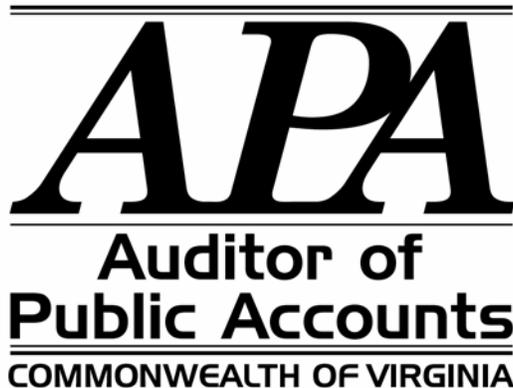


**DEPARTMENT OF EDUCATION  
INCLUDING  
DIRECT AID TO PUBLIC EDUCATION  
AND  
THE VIRGINIA SCHOOLS FOR THE DEAF AND BLIND**

**REPORT ON AUDIT  
FOR THE YEAR ENDED  
JUNE 30, 2004**



## **AUDIT SUMMARY**

Our audit included the Department of Education, Direct Aid to Public Education, the Virginia School for the Deaf and Blind in Staunton, and the Virginia School for the Deaf, Blind, and Multi-Disabled in Hampton. Our audit for the year ended June 30, 2004, found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System;
- no matters involving internal control and its operation that we consider material weaknesses; and
- no instances of noncompliance or other matters that required reporting.

The Department of Education is the designated fiscal agent for the Comprehensive Services Act and we issue a separate report on this entity.

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## **THE DEPARTMENT'S FUNCTIONAL AREAS**

The Department of Education has four functional areas:

- Central Office
- Direct Aid to Public Education
- Virginia School for the Deaf and Blind in Staunton; Virginia School for the Deaf, Blind, and Multi-Disabled in Hampton; and the Virginia Schools for the Deaf and Blind Foundation
- Comprehensive Services Act for At-Risk Youth and Families

The Department's Central Office supervises the public school systems; provides training and technical assistance; and monitors the compliance with laws and regulations of 132 operational school divisions. The Department assists these school divisions, colleges, and universities in helping teachers and other staff improve their skills and licenses and certifies school personnel. The Department also serves as the pass-through agency for state and federal funds and determines the allocation of state money to local school divisions through direct aid to local school divisions.

During fiscal year 2004, the Department transferred over \$4.8 billion in state and federal funds to local school divisions. State dollars make up the majority of these funds, which support the Standards of Quality.

The Department also maintains operational control over the two schools for the deaf and blind. The schools provide comprehensive instructional programs and services to children with serious auditory and visual impairments and multi-disabilities that local school divisions cannot serve. The State Board of Education is the governing body of the Virginia Schools for the Deaf and Blind Foundation. The Foundation promotes the growth, progress, and welfare of the Schools for the Deaf and Blind.

The Department is the designated fiscal agent for the Comprehensive Services Act for At-Risk Youth and Families (CSA). Central Office staff process pool fund payments to localities for services performed assisting at-risk youth. We issue a separate report for CSA.

## **FINANCIAL OPERATIONS**

### Overview

The Department primarily receives General Fund appropriations, which account for over 83 percent of total funding. The Department also receives federal grants and collects fees for teacher licensure. The Schools for the Deaf and Blind receive funds from local school divisions, federal grants, and income from the Virginia Schools for the Deaf and Blind Foundation.

The Department acts as a pass-through agency for state and federal funds and determines the allocation of funds to local school divisions. Over \$4.8 billion in state and federal funding goes through to local school divisions primarily for public education and local school functions.

Standards of Quality funding makes up approximately 60 percent of all aid sent to local school divisions with another 21 percent from special state revenue sharing, which consists of a portion of net revenue from the state sales and use tax and lottery profits. Sales and use tax disbursements go to each school division using census data of school-age children within the school divisions. The school divisions receive

lottery profit allocations based on the number of students reported for each school division in the spring multiplied by the per pupil amount determined by the General Assembly. The Department allocates funds to each locality based on demographic and census information gathered from local school divisions, following the provisions outlined in the Appropriation Act and federal grant agreements.

Financial Activity

Table 1 summarizes the Department's budget to actual expenses.

