



**UNITED STATES DEPARTMENT OF EDUCATION**  
OFFICE OF INSPECTOR GENERAL

AUDIT SERVICES  
Chicago/Kansas City/Dallas Audit Region

June 30, 2009

**Control Number**  
**ED-OIG/A06H0017**

Mr. Robert Scott  
Commissioner of Education  
Texas Education Agency  
1701 N. Congress Avenue  
Austin, TX 78701

Dear Mr. Scott:

This **Final Audit Report**, Control Number ED-OIG/A06H0017, entitled *Adequacy of Houston Independent School District's Fiscal Controls over Accounting for and Using Federal Funds*, presents the results of our audit. The objective of the audit was to determine whether Houston Independent School District (HISD) had adequate fiscal controls over accounting for and using Federal funds. Our audit covered HISD's system of internal control as of June 30, 2006, and Federal funds expended for the period July 1, 2005, through June 30, 2006 (school year 2005-2006). We also reviewed HISD's purchase card (P-card) charges from August 2006 through June 2007.

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## BACKGROUND

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HISD is the seventh largest local educational agency (LEA) in the country and the largest in the State of Texas, with an enrollment of 209,879 students (as of school year 2005-2006) in 308 schools. Demographically, the HISD student body was 58 percent Hispanic, 30 percent African American, 9 percent Caucasian, 3 percent Asian, and less than 1 percent Native American. About 82 percent of the students were economically disadvantaged. HISD received Federal grants through 41 Department programs during school year 2005-2006. The four largest Federal programs were (1) Title I, Part A—Improving Basic Programs; (2) Individuals with Disabilities Education Act (IDEA)—Part B; (3) Temporary Emergency Impact Aid for Displaced Students; and (4) Title II, Part A—Improving Teacher Quality.

The Title I, Part A program provides financial assistance through state educational agencies to LEAs and public schools with high numbers or high percentages of economically disadvantaged children. The purpose of the funding is to provide additional academic support and learning opportunities to help all children meet state academic content and student academic achievement standards. The IDEA, Part B, program provides assistance for special education and related services to children with disabilities. The Temporary Emergency Impact Aid for Displaced Students program was a one-time only emergency grant for school year 2005-2006. The program provided funding to state educational agencies to cover the cost of educating students

who were displaced by Hurricanes Katrina and Rita. The Title II, Part A, program provides assistance to improve the quality and number of teachers and principals.

Use of Federal funds is governed by the relevant law and program regulations, the Education Department General Administrative Regulations, the requirements described in Office of Management and Budget (OMB) Circular A-87, and the requirements set forth by the Texas Education Agency (TEA).<sup>1</sup> Funds for all Federal programs are requested through a budget, which must be approved by TEA. During school year 2005-2006, HISD expended the following Federal funds:

<b>Program</b>	<b>Amount</b>
Title I, Part A	\$93,231,872
IDEA, Part B	\$33,693,488
Temporary Emergency Impact Aid for Displaced Students	\$32,994,734
Title II, Part A	\$13,255,801
Other	\$49,632,031
<b>Total</b>	<b>\$222,807,926</b>

During school year 2005-2006 and from August 2006 through June 2007, HISD used P-cards to expend over \$21 million of Federal funds. HISD's Procurement Manager stated that HISD typically has over 900 P-card holders at any one time. HISD encourages its P-card holders to use the P-cards for small charges (less than \$500) because it allows school and other district staff to purchase needed items immediately rather than through the normal requisition process.

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## AUDIT RESULTS

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As of June 30, 2006, HISD generally had an adequate system of fiscal controls over accounting for and using Federal funds. We identified the system of internal control over Federal programs at HISD through discussions with HISD staff and reviews of policies and procedures. We compared HISD's system to the Government Accountability Office's *Standards for Internal Control in the Federal Government*. The five standards for internal control are control environment, risk assessment, control activities, information and communication, and monitoring. We evaluated the control relevant to our audit objectives within these categories and concluded that they were adequate to provide reasonable, but not absolute, assurance that HISD would properly account for and use Federal funds.

However, during school year 2005-2006, HISD did not always use Federal funds in accordance with all applicable Federal and state requirements. Of the \$21.7 million in costs that we sampled, HISD charged three Federal programs with unallowable costs of \$62,772 and inadequately documented costs of \$82,712.<sup>2</sup> In addition, HISD's P-card use was not always in

<sup>1</sup> All OMB Circular A-87 citations refer to the 05/10/2004 revised version. All citations from TEA's *Federal Cost Principles Side By Side Matrix* refer to the 4/28/2006 updated version. All citations from TEA's schedule of instructions for the Consolidated Application for Federal funding refer to the 9/1/2005 version.

<sup>2</sup> See Attachment 1 for the Federal programs charged with the unallowable and inadequately documented costs described in this report.

accordance with Federal and state regulations and rules. Of the \$31,934 in P-Card costs that we sampled, HISD charged unallowable costs of \$2,064 and inadequately documented costs of \$4,731 to Federal programs.

We provided a draft of this report to TEA for review and comment on April 2, 2009. We received TEA's comments, along with additional documentation, on May 1, 2009. In its comments, TEA recognized the specific issues in the draft report and provided comments and additional documentation for some of the issues. After reviewing supplemental supporting documentation provided by HISD in response to the draft of this report, TEA concluded that \$70,094 in costs was still unallowable or inadequately documented and only a portion of the payroll for employees who worked on multiple activities would be allowable.

We made changes to our finding and the recommendations in response to TEA's comments and to reflect our review of the additional documentation. We concluded that \$152,279 was still unallowable or inadequately documented. Questioned costs, except for payroll, are shown by grant in Attachment 1. TEA's comments are summarized at the end of the findings. Except for personally identifiable information protected under the Privacy Act of 1974 (5 U.S.C. § 552a), the entire narrative of TEA's comments is included as Attachment 2 to this report. Because of the voluminous nature of the additional documentation TEA provided with its comments, we have not included them in the Attachment. Copies of the additional documentation, less any personally identifiable information, are available on request.

#### **FINDING NO. 1 – HISD Charged Federal Programs \$145,484 in Unallowable and Inadequately Documented Costs**

During school year 2005-2006, HISD did not always use Federal funds in compliance with the law, regulations, and state requirements. We reviewed over \$21.7 million of HISD's \$222.8 million in Federal expenditures and found that Federal expenditures were not always allowable or adequately documented. We determined that \$145,484 of the \$21.7 million reviewed were either in violation of Federal, state, or district guidelines (\$62,772) or lacked documentation adequate to substantiate the expenditures (\$82,712).<sup>3</sup> The following table summarizes the results of our audit testing.

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<sup>3</sup> Our sample sizes were not sufficient to project their results to the transactions we did not test.

