

August 25, 2017

Caprice Young, Ed.D., Chief Executive Officer
Magnolia Public Schools
250 East 1st Street, Suite 1500
Los Angeles, CA 90012

Dear Chief Executive Officer Young:

This is the eighth management letter from the Fiscal Crisis and Management Assistance Team (FCMAT) regarding the Magnolia Public Schools (Magnolia). On August 31, 2015, Magnolia entered into an agreement with FCMAT for fiscal oversight services, and in August 2016, an amended study agreement was signed. The amended agreement states that FCMAT will perform the following scope of work:

The Magnolia Educational and Research Foundation, DBA Magnolia Public Schools is requesting FCMAT to perform monthly fiscal oversight services in accordance with the charter's settlement agreement with its authorizer, the Los Angeles Unified School District (LAUSD) for the 2015-16 fiscal year. The charter operates 11 K through 12 schools serving 3,790 students throughout California. The charter schools operate under the approval of four authorizing agencies that include the California State Board of Education, Santa Clara County Office of Education, the LAUSD, and San Diego Unified School District.

This agreement is for July 2015 monthly fiscal oversight of the following foundation schools authorized by the LAUSD:

Magnolia Science Academy
Magnolia Science Academy 2
Magnolia Science Academy 3
Magnolia Science Academy 4
Magnolia Science Academy 5
Magnolia Science Academy 6
Magnolia Science Academy 7
Magnolia Science Academy 8 (Bell)

FCMAT

Michael H. Fine, Chief Executive Officer

1300 17th Street - CITY CENTRE, Bakersfield, CA 93301-4533 • Telephone 661-636-4611 • Fax 661-636-4647
755 Baywood Drive, 2nd Floor, Petaluma, CA 94954 • Telephone: 707-775-2850 • Fax: 661-636-4647 • www.fcmat.org
Administrative Agent: Mary C. Barlow - Office of Kern County Superintendent of Schools

Further, this agreement is for August 2015, May 2016 and June 2016 monthly fiscal oversight of the following foundation schools authorized by the LAUSD:

Magnolia Science Academy 6

Magnolia Science Academy 7

Magnolia Science Academy 8 (Bell)

As part of the charter renewal process, the foundation agreed to specific terms and conditions in accordance with section 8 of the settlement agreement between the foundation and LAUSD, which is attached, marked exhibit "A" and made part of this agreement. The terms and conditions require the charter to be subject to monthly fiscal oversight during the 2015-16 fiscal year by FCMAT or "a reasonably equivalent fiscal organization."

Scope of work:

For only the months and foundation schools identified above:

1. Review a sample of monthly financial transactions that have been entered and processed in the charter's accounting system. This will include sample testing of various general ledger, budget, accounts payable, accounts receivable, and payroll transactions. Testing for this review will be based on sample selections; it will not include all transactions and records for this period. Documents chosen for testing will also be reviewed for proper authorization. Sample testing and review results are intended to provide reasonable, but not absolute assurance regarding the accuracy of the charter school's financial transactions, bank records and reporting.
2. Evaluate monthly reports including but not limited to profit and loss, balance sheet, cash flow statements and interim reporting requirements.
3. Review each completed report for accuracy, reasonableness, and make recommendations, if any.
4. Compare budget to actuals and make recommendations regarding any areas that may exceed the budget.
5. Review the bank reconciliations and compare to the general ledger or balance sheet accounts.
6. Prepare a monthly management letter summarizing FCMAT's findings, and make recommendations or suggest action steps (if applicable).

Following FCMAT's seventh management letter dated June 27, 2016, Magnolia and FCMAT entered into the amended study agreement. Magnolia staff continued to provide responses to FCMAT's follow-up questions and post documents to SharePoint that the study team had requested to complete its review and testing of financial transactions. Transactions selected for testing were analyzed based on industry standards, best practices, and the team's judgment and technical expertise in school finance and accounting. The following findings and recommendations are the result of the team's review and testing of the information provided. At Magnolia's request, the findings and recommendations for each month's review and testing are included in this management letter.

July 2015

Payroll

New Employees

FCMAT compared payroll registers from June 2015 and July 2015 to attempt to identify newly hired employees. For each employee paid in July 2015 who was not included on the June 2015 payroll registers, the team requested their contract with Magnolia, signed Form I-9, verification of tuberculosis testing and results, fingerprint and background clearance and certification of membership in the California Public Employees' Retirement System (PERS) or California State Teachers' Retirement System (STRS).

For the month of July 2015, FCMAT identified 13 employees as new by the above process; however, Magnolia reported that all 13 were returning employees who did not receive a paycheck in June based on the charter school's payroll cycles. Magnolia provided FCMAT with offers of at-will employment and/or at-will employment agreements as evidence of their continuous employment, which showed that all 13 employees had been hired prior to July 1, 2015. However, an at-will employment agreement was provided for one person that reflected employment was to commence effective November 9, 2012 but the agreement was not executed by either the employee or Magnolia until January 2013.

Even though the 13 employees were not newly hired as of July 2015, Magnolia reported that none of them had a PERS/STRS certification form on file and that, at that point in time, no system had been established to track part-time employees for PERS/STRS eligibility. Although the July payroll registers showed PERS/STRS contributions for several of these employees, the lack of certifications and a tracking system for part-time employees raises questions as to whether all of those who qualified to participate in either of these retirement plans were enrolled.

Recommendations

The charter schools should:

1. Ensure that all new employees complete proper hiring documentation and procedures prior to their first day of work including, but not limited to, signing an employment contract and completion of a PERS/STRS certificate.
2. Review their employee records to determine the date each eligible employee qualified to participate in PERS/STRS and compare that to the reporting made to the applicable agency. If the charter finds that employees qualified but were not enrolled, or were not enrolled timely, work with PERS/STRS to update their reporting and determine if any penalties and/or interest are due.

Payroll Transactions

FCMAT reviewed Magnolia's MPS Employee Pay Raise Scale, adopted on May 2, 2014, to determine the process by which the charter determines employees' pay. Based on the date the scale was adopted, board minutes were reviewed to determine if there had been board-approved changes to salary schedules. On March 25, 2015, the board approved a 1.5% increase to both base pay and employee qualifications pay (EQP). FCMAT's review of the board agenda item provided in support of the salary increase found that its stated budget implications were related to the 2015-16 fiscal year, but it lacked a specific date of implementation and information regarding to which specific employee group(s) the salary increase

applied. A 2015-16 Pay Raise Salary Scale was presented to the board on April 15, 2015 to reflect revisions generated by the increases approved on March 25, 2015.

FCMAT reviewed the April 11, 2015 MPS Pay Raise Salary Scale spreadsheets to determine if employees' salaries conformed to the amounts in the 2015-16 Pay Raise Salary Scale and found the following:

- MSA 1 – The position of after school coordinator is not listed among the classified positions on the 2015-16 Pay Raise Salary Scale and, consequently, the base salary attached to this position is missing.
- MSA 4 – The position of part-time office technician is not listed among the classified positions on the 2015-16 Pay Raise Salary Scale and, consequently, the base salary attached to this position is missing.
- MSA 8 – The base salary for the position of custodian is \$23,000 in the April 11, 2015 MPS Pay Raise Scale spreadsheets but should be \$23,345 based on the 2015-16 Pay Raise Salary Scale. While this employee was not among the items tested below, review of the July 31, 2015 payroll register shows that the employee is paid at a base salary of \$22,537, which is less than the base salary listed in the 2015-16 Pay Raise Salary Scale.
- Multiple employees had EQP that did not conform to Magnolia's formula amounts provided in the 2015-16 Pay Raise Salary Scale. Those increases, as presented to the board, were to be valued at \$508 per point for prior experience for both certificated and classified employees. Magnolia Public Schools (MPS) experience was to be valued at \$1,015 and \$761 per point for certificated and classified employees, respectively. However, the April 11, 2015 MPS Pay Raise Scale spreadsheets use a \$507.50 value for prior experience for both classes of employees and \$761.25 for MPS experience for classified employees. Rounding after the calculation is made for each employee further complicates the situation. While the differences between the amounts provided to the board and those listed in the April 11, 2015 MPS Pay Raise Scale spreadsheets are minimal, and in most cases less than \$2 in a pay period, this condition allows for employees' payroll to be inaccurate and does not provide a consistent methodology across all schools and employees.
- There is no standardized schedule of hourly rates to ensure consistent pay to employees in the same job classification.

FCMAT randomly selected four employees per school for testing, a total of 32 employees in Magnolia's July payroll. The testing process included comparing the wages/salaries as listed in the Paychex payroll registers to Magnolia's April 11, 2015 MPS Pay Raise Salary Scale spreadsheets and 2014-15 or 2015-16 Offer of At-Will Employment to identify any discrepancies. FCMAT recalculated payroll benefit amounts based on the gross pay listed in the Paychex payroll registers to ensure accuracy and then traced the amounts shown on the Paychex payroll registers to Magnolia's general ledger. FCMAT found the following anomalies in the payroll items sampled:

- Four employees were paid gross wages for which Magnolia did not provide FCMAT with supporting documentation for the amount. Magnolia's failure to substantiate the gross wages could result in over- or under-payments to employees as well as inaccurate withholding and payments for statutory benefits. FCMAT did not make any further evaluation regarding the gross wages.

- Five employees were paid at an hourly rate. FCMAT was provided with timesheets for two of the five. One was completed via Vertex42.com and included the employee's name, hours worked per day and total for the period as well as signatures from the employee and supervisor. The other was a manual timesheet that did not include the employee's name, the number of hours worked per day or total for the period. Each arrival time was signed by the employee, and the supervisor signed the timesheet. Neither timesheet provided the hourly wage to be paid or calculations to tie it to the payroll register. Magnolia did not provide FCMAT with the timesheets submitted and used to calculate the gross wages paid for the remaining three employees.
- Two employees were paid an amount for declination of health insurance benefits that did not conform to the \$150 per month as posted in the Magnolia Public Schools Employee Handbook 2015-16. FCMAT reviewed copies of each employee's signed declination of coverage that indicated payments for less than \$150 were based on the employee declining specific items: one declined medical insurance and the other declined dental and vision. Magnolia reported that this was the rationale behind the partial payments; however, FCMAT found nothing in the handbook to support the practice.
- Three employees received a sum for vacation pay. While FCMAT was provided with a spreadsheet that showed the amount paid, there was no backup documentation such as absence records provided to support the amount reflected in the spreadsheet.
- Six employees were paid sums for vacation cash out that did not match the absence records provided to FCMAT. Two employees were overpaid: one for \$125 and another for \$94. Four employees were underpaid: two for \$750, one for \$188 and another for \$94.
- Six employees received a stipend payment. FCMAT requested supporting documentation for the amount paid, and while Magnolia supplied summer school sign-in sheets, invoices and a timesheet, none tied back to the amounts paid to employees. No documentation related to a stipend was provided.
- Five classified employees' wages reflected no payment to PERS. FCMAT inquired about why each particular employee did not qualify for PERS. Magnolia and EdTec staff reported that EdTec was responsible to monitor hourly employees to determine when or if they reached 1,000 hours for inclusion in PERS. However, Magnolia maintained no documentation regarding any individual employee's inclusion in PERS.
- One employee's record on the Paychex Payroll Report showed that state disability was not paid on their wages. Magnolia reported that these taxes had been paid through the August 2015 payroll for this employee. FCMAT reviewed both payrolls for the month of August and found that only the taxes due on the employee's wages paid for that specific payroll period were paid. No other amounts were added for July 2015.
- MSA 7 – FCMAT was unable to trace the employer's STRS and PERS expense from the Paychex payroll register to the general ledger due to differing amounts for these items between the payroll register and the general ledger. Through consultation with EdTec, it was determined that \$910.74 of PERS expense was reported as STRS expense. EdTec reported that it would post a correcting journal entry in Magnolia's April 2016 financial statements.
- All Schools – The employer's expense for workers compensation insurance is not included in the monthly payroll calculations and deductions completed by Paychex. Instead, monthly payments

are made to the insurance carrier, CharterSafe, and then reconciled after the end of the fiscal year. Due to this practice, FCMAT is unable to test this aspect of payroll.

