
Status Report on Monitoring Fiscal Accountability of the Department of Education: Case Study - Royal Elementary School

A Report to the
Governor
and the
Legislature of
the State of
Hawaii

Report No. 95-23
November 1995



THE AUDITOR
STATE OF HAWAII

The Office of the Auditor

The missions of the Office of the Auditor are assigned by the Hawaii State Constitution (Article VII, Section 10). The primary mission is to conduct post audits of the transactions, accounts, programs, and performance of public agencies. A supplemental mission is to conduct such other investigations and prepare such additional reports as may be directed by the Legislature.

Under its assigned missions, the office conducts the following types of examinations:

1. *Financial audits* attest to the fairness of the financial statements of agencies. They examine the adequacy of the financial records and accounting and internal controls, and they determine the legality and propriety of expenditures.
2. *Management audits*, which are also referred to as *performance audits*, examine the effectiveness of programs or the efficiency of agencies or both. These audits are also called *program audits*, when they focus on whether programs are attaining the objectives and results expected of them, and *operations audits*, when they examine how well agencies are organized and managed and how efficiently they acquire and utilize resources.
3. *Sunset evaluations* evaluate new professional and occupational licensing programs to determine whether the programs should be terminated, continued, or modified. These evaluations are conducted in accordance with criteria established by statute.
4. *Sunrise analyses* are similar to sunset evaluations, but they apply to proposed rather than existing regulatory programs. Before a new professional and occupational licensing program can be enacted, the statutes require that the measure be analyzed by the Office of the Auditor as to its probable effects.
5. *Health insurance analyses* examine bills that propose to mandate certain health insurance benefits. Such bills cannot be enacted unless they are referred to the Office of the Auditor for an assessment of the social and financial impact of the proposed measure.
6. *Analyses of proposed special funds* and existing *trust and revolving funds* determine if proposals to establish these funds and existing funds meet legislative criteria.
7. *Procurement compliance audits* and other *procurement-related monitoring* assist the Legislature in overseeing government procurement practices.
8. *Fiscal accountability reports* analyze expenditures by the state Department of Education in various areas.
9. *Special studies* respond to requests from both houses of the Legislature. The studies usually address specific problems for which the Legislature is seeking solutions.

Hawaii's laws provide the Auditor with broad powers to examine all books, records, files, papers, and documents and all financial affairs of every agency. The Auditor also has the authority to summon persons to produce records and to question persons under oath. However, the Office of the Auditor exercises no control function, and its authority is limited to reviewing, evaluating, and reporting on its findings and recommendations to the Legislature and the Governor.



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OVERVIEW

THE AUDITOR
STATE OF HAWAII

Status Report on Monitoring Fiscal Accountability of the Department of Education: Case Study - Royal Elementary School

Summary

Section 296-92, Hawaii Revised Statutes (HRS), directs the State Auditor to prepare annual fiscal accountability reports of the expenditures of the Department of Education and evaluations of its programs. Section 296-92 HRS, further requires that these annual fiscal accountability reports distribute expenditures according to the following categories: administration, facility support and operations, teacher support/training, pupil support and classroom instruction.

In our first annual fiscal accountability report released in February 1995, we found that the department's attribution of cost by function did not reliably identify how educational dollars are spent. Consequently, for our second annual fiscal accountability report, we did not attempt to categorize statewide expenditures by function. Rather, we focused on identifying costs at a single school in order to allow us to manually examine in some detail all expenditures attributed to the school. We selected the FY1993-94 operational costs for Royal Elementary School as the subject of this examination.

We reviewed the department's current expenditure reports from its Financial Management System and found the reports lacking in detail to identify how the \$1 billion appropriated for public education is being spent. The department claims 94 percent of state and district expenditures are for services provided directly to school sites; however, the department cannot identify expenditures made on behalf of schools. The department is also unable to identify support agencies' operational costs either on a school-by-school or a programmatic basis. The lack of expenditure reports which attribute costs by function and location resulted in our manual calculation of the operational cost for Royal Elementary School during FY1993-94. Cost estimates for programs by site and function were developed by reviewing expenditure reports and by interviewing pertinent personnel to determine the scope and purpose of services provided to Royal Elementary School.

Based on these cost estimates, we were able to calculate the per pupil cost for Royal Elementary School during FY1993-94 to be \$5,705. We were also able to provide per pupil costs for students with special needs and compared these expenditures to per pupil costs for students receiving regular education.

The department has not fully utilized its Financial Management System (FMS) to perform financial analyses and assist in decision making. Program specialists were unfamiliar with the FMS expenditure reports and in several cases failed to detect expenditures charged to incorrect accounts. We found this to be of concern since FMS was intended to integrate the department's budgeting and accounting systems. Finally, object codes currently used in the FMS reports may be used to help identify costs by functions. Such cost data would provide more meaningful information than is currently available.

Recommendations and Response

In order to account for expenditures by the categories required in Section 296-92, HRS, we recommend the department identify all personnel costs by function and location in FMS and work with the governor to ensure support agencies report school level expenditures annually on a school-by-school basis. We also recommend that the department assess and report to the 1997 Legislature whether the FMS can be used to report personnel costs by program, function, and site and whether object codes can be used to identify other costs by function in the FMS.