	Universe Size	Universe Dollar Amount	Sample Size	Sample Dollar Amount	Allowable	Unallowable	Inadequately Documented
<b>Payroll</b>	13,844	\$240,993,728 <sup>4</sup>	53	\$322,393 <sup>4</sup>	\$239,681	\$0	\$82,712
<b>Non-Payroll, Non-Title I Samples</b>							
Supplies	16,939	\$24,128,713	33	\$7,084,864	\$7,023,088	\$61,776	\$0
Other Operating	5,991	\$2,880,315	30	\$576,911	\$576,732	\$179	\$0
Capital Outlay	1,188	\$10,523,043	29	\$4,425,541	\$4,425,541	\$0	\$0
Contract Services	5,942	\$32,549,367	36	\$6,525,470	\$6,525,470	\$0	\$0
<b>Title I Samples</b>							
Supplies	22,846	\$13,743,844	29	\$380,577	\$380,577	\$0	\$0
Other Operating	5,158	\$1,686,921	32	\$98,219	\$98,219	\$0	\$0
Capital Outlay	500	\$2,950,915	32	\$837,107	\$836,290	\$817	\$0
Contract Services	3,011	\$7,582,625	31	\$1,542,190	\$1,542,190	\$0	\$0
<b>Negative Expenses</b>	3,482	-\$1,397,804	20	-\$56,917	-\$56,917	\$0	\$0
<b>Totals</b>	<b>78,901</b>	<b>\$335,641,667<sup>4</sup></b>	<b>325</b>	<b>\$21,736,355</b>	<b>\$21,590,871</b>	<b>\$62,772</b>	<b>\$82,712</b>

### HISD Used Federal Funds For Unallowable Expenditures

Contrary to OMB Circular A-87, HISD charged \$61,955 in food and travel expenses and \$817 in non-grant related expenses to Federal programs during school year 2005-2006. Unallowable costs charged to a Federal program constitute a debt to the Federal government and harm the Federal interest. When a grantee uses Federal funds for unallowable costs, those funds are not available to pay for items and services that will advance the program.

#### Food and Travel Expenditures

HISD charged \$61,776 in prohibited catered food and \$179 in duplicated travel expenditures to Federal programs. HISD conducted a 5-day training conference and charged the costs for catered breakfasts all 5 days and the cost for 1 ice cream social to the Title II, Part A Leadership Development program. Based on catering contracts, HISD provided breakfasts for 800 teachers each day and 1,000 servings of ice cream and beverages on 1 day. According to OMB Circular A-87, Attachment A, paragraph C.1.c., to be allowable under Federal awards, costs must be authorized or not prohibited under state or local laws or regulations. *TEA's Federal Cost Principles Side By Side Matrix* (TEA's matrix) allows for a light lunch during an all day meeting or training session when it is impractical for participants to obtain lunch on their own or a

<sup>4</sup> The universe of salaries included all salaries paid, regardless of the source of the funding; thus, the total universe in this table exceeds the \$222,807,926 HISD expended in Federal funds. Our sample of 53 employees included total salaries of \$2,563,249, of which \$322,393 was paid with Federal funds. One of the 53 employees in our sample was terminated and did not receive any salary in the months that we reviewed.

working lunch during an all day meeting or training session. However, TEA's matrix states that unallowable food includes refreshments of any kind, including beverages and snack foods for staff meetings, staff training, and breakfast.

In addition, HISD reimbursed an elementary school principal twice for a hotel expenditure of \$179. HISD charged the Fund for the Improvement of Education program for a hotel expenditure based on the hotel charge on the principal's credit card bill and then again based on the hotel invoice. OMB Circular A-87 allows travel costs for transportation and related items incurred by employees who are in travel status on official business of the governmental unit. However, paying for the same cost twice is not allowable.

#### Non-Grant Related Expenditures

HISD charged the Title I, Part A program \$817 for electrical work to install an LCD monitor in the school's lunchroom for use in the Title I professional Development program. However, the electrical work did not aid in the efficient performance of the Title I, Part A program. According to HISD, the electrical work was charged to the Title I, Part A program because the school was planning to use the LCD monitor in its teacher training. However, the LCD monitor was installed in a lunchroom where it can be used for purposes other than teacher training alone. Therefore, we do not consider the cost to be reasonable.

OMB Circular A-87, Attachment A, (C) provides that, to be allowable under Federal awards, costs must meet the general criteria of being necessary and reasonable for the proper and efficient performance and administration of the award.

#### **HISD Did Not Provide Adequate Documentation for All Expenditures of Federal Funds**

For school year 2005-2006, HISD did not always maintain adequate documentation to support \$82,712 of Federal payroll expenditures. Adequate documentation, such as purchase orders, invoices, cancelled checks, receiving reports, time sheets, and employee certifications, must be maintained to determine allowability of expenditures charged to Federal programs.

#### Inadequate Documentation of Federal Payroll Expenditures

HISD did not provide adequate documentation to support \$82,712 of Federal payroll expenditures. OMB Circular A-87, Attachment B, Section 8 (h), Support of Salaries and Wages states —

- (3) Where employees are expected to work solely on a single Federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification.
- (4) Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation.

For school year 2005-2006, HISD incurred \$241 million in payroll expenses for 13,844 employees.<sup>5</sup> We randomly selected 52 employees who were paid for the months of August 2005 and May 2006. Of the 52, 18 were full-time general fund employees who worked only part-time on federally funded activities during June 2006. Therefore, we expanded our review to include payroll for June 2006 for these 18 employees. For all 52 employees, we requested supporting documentation such as employment contracts, semi-annual certifications (certifications), and personnel activity reports (PARs.) Payroll supporting documentation that HISD presented consisted of employment contracts, certifications, PARs, as well as copies of computer print screens of leave and earning statements and payment screens. HISD provided adequate documentation for 14 of the 52 sample employees. Ten of the remaining 38 employees worked full-time on a Federal program and were required to provide certifications. However, TEA waived this Federal requirement for all LEAs in school year 2005-2006.<sup>6</sup>

HISD could not provide adequate documentation for 28 of the 52 (54 percent) employees that worked on multiple activities and should have been required to submit monthly PARs documenting how their time was spent. For 15 of the 28 employees, the required monthly PARs were not provided. HISD provided weekly sign in and out sheets for 8 employees. However, these sheets failed to identify the Federal program or the amount of time charged to the Federal program. HISD also provided annual PARs for 3 employees indicating the percentage of time the employees spent annually on each program instead of the required monthly accounting for time. For the remaining 2 employees, HISD provided PARs that supported only part of the payroll costs paid to the employees. HISD's Chief Financial Officer (CFO) stated that she was unaware of the requirement for certifications. The CFO agreed to start obtaining the certifications and the PARs.

## Recommendations

We recommend that the Assistant Secretary for Elementary and Secondary Education instruct TEA to require HISD to:

- 1.1 Refund to the Department \$62,772 of Federal funds expended for unallowable costs;
- 1.2 Refund to the Department \$82,712 in inadequately documented costs or provide adequate documentation to support that amount;
- 1.3 Provide reasonable assurance that, for the \$238,430,479 in payroll expenses not included in our sample, personnel activity reports exist for employees who worked on multiple activities to support the amounts charged to Federal programs; and
- 1.4 Provide additional training for all personnel involved with the administration of Federal programs.