Table 1

Analysis of Original to Final Budget

<u>Functional Area</u>	<u>Original Budget *</u>	<u>Adjusted Budget</u>	<u>Actual Expenses</u>
<b>Direct Aid to Public Education:</b>			
General fund	\$4,069,907,268	\$4,068,761,117	\$4,053,188,011
Special funds	176,327,733	176,472,733	121,313,188
Federal fund	<u>569,792,100</u>	<u>838,419,768</u>	<u>644,935,176</u>
Total	<u>4,816,027,101</u>	<u>5,083,653,618</u>	<u>4,819,436,375</u>
<b>Central Office operations:</b>			
General fund	46,909,850	49,156,975	45,710,967
Special funds	2,988,873	3,470,213	2,161,619
Federal fund	<u>46,769,916</u>	<u>46,912,271</u>	<u>29,288,791</u>
Total	<u>96,668,639</u>	<u>99,539,459</u>	<u>77,161,377</u>
<b>Virginia Schools for the Deaf and Blind:</b>			
General fund	12,302,915	12,620,612	12,617,857
Special funds	714,901	815,558	679,052
Federal fund	<u>438,525</u>	<u>788,510</u>	<u>612,058</u>
Total **	<u>13,456,341</u>	<u>14,224,680</u>	<u>13,908,967</u>
Total **	<u>\$4,926,152,081</u>	<u>\$5,197,417,757</u>	<u>\$4,910,506,719</u>

Source: Commonwealth Accounting and Reporting System

\* Original Budget includes those funds as appropriated in the 2004 Acts of Assembly (Chapter 943)

\*\* Does not include capital project appropriations and expenditures incurred by the Virginia Schools for the Deaf and Blind

The variance between Direct Aid to Public Education's budgeted and actual spending of General Funds is due to several reasons. During the appropriation process, the Department bases its General Fund direct aid spending estimates on projected average daily membership (ADM) of students at localities throughout the Commonwealth. In fiscal 2004, actual ADM was lower than projected ADM, resulting in less General Fund expenses than expected. Additionally, localities' participation was lower than expected for certain programs including the At-Risk, K-3 Class Size Reduction, and Standards of Learning (SOL) Algebra Readiness programs. Finally, actual spending was lower than projected in several projects including education projects in hospitals, clinics, and detention homes; Project Graduation; and individual student alternative education programs.

The change in Direct Aid to Public Education's budgeted to actual spending of special funds is the result of processing of disbursements from the Literary Fund. While the appropriation authorizing the use of literary funds is contained in the Direct Aid to Public Education budget, the actual disbursement occurs in the Department of the Treasury and appears as an expense in that agency's records. We issue a separate report on the Literary Fund.

The increase in the Central Office's General Funds budget is due to reappropriations for certain education program balances, restoration of funds previously reduced for Virginia Information Technologies Agency operations, and adjustments made to the Partnership in Achieving Successful Schools initiative. Additionally, overall budgeted and actual spending of General Funds were lower than expected in several programs including Education for a Lifetime, vocational education administration, Governor's Schools, electronic classrooms, At-risk Four-Year-Olds, and general equivalency diploma. Position vacancies resulted in lower personnel expenses than expected and the increase in other administrative costs, including rent, agency renovation, recruitment, warehouse storage, and postage was lower than anticipated.

During fiscal year 2004, the Virginia School for the Deaf and Blind in Staunton experienced increased expenses when their steam provider discontinued service and the school contracted with a temporary boiler provider to obtain heat and hot water. During the same time, the school collected more special revenue than expected from localities for tuition reimbursement. The school also requested and received a \$100,000 increase to their adjusted special revenue budget. Since the school received additional General Funds, the additional special revenue budgeted funds were not spent, resulting in the variance between special revenue adjusted budget and actual expenses.

The overall variances in the federal funds between the original and adjusted budgets occur because the Department compiles the estimates of federal awards up to two years in advance. The Department does not receive notification of actual award amounts or new programs until the beginning of the fiscal year, which is after the approval of the original budget. Therefore, the Department must request increases to appropriations for new grants and in federal award amounts during the fiscal year. Other fluctuations occur between the adjusted budget and actual expenses due to the administration of the federal programs. To allow localities time to establish their programs and request reimbursements, many federal grant programs contain extended periods of availability. As a result, not all expenses for a particular grant may occur in one given fiscal year. For example, the Department requires additional start-up time for new awards to establish administrative support, communicate federal requirements and standards, and allocate funding to the localities. Once the localities receive notice of their grant allocation amount and program requirements, the localities require time to implement the new programs. This results in fewer expenses during the first state fiscal year of award availability than in the following years. Unanticipated increases in existing federal awards have a similar impact on state and local governments. When unanticipated additional funds become available, localities require time to develop new or adapt existing programs that comply with grant conditions before requesting additional program funds.

