

OFFICE OF THE BOARD OF EDUCATION

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**OAKLAND UNIFIED
 SCHOOL DISTRICT**

Community Schools, Thriving Students

BOARD OF EDUCATION 2013

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June 19, 2013

The Honorable John Chiang
 California State Controller
 P.O. Box 942850
 Sacramento, California 94250-5872

The Honorable Tom Torlakson
 State Superintendent of Public Instruction
 1430 N Street
 Sacramento, CA 95814-5901

Dear Superintendent Torlakson and Controller Chiang:

The purpose of this letter is to advise you that the Oakland Unified School District (the "District") Board of Education directed the Staff to issue a Request for Proposal ("RFP") for auditing services for the District for fiscal years 2011-12 and 2012-13. The RFP required that 1) the firms submitting proposals specialize in Annual Audits of school districts, 2) the audits conform to the State Controller's Office Standards and Procedures for Audits of California K-12 Local Educational Agencies, and 3) the audit firm selected by the District be from the SCO approved list.

The District's Board made this decision because there has not been a full financial audit of the District in ten years. As you know, under S.B. 39, the State Controller's Office is required to conduct the annual financial audits of the District until such time as the State Superintendent determines that the District is financially solvent. However, since the SCO completed the first audit of the District under S.B. 39 in November 2005 (the Fiscal Year 2003-04 audit), the SCO has stated it cannot express an opinion on the District's financial statements or accompanying schedule of revenues and expenditures. Again in the 2010-11 Audit, issued by the SCO on May 17, 2013, the SCO stated it is unable to express an opinion on the District's financial statements. District staff was told by the SCO Staff that even if 100 per cent of the District's revenues were audited, SCO would not express an opinion as to whether the District's financial statements are fairly presented and in conformity with generally accepted accounting principles. The Board believes under these circumstances, it is imperative that the District obtain an independent and objective assessment of the District's financial health and internal controls.

The District staff has shared with your staffs the consequence for the District of the lack of current audits. Because the District has no current financial audit, the securities rating agencies have withdrawn their rating of the District (i.e., the District currently has no credit

rating). Many large investment funds cannot invest in the District's bonds without audits or ratings. One major investment bank, JP Morgan, resigned its appointment to serve as the District's underwriter because it could not meet its regulatory responsibilities selling bonds without a current audit.

Fewer investors means there is less demand for the District's bonds, and the investors who are willing to purchase the District's bonds can charge higher interest rates.

This additional cost to the taxpayers of Oakland due to the District's selling general obligation bonds without ratings is quantifiable. The District sold \$31 million of non-rated bonds in March 2012. The interest rates were, on a weighted average basis, 1.4% higher than an "A" rated bond. The 1.4% over the repayment of the bonds is an additional \$6 million that Oakland taxpayers have to pay because the District's bonds are non-rated (because there has not been a financial audit).

The District requests that the SCO agree that the audits contracted for under the RFP be accepted by the SCO in lieu of the audit under S.B. 39. As you know, S.B. 39 also provides that "[a]t the discretion of the Controller, the audit may be conducted by the Controller, his or her designee **or an auditor selected by the county superintendent and approved by the Controller.**" The District is currently working with Alameda County Superintendent Jordan to obtain her concurrence to enter into a contract with Vavrinek, Trine, Day & Co., LLP to perform the 2011-12 and 2012-13 audits.

If the SCO does not agree to accept such audits, the District will contract for auditing services as provided in the RFP in order that 1) the Board may obtain current, independent assessment of the District's, and 2) the District can meet its obligations to investors in our general obligation bonds and the voters of Oakland who gave overwhelming approval to the District's bond measure on the November 2012 ballot (85% approval by the voters of Oakland). In the meantime, the Board, the District's State Trustee and District Staff will continue to work with your Staffs to respond to continuing questions.

I look forward to your response. Please let me know if you have any questions.