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<sup>5</sup> Total dollar amount and number of employees includes all HISD payroll expenses for all HISD teaching staff, not just the Federal portion of payroll expenses for those working solely or part-time on Federal programs.

<sup>6</sup> Texas is a ED-Flex state under the authority granted in the Education Flexibility Partnership Act of 1999. ED-Flex states can grant administrative waivers regarding various recordkeeping provisions that reduces the administrative burden and provides additional time for instruction and planning.

## **TEA Comments on FINDING NO. 1 and OIG Response**

TEA reviewed HISD's draft report response and partially concurred with our finding. TEA concurred that \$62,772 of the total \$350,193 in questioned costs were unallowable. TEA also concurred that some portion of the \$147,865 in Federal payroll expenditures was inadequately documented. However, TEA was unable to determine, with the information provided in the draft report, how much of the questioned Federal payroll expenditures was inadequately documented. TEA did not concur that the \$138,006 in capital outlay expenditures were unallowable or the \$1,550 in other operating costs was inadequately documented. Below are TEA's comments to specific issues identified in the draft audit report.

### **Food and Travel Expenditures.**

*TEA Comments.* TEA concurred that the \$61,776 in prohibited catered food and \$179 in duplicated travel expenditures are not allowable.

### **Cost Incurred without Prior TEA Approval.**

*TEA Comments.* TEA did not concur and stated that, for school year 2005-2006, districts were required to request approval through TEA's Standard Application System (SAS) budget schedules only for capital outlay items costing \$5,000 or more per unit. TEA did not concur with OIG's interpretation that "net invoice price" applies to a group of items that, in aggregate, costs \$5,000 or more but believes the \$5,000 applies to individual items. TEA stated it exercised its authority pursuant to OMB Circular A-87, Section 15.b, and paragraph (4) that permits the awarding agency to waive the prior approval requirement for equipment of more than \$5,000. In addition, based on additional documentary evidence provided by HISD, TEA concluded that \$119,256 of the \$138,006 questioned was purchased using a Federal award, and therefore, TEA prior approval was not required. TEA further noted that the remaining \$18,750 pertained to an agency's Notice of Grant Award (NOGA) and that the agency approved the purchase in question.

*OIG Response:* We do not agree with TEA that the \$5,000 threshold applies to individual items in a set and not to the set or groups of items. Because the invoice shows only one price for the cart and the 30 laptop computers, we consider the 30-port rolling cart and computers as one unit, and its purchase should require approval by the awarding agency. However, we eliminated this finding because the additional documentation provided by TEA showed that the Department was the awarding agency for \$119,256. Therefore, TEA's prior approval was not required. Also, the additional documentation showed that the items were included in the grant application approved by the Department. For the remaining \$18,750, TEA provided evidence that the purchase of the mobile cart was approved in the NOGA.

### **Non Grant Related Expenditures.**

*TEA Comments.* TEA concurred that the \$817 for electrical work is not allowable under Title I, Part A and should be refunded to the Department.

Inadequate Documentation of Federal Payroll Expenditures.

*TEA Comments:* TEA partially concurred with this finding. TEA concurred that employees who worked on multiple activities should have submitted proper personnel activity reports to the HISD Accounting office. TEA concurred that the portion of payroll related to these employees should be disallowed and repaid to the Department.

However, TEA did not concur that the payroll was inadequately documented for 10 employees working full-time on a Federal program and were missing semi-annual certifications. As an ED-Flex state, TEA provided a statewide waiver to LEAs specifically related to the semi-annual certification required under OMB Circular A-87 for employees who worked on a single grant program or cost objective for school year 2005-2006.

*OIG Response:* We modified the payroll finding to exclude the payroll costs for the 10 full-time employees who did not have the certifications. The additional documentation provided by TEA demonstrated that all Texas LEAs were provided a waiver for school year 2005-2006.

Inadequate Support for Other Operating Expenditures.

*TEA Comments.* TEA did not concur that HISD charged a Federal program for a \$1,550 annual membership fee without adequate documentation.

*OIG Response.* The cancelled check documenting that the fee was paid by the River Oaks PTO was not presented to us during our audit. HISD provided only a copy of the \$1,550 invoice. After reviewing the additional documentation, we modified our report to eliminate the \$1,550 in questioned costs.

**Recommendations:**

*TEA Comments:* After reviewing additional documentary evidence provided by HISD, TEA concluded that only \$62,772 of the \$200,788 was unallowable and should be refunded to the Department. Of the \$149,415 in inadequately documented costs, TEA concluded that only \$1,550 was allowable after reviewing HISD's response to the draft audit report. TEA concurred that only a portion of the remaining \$147,865 in payroll costs was inadequately documented and should be disallowed and refunded to the Department. HISD agreed to revise its monthly Time & Effort Log to document Federal programs and the amount of time charged to the programs. HISD also agreed to develop procedures to ensure that the semi-annual certifications and/or personnel activity reports are obtained for all personnel whose salaries and wages are charged to Federal programs by July 1, 2009. HISD also agreed to develop some additional guidance to help train personnel involved with the administration or use of Federal program funds by July 1, 2009.

*OIG Response.* TEA submitted additional documentation, not presented by HISD during our fieldwork that demonstrated some of the questioned costs in the draft report were adequately documented and allowable. We reviewed the additional documentation and modified recommendation 1.1 to request \$62,722 of unallowable costs to be returned. We modified recommendation 1.2 to reflect \$82,712 as inadequately documented payroll costs that require additional documentation or should be returned. We modified recommendation 1.3 by excluding periodic certifications for employees who work full-time on Federal programs; however, we did

not remove the recommendation. In its response, TEA did not address our recommendation to conduct a full review of HISD's support for payroll charged to Federal programs for employees who worked on multiple activities to provide reasonable assurance that the \$238,430,479 in payroll expenses not included in our sample is supported by personnel activity reports. We did not modify recommendation 1.4.

## **FINDING NO. 2 – Improper P-card Purchases Charged To Federal Programs**

HISD charged P-card purchases to Federal programs for items that were either unallowable or not adequately documented. We analyzed the P-card charges databases obtained from HISD and Chase Bank for school year 2005-2006 and from August 2006 through June 2007. We judgmentally selected 130 P-card purchases totaling \$31,934 in Federal charges.<sup>7</sup> Of the 130, 41 (32 percent) were in violation of Federal or state guidelines or had inadequate or no documentation to substantiate the charge. Specifically, 17 P-card charges, totaling \$2,064, were in violation of Federal and state guidelines. The remaining 24, totaling \$4,731, had inadequate or no documentation to substantiate the transaction.

### **Unallowable P-card Charges**

Of 130 P-card purchases randomly selected for review, 17 purchases totaling \$2,064 were for food, beverages, and gifts. HISD allowed 11 Federal P-card charges totaling \$804 for prohibited food and beverages and 6 Federal P-card charges totaling \$1,260 for prohibited gifts. According to OMB Circular A-87, Attachment A, paragraph C.1.c., to be allowable under Federal awards, costs must be authorized or not prohibited under state or local laws or regulations. TEA's matrix prohibits breakfast and refreshments of any kind, including beverages, and snack foods, for staff meetings or staff training. Exceptions include a light lunch or working lunch during an all day meeting or training session when documented that it is impractical for participants to obtain lunch on their own and refreshments at parental involvement activities when necessary for attendance. TEA requires the grantee to maintain an agenda that clearly identifies the exercise or activity that the participants are engaged in and should retain a representative sample of the work product if any. Additionally, TEA's matrix also states that full meals for parents and/or students are not allowable.