Recommendations

The charter schools should:

1. Include a specific implementation date and language to identify the positions/classifications affected on all board agenda items related to payroll increases.
2. Carefully review base salaries to ensure against over- and under-payments.
3. Carefully review their application of the points associated with employee qualifications pay to ensure that the final calculation complies with the formula approved by the board in the 2015-16 Pay Raise Salary Scale.
4. Develop a salary schedule for positions with hourly rates of pay.
5. Ensure that supporting documentation exists for all elements of a payroll transaction including gross pay, whether that is salary or timesheet/hourly pay, payroll increases/changes, PERS/STRS, declination of health insurance, vacation pay and stipends. Keep such items in individual payroll files.
6. Carefully review the payroll registers to ensure that all required statutory benefits are paid.
7. Review the payroll registers in conjunction with the journal entries made by EdTec to ensure that payroll information has been correctly recorded in the general ledger.

Accounts Payable

FCMAT reviewed July 2015 financial system reports provided by Magnolia and performed the following procedures:

- Analyzed data in the general ledger reports and selected a sample of individual transactions for review, including checks issued for accounts payable transactions, journal entries, and Automated Clearing House (ACH) electronic transactions. The general ledger has the following types of accounts payable document numbers:
 - Check – used for an ACH or electronic payment.
 - Bill Payment – used for a paper check.
 - Journal – used for a journal entry.
- Requested from Magnolia all supporting documentation for each selected transaction.
- Reviewed documentation received for each transaction to determine whether:
 - Authorization was obtained and documented in advance of the expenditure.
 - Goods or services were received and an obligation was incurred.
 - Invoices and/or agreements were reviewed and approved for payment.
 - Transactions were processed timely, accurately and properly recorded.

A combined sample of 133 transactions was tested for all eight schools: 38 checks/ACH, 33 bill payments, and 62 journals. FCMAT tested the transactions for the following attributes and found exceptions as indicated below for each school:

1. No signed requisition was used to start the purchase.
2. No purchase order was attached.
3. The purchase order was dated after receipt of the item/service.
4. The service contract was not signed by both parties (charter signatory and consultant).
5. A signed contract for ongoing services was not present and signed by an authorized Magnolia Science Academy (MSA) signatory.
6. The invoice or detailed receipt was not attached.
7. The invoice was not initialed or signed to approve payment or a receiving document was not attached.
8. The invoice or detailed receipt was not stamped "Paid."
9. The invoice was not paid timely.
10. Other, not described above.

Of the 133 transactions tested, 41 (31%) were traced and agreed to source documentation and did not include exceptions. The remaining 92 transactions had one or more exceptions per transaction.

MSA 1

Fifteen transactions were selected, including six checks/ACH, four bill payments, and five journals. Four of the 15 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 6, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- One check and one bill payment were issued for an amount different than the invoice.
- Two payments were made to vendors using a debit card, and no vendor name was printed on the purchase order.
- One monthly ACH payment was made without an invoice. A copy of the bank statement was attached; however, that is not proper documentation for the transaction.
- Journals did not include descriptions and detail on the general ledger.

MSA 2

Eighteen transactions were selected, including three checks/ACH, eight bill payments, and seven journals. Six of the 18 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 3, 5, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- One transaction included a purchase order that was issued on the invoice date. Payment was requested by the payee and did not include a second authorizer.
- One transaction was listed as uncategorized.

- Journals did not include descriptions and detail on the general ledger.

MSA 3

Twenty-one transactions were selected, including 10 checks/ACH and 11 journals. Nine of the 21 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 3, 7, 8 as enumerated above, and/or the following Other exceptions:

- ACH transfers were listed as checks on the general ledger.
- A temporary clearing account was used for transactions paid by ACH until correct account codes are provided and charged.
- Journals did not include descriptions and detail on the general ledger.

MSA 4

Thirteen transactions were selected, including three checks/ACH, two bill payments, and eight journals. Six of the 13 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 5, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- One payment was issued for an amount different from the invoice total.
- A temporary clearing account was used for transactions paid by ACH until correct account codes are provided and charged.
- Journals did not include descriptions and detail on the general ledger.

MSA 5

Thirteen transactions were selected, including four checks/ACH, two bill payments, and seven journals. Four of the 13 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 5, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- Journals did not include descriptions and detail on the general ledger. Follow-up comments provided to FCMAT indicated that MSA51004 was a withdrawal, but no supporting documentation was supplied.
- A temporary clearing account was used for transactions paid by ACH until correct account codes are provided and charged.
- One transaction was listed as uncategorized.

MSA 6

Eighteen transactions were selected, including seven bill payments and 11 journals. Six of the 18 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 5, 6, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- One payment was issued from an estimate; no invoice was attached.
- Three journals were listed as uncategorized.
- Journals did not include descriptions and detail on the general ledger. Follow-up comments provided to FCMAT indicated that MSA61018 and MSA61017 were withdrawals and MSA61008 was an “R/C of deposit,” but no supporting documentation was supplied.

MSA 7

Seventeen transactions were selected, including eight bill payments and nine journals. Three of the 17 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 4, 5, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- Check requests were not signed.
- One purchase order did not have the vendor name printed on it, and the payment was processed from an e-mail requesting payment.
- Payment to an individual for home visits was made through the accounts payable process.
- One journal was listed as uncategorized.
- Journals did not include descriptions and detail on the general ledger. Follow-up comments provided to FCMAT indicated ACH payments to GE Capital and QuickBooks, but no supporting documentation was supplied.

MSA 8

Eighteen transactions were selected, including 12 checks/ACH and six journals. Three of the 18 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 3, 6, 7, 8 as enumerated above, and/or the following Other exceptions:

- Journals did not include descriptions and detail on the general ledger. Follow-up comments provided to FCMAT indicated that MSA81002 was for charter management organization (CMO) fees and MSA81003 was a withdrawal, but no supporting documentation was supplied.
- Two debit card transactions for travel exceeded the purchase order amount.
- A bank statement was used as a receipt.
- A temporary clearing account was used for transactions paid by ACH until correct account codes are provided and charged.

The charter schools' accounts payable process begins with a request entered in the purchasing system (COOLSIS) and electronically routed for approval. Once the purchase is approved the items are ordered. When items are received a check request is prepared and approved electronically, and then payment is processed in the EdTec financial system. The purchasing system tracks each step of the process and provides an opportunity for comments and notations. The invoice is not signed by the receiving party but is attached to the check request. Some of the charter schools do not require a wet signature on the check request, but rather rely on electronic approvals. Invoices are not stamped "paid" at the time payment is made to the vendor.

Best accounting practices require a signature of the person reviewing the receiver document and/or the invoice to indicate it has been verified for accuracy and the goods/services have been received. It is then forwarded to accounts payable for payment. When payment is generated the invoice is stamped "paid."

Magnolia Public Schools Accounting Policies, Procedures and Forms, SOP#PUR104 Revision:2 states, "All accounts payable and cash disbursements will have documented pre-approval" and "Approvals for reimbursement requests must be obtained prior to purchase." The standard operating procedure (SOP) also states, "The quantities shown shipped or delivered on the invoice will be compared to the packing slip and/or receiving reports if items have been received by the designee of each site." The SOP further states that accounts payable invoices should normally be paid within seven days or sooner of the payment

term and invoices are to be stamped “paid” once processed. The sampling of transactions shows that the SOP and best accounting practices are not consistently followed. For example, invoices are not signed indicating they have been compared to the receiving document, some check requests do not have hard signatures, and invoices are not stamped “paid.”

Magnolia allows the use of debit cards, and numerous debit card transactions are used for Amazon purchases and travel expenses. According to Magnolia’s SOP, all accounts payable and cash disbursements will be preapproved. However, the use of debit cards does not follow this procedure. For example, MSA 8 made 234 debit card transactions to Amazon without prior approval, and 221 of the transactions were for less than \$5.00 each.

Electronic transfers/ACH are processed for monthly ongoing expenses as well as one-time payments. These expenses do not have prior approval. Contracts or agreements for these expenses should be renewed annually, or as applicable, if the service is to continue, and purchase orders should be created and approved annually. Payments can then be referenced to the purchase order when posted to the general ledger.

Journal entries are assigned a unique number at each charter school. The documents provided to FCMAT included a printed document number on the general ledger but no description or detail was recorded, making it difficult to determine the source of the entry. This process requires additional documentation to be provided to verify entries. These entries include but are not limited to: payroll and payroll expenses, textbook purchases, CMO fees, apportionments, property tax, and temporary clearing. It is important to include a brief description for each general ledger entry to provide for proper review and analysis.

The charter schools use a temporary clearing account for posting some general ledger entries, and ACH activities for each week are entered as one journal number. The amounts recorded represent actual cash transactions that have occurred in the bank per retrieval of cash activities from the online banking portal. EdTec staff indicated the entry is done so the most accurate depiction of cash balances in the accounting system is available while awaiting the details from the school. These entries are later moved without detail to expense accounts, making it challenging to follow the trail of entries. Staff indicated that DB manual check cover sheets are created; however, these cover sheets are not attached to the transaction.

The process of posting journal entries to the general ledger based on information directly from the bank account poses concerns. Without prior approval for the purchase and a reported delay of up to seven days prior to reversing the original entry, reviewing each transaction and posting them to the correct expense accounts, there is an increased opportunity for fraud. In addition, when the reversal of the journal entry occurs in the following month, it is more challenging to balance the bank statement to the general ledger and complete the reconciliation.

Some school expenses are coded to “uncategorized expense.” When the correct account is determined, the expense is transferred. If expense reports are run prior to moving the transactions to the correct account, the account totals are inaccurate. All purchases should be preapproved with the correct account code to eliminate the need to post transactions as uncategorized.

FCMAT’s review of the sampled transactions indicates that some payments were not made timely. Best practices provide for the payment of undisputed invoices within 30 days of the invoice date.