The Department of Education basically concurred with our recommendations. The department acknowledges the need to improve its financial management system to permit the tracking of expenditures by cost and function. The department indicated its willingness to develop a pilot project that explores the applicability of an electronic financial management system to report personnel cost by function. However, the department indicated it will need additional funding from the Legislature to conduct such a pilot study. The department also noted the need to work with the Department of Accounting and General Services to develop and implement a new payroll system capable of distributing personnel costs by function and location.

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Submitted by

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STATE OF HAWAII

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Foreword

This is the second report prepared in response to Section 296-92, Hawaii Revised Statutes (HRS), which directs the State Auditor to prepare annual fiscal accountability reports and evaluations of the Department of Education. In our first annual fiscal accountability report we examined the department's attribution of central costs to school costs. In this second report we identify the expenditure costs at the school level by location and function using one elementary school (Royal Elementary School) as our sample. We also review and provide comments on the department's current financial expenditure reports and Financial Management System (FMS).

We wish to express our appreciation for the cooperation and assistance extended to us by the officials and staff of the Department of Education, other state agencies, and individuals whom we contacted during the course of our audit.

Marion M. Higa
State Auditor

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Chapter 1

Introduction

Section 296-92, Hawaii Revised Statutes (HRS), enacted as Act 272 by the Legislature in 1994, directs the State Auditor to prepare annual fiscal accountability reports and evaluations of the Department of Education (DOE). The reports shall include but not be limited to an examination of the department's expenditures for: 1) administration, 2) facilities and operations, 3) teacher support and development, 4) pupil support, 5) instructional support, and 6) classroom instruction. It also directs the Auditor to report on the efficiency of the department, districts, and schools in delivering resources to the classroom. The results of the annual reports and evaluations are to be submitted to the Legislature 20 days prior to the convening of each legislative session.

Background

The Legislature has actively promoted education reform for several years. Reform efforts included directing more decision making to the school level along with greater fiscal and curriculum autonomy. Initiatives to increase decision making at the school level such as School Community Based Management (SCBM) and student centered schools were at the core of the Legislature's reform efforts. These initiatives were followed by legislative measures to improve the department's fiscal accountability.

An essential element in the success of school level initiatives is the availability of sufficient and dependable information. The department should provide accurate program costs, personnel information and other expense information for each of the 242 public schools to support school level decentralized decision making. The Legislature also needs this type of information for its decision making processes.

In recognition of the importance of education to Hawaii, the Legislature appropriated close to \$1 billion for FY1994-95 to the Department of Education. However, the Legislature also found that the department's budget practices obscured funding decisions concerning individual schools. Basic departmental expenditure information did not identify the amount of appropriated funds that actually reached the schools and students. This lack of clear expenditure information made it difficult for the Legislature to assess the effectiveness of educational reforms initiated by the Legislature.

The Micro-Financial Analysis Model

The difficulty in obtaining meaningful expenditure data from the Department of Education resulted in legislative action to improve the department's accountability for its actions. In 1993, the Legislature directed the State Auditor to study the feasibility of applying a model that would categorize and analyze expenditures down to the school level. The Auditor contracted with Dr. Bruce S. Cooper to test the feasibility of applying his Micro-Financial Analysis Model (MFA) to Hawaii.

Dr. Cooper's model identifies expenditures by school or by central office location. The model also identifies expenditures by five cost functions at each location: a) administration, b) facilities and operations, c) staff development, d) pupil support, and e) classroom instruction. The MFA model was modified for Hawaii since we have two "central office" cost centers: the state office and the seven district offices.

The model was also modified to accommodate the department's assertion that state and district office expenditures could not be segregated by the five functional categories. Therefore costs for three functions—administration, facilities and operations, and teacher support—were combined into a single category identified as "A" for the state office and "A" for district offices. Costs for pupil support and instructional support were combined into the Instructional and Pupil Support category and designated "E" for the state office and "E" for the district offices. Exhibit 1.1 summarizes the functions at each location as the model was applied to Hawaii.

Using this modified model, the department reported that 94 percent of state and district office expenditures were directly attributed to schools. The remaining six percent was attributed to state and district offices' expenditures for administrative purposes. Based upon Dr. Cooper's observation that the six percent for administrative costs seemed unreasonably low, the Auditor recommended that further research be done to verify what resources expended at the state and district offices can actually be attributed to staff and programs at the school level.

Subsequent Reports

As a follow-up to this recommendation and in accordance with the requirements of Section 296-92, HRS, in 1994 we tested the reliability of the department's attribution of central costs to school costs. The February 1995 report, *Status Report on Monitoring Fiscal Accountability of the Department of Education*, Report No. 95-5, noted that the department's assignment of program to function resulted in attributing costs to inaccurate expenditure categories. We recommended DOE report expenditures by location and function and account for program differences in functional costs at the state, district, and school levels.