The 11 Federal P-card charges for food and beverages included a charge of \$213 for breakfast and snacks for a teacher professional development day and smaller charges for food and beverages for counselors' meals and a party platter for teachers. Principals at these schools approved these meals as Federal expenditures and receipts were provided to HISD. However, these meals were unallowable because they lacked documentation to show that it was impractical for participants to obtain lunch on their own or that it was a working lunch during an all day meeting or training session.

The six Federal P-card charges totaling \$1,260 for gifts included charges for movie tickets, gift cards, t-shirts, flowers, and lotion. Like the prohibited food and beverage charges, school

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<sup>7</sup> Initially, we judgmentally selected 156 P-card purchases. However, we determined that 26 of the 156 P-card charges were not paid with Federal funds. We selected part of our sample from the August 2006 to June 2007 database we obtained directly from Chase Bank. However, the Federal accounting codes provided by Chase Bank for each P-card purchase were not always the accounting codes to which the P-card purchase was billed, resulting in the non-Federal P-card charges being selected for review. See the *Potential Internal Control Weakness with P-card System at HISD* section of this report.

principals approved these gifts as Federal expenditures and receipts were provided to HISD. However, the matrix states that gifts or items that appear to be gifts are unallowable. HISD stated that the movie tickets and gift cards were student incentives. However, the matrix states that acceptable awards and incentives include certificates, plaques, ribbons, and small trophies nominal in cost, or inexpensive instructional related items such as pens/pencils to be used in the classroom.

### **Inadequately Documented P-card Charges**

In addition to the 17 unallowable P-card charges, HISD maintained inadequate documentation to substantiate Federal allowability for 24 (totaling \$4,731) of the 130 randomly selected P-card charges. According to OMB Circular A-87 Attachment A (C), to be allowable, costs must be necessary and reasonable for proper and efficient performance and administration of Federal awards and must be adequately documented.

Even though at the time of purchase school principals approved the 24 P-card charges as Federal expenditures, HISD did not have adequate documentation, such as purchase card receipts, cash register receipts, invoices, and justification that the P-card charges was an allowable charge. Specifically:

- Sixteen (16) totaling \$1,962 were for food and beverages. HISD allowed P-card charges for breakfasts, lunches, snacks, and beverages for teachers, staff, and parents. When the P-card charge was for a training session lunch, HISD did not provide documentation that the session was all day or that it was impractical for participants to obtain lunch on their own. HISD did provide purchase card receipts for breakfast items (donuts, pastries, coffee, and juices) as well as snacks and beverages for afternoon activities, which can be allowable expenses if necessary for parental attendance. However, HISD did not provide copies of agendas, lists of participants, or other documentation to support the purpose for each cost.
- Eight(8) totaling \$2,769 were for other items, such as an LCD TV, an LCD projector bulb, electrical wiring and fixtures, microphones, ink cartridges, and cleaning supplies. Any of these items could have been allowable if necessary and reasonable for proper and efficient performance and administration of a Federal program. However, the supporting documentation provided by HISD did not include adequate evidence to make a determination of allowability. For the LCD TV, school officials stated that the TV was used strictly for 21st Century parent classes. However, school officials did not provide how access was being restricted to parenting classes or even the location of the LCD TV.

### **Potential Internal Control Weaknesses with P-card System at HISD**

For certain HISD P-card holders, HISD's accounting system automatically selects Federal program accounting codes to bill P-card charges, and HISD relies on its staff to manually change to the appropriate accounting code when entering the P-card charge or reviewing the charge. HISD's procurement manager stated that, when HISD employees are issued a P-card, the employees identify the primary program that the P-card card will be used for and the program's accounting code becomes the automatic accounting code billed for all P-card charges for that employee—unless manually changed by the employee or the reviewer. For a Title I coordinator, all P-card charges would be billed to Title I accounting codes unless the coordinator or the reviewer were to manually change the accounting code in the computer system. Automatically

selecting a Federal program accounting code to bill P-card charges could result in inappropriate Federal P-card charges.

### **Recommendations**

We recommend that the Assistant Secretary for Elementary and Secondary Education instruct TEA to require HISD to:

- 2.1 Provide training for all P-card cardholders and reviewers regarding acceptable and adequately documented Federal P-card charges;
- 2.2 Provide reasonable assurance that the remaining P-card charges paid by a Federal program at HISD in school year 2005-2006 have adequate records to show allowability as a Federal expenditure;
- 2.3 Refund to the Department \$2,064 of Federal funds expended for unallowable P-card charges;
- 2.4 Refund to the Department \$4,731 in inadequately documented P-card charges or provide adequate documentation to support that amount; and
- 2.5 Prevent HISD's accounting system from automatically selecting Federal program accounting codes to bill P-card charges.

### **TEA Comments to FINDING NO. 2 and OIG Response**

*TEA Comments:* TEA partially concurred that P-card purchases were not allowable or were inadequately documented. HISD provided TEA additional information and documentary evidence that certain P-card purchases were not charged to Federal programs but were charged to a state-funded pre-kindergarten expansion grant, the food service fund, or a capital assets/long-term debt fund. After reviewing the documentation, TEA concurred with our finding that HISD had maintained inadequate documentation for \$6,374 in charges. TEA also observed inconsistencies in some of the documentation provided and noted that the documentation did not include itemized third-party records. For the \$2,700 in unallowable costs, TEA did not concur and concluded that two charges totaling \$475 should not have been questioned because the charges were paid by a state-funded pre-kindergarten expansion grant and not a Federal program. TEA also concluded that nine additional charges, totaling \$1,276, should not have been questioned because the charges were paid from non-Federal sources.

TEA concurred that the P-card system automatically selecting a Federal program accounting code to bill P-card charges is an internal control weakness and could result in inappropriate Federal P-card charges.

*OIG Comments:* After reviewing the additional documentation, we agreed with TEA that not all the charges questioned in the audit report should be considered inadequately documented or unallowable. We have reduced our original unallowable P-card charges from \$2,700 to \$2,064 and the original inadequately documented charges from \$6,374 to \$4,731. This reflects amounts TEA accepted plus two additional charges, totaling \$527, for which we had additional documentation that was not provided to TEA.

## **Recommendations:**

*TEA Comments:* After reviewing the documentation, TEA concurred that HISD had maintained inadequate documentation for \$6,374 in charges. TEA concluded that \$1,751 was paid by non-Federal sources, leaving \$949 of the \$2,700 as unallowed costs charged to Federal programs and should be questioned. TEA agreed that HISD did not demonstrate that its use of Federal funds was an allowable activity and was adequately supported. HISD also agreed to develop some additional guidance documentation for P-card training of personnel involved with the administration or use of Federal program funds by July 1, 2009. HISD has already completed a review of all P-card cardholder accounts and changed the default budgets to the general fund account. Additionally, on a quarterly basis, HISD agreed to conduct a review of the P-card default budgets to ensure that they are set to non-Federal accounts.

