Item 7

Information/Action Item

Update on Audits

SUMMARY OF THE ISSUE(S):

The Commission's auditors perform independent assessments of the administration of the Commission's programs to provide assurance to the Commission that institutions are adequately administering Commission programs. With the current staffing level, the program compliance auditors are able to conduct institutional reviews of the eligible institutions, on average, every seven to eight years and Cal-SOAP consortia reviews once every three years.

Institutions are selected for review based upon a variety of factors, including but not limited to, the date of the prior review, the number of findings, the liability associated with findings, the number of recipients/dollar value of funds administered, cohort default rate/graduation rate ineligibility, results of federal program reviews and volume/frequency of programs issues raised by staff and/or other stakeholders. The most common program compliance findings from full audits are Cal Grant funds not reconciled; incorrect disbursement due to enrollment status; education level verified incorrectly; Cal Grant income ceiling level exceeded; and Cal Grant funds not deposited and maintained in an interest bearing account.

The Commission's Internal Auditor assists the Commission in the discharge of its oversight responsibilities and to identify and mitigate risk as it relates to its operations and processes.

The following is an update on the Commission's program compliance and internal audit processes and activities.

RECOMMENDATION:

The Internal Audit on departmental succession planning will be reported to the Legislative, Audit and Budget Committee no later than the November Commission meeting.

BRIEF HISTORY OF KEY ISSUE(S):

The Commission has responsibility for the oversight and management of the state and federal financial aid programs it administers. The Commission evaluates the effective management of its programs through external audits of institutions and organizations, like the Cal-SOAP consortia, that participate in the Commission's programs. Any findings identified through these reviews requires that corrective action be instituted and the financial liability, if any, be returned. For the closed 2013/14 and 2014/15 fiscal years, the program compliance auditors returned approximately $475,000 to the state's General Fund and found an additional $99,770 in institutional liability. For the current 2015/16 fiscal year, closed audits have resulted in an additional $640,000 being returned to the State's General Fund and an additional $88,000 in institutional liability.

ANALYSIS:

Program Compliance Audits

The Program Compliance auditors perform independent assessments of the administration of the Commission's programs to provide assurance to the Commission that institutions are adequately administering Commission programs. Program Compliance audits can consist of a full audit that encompasses all aspects of program administration or a focused audit of a particular issue, such as whether Commission funds are deposited in an interest-bearing account.

The Commission currently has three Associate Management Auditors that are dedicated to institutional audits and one Associate Management Auditor that is acting in a Staff Management Auditor capacity. This is a decrease from the seven Associate Management Auditors and one Staff Management Auditor position that the Commission had in 2008-09. With only three program compliance auditors performing audits, the Commission's external audit cycle remains higher than is desirable to ensure that the institutions and entities participating in the Commission's programs comply with applicable laws, policies, and contracts. With the current staffing level, the program compliance auditors will be able to conduct institutional reviews of the eligible institutions, on average, every seven to eight years and Cal-SOAP consortia reviews once every three years.

Institutions are selected for review based upon a variety of factors, including but not limited to, the date of the prior review, the number of findings, the liability associated with findings, the number of recipients/dollar value of funds administered, cohort default rate/graduation rate ineligibility, results of federal program reviews and volume/frequency of programs issues raised by staff and/or other stakeholders. Some additional adjustments to the scoring matrix for audit selection has resulted in the Commission identifying institutions with a significant number of findings for the 2015-16 audit cycle and an increase in the number of institutions placed in the Commission's At-Risk Program. It is anticipated that the 2015-16 audit cycle will result in more than $750,000 being returned to the state's General Fund.