Very truly yours,

David Kakishiba
President

cc: Bill Ashby, Chief Operating Officer, SCO
Carol Baez, Chief, Financial Audits Bureau, SCO
Peter Foggiato, CDE
Arlene Matsuura, CDE
Jeannie Oropeza, CDE
Superintendent Sheila Jordan, Alameda County Superintendent

Delivery to ccs: by email



September 27, 2013

Via E-Mail

Mr. George Lolas, Acting Chief Operating Officer
State Controller's Office

Mr. Jeff Brownfield, CPA, Chief Division of Audits
State Controller's Office

Ms. Carolyn Baez, Financial Audits Bureau
State Controller's Office

Mr. David Supan, Audit Manager
State Controller's Office

Re: OUSD Response to SCO Letter of September 5, 2013 – Letter of Engagement for 2011-12 Audit

Dear Mr. Lolas, Mr. Brownfield, Ms. Baez and Mr. Supan:

On behalf of the District, I am responding to your letter of September 5, 2013, which as per my email of September 13, 2013, the District did not receive until September 12th when it was forwarded to us by County Superintendent Jordan.

Initially, we appreciate the State Controller's Office commitment to proceed expeditiously with the 2011-12 audit. This is also the District's goal. However, a number of issues need to be addressed before the District can move forward. We will outline them below:

- 1) As you are aware, VTD will be converting the District's SACS files and preparing the unaudited financial statements for 2011-12. The District has provided the SACS files for 2011-12 to VTD. However, Lennie Danna, our assigned Partner has not been available to commence preparation of the unaudited financials. We understand that VTD is available to commence preparation of the financials the week of October 7th. However, as we discussed in our last meeting with SCO, the ability to prepare the financials is dependent on the resolution of some of the open issues noted below, including accounting for capital assets.
- 2) At various meetings with the SCO during the summer of 2013, both the SCO and the District agreed that in order for the 2011-12 audit to proceed successfully, better communications is needed, we need an agreed upon timeframe and workplan and that there are several critical issues that need to be resolved. These issues include: (a) accounting for capital assets, (b) use of bond proceeds, (c) the additional documentation SCO auditors represent they need to accept

the write off of stale accounts payables, and (d) the documentation SCO needs to "get comfortable" with the 2011-12 beginning balance (or the 2010-11 ending balance). Most recently, in a meeting of July 10, 2013, Bill Ashby requested that the District create a list of the issues that needed to be discussed and resolved prior to commencing the 2011-12 audit. The District provided this information to SCO on August 3 and again on September 11. (See, Attachment 1 for the complete list).

At the June 19, 2013 presentation of the 2010-11 Audit to a joint meeting of the District's Board of Education and Audit Committee, Carolyn stated to the Board, in response to a question,

Carolyn Baez: "Well first let me say since we've issued the report, our office has had communications meeting with District staff to again, let's move forward, what can we do in the future to hopefully achieve, give you an opinion, possibly a qualified opinion, but, so we plan to work with them exactly this is what we need from you and have a timeline. And our goal is to issue an opinion with the next audit." [Videotape of Board meeting at 36:23-27:36]

Given the difficulty the District and SCO have experienced in completing timely audits, the District's governing board has instructed staff to have an agreed communications' protocol, workplan and timeframe for completion of the 2011-12 audit prior to board approval of the engagement agreement for the 2011-12 audit. District staff is available to meet with SCO to begin work on these items; the District would ask VTD to participate in these meetings. We are aware that the engagement agreement will not include the communications' protocol, workplan or timeframe. The District has proposed previously in a meeting with Bill Ashby, Carolyn Baez and others from SCO, that a side letter be used to memorialize the agreements related to communications, the workplan and timeframe for the audit. However, to begin the audit without these critical agreements in place will decrease the likelihood of us achieving the agreed stated outcome – SCO being able to render an opinion on the District's financials.

- 3) As you are aware, the District issued an RFP for auditing services. Three auditing firms submitted proposals. I am attaching as Attachment 2, the schedule of professional fees submitted by all three firms. The fees for a full annual audit for 2011-12, including compliance, submitted by the three firms were as follows:

VTD	\$249,000
Vicenti, Lloyd Stutzman	\$222,250
Christy White	\$153,925

The District's Board has directed Staff to discuss with SCO the basis for the \$400,000 fee and to obtain an explanation as to why the SCO's fee is 60% higher than VTD.

- 4) As per my email of September 13, 2013, and as you are aware, the engagement agreement must be approved by the District's governing board. The Board has informed staff that it will not calendar the agreement with SCO for the 2011-12 audit until such time as staff can report that there is some understanding or at least corroborative discussion about items 2 and 3

September 27, 2013

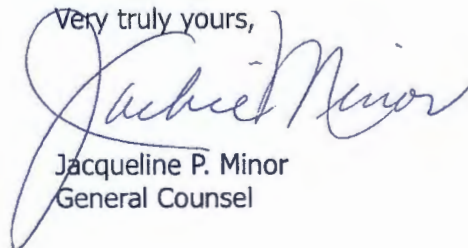
Page 3

above. The District's Board meets on the second and fourth Wednesdays of each month. The Board has informed me it is willing to consider a fair agreement that will in fact increase the likelihood of a successful outcome, which is SCO being able to render an opinion on the District's financials.