*OIG Comments:* TEA submitted additional documentation, some of which TEA concluded was adequate documentation to reduce the unallowable costs in the draft report. As stated above, we have reviewed and accepted some of the additional documentation and modified recommendation 2.3 to request \$2,064 of unallowable costs to be returned and recommendation 2.4 to reflect \$4,731 as inadequately documented costs which additional documentation should be provided or the costs returned. However, we did not modify recommendations 2.1, 2.2 or 2.5. With respect to recommendations 2.2. and 2.5, TEA stated that HISD has completed a review of all P-card cardholder accounts to ensure that the default budget was the general fund. However, TEA did not state whether Federal allowability of the transactions was part of the review. We still maintain that reasonable assurance be provided by HISD that the remaining P-card charges paid by a Federal program at HISD in school year 2005-2006 have adequate records to show allowability as a Federal expenditure.

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## **OTHER MATTERS**

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HISD did not always prevent employees from being accepted as an approved vendor for HISD. HISD policy states “that an individual is either an employee or a vendor, not an employee and vendor.” We compared extracts of 15,996 approved HISD vendors’ names and addresses to HISD employees’ names and addresses for school year 2005-2006. Two approved HISD vendors were also HISD employees. These two employees received \$3,715 for math instruction and decoration fees during school year 2005-2006. HISD needs to ensure that it enforces its policy that employees cannot be accepted as vendors so that it minimizes the risk of inappropriate payments.

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## **OBJECTIVES, SCOPE AND METHODOLOGY**

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The objective of the audit was to determine whether HISD had adequate fiscal controls over accounting for and using Federal funds. Our audit covered HISD’s system of internal control as of June 30, 2006, and Federal funds expended for the period July 1, 2005, through June 30, 2006. We also reviewed HISD’s P-card charges from August 2006 through June 2007.

To accomplish our objective, we

- Reviewed HISD's written policies and procedures for administering Federal programs to evaluate the adequacy of fiscal controls over Federal funds.
- We examined OMB Circular A-133 Single Audit Report for the year ended June 30, 2006.
- Requested and obtained an electronic copy of the *General Ledger Report of Expenditures* which included all charges against Federal programs for school year 2005-2006.
- Obtained a listing of all cash draws HISD made directly from the Department or through TEA for school year 2005-2006.
- Compared extracts of 15,996 vendor/employee names and addresses to determine whether HISD employees were also HISD vendors; and
- Compared P-card extracts provided directly from Chase Bank to HISD's computer system for all P-card charges for the period August 2006 through June 2007 to determine whether vendor data or purchase amounts had been changed.<sup>8</sup>

To test whether the costs HISD charged to the Federal programs during school year 2005-2006 were allowable under applicable law, regulations, and cost principles, we selected samples of transactions.<sup>9</sup> The universe and sample sizes are shown in the table on page 4 of this report. We separated the transactions recorded in the *General Ledger Report of Expenditures* into Title I and non-Title I universes, with each universe including four categories of transactions: (1) Supplies, (2) Other Operating, (3) Capital Outlay, and (4) Contract Services. We stratified each of the eight universes into four strata based on dollar increments of the transactions. We randomly selected 10 transactions from each of the strata except for the highest dollar increment strata for that universe. From the high strata, we selected all transactions. Negative expenditures were separated into a universe and stratified into two strata (less than \$2,000 and more than \$2,000), and we randomly selected 10 items from each strata. We requested and reviewed supporting documentation, such as purchase orders, invoices, canceled checks, and receiving reports, time sheets, and employee certifications. We considered a cost allowable, adequately documented, reasonable, and necessary if we were able to identify the purpose of the cost, proper approval, proof of receipt, and proof of payment or cancellation.

For payroll, we obtained a list of employees paid, at least in part, from Federal funds during school year 2005-2006. We stratified the universe into five strata of \$20,000 increments: (1) less than \$20,000; (2) \$20,000 but less than \$40,000; (3) \$40,000 but less than \$60,000; (4) \$60,000 but less than \$80,000; and (5) \$80,000 but less than \$100,000. We reviewed 100 percent of the employees in the fifth strata. We randomly selected 10 employees from each of the first 4 strata. We then selected 2 months of pay from the regular school year for the sample employees. We selected an additional sample month for general fund employees who received federally funded payroll only in the summer months.

From our randomly selected non-Title I Supplies sample, we judgmentally selected a single school year 2005-2006 capital outlay purchase invoice from four different HISD schools. We visited each of the four schools and verified that the capital outlay equipment was at the school

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<sup>8</sup> Chase Bank maintained the P-card extracts that it uploads to HISD for only 10 months; therefore, the data used for the comparison were outside the original audit period.

<sup>9</sup> Our sample sizes were not sufficient to project the results of the samples to the untested items in each universe.

and being used by school officials. We interviewed 15 employees at the administrative offices and 16 at campus levels to determine how HISD tracks grant expenditures and Title I funding.

To test whether P-card charges were allowable, we judgmentally selected a sample of 50 charges from HISD's databases of federally funded P-card charges for school year 2005-2006 and from August 2006 through June 2007. The universes of transactions for the 2 periods were 29,518 and 92,530 respectively. Because we noticed questionable charges, we further analyzed HISD's federally funded P-card charges. For each time period, we developed a universe of charges that were suspicious based on date, amount, vendor, or cardholder. From these two universes, we judgmentally selected three samples:

- Sample 1—34 P-card charges made up of one weekday and one weekend/holiday purchase from 17 individuals identified as having large amounts of charges;
- Sample 2—22 P-card charges made up of questionable Paypal charges; and
- Sample 3—50 P-card charges made up of questionable charges based on dates, vendors, and amounts.

We also relied, in part, on computer-processed data. HISD officials provided us with an electronic version of HISD's general ledger, which recorded all transactions associated with Federal funds for school year 2005-2006. To ensure the accuracy and completeness of the general ledger data, we compared the general ledger total expenditures to the schedule of expenditures reported in HISD's Single Audit report for the same period. We noted that the information on the source documents agreed with the information in the general ledger. We also noted that the general ledger included all expenditures related to the Federal programs for our audit period and did not include any transactions outside our audit period. We also verified the authenticity of the data by comparing selected fields to source documents. Therefore, we concluded that the data were adequately reliable to be used in meeting the audit's objective. We conducted our fieldwork at HISD between August 2007 and September 2008. We held an exit conference with HISD officials on March 27, 2009, to discuss the results of the audit. Our audit was performed in accordance with generally accepted government auditing standards (June 2003 revision) appropriate to the scope of the review described above.

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## ADMINISTRATIVE MATTERS

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Statements that managerial practices need improvements, as well as other conclusions and recommendations in this report, represent the opinions of the Office of Inspector General. Determinations of corrective action to be taken will be made by the appropriate Department of Education officials in accordance with the General Education Provisions Act.