Recommendations

The charter schools should:

1. Ensure that all purchases and disbursements, including debit card transactions, have documented preapproval, which includes a purchase order and/or contract.
2. Ensure that the person approving an invoice for payment signs it stating it is accurate and has been verified.
3. Stamp invoices “paid” once processed.
4. Include the description and detail of journal entries on the general ledger rather than leaving these items blank.
5. Process transactions with the appropriate account code rather than as uncategorized or through a temporary clearing account.
6. Renew contracts, as applicable, and complete purchase orders annually for monthly ongoing expenses, including ACH transfers.
7. Include the vendor name on all purchase orders, including those for debit card purchases.
8. Pay invoices timely.
9. Use separate and distinct transaction type names in the general ledger for ACH transfers and paper checks.
10. Process check requests only with authorizing signatures.
11. Ensure that payments are made from invoices, not estimates.
12. Ensure that notations are made on invoices if the payment amount differs from the invoice amount.
13. Determine if payments to individuals for home visits should be made through the payroll process.
14. Obtain proper authorization and increase the purchase order amount if a transaction exceeds the initial authorized amount.
15. Require itemized receipts or invoices for transactions, and do not make payments based on bank statements.

Bank Statements and Reconciliations

FCMAT reviewed July 2015 bank statements, reconciliation detail reports and general ledgers provided by Magnolia. Each bank statement was compared to the general ledger to match each transaction. Each reconciliation detail report was also compared to the bank statement and general ledger to match transactions, identify outstanding transactions, and determine whether the reconciliation detail report balanced to the general ledger. FCMAT found the following anomalies in the items reviewed:

MSA 1

- Twenty-five transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal.
- Withdrawal transactions on the bank statement had no description on the general ledger.
- Journal 11042 for \$33,853.63 was posted as uncleared for 6/30/15 on the reconciliation detail report. A second journal was posted as cleared for \$81.98. Sufficient detail was not provided to determine what was carried over from 2014-15 and what would continue to clear in future months.

MSA 2

- Twenty-four transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal.
- Withdrawal transactions on the bank statement had no description on the general ledger.
- DOM Wire did not have a description on the general ledger.
- Journal 21033 was outstanding from 6/30/15 and did not have detail to determine what would continue to clear in future months.

MSA 3

- Thirty-four transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal.
- Withdrawal transactions on the bank statement had no description on the general ledger.
- A difference of \$21,754.51 was posted to the general ledger from the bank statement for payroll, and was entered as an outstanding item on the reconciliation. FCMAT could not determine if this amount was for manual paper checks with the documentation provided.
- Detail was not provided to determine what would continue to clear in future months for the following outstanding debits:
 - Journal MSA31048, \$15 and \$6,115.27
 - Journal MSA31031, \$6,343.72
 - Journal MSA31001, \$21,754.51

MSA 4

- Twenty transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal.
- There was a difference of \$224.93 between the general ledger and the bank statement. This was listed as an outstanding deposit on the reconciliation, but was not an entry on the general ledger.
- Detail was not provided to determine what would continue to clear in future months for the following outstanding debits:

- Journal MSA41028, \$2,023.57
- Journal MSA41006, \$8,917.53
- Journal MSA41001, \$22,566.32

MSA 5

- Seventeen transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal.
- An outstanding deposit of \$525 dated 6/30/15 was entered on the reconciliation but could not be verified on the general ledger.
- Detail was not provided to determine what would continue to clear in future months for the following outstanding debits:
 - Journal MSA51027, \$6,134.38
 - Journal MSA51027, \$893.59
 - Journal MSA51001, \$6,685.54

MSA 6

- Seven transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal.
- Detail was not provided to determine what would continue to clear in future months for the following outstanding debits:
 - Journal MSA61025, \$3,253.22
 - Journal MSA61021, \$3,318.42
 - Journal MSA61021, \$135.41

MSA 7

- Bank statement balance (\$1,090,316.22) did not agree to the reconciliation or general ledger balances (\$1,088,129.33).
- Reconciliation listed payroll adjustment of \$11,184.08; however, it is unclear which journal in the general ledger included this transaction.
- Twenty-six transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal.
- Withdrawal transactions on the bank statement had no description on the general ledger.
- Detail was not provided to determine what would continue to clear in future months for the following outstanding debits:
 - Journal MSA71023, \$22,901.79
 - Journal MSA71023, \$1,563.22

- Journal MSA71123, \$688.93

MSA 8

- Detail was not provided to determine what would continue to clear in future months for the following outstanding debits:
 - Journal MSA81017, \$4,713.69
 - Journal MSA81001, \$13,870.74
 - Journal MSA 81006, \$30,077.64

FCMAT was unable to verify whether some of the transactions from the general ledger cleared in the bank account because multiple bank transactions were included as one journal entry on the general ledger, without individual check numbers or amounts. As many as 34 transactions on one bank statement were combined and posted as one journal entry to the general ledger, without detail. In addition, the reconciliation detail report showed journals of outstanding items to balance the general ledger and bank statement. These journals did not include the detail necessary to provide an audit trail of the cleared transactions and transactions that were carried to the following month. FCMAT requested but was not provided detail for these journals.

EdTec staff indicated that the ACH activities for the week that cleared the bank but were not yet entered in the general ledger are entered as one lump sum temporary journal that is then reversed several days later. At the time of reversal the temporary journal is cleared and the expense objects are debited and cash is credited with a unique debit transaction number (DB). However, when the reversal is done in the following month, the total is listed as an outstanding debit on the reconciliation detail report to balance the general ledger to the bank statement. Therefore, it is difficult to reconcile the bank statement without substantial supporting documentation.

The reconciliation detail reports and general ledgers do not have adequate descriptions for transactions, and the document numbers on the reconciliation detail reports do not consistently match those shown on the bank statements. Transactions cannot be verified without check numbers or descriptions of ACH transfers. Without detail for the journal entries, it is difficult to determine what has cleared the bank and what is outstanding and carried forward to the next month to properly verify transactions and balance the general ledger to the bank statement and complete the reconciliation detail report.

The total payroll amount is posted to the general ledger; however, manual payroll checks that have not cleared the bank account are shown on the reconciliation as uncleared and balances are carried to the next month. For example, Journal MSA21004 Payroll posted to the general ledger for \$149,921.16. The payroll expense on the bank statement through Paychex Inc. is \$130,716.18. An entry was recorded as cleared on the reconciliation detail report for \$130,716.18, and another entry was recorded as uncleared for \$19,204.98. Without a description or manual check numbers for the uncleared entry, it is difficult to verify the amount that cleared the following month.

The reconciliation detail report should reflect actual deposits and expense transactions. The total deposits on the reconciliation detail report should equal the total deposits on the bank statement, and the same for expenses. Adjusting journals posted to the general ledger as a “cleared deposit” should only be for items identified as deposits on the bank statement. However, numerous items were corrected by posting the same amount as a “cleared check.” This increased the total for both deposits and cleared checks or payments. If a deposit is posted in error, the correction should also be made as an adjustment to deposits,

not expenses. The method used reflects incorrect totals and makes it difficult to verify transactions. For example, Journal MSA81031 was posted as a cleared deposit for \$7,918.19 and also posted as Journal MSA81076 as a cleared check on both the reconciliation detail report and the general ledger.

EdTec prepares the monthly reconciliation detail reports. These reports are provided to Magnolia staff for review and comparison to the general ledger and bank statements for accuracy. The reports do not include staff signatures verifying they have been reviewed and that the totals agree with the general ledger and bank statements.

Recommendations

The charter schools should:

1. Include a description for each transaction on the general ledger and reconciliation detail report.
2. Include the details of checks and payments for journals posted to the general ledger. If posted as one large sum, include the breakdown of individual transactions in backup documentation.
3. Include outstanding items by individual check number on the reconciliation detail report to properly verify when each item has cleared the bank.
4. Include manual check numbers on entries to the reconciliation detail report for uncleared payroll expenses.
5. Post corrections to the general ledger using the same account code as the original transaction.
6. Ensure that the monthly bank statement is reconciled to the general ledger and that all transactions on the reconciliation detail report are also reflected on the general ledger.
7. Include the signatures of the individual who prepared the bank statement reconciliation and the individual who reviewed/approved it, and the respective dates of same, on the reconciliation documents.

Revenue, Journal Entries and Financial Statements

FCMAT used the following processes in its review of July 2015 revenue and journal entry transactions and financial statements:

- General Ledger Revenue – Reviewed revenue transactions from the general ledger and requested supporting documentation for those items chosen for testing. Analyzed documentation to verify the accuracy of amounts posted to the general ledger, determine whether appropriate account number(s) were used to post revenue, and check the reasonableness of amounts posted based on the number of students served by the charter school.
- General Ledger Journal Entries – Selected journal entries from the general ledger and requested backup documentation for those items chosen for testing. Evaluated backup documents for adequate support and/or explanation for the journal posting, including amount and account number verification and appropriateness of the posting.

- Cash Flow Statement – Evaluated operating activities for reasonableness based on expected revenue streams for charter schools and the number of students served. Verified whether cash flow statement amounts matched the general ledger and income statement, and whether receivables, liabilities, and the beginning and ending cash balances matched the general ledger and balance sheet.
- Income Statement – Evaluated reasonableness of amounts based on expected cash flow and the number of students served. Reviewed whether amounts matched applicable categories in the general ledger.
- Balance Sheet – Reviewed reasonableness of balance sheet and whether amounts matched applicable categories in the general ledger.
- Budget to Actuals – Compared actuals-to-date from the general ledger to the applicable budget categories. Reviewed whether expenses were within budget and revenues were appropriate based on expected cash flow and the number of students served.

FCMAT found the following anomalies in the items sampled and reviewed:

- General – The general ledgers do not have adequate descriptions for revenue transactions and journal entries. This makes it time consuming to find the offsetting entry to verify whether revenues and journal entries have been accurately posted. For example, when verifying a credit to cash made via a journal entry, the offsetting debit to another account must be reviewed. A matching description on the entries makes it easier to find in the general ledger. It is also a standard practice to provide descriptions for general ledger entries. Magnolia staff indicated that the information may be in the description/memo fields of other reports, but this does not help the reader who only has access to the general ledger.
- General – Payments made to the charter management organization (referred to as the home office) are made via a cash transfer between the home office bank account and the charter school's bank account. This process does not provide for appropriate checks and balances.
- MSA 1 – The general ledger did not match the income statement because uncategorized revenue of \$536 was not moved to object code 4325, instructional materials, in the general ledger. Backup documentation was requested but not provided to FCMAT.
- MSA 3 – A deposit of \$29,731 was posted to uncategorized income; however, the backup documentation provided, an email that requested various amounts on a spreadsheet to be moved from uncategorized income to the proper object/resource, was not sufficient to support the deposit. Therefore, FCMAT was unable to verify revenue.
- MSA 6 – Unable to verify the “Due To School 1” balance of \$181,177 because there was no corresponding entry in the general ledger for MSA 1. Magnolia staff indicated that, “This was from the beginning balance. This question has been asked of the auditor, and EdTec is still waiting for a response.”
- MSA 7 – Unable to verify the accuracy of the general ledger, balance sheet, or cash flow statement because:
 - The ending cash balance on the general ledger of \$1,044,209.18 and the ending balance on the cash flow statement of \$1,088,818.26 differed by \$44,609.08. The balance sheet dated

7/31/2015 showed cash in bank of \$1,088,818.26 and an audit adjustment of \$40,504.26, which was most of the difference.