Exhibit 1.1 Modified Micro-Financial Analysis Model--Functions By Site Location

STATE OFFICE FUNCTION: *	DISTRICT OFFICE FUNCTION: *	SCHOOL SITE FUNCTION:
<p>A. Administration, Facilities, Operations, Teacher Support and Development</p> <ul style="list-style-type: none"> • Superintendent, financial management and support services, staff, offices, supervisors, directors, including salaries plus fringe benefits. • State office buildings, lights, heat, air conditioning, repairs, maintenance upkeep, plus the cost of running the facilities and operations. Salaries and fringe for operations management staff at state office. • Planning, coordinating, and directing teacher in-service education, staff training director and staff who work out of the state office. 	<p>A'. Administration, Facilities, Operations, Teacher Support and Development</p> <ul style="list-style-type: none"> • District Superintendent, financial management and district support services, staff, offices, supervisors, directors, including salaries plus fringe benefits. • District office buildings, lights, heat, air conditioning, repairs, maintenance upkeep, plus the cost of running the facilities and operations. Salaries and fringe for operations management staff at district offices. • Planning, coordinating, and directing the teacher in-service education, staff training director and staff who work out of the district offices. 	<p>a. Administration</p> <p>Principal, assistants, secretaries. Office expenses, salaries plus fringe benefits.</p> <p>b. Facilities & Operations</p> <p>School site building costs, including utilities, repairs and custodial costs, bus services, food services.</p> <p>c. Teacher Support & Development</p> <p>Delivery of school-site staff development, mentoring, peer coaching, sabbatical leaves, other teacher support efforts.</p> <p>d. Pupil Support</p>
<p>E. Pupil and Instructional Support</p> <ul style="list-style-type: none"> • State office coordination and direction of student support function. Salaries and fringes, office and secretary for the pupil personnel and support functions, psychologists and others who direct and coordinate student services. • State office coordinators and directors of instructional programs who provide services to teachers in their classes. Costs of supporting instruction--such as screening textbooks, writing texts and materials, as well as purchase of direct materials. 	<p>E'. Pupil and Instructional Support</p> <ul style="list-style-type: none"> • District office coordination and direction of student support function. Salaries and fringes, office and secretary for the pupil personnel and support functions, psychologists and others who direct and coordinate student services. • District office coordinators and directors of instructional programs who provide services to teachers in their classes. Costs of supporting instruction--such as screening textbooks, writing texts and materials, as well as purchase of direct materials. 	<p>Out-of-classroom student support: guidance counselors, media and library staff, coaches, club leaders, and others who work with students. Salaries and fringe benefits, plus offices.</p> <p>e. Classroom Instruction</p> <p>Teachers' salaries and fringe for work done in classroom. Other classroom staff costs, including teacher aides, paraprofessionals; textbooks, material, computers used in classrooms; paper, chalk, and other disposables.</p>

* The MFA Model provides for the five school site functions at the central site (e.g., state and district offices). The DOE said it was unable to separate state and district offices' expenditures into the five functional areas. In applying the model to Hawaii, the functional categories for administration, facilities & operations, and teacher support were collapsed into one category, Administration (A, A'). The functional categories for pupil support and classroom instruction were merged into Instructional and Pupil Support (E, E').

In this second annual fiscal accountability report, we identify expenditure costs at the school level. A single school was selected in order to examine all expenditures attributed to the school in some detail. Royal Elementary School was selected as the test school site for this report.

Objectives

The objectives of this study were to:

1. Identify the operational costs of Royal Elementary School by functional category.
 2. Compare operational costs identified for Royal Elementary School with Department of Education's attribution of those costs.
 3. Make recommendations as appropriate.
-

Scope and Methodology

We identified Royal Elementary School's operational costs for FY1993-94 and compared these costs with the Department of Education's attribution of these costs to various functions. We included expenditures made by Royal Elementary School and the Honolulu District and state offices. In addition, we included any identified costs for services provided to Royal Elementary School by the Department of Accounting and General Services (DAGS), the Department of Health (DOH), the Department of Labor and Industrial Relations (DLIR), and the Attorney General's Office (AG).

We reviewed the purchase order descriptions for all supplies and equipment purchased by Royal Elementary School and interviewed school level personnel to determine these costs by function. We also identified and categorized costs for all school site instructional and support staff.

We limited our review of district and state office expenditures to those that involved department personnel and/or contracted services. These services comprise 85 percent of Honolulu District's total expenditures and 70 percent of the state office expenditures for FY1993-94. For each of these district and state offices' expenditures, a determination was made whether any cost could be attributed to Royal Elementary School. To determine the scope and costs of services provided to Royal Elementary School during FY1993-94, we interviewed district and state personnel and reviewed expenditure reports and other pertinent records.

**Royal Elementary
School**

The scope of this report was limited to Royal Elementary School. We did not generate a statewide expenditure report by function since we previously determined that the department's data did not accurately categorize expenditures by function (see Report No. 95-5). To determine Royal Elementary School's operational costs, we examined a customized expenditure report generated from the department's Financial Management System (FMS) as requested by the Auditor. This report identified all expenditures made by Royal Elementary School by program and by item or service purchased. We also examined the year-end DAFR 385A FMS report that identifies expenditures for all personnel and contracted services in the state and Honolulu District offices.

Royal Elementary School was selected as a test site for determining whether all operational costs incurred by state agencies to public schools could be identified and categorized into cost categories. We selected an elementary school to narrow the number of programs that we would be required to review in a short time frame. Royal Elementary School was selected since it is a mid-size elementary school and appears to be representative of schools in the Honolulu District.

