recovery Act funds for procurement of goods and services.¹⁰ According to state officials, OERI directives require recipients of Recovery Act funds to advertise contracts for \$5,000 or more and obtain multiple bids or price quotes for Recovery Act procurements, among other things.

In the course of our work, we observed that WSFCS has an internal control system in place for processing purchasing documents and payments of invoices, with defined segregation of duties among those approving purchases, paying invoices, and delivering payments to vendors. We also learned of efforts by administrators to improve processes to ensure that funds are well-spent. For example, according to WSFCS officials, the ESEA Title I office implemented additional controls over school purchases of food for parental involvement meetings to avoid overspending. However, we found several problems related to some of the Recovery Act expenditures we reviewed. Specifically, we found the following:

- *WSFCS expended \$38,400 of ESEA Title I funds¹¹ on a program that included some expenses that appeared to constitute entertainment, a potentially unallowable use of these funds.*¹² WSFCS officials told us that the LEA paid ESEA Title I Recovery Act funds to the Housing Authority of Winston-Salem (HAWs) for a 2009 summer educational program for students entitled the "Summer Teaching Enrichment Program" (STEP). According to STEP officials, the ESEA Title I funds comprised the majority of STEP's 2009 budget, which also included funding from a local corporation and the local police department.¹³ WSFCS and STEP officials described the program as providing remedial academic assistance in reading, math, science, and technology to help students retain educational gains over the summer months. Furthermore, the WSFCS Superintendent said that the district's arrangement with the STEP program was to use district funds to pay only for teachers' salaries, and that other sources of funds would be used to pay for noneducational activities. HAWs officials said that they were instructed by a WSFCS official to make sure that all of the children enrolled in the program

¹⁰North Carolina Office of Economic Recovery & Investment Directives 3 and 3(b) (May 2009 and January 2010), "Contract Provisions for the Procurement of Goods, Services, and Construction Projects Including Design Services and Internal Procurement Directives."

¹¹Of those funds, \$6,400 were Recovery Act ESEA Title I funds and \$32,000 were regular ESEA Title I funds.

¹²OMB Circular No. A-87 states that the costs of entertainment, including amusement, diversion, and social activities, and any costs directly associated with such costs (such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities) are unallowable.

¹³The total amount of Recovery Act and regular ESEA Title I funds, \$38,400, comprised 74 percent of STEP's total estimated budget of \$52,400.

attended ESEA Title I schools, and that they obtained confirmation from the district that all of the children did so. STEP officials told us that students spent approximately 3 hours, 4 days a week, on educational activities and 8 hours, 1 day a week, on academic field trips. STEP officials said that these field trips included trips to science centers, planetariums, and colleges. They also said that the program included workshops on conflict resolution and crime prevention. However, in our review of documents, we found evidence that in addition to paying teachers a total of \$17,270 in salaries, HAWS also used ESEA Title I funds to pay for STEP activities that included other salaries and field trip-related expenses, including tickets for movies, a water park, fast food, and other entertainment. For example, activities for students included a trip to the movie theatre to see movies entitled Ice Age (for K-5 graders) and Terminator (6-12 graders) for a total of \$405.50 and a trip to a water park, Wet and Wild Emerald Point, for \$961.23 (including food and locker rentals). The invoice that HAWS provided to WSFCS lacked supporting documentation for the full range of activities paid with ESEA Title I funds. Instead, payment was made at a rate of \$800 per child attending the program, but no attendance records were provided in support of the invoice. Furthermore, WSFCS officials told us that they did not provide oversight of STEP activities. Finally, we observed and WSFCS officials confirmed that the LEA's final purchase order for this expenditure did not specifically state that the grant was for teacher salaries, or that the children participating in the program must come from ESEA Title I schools. Also, we observed and WSFCS officials confirmed that the purchase order was not signed by the ESEA Title I Director, per the typical procedure WSFCS officials described to us during our visit. A WSFCS official with signature authority acknowledged that the signatures on the purchase order were not in accordance with LEA practice. In response to our observations, WSFCS officials reported to us that they plan to reprogram all or part of the ESEA Title I funds spent on this activity to nonfederal funding sources.

- *WSFCS staff could not provide documentation to show that the district obtained multiple bids or price quotes for contracts for goods and services.* WSFCS officials acknowledged that their practices were not in compliance with state management directives requiring competition or advertising. WSFCS could not provide us with documentation to show that the district solicited multiple bids or obtained multiple price quotes for contracts for goods purchased with Recovery Act funds. In response to our request for information on bids or price quotes for purchases of high-definition televisions, computers, and other electronic equipment (not purchased from state contractors) using ESEA Title I Recovery Act funds, WSFCS staff provided us with one list of various items, the chosen vendor for each of these items, and the items' price.

WSFCS officials also could not provide us with documentation of the district having obtained multiple bids or price quotes for contracts for services. A senior WSFCS official said that documentation was not available because the LEA does not solicit bids or obtain multiple price quotes for professional development services. WSFCS officials also acknowledged that for at least one contract, they were not in compliance with WSFCS's purchasing policy to solicit bids/price quotes for purchases of items costing more than \$5,000 but less than \$90,000.

Federal regulations state that grantees are responsible for managing the operations of grant and subgrant supported activities and must monitor grant and subgrant supported activities to ensure compliance with applicable federal requirements and achievement of performance goals.¹⁴ Therefore, we are referring our findings to your agency for follow-up. We are also sending copies of this report to the Superintendent of Winston-Salem/Forsyth County Schools, the North Carolina Office of the State Auditor, the U.S. Department of Education, and the U.S. Department of Education's Office of the Inspector General. In addition, this report will be available at no charge on GAO's Web site at <http://www.gao.gov>. We included the issues raised in this report, and any actions that DPI or WSFCS has taken to resolve them, in our report issued on May 26, 2010, and will follow up with you on the resolution of these issues.

If you or your staff have any questions about this report, please contact me at (202) 512-8403 or ashbyc@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report include Bryon Gordon, Assistant Director; Laura Acosta; Bonnie Derby; Brian Egger; Tahra Nichols; and Kathleen Peyman.

Sincerely yours,



Cornelia M. Ashby
Director, Education, Workforce, and Income Security Issues

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¹⁴34 C.F.R. § 80.40(a).

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