- The accounts receivable totals on the general ledger and the balance sheet differed by \$11,543.
- The audit adjustment of \$40,504.26 was noted on the balance sheet but was not posted to the general ledger. Magnolia staff indicated that the general ledger still “does not have the JE to true-up beginning balance.” Magnolia provided another general ledger to FCMAT; however, it appeared to be the same document as originally provided.
- Document number 44973 posted charter school expense of \$1,390 to object 9200 instead of object 5861, which was used at the other charter schools.

In July 2015 EdTec began providing back office services for the charter schools. Financial statement balances were moved to EdTec’s financial system while Magnolia staff were closing the books for 2014-15. Staff indicated that this transition period may have affected the amounts shown on the general ledgers and financial statements provided to FCMAT, as well as the lack of descriptions for journal entries posted to the general ledger.

Recommendations

The charter schools should:

1. Provide verbiage in the Name column of the general ledger for revenues and journal entries, and include the description and detail for these transactions.
2. Make payments to the charter management organization (home office) using the accounts payable process with appropriate approvals, rather than through a cash transfer between the applicable bank accounts.
3. Process transactions with the appropriate account code rather than as uncategorized.
4. Train staff to properly account for and post transactions, including those for loans between charter schools and audit adjustments, to ensure beginning and ending balances are accurate on the general ledger and financial statements.

August 2015

Payroll

Payroll Registers

Magnolia had two payroll cycles for all employee classifications during the month of August 2015. The first payroll cycle encompassed August 1 through August 15 but was paid on August 14 due to the 15th having fallen on a Saturday. The second payroll cycle encompassed August 16 through August 31, and employees received their payments on August 31.

FCMAT requested copies of payroll registers for both payroll cycles and found that the payroll periods listed on the reports did not conform to the payroll period being paid. For the payroll period ending on August 15, the payroll register states that the payroll period began on July 24, 2015 and ended on August

8, 2015. For the second payroll ending on August 31, the payroll register states that the payroll period began on August 4, 2015 and ended on August 13, 2015. The check dates were listed on the reports as August 14 and August 31. However, the payroll period dates, as listed, implied that there could be overlaps or missing dates in payroll periods resulting in possible duplicate payroll payments or payment having been missed.

FCMAT inquiries of both Magnolia and EdTec revealed that the report dates were the result of having recently changed payroll processing vendors but that the check dates should have been the controlling information for each report.

Recommendation

The charter schools should:

1. Carefully review payroll registers and any other payroll reports provided by their payroll processor to ensure that they reflect accurate information.

New Employees

FCMAT compared payroll registers from the July 31, 2015 payroll to the August 15, 2015 payroll as well as the August 15, 2015 payroll to the August 31, 2015 payroll to attempt to identify newly hired employees. For each employee paid in either of the August 2015 payrolls who was not included on the immediately prior payroll register, the team requested their employment offer from and contract with Magnolia, signed Form I-9, verification of tuberculosis testing and results, fingerprint and background clearance and certification of membership in the California Public Employees' Retirement System (PERS) or California State Teachers' Retirement System (STRS).

For the month of August 2015, FCMAT identified 18 employees as new by the above process. FCMAT's review of the documentation provided by Magnolia found the following anomalies:

- The Offers of At-Will Employment for
 - Ten offers were dated by the employee after the employee's start date.
 - Five offers did not reflect a signature by Magnolia.
- The At-Will Employment Agreements showed
 - Eleven agreements that had been dated by both the employee and Magnolia after the employee's start date.
 - Two documents that did not reflect a date next to the signature by Magnolia.
 - One document that did not reflect a signature by Magnolia.
 - One agreement that had discrepancies between it and the fingerprint and background clearance regarding the employee's start date.
- Fourteen employees (or 78% of those tested) had Form I-9s that had not been signed by Magnolia within three days of the employee's first date of employment as is required by Section 2 of that form.
- One employee's Form I-9 was missing their date of hire.

- One employee's tuberculosis testing results were not dated until after the employee's start date.

As stated in FCMAT's findings for July 2015, Magnolia reported that none of the employees tested had a PERS/STRS certification form on file and that, at that point in time, no system had been established to track part-time employees for PERS/STRS eligibility. Although the August payroll registers showed PERS/STRS contributions for several of these employees, the lack of certifications and a tracking system for part-time employees raises questions as to whether all of those who qualified to participate in either of these retirement plans were enrolled. Please also see the finding below related to PERS/STRS reporting found during payroll transaction testing.

Recommendations

The charter schools should:

1. Ensure that all new employees complete proper hiring documentation and procedures prior to their first day of work including, but not limited to, signing an offer of employment and employment contract, completion of Form I-9, TB test requirements, fingerprinting and criminal background clearance and completion of a PERS/STRS certification form.
2. Review their employee records to determine the date each eligible employee qualified to participate in PERS/STRS and compare that to the reporting made to the applicable agency. If the charter finds that employees qualified but were not enrolled, or were not enrolled timely, work with PERS/STRS to update reporting and determine if any penalties and/or interest are due.

Payroll Transactions

FCMAT reviewed Magnolia's MPS Employee Pay Raise Scale, adopted on May 2, 2014, to determine the process by which the charter determines employees' pay. Based on the date the scale was adopted, board minutes were reviewed to determine if there had been board-approved changes to salary schedules. On March 25, 2015, the board approved a 1.5% increase to both base pay and employee qualifications pay (EQP). FCMAT's review of the board agenda item provided in support of the salary increase found that its stated budget implications were related to the 2015-16 fiscal year, but it lacked a specific date of implementation and information regarding to which specific employee group(s) the salary increase applied. A 2015-16 Pay Raise Salary Scale was presented to the board on April 15, 2015 to reflect revisions generated by the increases approved on March 25, 2015.

FCMAT reviewed the April 11, 2015 MPS Pay Raise Scale spreadsheets to determine if employees' salaries conformed to the amounts in the 2015-16 Pay Raise Salary Scale and found the following:

- MSA 2 – The following item was identified in conjunction with the July review, but because the employee wasn't paid until August, the finding is included here. The base salary for one English language arts teacher is \$41,615 in the April 11, 2015 MPS Pay Raise Scale spreadsheets but should be \$40,600 based on the school location in the MPS Pay Raise Salary Scale. While this employee was not among the payroll samples tested below, review of the August 15, 2015 payroll register shows that the employee is paid at the higher rate.

- MSA 3 – The following items were identified in conjunction with the July review, but because the employees weren't paid until August, the finding is included here.
 - The base salary for two administrative assistants is \$32,480 in the April 11, 2015 MPS Pay Raise Scale spreadsheets but should be \$29,435 based on the MPS Pay Raise Salary Scale. While these two employees were not among the payroll samples tested below, review of the August 15, 2015 payroll register shows:
 - One administrative assistant is paid a base salary of \$27,936, which is less than the base salary listed in the MPS Pay Raise Salary Scale.
 - One administrative assistant is paid a base salary of \$32,480, which is more than the base salary listed in the MPS Pay Raise Salary Scale.
 - The base salary for an unfilled administrative assistant position is \$27,405 in the spreadsheets, but the MPS Pay Raise Salary Scale reflects a base salary of \$29,435 for this position.
- MSA 7 – One employee's EQP points totaled 9.75. This is in violation of the MPS Pay Raise Salary Scale, which states that this component of salary is to "be rounded to the lower multiple of one-half."
- MSA 8 – One employee's EQP points totaled 6.25. This is in violation of the MPS Pay Raise Salary Scale, which states that this component of salary is to "be rounded to the lower multiple of one-half."
- Multiple employees had EQP that did not conform to Magnolia's formula amounts provided in the 2015-16 Pay Raise Salary Scale. Those increases, as presented to the board, were to be valued at \$508 per point for prior experience for both certificated and classified employees. Magnolia Public Schools experience was to be valued at \$1,015 and \$761 per point for certificated and classified employees, respectively. However, the April 11, 2015 MPS Pay Raise Scale spreadsheets use a \$507.50 value for prior experience for both classes of employees and \$761.25 for MPS experience for classified employees. Rounding after the calculation is made for each employee further complicates the situation. While the differences between the amounts provided to the board and those listed in the April 11, 2015 MPS Pay Raise Scale spreadsheets are minimal, and in most cases less than \$2 in a pay period, this condition allows for employees' payroll to be inaccurate and does not provide a consistent methodology across all schools and employees.
- There is no standardized schedule of hourly rates to ensure consistent pay to employees in the same job classification.

FCMAT randomly selected four employees per school per payroll cycle for testing, a total of 24 employees in Magnolia's August payroll. The testing process included comparing the wages/salaries as listed in the Paychex payroll registers to Magnolia's April 11, 2015 MPS Pay Raise Scale spreadsheets and 2014-15 or 2015-16 Offer of At-Will Employment to identify any discrepancies. FCMAT recalculated payroll benefit amounts based on the gross pay listed in the Paychex payroll registers to ensure accuracy and then traced the amounts shown on the Paychex payroll registers to Magnolia's general ledger. FCMAT found the following anomalies in the payroll items sampled:

- Two classified employees' wages reflected no payment to PERS. FCMAT inquired about why each particular employee did not qualify for PERS. Magnolia and EdTec staff reported that

EdTec was responsible to monitor hourly employees to determine when or if they reached 1,000 hours for inclusion in PERS. However, Magnolia maintained no documentation regarding any individual employee's inclusion in PERS.

In Magnolia's further investigation of whether these two employees qualified for inclusion in PERS, it was discovered that one employee had reached the 1,000 hours qualification threshold in October 2014 but had not been enrolled in PERS until May 15, 2016.

Magnolia reported that it was aware it had not effectively managed enrollment of irregular-basis employees in PERS and was undertaking steps to ensure that all current and previous irregular-basis employees were properly included. Magnolia also acknowledged that it would be responsible for both the employer and employee contributions required to bring these employees up-to-date in PERS. However, Magnolia should be aware that PERS may levy additional sums such as interest and penalties.