- 5) Finally, I am attaching as Attachment 3, the report and presentation to the District's Board on September 25, 2013 on the successful sale of \$120,000,000 of the District's general obligation bonds approved by the Oakland voters in November 2012. The report was prepared and presented to the Board at a public meeting by the District's financial advisor, KNN and the lead underwriter, Siebert Brandford Shank. You will note on page 10, that the additional cost to Oakland property owners from the sale of these bonds, because the District's bonds are non-rated, due to the lack of a financial audit, is \$23.1 million dollars.

Deputy Superintendent Hal is available to arrange a meeting and discussion with SCO at any time to move this forward. We look forward to continuing to work with SCO to achieve our mutually stated goal -- SCO being able to render an opinion on the District's financials.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Jacqueline P. Minor". The signature is written in black ink and is positioned above the printed name and title.

Jacqueline P. Minor
General Counsel

Cc: David Kakishiba, Board of Education, President
Dr. Gary Yee, Superintendent
Vernon Hal, Deputy Superintendent
Carlene Naylor, State Trustee



September 27, 2013

Via E-Mail

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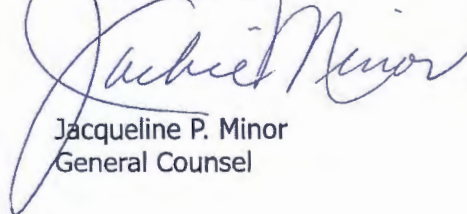
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Very truly yours,



Jacqueline P. Minor
General Counsel

Cc: David Kakishiba, Board of Education, President
Dr. Gary Yee, Superintendent
Vernon Hal, Deputy Superintendent
Carlene Naylor, State Trustee

AUDIT PLAN USING SCO & VTD

	Prepare Financial Statement	Audit State & Federal Compliance	Financial Audit
SCO	VTD	SCO	SCO
VTD	-	-	VTD

Legend:

- SCO – State Controller’s Office
- VTD - Vavrinek, Trine, Day and Company

SCO Audit - 2010-11 Findings (Summary)

Finding Information		OUSD Response		Financial Impact		Internal Controls		Finding Rectified?		
Section	# of Findings	Agree	Disagree	Questioned Cost	Reimburse Amount	No Procedure In Place	Procedure In Place/ Not Followed	YES	NO	WIP
Financial	16	9	7	\$ 12,019,586	\$ 135,530	2	3	4	-	3
Federal	14	14	-	\$ 3,952,200	\$ 765	7	7	11	-	3
State	14	13	1	\$ 10,866,092	\$ 3,635,201	3	9	8	-	6
Totals	44	36	8	\$ 26,837,878	\$ 3,771,496	12	19	23	-	12
WIP = Work In Progress										

SCO Audit - 2010-11 Findings (FINANCIAL)