#### Direct Aid to Public Education

As illustrated in Table 2, the majority of the Department's expenses are transfer payments, which are comprised mostly of direct aid. The largest contractual provider to the Department, Harcourt Brace, administers, grades, and evaluates Standards of Learning tests and other tests added with the implementation of the No Child Left Behind Act. Harcourt Brace received approximately \$25.2 million during fiscal year 2004.

Table 2

Direct Aid to Public Education and Central Office Operations Expenses by Type

		<u>Percent</u>
Personal services	\$ 21,348,505	0.44
Contractual services	71,871,225	1.47
Supplies and materials	633,887	0.01
Transfer payments	4,799,858,439	98.02
Continuous charges	1,409,075	0.03
Equipment	<u>1,476,621</u>	<u>0.03</u>
Total	<u>\$4,896,597,752</u>	<u>100.00</u>

Table 3

Direct Aid to Public Education Expenses by Program

		<u>Percent</u>
Standards of Quality	\$2,877,294,768	60.00
Special state revenue sharing	993,686,756	21.00
Categorical aid	535,415,260	11.00
Public school employee benefits	189,530,057	4.00
Other	<u>223,509,534</u>	<u>5.00</u>
Total	<u>\$4,819,436,375</u>	<u>100.00</u>

The Standards of Quality set minimum standards for programs and services each local school board should provide. The Department allocates funds to each locality based on information gathered from local school divisions following the provisions of the Appropriations Act and federal grant agreements. In addition to providing funds to localities, the Department also transfers federal assistance to other state agencies that administer educational programs.

The Department calculates most state entitlement payments based on the average daily membership for each school division and the total departmental appropriation. At the beginning of the fiscal year, the Department calculates 24 equal installment payments to each school division. After each school division reports its actual average daily membership as of March 31, the Department adjusts the remaining installment payments to reflect each school division's actual average daily membership. Table 4 shows expenditures in direct aid over the last five years. In 2004, total direct aid increased nearly \$179 million due to increases in student enrollment and per-pupil costs.

Table 4

Costs Pupil for Fiscal Years 2000-2004

	<u>FY 2000</u>	<u>FY 2001</u>	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>
Direct Aid to Localities expenses *	\$4,065,104	\$4,366,265	\$4,457,357	\$4,640,504	\$4,819,436
Total students **	1,124,547	1,134,218	1,155,430	1,155,430	1,163,262
Per pupil expenses ***	\$3,615	\$3,850	\$3,858	\$4,016	\$4,143
Total teachers	85,817	89,872	89,831	90,205	92,927

\* Dollars in thousands

\*\* Fiscal year end average daily membership

\*\*\* Direct Aid to Localities expenditures divided by total students

**DEPARTMENT HIGHLIGHTS**The No Child Left Behind Act of 2001

The No Child Left Behind Act of 2001 (Act) is a federal program intended to help close the achievement gap between disadvantaged and minority students and their peers, and to hold schools accountable for results. It includes:

- performance-based testing of all public school students;
- sanctions for schools that fail to make adequate yearly progress toward pass rates that increase yearly through the 2013-2014 school year;
- public access to schools' test results reported by grade, subject, and student subgroup; and
- expanded options for students to transfer out of failing or dangerous schools to better schools within the same district.

The Act requires that states create and administer annual assessment tests in reading and math in grades three through eight. States must disaggregate test results data for students by poverty levels, race, ethnicities, disabilities, and limited English proficiency. The Act prescribes up to 37 performance targets and each school must meet some or all of those targets. Schools must meet further standards for being safe and drug free. Divisions and schools that do not make sufficient yearly progress toward state proficiency goals will first receive assistance, then be subject to corrective action and ultimately, restructuring. Schools that meet or exceed objectives will be eligible for academic achievement awards.