The majority of program compliance reviews performed by the auditors are comprehensive "full audits" which evaluate compliance with the following areas: General Eligibility; Applicant Eligibility; Fund Disbursement and Refunds; Record Retention and File Maintenance; and Fiscal Responsibility. The most common program compliance findings from full audits are:

- Cal Grant funds not reconciled
- Incorrect disbursement due to enrollment status
- Education level verified incorrectly
- Cal Grant income ceiling level exceeded
- Cal Grant funds not deposited and maintained in an interest bearing account

California Student Aid Commission

Cal Grant Funds Not Reconciled

All participating institutions agree to use the funds advanced to it solely for payment to eligible recipients in the Cal Grant Program. Once the Commission advances Cal Grant funds, schools must determine and verify student eligibility before disbursing funds.

Under the terms of the Institutional Participation Agreement (IPA), institutions are required to reconcile payments no later than sixty (60) days after the end of the payment period. All Cal Grant funds must be properly recorded and allocated to the appropriate award year for which the funds were advanced and disbursed. The institution must also report adjusted payment transactions for transactions previously reported in error. The institution must reconcile all award year Cal Grant funds received and disbursed by the institution no later than December 31 following the award year (e.g., December 31, 2014, for the 2013-14 award year). The institution will bear the liability for payments not reported prior to the December month-end processing cycle.

An actual example of such an audit finding is the following. For the 2013-14 award year, an institution was advanced and reported a reconciled amount of $3,018,227 in Cal Grant payments. However, accounting records revealed the school disbursed $3,098,436 of which $87,761 was not reported to the Commission prior to the 2013-14 year-end reconciliation and cannot be reimbursed by the Commission. The institution thus has $87,761 in institutional liability for the 2013-14 award year.

In addition to the payments that were not reported to the Commission, the institution failed to appropriately reconcile certain payments. The total disbursements to be reimbursed by the Commission for the 2013-14 award year equaled $3,010,675 ($3,098,436 actual disbursements less $87,761 in unreported payments). Therefore, the institution disbursed $7,552 less than the amount advanced by the Commission ($3,018,227 Commission advanced and reconciled amount less $3,010,675 in reimbursable payments) which must be returned to the Commission.

Incorrect Disbursements Due To Enrollment Status

Institutions are required to verify eligibility at the time that Cal Grant funds are disbursed to the student or credited to the student’s account. The enrollment status must be determined according to the student’s attendance at the time Cal Grant funds are paid to the student. Enrollment status directly correlates to the amount of the Cal Grant award and the percentage of eligibility used. For example, an institution’s enrollment status policy is as follows:

Full-time	12 units or more
Three-quarter-time	9-11 units
Half-time	6-8 units

- For the Fall 2013 term, student No. 1 attempted 9 units and therefore was only eligible for a three-quarter time Cal Grant B award in the amount of $3,959 ($3,406 tuition + $553 access). The student, however, received a full-time payment of $5,279 ($4,542 tuition + $737 access). As a result, the ineligible amount of **$1,320** ($5,279 - $3,959) must be returned to the Commission.

- According to enrollment records, student No. 2 attempted and completed 12 units for the Fall 2013 term. The student was eligible for a full-time payment of $5,347 ($4,611 tuition + $736 access) but only received a three-quarter time payment of $4,010 ($3,458 tuition + $552 access); thus, the student's Cal Grant B award was not maximized.

<u>Education Level Verified Incorrectly</u>

A new Cal Grant recipient who continues to meet all program eligibility requirements and who demonstrates financial need may have his or her Cal Grant award renewed up to the maximum of the equivalent of four years of full-time attendance. Students in an institutionally-prescribed five year undergraduate program may be eligible to receive an additional year of Cal Grant program eligibility. The total number of years of Cal Grant Program eligibility is based upon the student's educational level (EL) in his or her course of study at the time of the initial Cal Grant award.

To ensure that new Cal Grant A and B recipients receive the correct amount of initial program eligibility, institutions must verify that Commission records reflect the recipient's correct EL for the term in which the first Cal Grant payment is made. To ensure that the student's program eligibility is correct, the Commission recommends that schools verify the EL for new recipients prior to making the Fall term payment.