Finding Information		OUSD Response		Financial Impact		Internal Controls		Finding Rectified?			Status/Comments
Finding #	Finding	Agree	Disagree	Questioned Cost	Reimburse Amount	No Procedure In Place	Procedure In Place/ Not Followed	YES	NO	WIP	
1	FC11-01	Going Concern Issues		1							
2	FC11-02	Bond Proceeds Inappropriately Transferred		1	\$ 2,093,782						
3	FC11-03	Bond Expended for Unallowable Activity		1	\$ 9,925,804						
4	FC11-04 ⁽¹⁾	Capital Assets Deficiencies	1			1				1	The District has engaged a third-party vendor to inventory capital assets. For the year beginning July 1, 2013, the Board has approved staff's request to add a Fixed Asset Management position. Recruiting for this position will begin June 2013. The District will continue to monitor staff's understanding and compliance with established capitalization policies and procedures and federal record keeping requirements. Currently working with a third party vendor to install Fixed Asset Module
5	FC11-05 ⁽¹⁾	Capital Assets Not Properly Recorded or Reported		1							The District has engaged a third-party vendor to inventory capital assets. For the year beginning July 1, 2013, the Board has approved staff's request to add a Fixed Asset Management position. Recruiting for this position will begin June 2013. The District will continue to monitor staff's understanding and compliance with established capitalization policies and procedures and federal recordkeeping requirements. The District will examine its understanding of generally accepted accounting principles. Currently working with a third party vendor to install Fixed Asset Module
6	FC11-06 ⁽¹⁾	Depreciation expense not allocated to correct function		1							For the year beginning July 1, 2013, the Board has approved staff's request to add a Fixed Asset Management position. Recruiting for this position will begin June 2013. The District will remind staff of the importance of allocating depreciation expense in a timely manner.
7	FC11-07	Associated student body and subsidiary funds not presented and not audited	1								
8	FC11-08	Revenue, receivables, deferred revenue, expenditures, and beginning fund balance not properly recorded or reported	1				1	1			
9	FC11-09	Accounts payable understated	1				1			1	
10	FC11-10	Beginning fund balance not audited	1							1	
11	FC11-11	Payroll - Inadequate internal controls	1				1				
12	FC11-12	Stale-dated warrants inappropriately recorded	1		\$ 135,530	1		1			The District has reviewed its practice and all stale-dated warrants. The practice has been changes as of June 30, 2013 and all transactions will be recorded in accordance with generally accepted accounting principles and in accordance with applicable laws and regulations. The District is currently reviewing the Stale Dated check log to ensure compliance with laws and regulations.
13	FC11-13	Inadequate controls over cash reconciliation process		1							
14	FC11-14 ⁽¹⁾	Due from grantor governments - Amount inappropriately reported as accounts receivable	1					1			
15	FC11-15	Outstanding obligations in warrant pass-through fund not adequate identified		1							
16	FC11-16 ⁽¹⁾	Inadequate disclosure of restructured related-party loan to Chabot Space and Science Center	1					1			
Totals:			9	7	\$ 12,019,586	\$ 135,530	2	3	4	-	3

WIP = Work In Progress

(1) Financial Statement Presentation/Concern will be Resolved When Audit is Performed By Outside Firm

SCO Audit - 2010-11 Findings (FEDERAL)

Finding Information		OUSD Response		Financial Impact		Internal Controls		Finding Rectified			Status/Comments		
Finding #	Finding	Repeat Findings?	07-08 Ref. No.	Agree	Disagree	Questioned Cost	Reimburse Amount	No Procedure In Place	Procedure In Place/ Not Followed	YES		NO	WIP
1	FC11-17	Inadequate Support for Salaries and Wages (Federal Time Accounting)	1	8-24	1	\$ 3,309,618			1			1	Procedures are uploaded into the tool, professional development to be provided during June 17 and 21 principal summer institute
2	FC11-18	Noncompliance with procurement and suspension and debarment requirements	1	8-9	1			1		1			Desktop procedures, including website for debarred vendor verification, have been developed and implemented for sites and Procurement and Distribution Services to verify eligible vendors prior to inclusion in the OUSD vendor database. Verification of vendors is also done for existing vendors on an annual bases at the start of the fiscal year
3	FC11-19	Inadequate controls over equipment and real property management	1	8-12	1			1				1	District conducted a full inventory of all equipment and real property during 2012-2013 which includes assigning a unique asset ID tag and number to all equipment valued at \$500 or greater. This also includes indicating funding source at point of receipt.
4	FC11-20	Inadequate internal controls over allowability of costs of federal awards	1	8-13	1			1		1			
5	FC11-21	Noncompliance with Sub-recipient Monitoring Requirements	1	8-11	1	\$ 332,511		1		1			District implemented SCO's recommendations
6	FC11-22	Title I, NCLB, Part A, Basic Grant Program; Title II, Improving Teacher Quality—Private School Funding and Services Requirements Not Met	1	8-16	1	\$ 243,972			1	1			Procedures have been re-written to meet the user friendly, easy to follow business & operation principles, procedures are provided in multiple ways to include a private school informational meeting, consultations, and emails
7	FC11-23	Title I, NCLB, Part A, Basic Grant Program – Schoolwide Plan Deficiencies	1	8-15	1	\$ 66,099			1	1			Procedures and requirements have been re-written to meet the business & ops principles and in addition a CSSSP toolkit has been developed to include such procedures and requirements
8	FC11-24	Title I, NCLB, Part A, Basic Grant Program – Noncompliance with Highly-Qualified Teacher Requirements	1	8-17	1				1	1			Procedures, requirements, and timeline have previously been developed and the HQT Committee meets annually to review timeline and process to include HR, State & Federal, and IT departments
9	FC11-25	Title I, NCLB, Part A, Basic Grant Program – Comparability Requirements Not Met	1	8-16	1			1		1			Procedures, requirements, and timeline have been developed and institutional memory has been created by placing a copy in shared drive
10	FC11-26	Interest earned on federal funds not calculated or remitted	1	8-10	1		\$ 1,801	1		1			
11	FC11-27	Child Care and Development Program-Eligibility records not provided	1	8-23	1				1	1			
12	FC11-28	National School Lunch Program – Reimbursement claim discrepancies	1	7-20 (06-07 Audit)	1		\$ (1,036)		1	1			Email form SCO stated: Finding incorrectly reported this as an understatement of \$1,036; it should have been reported as an overstatement of \$1,036. (OUSD identified it as an understatement as per the finding)
13	FC11-29	National School Lunch Program – Noncompliance with eligibility requirements	1	8-14	1			1		1			Written procedures have been developed to avoid the mis-interpretation of meal application processes as it relates to income standards. This will ensure that meal applications are properly processed.
14	FC11-30	Special Education Program – Individualized Education Plan (IEP) deficiencies	1	8-21	1				1			1	
Totals:			14		14	-	\$ 3,952,200	\$ 765	7	7	11	0	3