If you have any additional comments or information that you believe may have a bearing on the resolution of this audit, you should send them directly to the following Department of Education official, who will consider them before taking final Departmental action on this audit:

Joseph Conaty  
Acting Assistant Secretary  
Office of Elementary and Secondary Education  
U.S. Department of Education  
400 Maryland Ave., SW  
Washington D.C. 20202

It is the policy of the U.S. Department of Education to expedite the resolution of audits by initiating timely action on the findings and recommendations contained therein. Therefore, receipt of your comments within 30 days would be appreciated.

In accordance with the Freedom of Information Act (5 U.S.C. § 552), reports issued by the Office of Inspector General are available to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act.

Sincerely,

/s/

Gary D. Whitman  
Regional Inspector General for Audit

**Federal Programs Charges With Unallowed and Inadequately Documented Costs**

<b>Federal Programs</b>	<b>Description of Charge(s)</b>	<b>Amount</b>
<b>DIRECT FEDERAL</b>		
Fund for the Improvement of Education	Duplicated Travel Expenditures	\$ 179.00
Project Leeks	P-Card Charges –Unallowed Food	229.37
Transition To Teach	P-Card Charges –Inadequately Documented-Food	48.67
<b>Sub-total</b>		<b>\$ 457.04</b>
<b>FLOW THROUGH TEA</b>		
Title I	Non Grant Related Expenditures	\$ 817.50
	P-Card Charges –Unallowed Food and Gifts	1,309.54
	P-Card Charges –Inadequately Documented-Food and Other	3,043.63
<b>Sub-total--Title I –</b>		<b>\$5,170.67</b>
Title II –	Prohibited Catered Food	61,776.00
Title III –LEP	P-Card Charges –Inadequately Documented-Food	8.68
Title IV-Part A	P-Card Charges –Inadequately Documented-Food	351.75
Title VII- Dual Language	P-Card Charges –Unallowed Food	28.47
Smaller Learning	P-Card Charges –Unallowed Gifts	497.00
Vocational Education	P-Card Charges –Inadequately Documented-Other	499.10
21 <sup>ST</sup> Century	P-Card Charges –Inadequately Documented-Other	779.61
<b>Sub-total</b>		<b>\$69,111.28</b>
<b>Total</b>		<b>\$69,568.32</b>

[Graphic Deleted]

# TEXAS EDUCATION AGENCY

1701 North Congress Ave.\* Austin, Texas 78701 -1494 \* 512/463-9734 \* FAX: 512/463-9K3K \* <http://www.tca.statc.tx.us>

Robert Scott  
Commissioner

May 1, 2009

Gary D. Whitman  
Regional Inspector General for Audit  
U. S. Department of Education  
Office of Inspector General  
500 West Madison Street, Suite 1414  
Chicago, IL 60661

Dear Mr. Whitman:

On April 7, 2009, the Texas Education Agency (TEA) received the Draft Audit Report, ED-OIG/A06H0017, entitled *Adequacy of Houston Independent School District's Fiscal Controls over Accounting for and Using Federal Funds* dated April 2, 2009. The TEA appreciates the opportunity to respond to the Office of Inspector General's (OIG) findings outlined in its draft report. The response is due to OIG within thirty days after the date of the OIG letter.

Attached is a copy of the TEA's response to the findings. If you have any questions, please contact Rita Chase, Director, Division of Financial Audits, at 512-463-7595.

Thank you for your cooperation.

Sincerely,

/s/

Robert Scott  
Commissioner of Education

RS:rc

Enclosures

cc: Abelardo Saavedra, Superintendent, Houston Independent School District  
Ray Glynn, Deputy Commissioner for School District Leadership and Educator Quality  
Laura Taylor, Associate Commissioner for Accreditation  
Nora Hancock, Associate Commissioner, Office for Planning, Grants, and Evaluation  
Earin Martin, Chief Grants Administrator and Director of Discretionary Grants and eGrants  
Cory Green, Director, NCLB Program Coordination

Texas Education Agency  
Response to Draft Audit Report: ED-OIG/A06H0017

Submitted to:  
Mr. Gary D. Whitman  
Regional Inspector General for Audit  
U.S. Department of Education  
Office of Inspector General  
500 West Madison Street, Suite 1414  
Chicago, IL 60661

The Texas Education Agency (TEA) appreciates the opportunity to respond to the Office of Inspector General's (OIG) findings outlined in its draft report dated April 2, 2009 about whether the Houston Independent School District (ISD) had adequate fiscal controls over accounting for and using federal funds. The audit covered Houston ISD's system of internal control as of June 30, 2006, and federal funds expended for the period July 1, 2005 through June 30, 2006. During this grant period, the Houston ISD expended \$222,807,926 of federal funds. Also covered in the audit was a review of Houston ISD's purchase card (P-card) charges from August 2006 through June 2007. During this period, the Houston ISD used P-cards to expend over \$21 million of federal funds. As required, the TEA's response is being submitted to the OIG within 30 days of the date of the OIG letter.

The TEA and Houston ISD recognize the specific issues provided in the draft audit report and provide the following responses to these findings and recommendations.

**I. SUBJECT: Response to Finding #1: Houston ISD Charged Federal Programs \$350,193 in Unallowable and Inadequately Documented Costs**

The finding concludes that the Houston ISD did not always use federal funds in compliance with the law, regulations, and state requirements.

As discussed in the draft report dated April 2, 2009, the Office of Inspector General (OIG) of the United States Department of Education questioned \$350,193 in costs charged to various awards to the Houston ISD for the 2005-2006 school year. The TEA auditors concluded their review of the Houston ISD response to the OIG draft report, including the attached schedules and concluded that \$62,772 in costs were still unallowable or inadequately documented. Of the \$350,193 in questioned cost, \$147,865 is for payroll, the TEA is not able to determine with the information provided in the report how much of the questioned cost is unallowable.

**Houston ISD Used Federal Funds for Unallowable Purposes**

Food and Travel Expenditures. Houston ISD charged \$61,776 in prohibited catered food and \$179 in duplicated travel expenditures to federal programs.

The TEA and Houston ISD agree that these expenditures are not allowable.

Expenditures Without Required TEA Approval. Houston ISD charged federal programs for \$138,006 in capital outlay without obtaining TEA's prior approval. The \$138,006 was used to purchase 2 sets of 30 laptop computers, including a 30-port rolling cart for each set.

The TEA and Houston ISD offer the following response with regard to the disallowance of \$138,006 in capital outlay.

For the audit year of 2005-2006, school districts were required only to request (i.e., specifically list) capital outlay items costing \$5,000 or more per unit in the Standard Application System (SAS) budget schedules. In addition, the instructions for preparing the budget schedule for capital outlay state at the very beginning of the instructions that this schedule is to request items with a unit cost of \$5,000 or more.

OMB Circular A-87, Section 15. Equipment, addresses two sections: a) definitions which apply and b) rules of allowability which apply to equipment and other capital expenditures.