Our work was performed from March through June 1995 in accordance with generally accepted government auditing standards.

Chapter 2

Findings and Recommendations

This chapter presents findings and recommendations from our review of the Department of Education's financial management system as applied to Royal Elementary School's operational costs for FY1993-94. We found that the department could not clearly identify operational costs at the school level, thus limiting assurance of fiscal accountability. We also found similar limitations in determining operational expenditures by support agencies.

Summary of Findings

1. The Department of Education does not have adequate state, district and other support agency expenditure information to determine the operational costs of specific schools and programs.
2. The financial analysis capabilities of the Department of Education's Financial Management System (FMS) are not fully used.

Inadequate Expenditure Data Results in Lack of Accountability

The Department of Education's expenditure reports do not provide details that account for how the \$1 billion appropriated for public education by the Legislature is being spent. State and district office expenditures for services and goods provided directly to schools are not identified. In addition, the Legislature and the department lack expenditure information from agencies that provide support services for the Department of Education. For example, the department does not have support agencies' costs for such services as repair and maintenance and diagnostic and mental health programs. The department cannot identify support agencies' operational costs either on a school-by-school or programmatic basis. Therefore, program cost effectiveness and differences in the efficiency of service delivery among schools are not measurable. As a result, the department is unable to accurately report to the Legislature on school system expenditures.

Despite shortcomings in the department's expenditure reports, manual estimates of Royal Elementary School's operational costs are possible. However, manual processes are time consuming and inefficient. Florida's Department of Education successfully uses its electronic financial management system to attribute costs among programs and sites receiving services and can serve as a guide for Hawaii's educational system.

Managers and decision makers need cost data

The department's FMS system was created to provide more accurate, timely, and comprehensive financial information for state, district and school decision makers. However, we found that as currently used, FMS does not generate information or reports with sufficient detailed expenditure information to permit tracking and accountability. The Legislature is unable to determine whether legislative intent and departmental educational goals are being achieved. For example, Act 272, Session Laws of Hawaii 1994, amended Section 296-15.6, Hawaii Revised Statutes, to promote the restructuring and down-sizing of the department's state and district offices. The restructuring re-directs these resources to the school and classroom levels. However, limitations in FMS make it difficult to monitor restructuring efforts. For example, because personnel costs are not categorized by function in the FMS, it was difficult to measure the extent to which state and district personnel resources are being re-directed to programs at the school level programs.

Similarly, state and district offices reported that 94 percent of their expenditures during FY1992-93 were for services and goods provided directly to schools. However, FMS expenditure reports do not identify state and district level expenditures by schools. Therefore, it was difficult to determine how much of these reported expenditures actually reached school level.

Based on our review of Royal Elementary School, we determined that FMS can identify individual school expenditures but FMS is limited in its ability to identify state and district offices' expenditures at the school level. The FMS uses program and organizational identification numbers to account for expenditures. Each school is assigned a unique organization identification number. Therefore, FMS can easily identify and classify individual school expenditures. We reviewed all the expenditures made under Royal Elementary School's assigned organizational identification number to determine the appropriate cost by function for each expenditure. Exhibit 2.1 lists the expenditures incurred by the school by function.

However, state and district offices' expenses are not as easily tracked to individual schools. While the state office and each district office are also assigned organizational identification numbers, FMS does not link these expenditures to individual schools. Thus in order to identify the state and district level services provided to Royal Elementary, we interviewed program specialists for approximately 200 department programs. Once we identified state and district services for Royal Elementary School, we manually calculated the proportional cost of the total state and district expenditures for these services. Costs for state and district services provided to Royal Elementary School are identified by function in Exhibit 2.1.

Exhibit 2.1 Operational Expenditures Royal Elementary School, FY1993-94

	A	A'	a	B	B'	b	C	C'	c	D	D'	d	E	E'	e	Totals
DOE Expenditures																
State Office	0	0	1,258	0	0	11,060	2,654	0	25	0	0	0	0	0	1,201	
Honolulu District Office	0	778	29,422	0	0	414	0	0	22,782	0	9,820	75,822	0	0	10,843	
Royal Elementary School	0	0	124,627	0	0	238,655	0	0	300	0	0	87,853	0	0	962,354	
Total DOE																1,579,868
Fringe Benefits, DOE	230		43,614	0	0	48,802	784	0	6,739	0	2,902	46,069			273,401	422,541
Other Agencies' Support																2,002,409
DOH																
Student Health Services	0	960	0	0	0	0	0	0	0	0	0	12,338	0	0	69	
Vision/Hearing Screening	0	0	0	0	0	0	0	0	0	0	0	858	0	0	0	
Occupational Therapy	0	0	0	0	0	0	0	0	0	0	0	1,157	0	0	0	
Physical Therapy	0	0	0	0	0	0	0	0	0	0	0	547	0	0	0	
Dental Hygiene	0	0	0	0	0	0	0	0	0	0	0	276	0	0	368	
Clinical Consultative Services	0	0	0	0	0	0	0	0	0	0	0	11,250	0	0	0	
Total DOH																27,823
Fringe Benefits, DOH	284											7,809			129	8,222
DAGS																36,045
Physical Plant Operations and Maintenance																
Student Transportation	0	0	0	0	0	35,147	0	0	0	0	0	0	0	0	0	
Total DAGS																35,447
Fringe Benefits, DAGS						2,899										2,899
DLIR																
AG																
Total Expenditures by Function	0	2,252	198,921	0	0	337,277	3,438	0	29,846	0	12,722	243,979	0	0	1,248,365	2,076,800
Total Expenditures by % of Function	0%	0.1%	9.6%	0%	0%	16.2%	0.2%	0%	1.4%	0%	0.6%	11.7%	0%	0%	60.1%	
Total Operating Expenditures																2,076,800

Note: Operating expenditures include all costs other than capital improvement projects.