- One employee's semi-monthly payroll reflected a deduction for health and welfare insurance; however, the amount deducted was the full monthly employee portion of the insurance premium. This resulted in the employee paying double the amount necessary for health care coverage. Magnolia indicated it was conducting a review of benefit deductions for all employees to ensure that proper amounts were deducted and reported, and that any amounts due to employees would be included in their November 30, 2016 paycheck.
- One employee was paid for two hours of overtime and FCMAT was supplied with a copy of the employee's timesheet, which reflected the additional time worked. After inquiry regarding the calculation of the hourly overtime rate, Magnolia provided FCMAT with a calculation that determined the employee's hourly wage was \$12.44 and concluded that the employee was paid \$13.47 per hour in error. Based on Magnolia's calculation, it appears that the employee was paid at a straight time rate, and the employee's overtime rate was \$18.66 per hour. While the employee was paid in error, that error was not an overpayment as Magnolia reported to FCMAT but an underpayment of \$5.19 per hour.
- One employee's timesheet reflected she worked 7.0 hours on one day (a start time of 9 a.m. and an end time of 4 p.m.) but did not reflect a start and stop time for a meal period as required by Labor Code Section 512 and the California Industrial Welfare Commission Wage Orders. Pursuant to Labor Code Section 226.7, if the employer fails to provide meal or rest/recovery breaks in accordance with state law, "the employer shall pay the employee one additional hour of pay at the employee's regular rate of compensation for each workday that the meal or rest or recovery period is not provided." Magnolia reported to FCMAT that not all timesheets for the period reviewed contained recorded start/stop times for meal/rest periods and that, beginning in 2016-17, employees are required to track their meal periods.
- All Schools – The employer's expense for workers compensation insurance is not included in the monthly payroll calculations and deductions completed by Paychex. Instead, monthly payments are made to the insurance carrier, CharterSafe, and then reconciled after the end of the fiscal year. Due to this practice, FCMAT is unable to test this aspect of payroll.

Recommendations

The charter schools should:

1. Include a specific implementation date and language to identify the positions/classifications affected on all board agenda items related to payroll increases.
2. Carefully review base salaries to ensure against over- and underpayments.
3. Carefully review their application of the points associated with employee qualifications pay to ensure that the final calculation complies with the formula approved by their board in the 2015-16 Pay Raise Salary Scale.
4. Develop a salary schedule for positions with hourly rates of pay.
5. Conduct a thorough audit of all employees to ensure proper enrollment in the applicable retirement system, and be prepared to pay the employer and employee share of contributions to date as well as any interest and penalties levied by PERS.
6. Review all health and welfare benefits deductions made to employee payroll to ensure that proper amounts were withheld and return any overages to employees immediately.
7. Ensure that supporting documentation exists for all elements of a payroll transaction including gross pay, whether that is salary or timesheet/hourly pay, payroll increases/changes, PERS/STRS, declination of health insurance, vacation pay and stipends. Keep such items in individual payroll files.
8. Carefully review the payroll registers to ensure that all required statutory benefits are paid.
9. Develop a timesheet/time keeping system that tracks employees' start/stop times for meal/rest periods.

Accounts Payable

FCMAT reviewed August 2015 financial system reports provided by Magnolia and performed the following procedures:

- Analyzed data in the general ledger reports and selected a sample of individual transactions for review, including checks issued for accounts payable transactions, journal entries, and Automated Clearing House (ACH) electronic transactions. The general ledger has the following types of accounts payable document numbers:
 - Check – used for an ACH or electronic payment.
 - Bill Payment – used for a paper check.
 - Journal – used for a journal entry
- Requested from Magnolia all supporting documentation for each selected transaction.
- Reviewed documentation received for each transaction to determine whether:

- Authorization was obtained and documented in advance of the expenditure.
- Goods or services were received and an obligation was incurred.
- Invoices and/or agreements were reviewed and approved for payment.
- Transactions were processed timely, accurately and properly recorded.

A combined sample of 62 transactions was tested for MSA 6, MSA 7, and MSA 8: 14 checks/ACH, 20 bill payments, and 28 journals. FCMAT tested the transactions for the following attributes and found exceptions as indicated below for each school:

1. No signed requisition was used to start the purchase.
2. No purchase order was attached.
3. The purchase order was dated after receipt of the item/service.
4. The service contract was not signed by both parties (charter signatory and consultant).
5. A signed contract for ongoing services was not present and signed by an authorized Magnolia Science Academy signatory.
6. The invoice or detailed receipt was not attached.
7. The invoice was not initialed or signed to approve payment or a receiving document was not attached.
8. The invoice or detailed receipt was not stamped “paid.”
9. The invoice was not paid timely.
10. Other, not described above.

Of the 62 transactions tested, 15 (24%) were traced and agreed to source documentation and did not include exceptions. The remaining 47 transactions had one or more exceptions per transaction.

MSA 6

Thirteen transactions were selected, including one check/ACH, five bill payments, and seven journals. Four of the 13 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 3, 7, 8 as enumerated above, and/or the following Other exceptions:

- A temporary clearing account was used for transactions paid by ACH until correct account codes are provided and charged.
- One transaction was listed as uncategorized.

MSA 7

Twenty transactions were selected, including seven checks/ACH, five bill payments, and eight journals. Five of the 20 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 6, 7, 8 as enumerated above, and/or the following Other exceptions:

- A temporary clearing account was used for transactions paid by ACH until correct account codes are provided and charged.

- Four transactions were listed as uncategorized.

MSA 8

Twenty-nine transactions were selected, including six checks/ACH, 10 bill payments, and 13 journals. Six of the 29 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 4, 5, 7, 8 as enumerated above, and/or the following Other exceptions:

- A temporary clearing account was used for transactions paid by ACH until correct account codes are provided and charged.
- Requisition dated in May for eighth-grade graduation using fundraising funds. Order was placed and paid for in August, after graduation.
- Eleven journal transactions were listed as uncategorized.

The charter schools' accounts payable process begins with a request entered in the purchasing system (COOLSIS) and electronically routed for approval. Once the purchase is approved the items are ordered. When items are received a check request is prepared and approved electronically, and then payment is processed in the EdTec financial system. The purchasing system tracks each step of the process and provides an opportunity for comments and notations. The invoice is not signed by the receiving party but is attached to the check request. Some of the charter schools do not require a wet signature on the check request, but rather rely on electronic approvals. Invoices are not stamped "paid" at the time payment is made to the vendor.

Best accounting practices require a signature of the person reviewing the receiver document and/or the invoice to indicate it has been verified for accuracy and the goods/services have been received. It is then forwarded to accounts payable for payment. When payment is generated the invoice is stamped "paid."

Magnolia Public Schools Accounting Policies, Procedures and Forms, SOP#PUR104 Revision:2 states, "All accounts payable and each cash disbursements will have documented pre-approval" and "Approvals for reimbursement requests must be obtained prior to purchase." The standard operating procedure (SOP) also states, "The quantities shown shipped or delivered on the invoice will be compared to the packing slip and/or receiving reports if items have been received by the designee of each site." The SOP further states that accounts payable invoices should normally be paid within seven days or sooner of the payment term and invoices are to be stamped "paid" once processed. The sampling of transactions shows that the SOP and best accounting practices are not consistently followed. For example, invoices are not signed indicating they have been compared to the receiving document, some check requests do not have hard signatures, and invoices are not stamped "paid."

Magnolia allows the use of debit cards, and numerous debit card transactions are used for online purchases including, but not limited to, Amazon, Barnes and Noble, Wal-Mart, Michaels, Scholastic Inc., and Lakeshore Learning. According to Magnolia's SOP, all accounts payable and cash disbursement will be preapproved. However, the use of debit cards does not follow this procedure. For example, MSA 7 made 24 debit card transactions without prior approval.

Electronic transfers/ACH are processed for monthly ongoing expenses as well as one-time payments. These expenses do not have prior approval. Contracts or agreements for these expenses should be renewed annually or as applicable if the service is to continue, and purchase orders should be created and approved annually. Payments can then be referenced to the purchase order when posted to the general ledger.

The charter schools use a temporary clearing account for posting some general ledger entries, and ACH activities for each week are entered as one journal number. The amounts recorded represent actual cash transactions that have occurred in the bank per retrieval of cash activities from the online banking portal. EdTec staff indicated the entry is done so the most accurate depiction of cash balances in the accounting system is available while awaiting the details from the school. These entries are later moved without detail to expense accounts, making it challenging to follow the trail of entries. Staff indicated that DB manual check cover sheets are created; however, these cover sheets were not attached to the transaction.

The process of posting journal entries to the general ledger based on information directly from the bank account poses concerns. Without prior approval for the purchase and a reported delay of up to seven days prior to reversing the original entry, reviewing each transaction and posting them to the correct expense accounts, there is an increased opportunity for fraud. In addition, when the reversal of the journal entry occurs in the following month, it is more challenging to balance the bank statement to the general ledger and complete the reconciliation.

Some school expenses are coded to “uncategorized expense.” When the correct account is determined, the expense is transferred. If expense reports are run prior to moving the transactions to the correct account, the account totals are inaccurate. All purchases should be preapproved with the correct account code to eliminate the need to post transactions as uncategorized.

Recommendations

The charter schools should:

1. Ensure that all purchases and disbursements, including debit card transactions, have documented preapproval, which includes a purchase order and/or contract.
2. Ensure that the person approving an invoice for payment signs it stating it is accurate and has been verified.
3. Stamp invoices “paid” once processed.
4. Require itemized receipts or invoices for transactions, and discontinue making payments based on bank statements.
5. Process transactions with the appropriate account code rather than as uncategorized or through a temporary clearing account.
6. Renew contracts, as applicable, and complete purchase orders annually for monthly ongoing expenses, including ACH transfers.
7. Include the vendor name on all purchase orders, including those for debit card purchases.
8. Use separate and distinct transaction type names in the general ledger for ACH transfers and paper checks.
9. Process check requests only with authorizing signatures.
10. Pay invoices timely.
11. Expend fundraising dollars in the appropriate fiscal year.

Bank Statements and Reconciliations

FCMAT reviewed August 2015 bank statements, reconciliation detail reports and general ledgers provided by Magnolia. Each bank statement was compared to the general ledger to match each transaction. Each reconciliation detail report was also compared to the bank statement and general ledger to match transactions, identify outstanding transactions, and determine whether the reconciliation detail report balanced to the general ledger. FCMAT found the following anomalies in the items reviewed:

MSA 6

- Reconciliation detail report does not have descriptions; only document numbers are referenced.
- Five transactions on the bank statement were combined and posted to the general ledger. Two versions of the general ledger were submitted to FCMAT. The second general ledger included descriptions and check numbers, which allowed FCMAT to verify transactions, but the report did not include beginning and ending balances.
- Journal MSA61025 continued to carry over from 6/30/2015 as uncleared, and detail was not provided for this transaction to determine if it would clear in future months.
- Journal MSA61034 was posted as a deposit as well as an expense. The total of these two entries equals the Paychex withdrawal shown on the bank statement.

MSA 7

- The bank statement and reconciliation detail report balance (\$1,023,780.51) did not agree with the general ledger balance (\$995,273.98).
- Journals MSA71123 and MSA71023 continued to carry over from 2014-15 as uncleared, and detail was not provided for these transactions to determine what would clear in future months.
- Reconciliation detail report does not have descriptions; only document numbers are referenced.
- Ten transactions on the bank statement were combined and posted to the general ledger. Two versions of the general ledger were submitted to FCMAT. The second general ledger included descriptions and check numbers, which allowed FCMAT to verify transactions, but the report did not include beginning and ending balances.
- Journal MSA71046 was included on the first general ledger submitted, but not the second. Other documents, such as the bank reconciliation, were not updated to match the updated general ledger.