In May 2003, the Department submitted the Virginia Consolidated State Application Accountability Plan to the U.S. Department of Education, which prescribes how Virginia will implement the requirements. The Act requires performance-based testing by subject and grade range, but does not mandate their precise content. Since Virginia has already implemented performance-based testing in its Standards of Learning program before the Act's passage, it is able to use those tests to partially satisfy the Act's requirements.

To meet the additional data collection, analysis, and reporting requirements of the Act, the Department is developing the Education Information Management System (EIMS). The Commonwealth's Information Technology Investment Board recommended EIMS for funding and identified it as a priority system in their September 1, 2003, report to the Governor and General Assembly. At that point, the Department had spent nearly \$1 million to develop the system requirements and prepare a Request for Proposal. During the fiscal 2004 Legislative session, the Department received General Fund appropriations

totaling about \$14 million in the 2005-2006 biennium to pay for EIMS, which is planned for completion by June 2006.

In fiscal 2004, the Department entered into a contract with Pearson Education Measurement to develop EIMS. As of October 2004, 32 school divisions have piloted EIMS.

The Act's provisions may present new risks for school divisions. For example, parents with children in schools that fail to meet state standards for at least two consecutive years, or children who are victims of violent crime or who attend schools that are persistently dangerous may transfer their children to a better-performing public school, including a public charter school, within their district. Students from low-income families in schools that fail to meet state standards for at least three years are eligible to receive supplemental educational services including tutoring, after-school services, and summer school. These actions may result in additional costs for localities and school divisions. At this early stage of implementing the Act, the Commonwealth cannot determine the effect of these variables.

### Standards of Learning

The Board of Education establishes the Standards of Learning and adopted revisions during fiscal year 2001. The standards are the minimum requirements for student in the following subjects: English; mathematics; science; history/social science; computer/technology; visual and performing arts; foreign language; health; physical education; and driver education. The standards set targets and expectations for both teachers and students. The Board also approved a review schedule for all Standards of Learning in each subject area at least once every seven years.

### Governor's Schools

The Virginia Governor's School program is a state and local supported program that includes summer residential, summer regional, and academic-year programs serving more the 7,500 gifted students. The program presently offers 16 academic-year Governor's Schools; 7 summer residential Governor's Schools; and 20 summer regional Governor's Schools. The academic-year Governor's Schools provide subjects including arts, government and international studies, global economies and technology, mathematics, science, and technology. The summer residential Governor's Schools provide gifted high school juniors and senior educational experience in visual and performing arts, humanities, mathematics, science, technology, medicine, life science, engineering, and marine science. The summer regional Governor's Schools that serve gifted elementary and middle school students provide educational experience in arts, science, and humanities. In fiscal 2004, the Department spent \$8,668,285 on the Governor's Schools program.

### Charter Schools

Charter Schools are public, nonsectarian, nonreligious, or nonhome-based alternative schools located within a public school division. A charter school may be a new public school or the conversion of all or part of an existing public school. Any person, group, or organization may submit an application to develop a charter school to the local school board in school divisions that have adopted resolutions to accept such applications. Charter schools may receive state and federal funding and are subject to the requirements of the Standards of Quality, including the Standards of Learning and the Standards of Accreditation. There are presently five public charter schools in Virginia and enrollment is open to all students within the relevant school division on a space-available basis. In fiscal 2004, the Department spent \$978,072 on the Charter Schools program.

**VIRGINIA SCHOOLS AND FOUNDATION FOR THE DEAF AND BLIND**

The Virginia School for the Deaf and Blind in Staunton (School in Staunton) and the Virginia School for the Deaf, Blind, and Multi-Disabled in Hampton (School in Hampton) provide comprehensive instructional programs and services to children with serious auditory and visual impairments and multiple disabilities that local school divisions cannot serve.

As illustrated in Table 4, fiscal year 2004 operating expenses for the Schools for the Deaf and Blind totaled \$13.9 million including \$10.6 million in personal services. The Schools also had capital expenditures of \$1,106,730 during fiscal year 2004. This includes approximately \$954,000 at the School in Staunton to provide boiler replacement, sprinklers and fire alarms, and handicapped access; and approximately \$70,000 at the School in Hampton for air-conditioning replacement.