The following definitions are provided in OMB Circular A-87, Section 15(a):

- (1) "Capital Expenditures" means expenditures for the acquisition cost of capital assets (equipment, building, land), or expenditures to make improvements to capital assets that materially increase their value or useful life. Acquisition cost means the cost of the asset including the cost to put it in place. Acquisition cost for equipment, for example, means the net invoice price of the equipment, including the cost of any modifications, attachments, accessories, or auxiliary apparatus necessary to make it usable for the purpose for which it was acquired. Ancillary charges, such as taxes, duty, protective in-transit insurance, freight, and installation may be included in, or excluded from the acquisition cost in accordance with the governmental unit's regular accounting practices.
- (2) "Equipment" means an article of nonexpendable, tangible personal property having a useful life of more than one year and an acquisition cost which equals or exceeds the lesser of the capitalization level established by the governmental unit for financial statement purposes, or \$5,000.

The TEA views the interpretation of "net invoice price" somewhat differently than OIG views it. Because these definitions point to "the cost of the asset" and "an article of nonexpendable, tangible personal property" as a single item, the TEA does not necessarily interpret that this means the "net invoice price" always applies to a group of items that, in the aggregate, costs \$5,000 or more. Houston ISD would account for these funds in accordance with its regular accounting practices.

OMB Circular A-87, Section 15(b) states "rules of allowability shall apply to equipment and other capital expenditures."

Additionally OMB Circular A-87, Section 15(b) (4) states: "Federal awarding agencies are authorized at their option to waive or delegate the prior approval requirement." And, an awarding agency is defined as follows in OMB Circular A-87: "Awarding agency" means (a) with respect to a grant, cooperative agreement, or cost reimbursement contract, the Federal agency, and (b) with respect to a subaward, the party that awarded the subaward.

The TEA exercised this authority in OMB Circular A-87, Section 15(b)(4) that permits the awarding agency to waive the prior approval requirement for equipment less than \$5,000 in the No Child Left Behind (NCLB) consolidated grant application, and provided districts with that guidance based on the TEA's 2005-2006 NCLB consolidated grant application, and provided districts with that guidance.

The TEA auditors observed that the Houston ISD provided copies of the following documentation.

- a). A schedule itemizing the amounts questioned by the OIG.
- b). Grant Award Notification from the USDE for Award Number P334A050073, College For All (CFDA No. 84.334A, Gaining Early Awareness and Readiness for Undergraduate Programs (GEAR-UP) program).
- c). Project Budget Summary Form from the USDE e-Application system indicating that the Houston ISD was GEAR-UP budget included an approved line item for equipment.
- d). Equipment Purchases form indicating that the USDE approved the purchase of 180 laptop computers and six computer carts.
- e). eGrants NOGA summary for NOGA ID 066160027110079 and eGrants schedules BS6000 and BS6600.
- f). Internal accounting documents, vendor invoices and packing slips.

Based on the documentary evidence provided, the TEA concluded that \$119,256 of the \$138,006 questioned pertained to an USDE federal award and not a TEA grant. Although the TEA approval for the amounts questioned was not required, Houston ISD did provide documentary evidence indicating that the USDE approved the use of federal funds. The TEA further noted that the remaining \$18,750 pertained to an agency NOGA and that the agency approved the purchase in question.

In addition, in its 2005-2006 NCLB Application for Federal Funding, Houston ISD had four different "mobile computer labs" (i.e., equivalent to laptop computers with a rolling cart) budgeted and approved from Title I Part A for four different campuses.

It is therefore the recommendation of the TEA that the OIG accept the information demonstrating that Houston ISD did have the computers and cart budgeted, as well as accept the TEA's waiver of requiring specific approval for the items costing less than \$5,000 as stated in the TEA's 2005-2006 NCLB consolidated grant application instructions and not disallow the \$138,006 in capital outlay, provided that Houston ISD complied with all other requirements and conditions of the grant. This includes, but is not limited to, obligating funds within the period of availability, complying with their local capitalization policy, and expending funds that are reasonable and necessary to carry out the objectives of the applicable grant projects.

Non Grant Related Expenditures. Houston ISD charged the Title I, Part A program \$817 for electrical work to install an LCD monitor in the schools' lunchroom for use in the Title I, Professional Development program.

The TEA and Houston ISD agree that the \$817 for electrical work is not allowable under Title I, Part A and should be disallowed and repaid to the USDE.

## **Houston ISD Did Not Provide Adequate Documentation For All Expenditures Of Federal Funds**

Inadequate Documentation of federal Payroll Expenditures. Houston ISD did not provide adequate documentation to support \$147,865 of federal payroll expenditures.

Texas is an Ed-Flex state under the authority granted in the Education Flexibility Partnership Act of 1999 (Ed-Flex Act). The TEA provided a statewide waiver to LEAs specifically related to the semi-annual certification required under OMB A-87 for employees that worked on a single grant program or cost objective. Following is the language from Appendix 12 to the 2005-2006 NCLB Consolidated Application for Federal Funding.

The following statewide **administrative waivers** address the regulations governing the application for funds and various recordkeeping provisions. These administrative waivers have been automatically granted to all LEAs, as applicable, for the duration of the state's waiver authority under Ed-Flex, contingent on the state's meeting the evaluation criteria stated below. It is anticipated that these waivers will reduce the administrative burden and provide additional time for instruction and planning, resulting in improved student performance:

**3. Certification that an Employee is Funded from a Single Fund Source or Cost Objective** [OMB Circular A-87, Attachment B, Number 11(h)(3)] This waiver eliminates the requirement that charges for salaries and wages be supported by a semi-annual certification that the employee worked solely on that program for the period covered by the certification. This waiver is allowable as long as the employee's job description clearly states that the employee is assigned 100 percent to the program or single cost objective.

Therefore, the TEA does not agree with this finding related to inadequate documentation for federal payroll expenditures as it specifically relates to those 10 employees working full-time on a federal program who were missing the semi-annual certification if this program was part of the Ed-Flex waiver. The semi-annual certification would not be required for these employees pursuant to the Ed-Flex waiver provided by the TEA.

However, the TEA does agree with the finding related to the employees who worked on multiple activities and should have submitted proper personnel activity reports to the Houston ISD Accounting office. Therefore, the TEA agrees that only the portion of payroll related to these employees should be disallowed and repaid to the USDE.

Inadequate Support for Other Operating Expenditures. Houston ISD charged a federal program for a \$1,550 annual membership fee without adequate documentation.

Houston ISD provided adequate documentation demonstrating that the \$1,550 in non-Title I cost was an allowable cost. Houston ISD provided copies of the invoice and supporting documentation of the \$1,550 from International Baccalaureate Organization and the cancelled check documenting that the fee was paid by the River Oaks PTO. The District reimbursed River Oaks PTO for the fee payment through the FIE Earmark – International Baccalaureate Implementation grant, award #U215K040405, as authorized by the Department of Education.

## **II. SUBJECT: Response to Finding #2 – Improper P-card Purchases Charged To Federal Programs**

The finding concludes that Houston ISD charged P-card purchases to federal programs for items that were either unallowable or not adequately documented.