MSA 8

- Reconciliation detail report does not have descriptions; only document numbers are referenced.
- Multiple transactions on the bank statement were combined and posted to the general ledger as one entry without descriptions or check numbers. Therefore, it is difficult to determine what transactions are included in the journal. Two versions of the general ledger were submitted to FCMAT. The second general ledger included descriptions and check numbers, which allowed FCMAT to verify transactions, but the report did not include beginning and ending balances.
- Check numbers are not sequential, and journals posted do not have descriptions that include check numbers, making it difficult to determine what has cleared and what is outstanding.

FCMAT was unable to verify whether some of the transactions from the general ledger cleared in the bank account because multiple bank transactions were included as one journal entry on the general ledger, without individual check numbers or amounts. As many as 10 transactions on one bank statement were combined and posted as one journal entry to the general ledger, without detail. In addition, the reconciliation detail report showed journals of outstanding items to balance the general ledger and bank statement. These journals did not include the detail necessary to provide an audit trail of the cleared transactions and transactions that were carried to the following month. FCMAT requested but was not provided detail for these journals.

EdTec staff indicated that the ACH activities for the week that cleared the bank but were not yet entered in the general ledger are entered as one lump sum temporary journal that is then reversed several days later. At the time of reversal the temporary journal is cleared and the expense objects are debited and cash is credited with a unique debit transaction number (DB). However, when the reversal is done in the following month, the total is listed as an outstanding debit on the reconciliation detail report to balance the general ledger to the bank statement. Therefore, it is difficult to reconcile the bank statement without substantial supporting documentation.

The reconciliation detail reports and general ledgers lack adequate descriptions for transactions, and the documentation numbers on the reconciliation detail reports do not consistently match those shown on the bank statements. Transactions cannot be verified without check numbers or descriptions of ACH transfers. Without detail for the journal entries, it is difficult to determine what has cleared the bank and what is outstanding and carried forward to the next month to properly verify transactions and balance the general ledger to the bank statement and complete the reconciliation detail report.

The total payroll amount is posted to the general ledger; however, manual payroll checks that have not cleared the bank account are shown on the reconciliation as uncleared and balances carried to the next month. For example, Journal MSA61034 Payroll posted to the general ledger for \$22,718.66. The payroll expense on the bank statement through Paychex Inc. is \$19,085.69. An entry was recorded as cleared on the reconciliation detail report for \$20,462.86, and another entry was recorded as uncleared for \$3,253.22. An additional journal was posted as a cleared deposit of \$1,377.17. Without a description or manual check numbers for the uncleared entry, it is difficult to verify the amount that cleared the following month.

The reconciliation detail report should reflect actual deposits and expense transactions. The total deposits on the reconciliation detail report should equal the total deposits on the bank statement, and the same for expenses. Adjusting journals posted to the general ledger as a “cleared deposit” should only be for items identified as deposits on the bank statement. The method used reflects incorrect totals and makes it difficult to verify transactions. For example, Journal MSA61034 was posted as a cleared deposit for \$1,377.17 to correct a payroll expense posting.

EdTec prepares the monthly reconciliation detail reports. These reports are provided to Magnolia staff for review and comparison to the general ledger and bank statements for accuracy. The reports do not include staff signatures verifying they have been reviewed and that the totals agree with the general ledger and bank statements.

Recommendations

The charter schools should:

1. Include a description for each transaction on the general ledger and reconciliation detail report.
2. Include the details of checks and payments for journals posted to the general ledger. If posted as one large sum, include the breakdown of individual transactions in backup documentation.
3. Include outstanding items by individual check number on the reconciliation detail report to properly verify when each item has cleared the bank.
4. Include manual check numbers on entries to the reconciliation detail report for uncleared payroll expenses.
5. Post corrections to the general ledger using the same account code as the original transaction.
6. Ensure that the monthly bank statement is reconciled to the general ledger and that all transactions on the reconciliation detail report are also reflected on the general ledger.
7. Include the signatures of the individual who prepared the bank statement reconciliation and the individual who reviewed/approved it, and the respective dates of same, on the reconciliation documents.
8. Ensure that all affected reports are updated when a financial document such as the general ledger is updated. For example, if a cash entry is changed in the general ledger after the bank reconciliation is completed, then the bank reconciliation must be updated so that month-end cash matches.

Revenue, Journal Entries and Financial Statements

FCMAT used the following processes in its review of August 2015 revenue and journal entry transactions and financial statements:

- General Ledger Revenue – Reviewed revenue transactions from the general ledger and requested supporting documentation for those items chosen for testing. Analyzed documentation to verify the accuracy of amounts posted to the general ledger, determine whether appropriate account number(s) were used to post revenue, and check the reasonableness of amounts posted based on the number of students served by the charter school.
- General Ledger Journal Entries – No journal entries pertaining to revenue transactions were selected for review.
- Cash Flow Statement – Evaluated operating activities for reasonableness based on expected revenue streams for charter schools and the number of students served. Verified whether cash flow statement amounts matched the general ledger and income statement, and whether

receivables, liabilities, and the beginning and ending cash balances matched the general ledger and balance sheet.

- Income Statement – Evaluated reasonableness of amounts based on expected cash flow and the number of students served. Reviewed whether amounts matched applicable categories in the general ledger.
- Balance Sheet – Reviewed reasonableness of balance sheet and whether amounts matched applicable categories in the general ledger.
- Budget to Actuals – Compared actuals-to-date from the general ledger to the applicable budget categories. Reviewed whether expenses were within budget and revenues were appropriate based on expected cash flow and the number of students served.

FCMAT found the following anomalies in the items sampled and reviewed:

- General – Payments made to the charter management organization (referred to as the home office) are made via a cash transfer between the home office bank account and the charter school's bank account. This process does not provide for appropriate checks and balances.
- MSA 6 – Unable to verify the Due To amount and accounts receivable balances because:
 - The "Due To School 1" balance of \$181,176.82 had no corresponding entry in the general ledger for MSA 1. Magnolia staff indicated that "This was from the beginning balance. This question has been asked of the auditor, and EdTec is still waiting for a response." The backup document provided (Account QuickReport for MSA 6 for 6/30/2015) showed this balance as a MSA 6 Loan Payable with a memo saying it was to be reclassified. It is unclear what the status of this loan was on August 31, and the August 2015 general ledger for MSA 1 did not show any activity or balance in the Due From object code.
 - There are negative accounts receivable balances on the general ledger and the balance sheet for the following objects:
 - 9212 AR - Title II of \$17.00 (MSA61010)
 - 9230 AR - State Aid of \$105,381.00 (MSA61009)
 - 9233 AR - Lottery of \$6,832.64 (MSA61010)

These postings should have cleared accounts receivable amounts set up for the 2014-15 year end. It appears these amounts were not set up in the prior year, or were set up under an incorrect object. These balances will remain outstanding until correct postings are made to the general ledger.

- MSA 7 – Unable to verify accuracy of the general ledger, balance sheet, or cash flow statement because:
 - The beginning cash balance on the general ledger was \$1,044,209.18 and the beginning balance on the cash flow statement was \$1,088,818.26, a difference of \$44,609.08. This difference was noted in the July 2015 findings.
 - The ending cash balance on the general ledger was \$979,860.36 while the ending cash balance on both the cash flow statement and balance sheet reflected \$1,024,469.44, a difference of \$44,609.08.

- The accounts receivable total on the general ledger was \$138,769.22 and the balance sheet receivables showed \$150,312.48, a difference of \$11,543.26.
- The accounts payable/accrued accounts payable total on the general ledger was \$832,349.76 and the balance sheet showed \$847,940.87, a difference of \$15,591.11.
- The accounts payable-other total on the general ledger was \$396.73 and the balance sheet showed \$453.70, a difference of \$56.97.
- An audit adjustment of \$40,504.26 was reflected on the balance sheet but was not posted in the general ledger. As noted in the July 2015 findings: Magnolia staff indicated that the general ledger still “does not have the JE to true-up beginning balance.”
- The beginning fund balance, audit adjustment, and net income shown on the balance sheet were the same as the July amounts so did not match the cash flow or income statements. The statements did not match the updated general ledger dated September 29, 2016.
- Document #45191 was incorrectly posted to other local revenue object 8699 on 8/11/2015. This was a vendor reimbursement for overpayment made by the charter school. Reimbursement should have been posted to offset the expense object it was originally paid from. The posting error caused an \$8,313.45 overstatement of both revenue and expense for the month.
- No backup documentation was provided for two deposits posted on 8/31/2015: Doc #45706 for \$231.00 (uniforms) and Doc #45705 for \$163.00 (fundraising).
- MSA 8 – Unable to verify accounts receivable and accounts payable balances because:
 - There are negative balances on the general ledger and balance sheet for objects:
 - 9213 AR - Title III of \$139.00 (Doc #45435)
 - 9295 Due from Other Funds of \$0.02 (From prior year posting)
 - 9540 Payroll Liability - Federal of \$1,980.61 (MSA81018 and MSA81027)
 - 9550 Retirement Liability - PERS of \$2,648.87 (MSA81004)
 - 9555 Retirement Liability - STRS of \$21,657.20 (MSA81004)

These postings should have cleared accounts receivable or current liability amounts set up for a prior period. It appears these amounts were not set up, or were set up under an incorrect object code. These balances will remain outstanding until correct postings are made to the general ledger.
- No backup documentation was provided for the 8/18/2015 deposit: Document #45436 for \$396.99 in uncategorized revenue.

In July 2015 EdTec began providing back office services for the charter schools. Financial statement balances were moved to EdTec's financial system while Magnolia staff were closing the books for 2014-15. Staff indicated that this transition period may have affected the amounts shown on the general ledgers and financial statements provided to FCMAT.

Recommendations

The charter schools should:

1. Make payments to the charter management organization (home office) using the accounts payable process with appropriate approvals, rather than through a cash transfer between the applicable bank accounts.
2. Review and verify that all monthly statement amounts match what is posted to the general ledger for that month.
3. Process transactions with the appropriate account code rather than as uncategorized.
4. Ensure interschool loans are accounted for accurately and timely at each school, and for each month there was activity. This will ensure loans between Magnolia schools are balanced.
5. Ensure that receipts posted to accounts receivable accounts clear the amounts originally set up for that receivable, and that the postings are accurate and timely. Post any differences between what was expected to be received and what was actually received to current year revenue.
6. Ensure that payments posted to liability accounts clear the amounts originally set up for that liability, and that the postings are accurate and timely. Post any differences between what was expected to be paid and what was actually paid to current year expense.
7. Train staff to properly account for and post transactions such as the following:
 - a. Loans between charter schools
 - b. Audit adjustments
 - c. Set up and clearing of accounts receivables and liabilities
 - d. Obtaining necessary backup documents to post income and expenditures without using “uncategorized” account codes
 - e. Monthly review and verification of financial statements
8. Provide necessary oversight to ensure monthly postings are appropriate and complete, transactions are posted to the correct object codes, and all financial statements match the general ledger.
9. Scan or file all backup documentation timely to prevent misplaced support items.