Moreover, the maximum award amount for the Cal Grant B program for a first-year student covers living expenses, books, technology, supplies and transportation, but not tuition and fees. At four-year institutions and private institutions with two-year programs, the grant also covers tuition and fee award amounts beyond the freshman year.

For example, an institution has a grade level policy that establishes the number of units associated with each of the four grade levels as follows:

Grade Level	Number of Units
1	0 –29
2	30-59
3	60-89
4	90+

- A review of Commission and Institutional records revealed that the institution certified student No. 1 as an EL 2. However, the student's academic transcripts indicated that the student completed 62 units prior to the start of the Fall 2013 term. Based upon the Institution's grade level policy, the student should have been certified as an EL 3, and was only eligible to receive 200% of full-time Cal Grant eligibility.

- In the case of student No. 2, the Cal Grant B recipient was certified as an EL 2 but had no transfer units and only completed 21.0 units prior to the start of the Fall 2013 term. Therefore, the student should have been certified as an EL 1. Commission and Institutional records indicate that the student received a Cal Grant B Tuition/Fee award of $2,832 and a Cal Grant B Access award of $737 for the award year. The student was solely eligible to receive the access award of $737 based upon the student's grade level. Thus, the $2,832 tuition award is deemed ineligible and must be returned to the Commission.

California Student Aid Commission

Income Ceiling Level Exceeded

Initial and renewal Cal Grant applicants with financial need whose income does not exceed the income and asset ceiling levels and who meet other selection criteria are eligible for a Cal Grant award. All Cal Grant applicants must submit a completed official financial aid application known as the Free Application for Federal Student Aid (FAFSA) or the California Dream Act Application annually to determine eligibility. For the FAFSA, the Commission electronically draws down applicant information from the Central Processing System (CPS) contractor selected by the U.S. Department of Education. The CPS also provides institutions with the Institutional Student Information Record (ISIR) that contains all of the information provided on the FAFSA.

The family income for a dependent student is the parent's total income (TI) as calculated by the Federal Processor. TI is the sum of the taxable and untaxed income, minus amounts reported in the income but excluded from the formula. Cal Grant income and asset ceilings are set by the Commission in accordance with the provisions of California Education Code 69432.7(k) and are adjusted annually.

Prior to disbursing any Cal Grant funds, a qualifying institution is obligated, under the terms of its IPA with the Commission, to resolve any conflicts that may exist in the data the institution possesses relating to that individual.

The following table indicates the income ceiling levels for new and renewal Cal Grant recipients who are either dependent students or independent students with dependents other than a spouse, for the 2013-14 award year:

INCOME LIMITS		
Family Size:	Cal Grant A and C	Cal Grant B
Six or more	$96,100	$52,800
Five	$89,100	$48,900
Four	$83,100	$43,700
Three	$76,500	$39,300
Two	$74,700	$34,900

An example of this type of finding is as follows:

- A review of the file for student No. 1 revealed that the independent Cal Grant B recipient's original FAFSA indicated a TI amount of $29,941 with 2 in the household. However, based upon federal verification, the TI increased to $35,340 which exceeds the income ceiling level of $34,900 for a household size of 2 as indicated in the table above.

  Commission and Institutional records revealed that the student received Cal Grant funds in the amount of $5,472 for the 2013-14 award year, which they were not eligible to receive. Prior to the on-site audit, the Institution returned the ineligible funds in the amount of $5,472 via check to the Commission.

California Student Aid Commission

Cal Grant Funds Not Deposited and Maintained in an Interest Bearing Account

As required by the IPA, institutions must maintain Cal Grant funds in an interest-bearing account or an investment account at a financial institution with a presence in California whose accounts are insured by the Federal Deposit Insurance Corporation (FDIC) or the Federal Savings and Loan Insurance Corporation (FSLIC) or secured by collateral of value reasonably equivalent to the amount of Cal Grant Program funds in the account. Furthermore, these funds must be identified as "State" funds.