Of the \$2,700 questioned because the amounts were in violation of federal and state guidelines and of the \$6,374 questioned because the amounts were not adequately documented or were not documented, Houston ISD provided information and documentary evidence indicating that certain amounts pertained to a state funded Pre-Kindergarten Expansion grant, the Food Service fund or a capital assets/long-term debt fund. Accordingly, the TEA concurred that certain amounts charged to each fund source were not allowable or were inadequately supported.

Unallowable P-card Charges. Houston ISD allowed the use of P-cards for unallowable federal purchases of \$2,700.

Houston ISD provided information and documentary evidence indicating that certain amounts pertained to a state funded Pre-Kindergarten Expansion grant, the Food Service fund or a capital assets/long-term debt fund. Accordingly, The TEA concurred that the amounts charged to each fund source were not allowable or were inadequately supported. However, the TEA determined that only the amounts charged to the Pre-Kindergarten Expansion grant actually pertained to an agency NOGA. Accordingly, the amount of \$475.25 constitutes a questioned cost and the amount of \$1,276.27 did not constitute a refundable questioned cost (i.e., an amount that may be disallowed pursuant to 34 CFR 80.43) since it pertained to non-grant fund sources.

Inadequately Documented P-card Charges. Houston ISD maintained inadequate or no documentation to substantiate randomly selected P-card charges.

After reviewing the documentation provided by Houston ISD, the TEA concurs with the OIG finding. The district did not demonstrate that its use of federal funds for food pertained to an allowable activity and was adequately supported. Specifically, the district did not provide contemporaneous records clearly identifying the business related purpose for each disbursement and benefit to the grant program. Also, the district did not reference the associated need, goal, strategy and activity described in the applicable Campus Improvement Plans (CIPs). Lastly, in certain instances, auditors observed inconsistencies in the documentation provided or noted that the documentation did not include itemized third-party records.

Potential Internal Control Weaknesses with P-card System at Houston ISD. Houston ISD's accounting system automatically selects federal program accounting codes to bill P-card charges, and Houston ISD relies on its staff to manually change to the appropriate accounting code when entering the P-card charge or reviewing the charge.

The TEA and Houston ISD agree with OIG's assessment that automatically selecting a federal program accounting code to bill P-card charges could result in inappropriate federal P-card charges. Houston ISD has completed a review of all P-card cardholder accounts and changed the default budgets to the general fund account. Additionally, on a quarterly basis, they will conduct a review of the P-card default budgets to ensure that they are set to non-federal accounts.

The Office of Inspector General (OIG) recommends that the Assistant Secretary for the Office of Elementary and Secondary Education instruct the TEA to require Houston ISD to:

**Recommendation:**

**1.1** Refund to the Department \$200,788 of federal funds expended for unallowable cost.

**Response:**

Of the \$200,788 in costs questioned by the OIG because the Houston ISD used the grant funds for unallowable purposes, the TEA auditors concluded that \$62,772 was unallowable after having reviewed the Houston ISD response to the OIG draft report. By July 1, 2009, Houston ISD will develop some additional guidance documentation for training of personnel involved with the administration or use of federal program and funds.

**Recommendation:**

**1.2** Refund to the Department \$149,415 in inadequately documented costs or provide adequate documentation to support that amount.

**Response:**

Of the \$149,415 in costs questioned by the OIG because the Houston ISD did not provide adequate documentation to support the cost, the TEA auditors concluded that \$1,550 was allowable after having reviewed the Houston ISD response to the OIG draft report. The remaining \$147,865 is payroll and the TEA does not agree with this finding related to inadequate documentation for federal payroll expenditures as it specifically relates to those 10 employees working full-time on a federal program who were missing the semi-annual certification due to Texas being an Ed-Flex state unless the Ed-Flex waiver did not apply to the federal program.

The TEA and Houston ISD agree with the finding related to the employees who worked on multiple activities and should have submitted proper personnel activity reports to the Houston ISD Accounting office. Therefore, the TEA agrees that only the portion of payroll related to these employees should be disallowed and repaid to the USDE.

**Recommendation:**

**1.3** Provide reasonable assurance that, for the \$238,430,479 in payroll expenses not included in our sample, periodic certifications and personnel activity reports exists to support the amounts charged to federal programs.

**Response:**

Houston ISD has revised its monthly Time & Effort Log to document the federal program and the amount of time charged to the program. Additionally, by July 1, 2009, they will develop procedures to ensure that the semi-annual certifications and/or personnel activity reports are obtained for all personnel whose salaries and wages are charged to federal programs.

**Recommendation:**

**1.4** Provide additional training for all personnel involved with the administration of federal programs.

**Response:**

By July 1, 2009, Houston ISD will develop some additional guidance documentation for training of personnel involved with the administration or use of federal program and funds.

**Recommendation:**

**2.1** Provide training for all P-card cardholders and reviewers regarding acceptable and adequately documented federal P-card charges.

**Response:**

By July 1, 2009, Houston ISD will develop some additional guidance documentation for P-card training of personnel involved with the administration or use of federal program and funds.

**Recommendation:**

**2.2** Provide reasonable assurance that the remaining P-card charges paid by a federal program at Houston ISD in school year 2005-2006 have adequate records to show allowability as a federal expenditure.

**Response:**

Houston ISD has completed a review of all P-card cardholder accounts and changed the default budgets to the general fund account. Additionally, on a quarterly basis, they will conduct a review of the P-card default budgets to ensure that they are set to non-federal accounts.

**Recommendation:**

**2.3** Refund to the Department \$2,700 of federal funds expended for unallowable P-card charges.

**Response:**

Houston ISD provided information and documentary evidence indicating that certain amounts pertained to a state funded Pre-Kindergarten Expansion grant, the Food Service fund or a capital assets/long-term debt fund. Accordingly, the TEA concurred that the amounts charged to each fund source were not allowable or were inadequately supported. However, the TEA determined that only the amounts charged to the Pre-Kindergarten Expansion grant actually pertained to an agency NOGA. Accordingly, the amount of \$475.25 constitutes a questioned cost and the amount of \$1,276.27 did not constitute a refundable questioned cost (i.e., an amount that may be disallowed pursuant to 34 CFR 80.43) since it pertained to non-grant fund sources. The questioned cost should be refunded to the Department.

**Recommendation:**

**2.4** Refund to the Department \$6,374 in inadequately documented P-card charges, or provide adequate documentation to support that amount.

**Response:**

TEA concurs with the USDE OIG that Houston ISD should refund the Department the questioned cost. The district did not demonstrate that its use of federal funds was an allowable activity and was adequately supported.

**Recommendation:**

**2.5** Prevent Houston ISD's accounting system from automatically selecting federal program accounting codes to bill P-card charges.

**Response:**

Houston ISD has completed a review of all P-card cardholder accounts and changed the default budgets to the general fund account. Additionally, on a quarterly basis, they will conduct a review of the P-card default budgets to ensure that they are set to non-federal accounts.

The TEA and Houston ISD are committed to addressing these weaknesses and to strengthening the District's controls so it can better administer federal funds.