May 2016

Payroll

Payroll Registers

Magnolia had two payroll cycles for all employee classifications during the month of May 2016. The first payroll cycle encompassed May 1 through May 15 but was paid on May 13 due to the 15th having fallen on a Sunday. The second payroll cycle encompassed May 16 through May 31. While payroll reports were produced and dated May 27, 2016, due to planned absences by charter employees who processed payroll, employees received their payments on May 31.

FCMAT requested copies of payroll registers for both payroll cycles and found that several were missing signatures and dates from the person who prepared the payroll, the person who approved the payroll or both.

FCMAT inquiries of Magnolia revealed that this was an error in their process/procedures and that they have taken steps to ensure that the payroll registers will be signed and dated by the CFO on an ongoing basis.

Recommendation

The charter schools should:

1. Carefully review payroll registers prior to submittal for processing to ensure that the signatures of both the person who prepared the payroll and the person who approved the payroll are contained on the documents.

New Employees

FCMAT compared payroll registers from the April 30, 2016 payroll to the May 13, 2016 payroll as well as the May 13, 2016 payroll to the May 27, 2016 payroll to attempt to identify newly hired employees. No new employees were identified. Consequently, no additional testing was performed.

Payroll Transactions

FCMAT reviewed Magnolia's MPS Employee Pay Raise Scale, adopted on May 2, 2014, to determine the process by which the charter determines employees' pay. Based on the date the scale was adopted, board minutes were reviewed to determine if there had been board approved changes to salary schedules. On March 25, 2015, the board approved a 1.5% increase to both base pay and employee qualifications pay (EQP). FCMAT's review of the board agenda item provided in support of the salary increase found that its stated budget implications were related to the 2015-16 fiscal year, but it lacked a specific date of implementation and information regarding to which specific employee group(s) the salary increase applied. A 2015-16 Pay Raise Salary Scale was presented to the board on April 15, 2015 to reflect revisions generated by the increases approved on March 25, 2015.

FCMAT reviewed the April 11, 2015 MPS Pay Raise Scale spreadsheets to determine if employees' salaries conformed to the amounts in the 2015-16 Pay Raise Salary Scale and found the following:

- Multiple employees continued to have EQP that did not conform to Magnolia's formula amounts provided in the 2015-16 Pay Raise Salary Scale. Those increases, as presented to the

board, were to be valued at \$508 per point for prior experience for both certificated and classified employees. Magnolia Public Schools experience was to be valued at \$1,015 and \$761 per point for certificated and classified employees, respectively. However, the April 11, 2015 MPS Pay Raise Scale spreadsheets use a \$507.50 value for prior experience for both classes of employees and \$761.25 for MPS experience for classified employees. Rounding after the calculation is made for each employee further complicates the situation. While the differences between the amounts provided to the board and those listed in the April 11, 2015 MPS Pay Raise Scale spreadsheets are minimal, and in most cases less than \$2 in a pay period, this condition allows for employees' payroll to be inaccurate and does not provide a consistent methodology across all schools and employees.

- There also continues to be no standardized schedule of hourly rates to ensure consistent pay to employees in the same job classification.

FCMAT randomly selected four employees per school per payroll cycle for testing, a total of 24 employees in Magnolia's May payroll. The testing process included comparing the wages/salaries as listed in the Paycom payroll registers to Magnolia's April 11, 2015 MPS Pay Raise Scale spreadsheets and 2014-15 or 2015-16 Offer of At-Will Employment to identify any discrepancies. FCMAT recalculated payroll benefit amounts based on the gross pay listed in the Paycom payroll registers to ensure accuracy and then traced the amounts shown on the Paycom payroll registers to Magnolia's general ledger. FCMAT found the following anomalies in the payroll items sampled:

- One hourly employee's timesheet failed to reflect supervisor approval.
- Two employees' timesheets did not reflect a total of the hours worked, which can allow for errors in processing.
- One employee's timesheet reflected 37.5 hours of work, but the employee was paid for 38 hours pursuant to the Paycom payroll register. Magnolia was unable to provide FCMAT with documentation supporting the additional 0.5 hour paid but provided the explanation that this was a keying error.
- One employee's timesheet reflected 62.5 hours of work, after the deduction of 30 minutes each day for a meal period. However, the timesheet did not provide space for the start/end time for meal periods to verify they were taken. The payroll register showed the employee was paid for 62 hours due to a math error on the timesheet. Neither the employee nor his supervisor signed the timesheet.
- Five employees' timesheets reflected their work hours but did not reflect a start and stop time for a meal period as required by Labor Code Section 512 and the California Industrial Welfare Commission Wage Orders. Magnolia did not have a consistent timesheet form during the period being tested. Some simply record the start/stop time for each day, others include a column for overtime hours and yet another form includes start/end time for meal periods. Having a consistent form for all schools ensures that meal times are recorded and lessens calculation errors in payroll processing. Magnolia reported to FCMAT that all timesheets for the period reviewed did not record start/stop times for meal/rest periods and that, beginning in 2016-17, employees are required to track their meal periods.
- One employee's offer letter contained line items that should have totaled \$50,500 in annual wages; however, the total listed on the offer letter was \$55,000. Magnolia's research revealed that

the correct amount was \$50,500. Using that number, FCMAT computed the bimonthly salary for this employee to be \$2,104.17 -- \$50,500 divided by 12 months and then divided by two pay periods per month. The Paycom payroll register reflected a bimonthly salary of \$2,083.33. Magnolia asserted that the employee's payroll should be divided by 22 pay periods; however, that would produce an amount of \$2,295.45 per pay period. FCMAT requested further research on the issue, but Magnolia was unable to provide FCMAT with an explanation for the discrepancy.

- Four certificated employees were paid stipends ranging from \$100 - \$400. Magnolia allows each school to set its own stipend schedule. However, Magnolia was unable to either provide FCMAT with the stipend schedules or documentation showing that the governing board had approved them.
- One classified employee's wages reflected no payment to PERS. FCMAT inquired about why this employee did not qualify for PERS. Magnolia and EdTec staff had previously reported that EdTec was responsible to monitor hourly employees to determine when or if they reached 1,000 hours for inclusion in PERS. However, Magnolia maintained no documentation regarding any individual employee's inclusion in PERS.

In Magnolia's further investigation of whether this employee qualified for inclusion in PERS, it was discovered that the employee had reached the 1,000 hours qualification threshold effective April 2016. Magnolia reported that it was aware it had not effectively managed enrollment of irregular-basis employees in PERS and was undertaking steps to ensure that all current and previous irregular-basis employees were properly included. Magnolia also acknowledged that it would be responsible for both the employer and employee contributions required to bring these employees up-to-date in PERS. However, Magnolia should be aware that PERS may levy additional sums such as interest and penalties.

- Five employees' employer contributions for PERS were calculated incorrectly in the Paycom payroll registers. Instead of using PERS' employer contribution rate of 11.847%, that number was rounded up to 11.85%. FCMAT inquired regarding which percentage was paid to PERS and Magnolia provided an Excel spreadsheet that was used for their calculation and payment of the PERS contribution. However, based on the documentation provided, FCMAT was unable to determine the exact amount that was paid to PERS. While Magnolia may not use the Paycom payroll register to remit the PERS contribution, it is used to post the PERS payroll expense to Magnolia's general ledger, and those same amounts are used in Magnolia's income statements. FCMAT reviewed the general ledger and balanced the Paycom payroll register to the entries in the general ledger. No adjustments to the general ledger were made to decrease the PERS expense to 11.847%. Consequently, the PERS expense in Magnolia's general ledger is overstated.
- Two employees' payrolls did not reflect withholding for state disability insurance, which would result in overpayments to these employees. Magnolia did not provide FCMAT with an explanation for this discrepancy.
- One employee's payroll withholding for state disability insurance (SDI) was underpaid by \$0.12. Magnolia's explanation was that their SDI rate was 0.89% instead of the 0.90% that had been used for all other employees tested. FCMAT requested documentation to support the change in rate, but none was provided.
- One regular certificated employee had Social Security taxes withheld from their paycheck although Magnolia is a STRS employer, and it is very rare for a certificated employee to

contribute into the Social Security system when the employer participates in STRS. Magnolia attributed this error to problems with the data transfer between Paychex and Paycom. During a telephone conference on the subject, Magnolia reported that the amount had been corrected on the employee's W-2, and they would have the funds returned to them via their personal tax return. However, it is unknown if Magnolia corrected the employer side of the transaction to obtain a return of the funds it paid on behalf of this employee.

- One employee's payroll did not reflect withholding for Medicare, which would result in an overpayment to this employee. Magnolia did not provide FCMAT with an explanation for this discrepancy.
- One employee's payroll withholding for Medicare was underpaid by \$0.18 due to using 1.4416% instead of the mandated 1.45%. All other employees tested reflected 1.45% withholding from their wages. Magnolia was unable to provide FCMAT with an explanation of why a different rate was used for this employee.
- One school's payroll Excel sheet noted a "spreadsheet error" and did not tie to the gross payroll reflected in the Paycom payroll register. Magnolia explained that there had been an error on the spreadsheet and provided FCMAT with the corrected spreadsheet and an e-mail that explained the error. Both of these documents should be kept with the original spreadsheet and payroll register in the file for the payroll period to provide a complete payroll file. This is especially significant given the personnel turnover that Magnolia has experienced to ensure that a record is kept to support financial transactions.
- All Schools
 - The employer's expense for workers compensation insurance is not included in the monthly payroll calculations and deductions completed by Paycom. Instead, monthly payments are made to the insurance carrier, CharterSafe, and then reconciled after the end of the fiscal year. Due to this practice, FCMAT is unable to test this aspect of payroll.
 - FCMAT's review of the May payroll registers revealed that state unemployment insurance had not been paid for any employee. Magnolia reported that this should have been reported and paid quarterly on form DE-9423. However, because of mistakes made during the implementation of its new payroll/hours system, payments had not been made. Magnolia further reported to FCMAT that processes and procedures had been corrected and implemented and payments were being brought current. FCMAT's requests for further details about how processes/procedures were changed, when past due payments were made and whether penalties were assessed were not answered.

Recommendations

The charter schools should:

1. Include a specific implementation date and language to identify the positions/classifications affected on all board agenda items related to payroll increases.
2. Carefully review base salaries to ensure against over- and underpayments.

3. Carefully review its application of the points associated with employee qualifications pay to ensure that the final calculation complies with the formula approved by the board in the 2015-16 Pay Raise Salary Scale.
4. Develop a salary schedule for positions with hourly rates of pay.
5. Ensure that both the employee and their supervisor execute all timesheets.
6. Carefully review, verify and math check all timesheets to ensure proper payment to employees.
7. Develop a timesheet/time keeping system to track employees' start/stop times for meal/rest periods.
8. Ensure that supporting documentation exists for all elements of a payroll transaction including gross pay, whether that is salary, stipends or timesheet/hourly pay, payroll increases/changes, PERS/STRS, declination of health insurance, vacation pay and stipends. Keep such items in individual payroll files. Items associated with rates of pay such as salary or stipend schedules and hourly pay rates should also reflect approval by the governing board.
9. Reconcile the amounts paid to employees with the amounts contained in the employees' final offer letters to resolve rounding and keying errors in gross wages. Ensure payment shortfalls are returned to employees and overpayments are collected from employees.
10. Conduct a thorough audit of all employees to ensure proper enrollment in the applicable retirement system, and be prepared to pay the employer and employee share of contributions to date as well as any interest and penalties levied by PERS.
11. Reconcile and adjust the general ledger PERS expense to the amounts actually paid.
12. Carefully review the payroll registers to ensure that all required statutory benefits are paid and that proper percentages are used in their calculation.
13. Ensure payroll report files include documentation of any corrections made to provide a complete record of the transaction.