Annual interest earned on Cal Grant funds constitute State funds and must be remitted to the Student Aid Commission on behalf of the State no later than March 1 following the calendar year for which the interest accrued (e.g., March 1, 2015, for calendar year 2014). Each year, the Commission issues a Special Alert to all institutions to remind them that the interest is due by March 1st of the year.

When returning interest, neither bank related fees associated with maintaining the account nor negative interest associated with an institution's use of non-state funds for Cal Grant students should be deducted from the accrued interest. Both these amounts reflect expenses that cannot be offset against the interest earned by the advance of State funds for the Cal Grant program.

In calculating the interest on the Cal Grant funds, an institution should utilize the same methodology as was used by its financial institution or investment pool to calculate interest on the account in which the Cal Grant funds were deposited. Findings related to non-interest bearing accounts would be the following.

- A review of the bank statements from Bank ABC and discussions with Institutional staff revealed that the bank account is a non-interest bearing account for which Cal Grant funds were deposited and maintained. Thus, the potential exists for loss of interest. The institution is required to submit documentation demonstrating that Cal Grant funds will be deposited in an interest bearing account.

Unscheduled Audits Update

In early July 2015, the Commission's audit staff made an unannounced audit of the Los Angeles Cal-SOAP Consortium. This audit required several trips to Los Angeles to interview the Cal-SOAP employees, employees of the fiscal agent California State University, Los Angeles, and the student tutors/employees of the high schools where tutoring services are being provided. The audit staff also requested and received a large volume of accounting documents related to the expenses being billed to the Cal-SOAP project including back-up documentation on salary, benefits, travel, mileage, phone charges, and other miscellaneous expenses. The auditors also requested and received documentation from the Consortium regarding its governance, including its board minutes. The draft audit was issued in January 2016. The audit response was received on April 8, 2016. Upon further review of the response, some additional documentation was required from the Consortium. This documentation is due to the Commission on May 31, 2016. This audit is not yet final.

California Student Aid Commission

Internal Audits

Internal Audit Plan Activities

The role of the Internal Auditor is to assist the Commission in the discharge of its oversight responsibilities and to identify and mitigate risk as it relates to its operations and processes. In February 2015, the Commission reviewed the risk assessment and adopted a three-year audit plan which prioritized the high risk areas to be audited as follows:

1. Departmental Succession Planning
2. Personally Identifiable Information (PII) Protection (which includes Network Security)
3. Cal Grant Program – Dream Act New Applicant Eligibility
4. Information Technology Modernization
5. Information Security Program

The Internal Audit on departmental succession planning is in process. This audit will be reported to the Legislative, Audit and Budget Committee upon completion.

In addition, the Internal Auditor is performing a review of the Commission's information technology inventory and surplus processes with observation and recommendation on areas where business improvement and additional internal controls could be implemented.

State Leadership Accountability Act

As a state body, the Commission must complete the reporting required by the State Leadership Accountability Act (SLAA) (formerly known as the Financial Integrity and State Manager's Accountability (FISMA) Act of 1983). SLAA was enacted to reduce the waste of resources and strengthen accounting and administrative control. SLAA requires each state agency head to maintain effective systems of internal accounting and administrative control, to evaluate the effectiveness of these controls on an ongoing basis, and to biennially review and prepare a report on the adequacy of the agency's systems of internal accounting and administrative control. Through the SLAA, the Commission performs a risk assessment and develops a corrective action plan to address the identified risks. The three highest areas of significant risk were identified as key person dependence (succession planning); staff training, knowledge and competence; and technology (outdated, incompatible).

The Commission's SLAA report was timely submitted in December 2015. The Commission continues to work on its corrective actions in response to the identified risks. The next Corrective Action Plan is due June 30, 2016.

Staff will be available at the meeting to discuss this information and respond to questions.

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