

## R4: “What is the general experience of savings potential identified in audits vs. the costs of the audit?”

First, to review, there are financial audits and performance audits. While it is not uncommon for auditors’ comments in financial audits to produce potential improvements for their clients, the primary objective of financial audits is to form and communicate opinions on the financial statements of the auditee.

The U.S. Government Accountability Office’s (GAO) *Government Audit Standards* recognizes four types of performance audits (April 2021 update, §1.22), listed in order of applicability to California Prop. 39 fund audits:

- Compliance audits – “... an assessment of compliance with criteria established by provisions of laws, regulations, contracts, and grant agreements, or other requirements ...” California Constitution Article XIII A Section 1.(b)(C) imposes upon districts that sell Prop. 39 bonds the “... (a) requirement that the school district board, community college board, or county office of education conduct an annual independent financial audit of the process for the sales of the bonds until all of these proceeds have been expended for the school facilities projects” and California Education Code §15278.(c)(1) provides that the CBOC shall “... (r)eceiving and reviewing copies of the annual independent performance audit requirement ...”

*The Guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting Appendix A: Local School Construction Bond Audits*, published by the State of California Education Audit Appeals Panel, describes the provisions for the annual performance audit:

Funds expended on specific projects listed in the text of the applicable ballot measure.

Funds expended for construction, renovation, furnishing, and equipping of school facilities constituting authorized bond projects.

Verify that the funds used to pay the salaries of district employees were allowable per Opinion 04-110 issued November 9, 2004, by the State of California Attorney General.

If the school district did not properly account for expenditures, include a finding in the audit report.

- Program effectiveness and results audits – “These are frequently interrelated with economy and efficiency objectives ... typically measure the extent to which a program is achieving its goals and objectives.”
- Internal control audits – “... relate to an assessment of one or more aspects of an entity’s system of internal control that is designed to provide reasonable assurance of achieving effective and efficient operations, reliability of reporting for internal and external use, or compliance with provisions of applicable laws and regulation.” In the Prop. 39 environment, the above should be considered to expand beyond financial control systems to comprehend construction program and project planning, budgeting, management, and reporting systems.
- Prospective analysis audits – “... provide analysis or conclusions about information that is based on assumptions about events that may occur in the future, along with possible actions that the entity may take in response to the future events.”

Compliance audits are statutorily required to be performed every year. To the extent that such audits identify potentially improper expenditures, there is potential for cost savings. Of

course, if the auditor opines that there are no reportable issues, there will be no specific potential savings, but there is value in the program stakeholders being assured that the program, and the taxpayer dollars involved, are being properly managed. (Prop. 39 compliance audit objectives can be extended beyond the minimum requirements cited above.)

Other than compliance audits, there is no statutory requirement for any other type of performance audit.

Program effectiveness and results audits are the type of performance audit that is most commonly associated with the identification of potential cost savings, including superior methods of operation. A comprehensive program effectiveness and results audit, covering all aspects of a Prop. 39 program, would be such a major undertaking (on any but a very small program) to be rare; therefore, a more common approach is to do a series of such audits on specific aspects of the program each year.

Internal control audits generally build on the internal control portions of the annual financial audit and go deeper into the specifics of the school construction program. It is common that, very early in new major construction programs, this type of internal control audit focus on the financial and program control aspects of the construction program, including policies and procedures, systems to process both financial aspects and results (e.g., projects proceeding on-time, on-budget, and meeting scope, quality, safety, compliance, and other standards). Internal control audits also test for compliance with standards and procedures, such as proper documentation of all approvals for an expenditure or action. Again, after the initial major program-kick-off review, it is common for there to be a rotating scope of internal control audits, such as focusing on procurement one year, change orders the next, then inspections, etc.

While the above three are common in Prop. 39 programs, prospective analysis audits are less frequent. In the Prop. 39 context, they can be useful in specific situations – such as reviewing if the work remaining on the original project list presented to the electorate is likely to be completed on-time and on-budget.

Most Proposition 39 compliance audits (Appendix A as described above) are performed by CPA firms that perform the district's single audit.

Performance audits, particularly of Prop. 39 school construction programs, may require experience and skill sets beyond what most financial auditors can provide, particularly for the three non-compliance types of performance audits. Some of the CPA firms that perform K-12 and community college single audits and Prop. 39 audits do have the specialized staff and experience to provide such services, but it is common for performance audits to be performed by other specialist organizations, or for CPA firms to join with other specialist organizations to perform such services. While only CPA firms may perform financial audits, performance audits may be performed by non-CPA firms and individuals – as long as the work is performed in accordance with Government Audit Standards and other applicable requirements.

Finally getting to response to the question that was asked, while it is always desirable for an audit to produce benefits that exceed the cost of the audit, it is not always easy, or even possible, to fully quantify the benefits. For example, identifying a weakness in controls could lead to improvements that reduce losses, but trying to project how much losses will be, or have been, lowered can be problematic. (How much fraud didn't occur because we improved controls? How large is the financial gain because of faster and more accurate reporting of activities? The recommended changes in process have led to projects being completed and ready for students faster, which improves the educational experience – how do we quantify the dollar value of this acceleration?)

The main objectives of the most common types of financial audits are to provide assurance that financial results reported can be relied upon and that proper controls are in place. Findings and recommendations that lead directly to cost savings, revenue enhancements, or other meaningful improvements in results that can be quantified should be regarded as a bonus.