State and district costs to support schools not tracked

The department lacks management controls to ensure expenditures for personnel are attributed accurately. As a result, the reliability of the expenditure data we identified for Royal Elementary School during FY1993-94 is limited. Program specialists and resource teachers we interviewed did not always keep records of services they provide to specific schools. As noted in our previous report, *Status Report on Monitoring Fiscal Accountability of the Department of Education*, Report Number 95-5, staff service records are kept by some staff, but there is no formal record keeping requirement or procedure.

In that report, we recommended that the department document state and district services delivered to school sites. In our current examination of Royal Elementary School costs, we found that the state and Honolulu District office staff have not standardized their procedures for tracking services they provide to school sites. As a result, we found it necessary to manually calculate the cost of services provided to Royal Elementary School based upon the department's available information.

Methods used to calculate the cost of services provided to Royal Elementary School varied because the department lacks a formal recordkeeping system of central services provided to schools. For example, costs for district staff services provided to Royal Elementary School on a regular basis were calculated by multiplying the staff hourly rate by the amount of time scheduled for the school. In other cases, state and district office personnel who provided unscheduled services to Royal Elementary were asked to estimate the percentage of total time for services attributed to Royal Elementary. Similar methods were used to calculate the cost of contracted services provided to Royal Elementary.

Generally, state and district office personnel maintain records of participants who attend central office sponsored teacher training workshops. In these cases we calculated the cost per school participant by dividing the contracted cost of training by the total number of workshop participants. The per participant cost was then multiplied by the number of Royal Elementary School participants in order to determine the school's cost. In some cases, the department could provide only the number of eligible schools for specific workshops and not the number of school participants. In these cases, the total cost of the workshop was equally distributed among participating schools.

Operational costs are manually determined

Despite the lack of consistent record keeping for central services provided directly to schools, we believe we developed a reasonable estimate of Royal Elementary School's FY1993-94 operational costs.

Using the operational costs we identified, we determined that the per pupil cost at Royal Elementary School for FY1993-94 was \$5,705. Program costs identified for specific program identification numbers were also used to develop separate cost estimates for the school's regular education, special education, gifted and talented, and limited English proficiency (SLEP) programs. Exhibit 2.2 compares the cost of educating students with special needs with students receiving regular education. The per pupil cost for special education students was almost twice the amount expended for regular education students.

Exhibit 2.2
Per Pupil Expenditures, Royal Elementary School
FY1993-94*

Total Expenditures Royal Elementary School	2,076,800	
Average Daily Enrollment	364	
Total Per Pupil Cost		5,705
Total Expenditures for Special Education	61,039	
Students receiving Special Education	16	
Per Pupil Cost Special Education		9,239
Total Expenditures for Students of Limited English Proficiency (SLEP)	13,995	
Students enrolled in SLEP	41	
Per Pupil Cost SLEP		5,765
Total Expenditures for Gifted and Talented	27,516	
Students in Gifted and Talented Program	39	
Per Pupil Cost Gifted and Talented		6,130
Total Per Pupil Expenditures Regular Instruction		5,424

* Per pupil cost for FY1993-94 is based on an average daily enrollment of 364 students. Per pupil cost for regular instruction was derived by subtracting the costs for special education, SLEP, and gifted and talented students from the overall operational expenditures of Royal Elementary School and dividing the base cost by the average daily student enrollment. Per pupil cost for special education, SLEP, and gifted and talented students was determined by adding the distributed program cost for each of these programs to the base amount for regular instruction.

In addition to developing Royal Elementary School's per pupil cost based on program expenditures, we compared operational costs at the school level with the department's attribution of these costs. Exhibit 2.3 compares the department's attribution of cost by function with our attribution of cost. The department's attribution of cost by function is based on program identification numbers. We reviewed all purchase orders and identified the function of each school site staff person to attribute cost by function. We found that the department's attribution of cost at the school level was close to our attribution of costs. For example, the department reported 8.3 percent of Royal Elementary's expenditures were for school level administration and 68.4 percent of the expenditures were for direct classroom instruction. Our distribution of costs produced similar results. We found 8.6 percent of all expenditures made by Royal Elementary were for school level administration costs and 68.1 percent were for direct classroom instruction. We believe the similarity of the result reflects the fact that most of the expenditures made at the school level are for teacher salaries which are categorized under direct classroom instruction.