WIP = Work In Progress

SCO Audit - 2010-11 Findings (STATE)

Finding Information			OUSD Response		Financial Impact		Internal Controls		Finding Rectified?			Status/Comments
Finding #	Finding	Agree	Disagree	Questioned Cost	Reimburse Amount	No Procedure In Place	Procedure In Place/ Not Followed	YES	NO	WIP		
1	SC 11-31	Attendance report variances	1			\$ 1,309	1		1			
2	SC 11-32	Attendance improperly reported by district	1			\$ 262		1	1			
3	SC 11-33	Attendance records not retained	1			\$ 835,298		1			1	
4	SC 11-34	Kindergarten continuance forms not signed, or not signed in a timely manner	1			\$ 3,194		1	1			Kindergarten continuance forms not signed, or not signed in timely manner. The District has provided training to the Accounting staff that will monitor the collection of forms and review the forms adequate and timely parental authorization.
5	SC 11-35	Independent Study Program Requirements reconciliation errors	1			\$ (262)	1				1	A procedure is being put in place for 2013-14 FY that will detach changes in attendance reporting at the school site level.
6	SC 11-36	Independent study Program Requirements compliance deficiencies	1			\$ 15,290		1			1	Improved procedures and processes are being developed for not only schools identified as Independent Study but also for regular schools that provide short term independent study
7	SC 11-37	Continuation education attendance recording, reporting, and internal control deficiencies	1				1				1	District continues to provide training to school site staff
8	SC 11-38	Instructional time program deficiencies	1					1	1			Procedures, requirements, and timeline have been developed and provided to all administrators in a memo format, in addition professional development workshops were provided in 12-13 and will continue into 13-14
9	SC 11-39	Deficiencies in compliance with instructional materials program requirements	1			\$ 2,147,698		1	1			
10	SC 11-40	Inaccurate calculation of administrator-to-teacher ratio		1		\$ 608,850					1	OUSD will establish processes and procedures. HR, Legal and Fiscal will take the lead.
11	SC 11-41	Minimum percentage requirement for classroom teacher salary not met (55%)	1		\$ 10,866,092						1	OUSD will establish processes and procedures. HR, Legal and Fiscal will take the lead. Waiver sent to ACOE on 9-26-13.
12	SC 11-42	School Accountability Report Card (SARC) Reporting Inaccuracies	1					1	1			
13	SC 11-43	Deficiencies in Class Size Reduction (CSR) Reports	1			\$ 23,562		1	1			
14	SC 11-44	After School Education and Safety program deficiencies; scope limitation in testing	1					1	1			The findings will be shared with after school partners implementing the grant program, including the programs included in the audit sample. Training will continue to be provided to all after school sites at our annual August Institute training on proper procedures and internal controls for attendance taking and record-keeping, and will monitor program sites at the beginning of the 2013-14 school year to ensure that proper procedures are followed for sign in/sign out, early release, and record-keeping. We are currently reviewing 2013-14 after school program plans to ensure that program schedules are compliant.

Totals: 13 1 \$ 10,866,092 \$ 3,635,201 3 9 8 - 6

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