Table 4

	<u>Operating Expenses by Type</u>			
	<u>Staunton</u>	<u>Hampton</u>	<u>Total</u>	<u>Percent</u>
Personal services	\$5,797,109	\$4,845,055	\$10,642,164	76.5
Contractual services	493,171	658,671	1,151,842	8.3
Supplies and materials	445,196	489,112	934,308	6.7
Continuous charges	641,695	316,630	958,325	6.9
Equipment	188,966	15,379	204,345	1.5
Other	<u>6,175</u>	<u>11,808</u>	<u>17,983</u>	<u>0.1</u>
Total	<u>\$7,572,312</u>	<u>\$6,336,655</u>	<u>\$13,908,967</u>	<u>100.0</u>

Source: Commonwealth Accounting and Reporting System

The School in Staunton serves 136 students including 106 residential students. During fiscal year 2004, the school experienced an increase in operating expenses when their steam provider discontinued service and the school contracted with a temporary boiler provider to obtain heat and hot water. The increase in expenses and the decrease in student population resulted in a per pupil expense of \$55,679 for fiscal year 2004.

The School in Hampton serves 83 students including 47 residential students. The school experienced a slight decrease in expenses and student population from fiscal year 2003, resulting in a per pupil cost of \$76,345.

Table 5

	<u>Cost Per Pupil for Fiscal Years 2003 and 2004</u>			
	<u>Staunton</u>		<u>Hampton</u>	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Operating expenses	\$7,572,312	\$6,942,108	\$6,336,655	\$6,568,747
Total students	136	155	83	85
Per pupil expenses	\$ 55,679	\$ 44,788	\$ 76,345	\$ 77,279

The Virginia Schools for the Deaf and Blind Foundation, Incorporated, supports and aids the Schools in the existing and future enterprises involving the Schools. The Foundation administers gifts, grants, bequests, and devices consistent with their terms and for the benefit of the Schools for the Deaf and Blind. The State Board of Education approves the Foundation's budget and acts as its governing board. The Assistant Superintendent of Finance serves as the Secretary/Treasurer of the Foundation, oversees the actions of the Foundation investor, and reports financial activities to the Board of Education. Annually, the Schools receive income from the Foundation's investments, which they must spend in accordance with a plan submitted to the Foundation's board. At December 31, 2003, the Foundation's investment portfolio was worth \$2,539,262, having earned \$44,764 during calendar year 2003. The Board approved calendar year 2003 disbursements to the School in Staunton of \$31,568 to the School in Hampton of \$31,910.



# Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts  
P.O. Box 1295  
Richmond, Virginia 23218

January 14, 2005

The Honorable Mark R. Warner  
Governor of Virginia  
State Capitol  
Richmond, Virginia

The Honorable Lacey E. Putney  
Chairman, Joint Legislative Audit  
and Review Commission  
General Assembly Building  
Richmond, Virginia

## INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Department of Education including the Direct Aid to Public Education, the Virginia School for the Deaf and Blind in Staunton, and the Virginia School for the Deaf, Blind, and Multi-Disabled in Hampton** for the year ended June 30, 2004. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

### Audit Objectives, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System and in the Department's accounting records, review the adequacy of the Department's internal control, and test compliance with applicable laws and regulations.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Department's operations. We also tested transactions and performed such other auditing procedures, as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

- Expenditures
- Revenues
- Federal grant management

We obtained an understanding of the relevant internal control components sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. We performed audit tests to determine whether the Department's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations.

The Department's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

Our audit was more limited than would be necessary to provide an opinion on internal control on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

#### Audit Conclusions

We found that the Department properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and in the Department's accounting records. The Department records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted no matters involving internal control and its operation that we consider to be material weaknesses. Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to financial operations may occur and not be detected promptly by employees in the normal course of performing their duties.

The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

#### EXIT CONFERENCE

We discussed this report with management at an exit conference held on February 14, 2005.

AUDITOR OF PUBLIC ACCOUNTS

JP/kva  
kva:

DEPARTMENT OF EDUCATION

BOARD MEMBERS  
As of June 30, 2004

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President

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Vice President

Iris Castro  
Scott Goodman  
David L. Johnson  
Thomas G. Johnson, Jr.

Gary L. Jones  
Ruby Rogers  
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