We were unable to compare the department's attribution of operational costs for Royal Elementary School at the state and district offices since there is no department identification for state and district expenditures made for individual schools. Since our attribution of costs at the state and district levels were exclusively for Royal Elementary, we were unable to compare the attribution of costs by function at the state and district levels.

While the expenditure information we generated is useful for financial analyses and accountability purposes, the manual methods required are cumbersome. Manually reviewing all departmental expenditures is labor intensive, cost inefficient, and impractical to conduct on a broader scale. We believe the department's FMS should be modified to generate reports identifying costs by function and location. Such a system has been successfully implemented by Florida's Department of Education.

Florida utilizes electronic financial management system

In 1973, the Florida State Legislature required its Department of Education to report expenditures on a school-by-school basis by cost function. Florida's Department of Education meets this legislative mandate by distributing the cost of salaries and benefits among programs and schools using an electronic financial management system.

Salaries and personnel benefits are usually the largest cost element of public education. Florida's Department of Education requires in its *Financial and Program Cost Manual* that personnel costs be distributed accurately among programs. This is accomplished by requiring all personnel to allocate their time by function among programs and sites receiving services.

**Exhibit 2.3
Comparative Summary of the Department of Education's and the Office of the Auditor's Attribution of Costs by Function for
Royal Elementary School FY1993-94**

Comparative Summary of Costs by Function *

	A		a		b		c		d		e		Excluded (A+)		Total Expenditures
	Pay	Other	Pay	Other	Pay	Other	Pay	Other	Pay	Other	Pay	Other	Pay	Other	
DOE Attribution															
Amount Expended	\$0	50	117,119	2,931	158,571	83,584	0	0	80,109	5,041	922,630	61,818	1,323	6,815	\$ 1,439,991
% of Total Expenditure (Excludes A+)	0.0%	0.0%	8.1%	0.2%	11.0%	5.8%	0.0%	0.0%	5.6%	0.4%	64.1%	4.3%	0.1%	0.5%	
Auditor's Attribution															
Amount Expended	\$0	0	116,915	7,713	153,678	84,977	0	300	80,080	7,773	913,171	49,183	0	0	\$ 1,413,790
% of Total Expenditure (Includes A+)	0.0%	0.0%	8.3%	0.5%	10.9%	6.0%	0.0%	0.0%	5.7%	0.5%	64.6%	3.5%	0.0%	0.0%	
Amount Expended	\$0	0	116,915	4,603	154,355	83,431	0	300	80,080	6,478	913,171	49,183	1,323	5,952	\$ 1,415,791
% of Total Expenditures (Excludes A+)	0.0%	0.0%	8.3%	0.3%	10.7%	5.9%	0.0%	0.0%	5.7%	0.5%	64.6%	3.5%	0.1%	0.4%	

* The comparative summary of expenditures does not include state and district expenditures made for Royal Elementary School. DOE expenditure data does not attribute costs by function to specific schools. Therefore, we are unable to compare our attribution of state and district expenditures to those reported by the department. This discrepancy was previously noted in Report No. 95-5.

Note: A+ is an after school child care program.

We believe the department should analyze Florida's central personnel cost distribution system to determine whether FMS can produce similar results. We were informed that FMS does not fully integrate payroll/personnel data into the system. FMS presently does not attribute state and district personnel services to specific schools. However, sound financial management and accountability that supports SCBM and student-centered schools require that personnel costs be accurately attributed to either central sites or schools. Without this level of information, the Legislature cannot ensure that appropriated funds are being expended as intended.

Support agencies' expenditures lack accountability

The Department of Education has not provided support agencies with direction to ensure that record keeping practices meet individual school requirements under School Community Based Management (SCBM). The Legislature has supported SCBM in the belief that the school is the basic unit of the educational system and should have the power to decide its curriculum and use of resources within a statewide framework. Since schools are given greater fiscal autonomy under SCBM, it is prudent for an individual school to be knowledgeable of all its expenditures, whether or not it actually expends the funds. This ensures that the school has a comprehensive and realistic understanding of its fiscal condition for planning and management purposes. However, support agencies generally do not report their expenditures at the school level. As a result, schools cannot track expenditures or compare support agencies' school level expenditures such as repair and maintenance of school facilities. Individual schools cannot determine whether support agency services are provided in a cost effective manner. Schools also cannot determine the differences in levels or types of service provided by a support agency to different schools.

The Legislature appropriated \$112 million to other state agencies to support public education in FY1994-95. Under present practices, the department and the supporting state agencies are unable to account to the Legislature for these expenditures at the school level. The Legislature is thus unable to determine if its directives are being implemented and how effectively appropriated funds are being utilized. As part of its implementation of SCBM, the department should work with the Governor to ensure that support agencies institute tracking methods which are appropriate to the individual schools', the department's, and the Legislature's needs.

FMS Financial Analysis Role is Limited

FMS is underutilized. Its capacity to perform financial analyses and assist in decision making are not fully tapped as a management tool. Improper charges to program accounts sometimes remain undetected

since department program personnel do not routinely review FMS reports. In addition, FMS's potential to identify expenditures by function has not been reviewed by the department.

FMS not fully utilized

FMS is intended to be a financial management tool that integrates the department's budgeting and accounting systems. However, we found FMS is not utilized for financial management. For example, program specialists we interviewed often were not familiar with FMS expenditure reports and did not always detect improper charges to their program accounts.

We found several cases in which expenditures were debited against incorrect accounts. In these cases program specialists were unaware of the improper charges until we inquired about the purpose of these expenditures. In one case the Honolulu District Office paid \$22,000 for a school custodian, charging the cost improperly to the district instead of the school receiving the custodial services. In another case, a program specialist reported a deficit of \$40,000 at the beginning of the fiscal year although the school had not yet expended any funds. FMS reports should be routinely reviewed by program specialists to ensure that their program accounts are properly debited. Tracking expenditures to ensure that they are correctly recorded is basic to good financial management. The failure to detect improper charges is indicative of the failure to use FMS for financial management purposes. This is of further concern since FMS is intended to integrate the department's budgeting and accounting systems.

FMS helps identify function of expenditures

FMS expenditure reports are capable of detailing expenditures by program and by general categories that identify costs by function. All expenditures are classified into specific object codes such as elementary teacher, district office teacher, state office teacher, educational supplies, textbooks, and custodial supplies. In our review of purchase orders for Royal Elementary School, we found that object codes are routinely assigned to purchases according to the intended use of the item. Object codes can therefore be used to identify costs by function.

Presently, there are no clear criteria and definitions for the use of object codes by cost function. However, we believe that using object codes to assign costs by function may be more manageable than allocating costs by program. Continuing to attribute expenditure functions by program requires that this be done for over 1,000 department programs at the state, district and school levels. This compares with the approximately 400 object codes presently in use. FMS currently identifies expenditure data by site (school, district, state), program, and object codes. Ensuring that use of object codes is uniformly applied would assure that expenditure by function reports generated using FMS would be consistent. This methodology will not disaggregate school level

expenditures made by the state and district offices on a school-by-school basis. However, we believe that it would provide more meaningful information than is currently available. Therefore the department should develop clear criteria for each object code and assess whether these codes can be used to identify expenditures by function.

Conclusion

Accurate information is necessary for the Department of Education and Legislature to ensure that funds are being expended appropriately. Our review of costs for personnel and contract services for Royal Elementary School showed that current FMS expenditure reports do not contain the detail needed to identify operational costs of specific schools in a feasible manner. In addition, accurate records of central office services provided to schools are not always kept by state office and district staff. Other state support agencies also do not report their expenditures by school site. As a consequence, meaningful and accurate school level expenditure reports cannot be generated for either the schools, the department, or the Legislature.

Recommendations

1. The Legislature should require the Department of Education to identify all personnel costs by function and location in the Financial Management System (FMS).
2. The Department of Education should work with the Governor to ensure that support agencies institute tracking methods to report school level expenditure annually on a school-by-school basis.
3. The Superintendent should require record keeping and reporting of state and district personnel that accounts for their time by function, program and school site. The Department of Education should report to the Legislature whether this information can be incorporated into FMS for the purpose of generating program expenditure reports by cost and location.
4. The Department of Education should improve its financial management by:
 - a. Requiring program specialists and schools to routinely review FMS expenditure reports for accuracy, and
 - b. Establishing clear criteria for the use of object codes. The department should evaluate the application of object codes in determining costs by function and report its findings to the 1997 Legislature.

Response of the Affected Agency

Comments on Agency Response

We transmitted a draft of this report to the Department of Education on October 11, 1995. A copy of the transmittal letter to the department is included as Attachment 1. The department's response is included as Attachment 2.

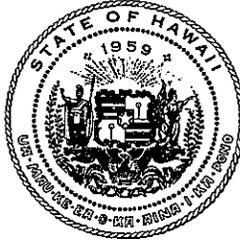
The Department of Education acknowledged that it currently does not track its expenditures by function and location. The department claims that to report all personnel costs by location and function would necessitate development of a new payroll system. This would require coordination with the Department of Accounting and General Services which administers the current payroll system. In order to do so, the department said it will need the Legislature to appropriate additional funds for this purpose. We note the department has not done any cost analysis to support this request to date.

The department reported it will work with the governor and other support agencies to explore how state agencies may track annual expenditure on a school-by-school basis. The department noted the need for a new payroll/personnel to help meet our recommendation that all expenditures be tracked by function and location.

The department also agreed with our recommendation to improve its financial management. It responded that administrators are encouraged to routinely review FMS expenditure reports and that the department will continue to train all administrators to review the reports for accuracy. The department did not specifically address our recommendation to evaluate and report to the 1997 Legislature on the application of object codes in determining costs by function. We affirm this may be a more manageable alternative to the current classification of function of expenditures by program. As we reported in our first fiscal accountability report, this method requires the function of over 1,000 programs to be disaggregated at the state, district and school level. The department has not done this to date.

ATTACHMENT 1

STATE OF HAWAII
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917



MARION M. HIGA
State Auditor

(808) 587-0800
FAX: (808) 587-0830

October 11, 1995

COPY

The Honorable Herman Aizawa
Superintendent of Education
Department of Education
Queen Liliuokalani Building
1390 Miller Street, Room 309
Honolulu, Hawaii 96813

Dear Dr. Aizawa:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *Status Report on Monitoring Fiscal Accountability of the Department of Education: Case Study - Royal Elementary School*. We ask that you telephone us by Friday, October 13, 1995, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Monday, October 23, 1995.

The Governor, and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

A handwritten signature in cursive script, appearing to read "Marion M. Higa".

Marion M. Higa
State Auditor

Enclosures

BENJAMIN J. CAYETANO
GOVERNOR



HERMAN M. AIZAWA, Ph.D.
SUPERINTENDENT

STATE OF HAWAII
DEPARTMENT OF EDUCATION
P.O. BOX 2360
HONOLULU, HAWAII 96804
October 19, 1995

RECEIVED

OCT 23 12 02 PM '95

OFFICE OF THE AUDITOR
STATE OF HAWAII

OFFICE OF THE SUPERINTENDENT

MEMO TO: Ms. Marion M. Higa, State Auditor
F R O M: *Herman M. Aizawa*
Herman M. Aizawa, Ph.D., Superintendent
SUBJECT: Status Report on Monitoring Fiscal Accountability of
the Department of Education: Case Study - Royal
Elementary School

Thank you for the opportunity to review and comment on the
Status Report on Monitoring Fiscal Accountability of the
Department of Education: Case Study - Royal Elementary School.

This report represents the third in a sequence of audits on
monitoring fiscal accountability of the DOE. It is based on a
three and a half month case study by your staff at Royal
Elementary School.

We are happy to learn that your staff's review corroborates
our attribution of costs at the school level. This helps to
validate reports generated by our Financial Management System
(FMS).

This report also confirms our prior assertions that
attributing the centralized services and functions to individual
schools would require intensive manual effort as our current
computerized applications are not designed to accommodate this
requirement. Indeed, as the report states, this effort is "labor
intensive, cost inefficient" (p. 12). Further, this exercise
would be required, not just by the DOE, but all the other state
agencies, DAGS, DOH, DLIR, and the AG's Office, that provide
centralized services to schools. This finding echoes one of the
caveats in educational research: that is, acquiring information
incurs costs; the issue is whether the use of the information
acquired makes it cost-effective.

The DOE's responses to the specific recommendations of the
report are provided below:

Recommendation #1: The legislature should require the Department
of Education to identify all personnel costs

by function and location in the Financial Management System (FMS).

DOE Response:

Currently, the Department of Education reports expenditures by program and location (school/office). The Financial Management System (FMS) cannot identify all personnel costs by functions and location as it currently exists. The DOE's payroll system must interface with the State system that is administered by DAGS. Neither system can accommodate the reporting of costs by function and location for employees who provide services to multiple locations.

The DOE will need to develop and implement a new payroll system in coordination with DAGS to comply with this recommendation.

Recommendation #2: The Department of Education should work with the Governor to ensure that support agencies institute tracking methods to report school level expenditure annually on a school-by-school basis.

DOE Response:

The DOE will explore alternatives with the Governor and the other support agencies to address this recommendation. However, we believe that these state agencies may encounter similar difficulties if they must provide actual managerial overhead cost on a school-by-school basis. They will also face the same constraints in terms of available resources that the DOE does.

Recommendation #3: The Superintendent should require record keeping and reporting of state and district personnel that accounts for their time by function, program and school site. The Department of Education should report to the Legislature whether this information can be incorporated into FMS for the purpose of generating program expenditure reports by cost and location.

DOE Response:

The limitations of existing computer applications, both in the DOE and in the other state agencies, described in Recommendations #1 and #2 also apply to Recommendation #3.

We are not familiar with the electronic financial management system, used by Florida's Department of Education, that is recommended in the report. The DOE is willing to explore the applicability of Florida's system in Hawaii.

If the Legislature feels that this effort will provide the kind of information it needs for decision making, the DOE is willing to conduct a pilot project. However, the DOE does not have the resources in its current budget for such a pilot. Additional resources, not to compete with DOE program needs, will have to be appropriated by the Legislature. Based on the report's findings, it would appear that one of the most essential components is a new payroll/personnel system which would improve the state's support infrastructure for all agencies.

Recommendation #4: The Department of Education should improve its financial management by:

- a. Requiring program specialists and schools to routinely review FMS expenditure reports for accuracy, and
- b. Establishing clear criteria for the use of object codes. The department should evaluate the application of object codes in determining costs by function and report its findings to the 1997 Legislature.

DOE Response:

- a. We concur with this recommendation. We have encouraged administrators at all levels to routinely review FMS expenditure reports. We will continue in our efforts to train all administrators to review these reports for accuracy.
- b. The DOE's use of object codes complies with the State Comptroller's requirements of all state agencies. DAGS compiles and analyzes information on a statewide basis, making consistency in the application of object codes by all departments essential.

In conclusion, we would like to re-emphasize that our existing computer systems can provide detailed financial reports for school expenditures. These systems are currently unable to readily accommodate the attribution of resources that are provided centrally by the DOE, as well as other state agencies. In order for the existing systems to provide the detailed financial reports on an individual school basis, additional resources must be appropriated by the Legislature, over and beyond each agency's budget, to develop the infrastructure for this purpose.

HMA-EHH:lsk

cc: Budget Branch
Chris Ito
Charles Kagawa