Accounts Payable

FCMAT reviewed May 2016 financial system reports provided by Magnolia and performed the following procedures:

- Analyzed data in the general ledger reports and selected a sample of individual transactions for review, including checks issued for accounts payable transactions, journal entries, and Automated Clearing House (ACH) electronic transactions. The general ledger has the following types of accounts payable document numbers:
 - Check – used for an ACH or electronic payment.
 - Bill Payment – used for a paper check.

- Journal – used for a journal entry.
- Requested from Magnolia all supporting documentation for each selected transaction.
- Reviewed documentation received for each transaction to determine whether:
 - Authorization was obtained and documented in advance of the expenditure.
 - Goods or services were received and an obligation was incurred.
 - Invoices and/or agreements were reviewed and approved for payment.
 - Transactions were processed timely, accurately and properly recorded.

A combined sample of 55 transactions was tested for MSA 6, MSA 7, and MSA 8: 16 checks/ACH, 24 bill payments, and 15 journals. FCMAT tested the transactions for the following attributes and found exceptions as indicated below for each school:

1. No signed requisition was used to start the purchase.
2. No purchase order was attached.
3. The purchase order was dated after receipt of the item/service.
4. The service contract was not signed by both parties (charter signatory and consultant).
5. A signed contract for ongoing services was not present and signed by an authorized Magnolia Science Academy signatory.
6. The invoice or detailed receipt was not attached.
7. The invoice was not initialed or signed to approve payment or a receiving document was not attached.
8. The invoice or detailed receipt was not stamped “paid.”
9. The invoice was not paid timely.
10. Other, not described above.

Of the 55 transactions tested, 15 (27%) were traced and agreed to source documentation and did not include exceptions. The remaining 40 transactions had one or more exceptions per transaction.

MSA 6

Fourteen transactions were selected, including three checks/ACH, eight bill payments, and three journals. Three of the 14 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 3, 6, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- Magnolia Educational and Research Foundation (MERF) transfer and MERF expense allocation transfer did not have board approval attached.
- Three purchase order/requisition forms did not include the vendor’s name, only the requestor’s name.

MSA 7

Twenty-one transactions were selected, including five checks/ACH, 11 bill payments, and five journals. Eleven of the 21 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- MERF loan transfer and MERF expense allocation transfer did not have board approval attached.
- Invoice for check DB051216 was requested by FCMAT but not provided.
- One reimbursement request form did not include the vendor's name. Another document did show the payee name.

MSA 8

Twenty transactions were selected, including eight checks/ACH, five bill payments, and seven journals. One of the 20 transactions had no exceptions. The remaining transactions included one or more of exceptions 1, 2, 3, 6, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- One reimbursement request form did not include the vendor's name. Another document did show the payee name.
- An automatic deduction was made from the checking account with no invoice or explanation provided.
- MERF loan transfer and MERF expense allocation transfer did not have board approval attached.

The charter schools' accounts payable process begins with a request entered in the purchasing system (COOLSIS) and electronically routed for approval. Once the purchase is approved the items are ordered. When items are received a check request is prepared and approved electronically, and then payment is processed in the EdTec financial system. The purchasing system tracks each step of the process and provides an opportunity for comments and notations. The invoice is not signed by the receiving party but is attached to the check request. Some of the charter schools do not require a wet signature on the check request, but rather rely on electronic approvals. Invoices are not stamped "paid" at the time payment is made to the vendor.

Best accounting practices require a signature of the person reviewing the receiver document and/or the invoice to indicate it has been verified for accuracy and the goods/services have been received. It is then forwarded to accounts payable for payment. When payment is generated the invoice is stamped "paid."

Magnolia Public School Accounting Policies, Procedures and Forms, SOP#PUR104 Revision:2 states, "All accounts payable and cash disbursements will have documented pre-approval" and "Approvals for reimbursement requests must be obtained prior to purchase." The standard operating procedure (SOP) also states, "The quantities shown shipped or delivered on the invoice will be compared to the packing slip and/or receiving reports if items have been received by the designee of each site." The SOP further states that accounts payable invoices should normally be paid within seven days or sooner of the payment term and invoices are to be stamped "paid" once processed. The sampling of transactions shows that the SOP and best accounting practices are not consistently followed. For example, invoices are not signed indicating they have been compared to the receiving document, some check requests do not have hard signatures, and invoices are not stamped "paid."

Magnolia allows the use of debit cards, and numerous debit card transactions are used for online purchases including but not limited to Amazon, Barnes and Noble, Wal-Mart, Michaels, Scholastic Inc.,

and Lakeshore Learning. According to Magnolia's SOP, all accounts payable and cash disbursement will be preapproved. However, the use of debit cards does not follow this procedure. For example, MSA 8 made 24 debit card transactions without prior approval.

Electronic transfers/ACH are processed for monthly ongoing expenses as well as one-time payments. These expenses do not have prior approval. Contracts or agreements for these expenses should be renewed annually, or as applicable, if the service is to continue, and purchase orders should be created and approved annually. Payments can then be referenced to the purchase order when posted to the general ledger.

The charter schools use a temporary clearing account for posting some general ledger entries, and ACH activities for each week are entered as one journal number. The amounts recorded represent actual cash transactions that have occurred in the bank per retrieval of cash activities from the online banking portal. EdTec staff indicated the entry is done so the most accurate depiction of cash balances in the accounting system is available while awaiting the details from the school. These entries are later moved without detail to expense accounts, making it challenging to follow the trail of entries. Staff indicated that DB manual check cover sheets are created; however, these cover sheets were not attached to the transaction.

The process of posting journal entries to the general ledger based on information directly from the bank account poses concerns. Without prior approval for the purchase and a reported delay of up to seven days prior to reversing the original entry, reviewing each transaction and posting them to the correct expense accounts, there is an increased opportunity for fraud. In addition, when the reversal of the journal entry occurs in the following month, it is more challenging to balance the bank statement to the general ledger and complete the reconciliation.

Some school expenses are coded to “uncategorized expense.” When the correct account is determined, the expense is transferred. If expense reports are run prior to moving the transactions to the correct account, the account totals are inaccurate. All purchases should be preapproved with the correct account code to eliminate the need to post transactions as uncategorized.

FCMAT's review of the sampled transactions indicates that some payments were not made timely. Best practices provide for the payment of undisputed invoices within 30 days of the invoice date.

Recommendations

The charter schools should:

1. Ensure that all purchases and disbursements, including debit card transactions, have documented preapproval, which includes a purchase order and/or contract.
2. Ensure that the person approving an invoice for payment signs it stating it is accurate and has been verified.
3. Stamp invoices “paid” once processed.
4. Process transactions with the appropriate account code rather than as uncategorized or through a temporary clearing account.
5. Renew contracts, as applicable, and complete purchase orders annually for monthly ongoing expenses, including ACH transfers.

6. Include the vendor name on all purchase requisitions, purchase orders, payment and reimbursement requests, including those for debit card purchases.
7. Pay invoices timely.
8. Use separate and distinct transaction type names in the general ledger for ACH transfers and paper checks.
9. Process check requests only with authorizing signatures.
10. Require itemized receipts or invoices for transactions, and do not make payments based on bank statements.
11. Include the board approval date and/or excerpt from the board meeting minutes as backup documentation for those items that require board approval.

Bank Statements and Reconciliations

FCMAT reviewed May 2016 bank statements, reconciliation detail reports and general ledgers provided by Magnolia. Each bank statement was compared to the general ledger to match each transaction. Each reconciliation detail report was also compared to the bank statement and general ledger to match transactions, identify outstanding transactions, and determine whether the reconciliation detail report balanced to the general ledger. FCMAT found the following anomalies in the items reviewed:

MSA 6

- Journal MSA61025 for \$55.71 was posted as uncleared for 6/30/15 on the reconciliation detail report. Sufficient detail was not provided to determine what was carried over from 2014-15 and what would continue to clear in future months. This amount was included as an outstanding debit to balance the general ledger to the bank statement.

MSA 7

- Journal MSA71023 for \$14,298.81 was posted as uncleared for 6/30/15 on the reconciliation detail report. Sufficient detail was not provided to determine what was carried over from 2014-15 and what would continue to clear in future months. This amount was included as an outstanding debit to balance the general ledger to the bank statement.

MSA 8

Detail was not provided to determine what was carried over from 2014-15 and what would continue to clear in future months. Detail was also not provided for outstanding debits for 2015-16 items older than six months. The following amounts were included to balance the general ledger to the bank statement:

MSA81017	6/30/15	\$2,140.00
MSA81032	8/14/15	\$ 358.26 (payroll)
MSA81103	11/13/15	\$ 148.86 (payroll)
Bill Payment 82137	9/2/15	\$ 25.00

The reconciliation detail report showed journals of outstanding items to balance the general ledger and bank statement. These journals did not include the detail necessary to provide an audit trail of the cleared transactions and transactions that were carried to the following month.

The reconciliation detail report should reflect actual deposits and expense transactions. The total deposits on the reconciliation detail report should equal the total deposits on the bank statement, and the same for expenses. Adjusting journals posted to the general ledger as a “cleared deposit” should only be for items identified as deposits on the bank statement. However, numerous items were corrected by posting the same amount as a “cleared check.” This increased the total for both deposits and cleared checks or payments. If a deposit is posted in error, the correction should also be made as an adjustment to deposits, not expenses. The method used reflects incorrect totals and makes it difficult to verify transactions. For example, Journal MSA71007 was posted as a cleared deposit for \$16,548.36 and also posted as Journal MSA71008 as a cleared check on both the reconciliation detail report and the general ledger.

EdTec prepares the monthly reconciliation detail reports. These reports are provided to Magnolia staff for review and comparison to the general ledger and bank statements for accuracy. The reports do not include staff signatures verifying they have been reviewed and that the totals agree with the general ledger and bank statements.

Recommendations

The charter schools should:

1. Include outstanding items by individual check number on the reconciliation detail report to properly verify when each item has cleared the bank.
2. Post corrections to the general ledger using the same account code as the original transaction.
3. Ensure that the monthly bank statement is reconciled to the general ledger and that all transactions on the reconciliation detail report are also reflected on the general ledger.
4. Include the signatures of the individual who prepared the bank statement reconciliation and the individual who reviewed/approved it, and the respective dates of same, on the reconciliation documents.

Revenue, Journal Entries and Financial Statements

FCMAT used the following processes in its review of May 2016 revenue and journal entry transactions and financial statements:

- General Ledger Revenue – Reviewed revenue transactions from the general ledger and requested supporting documentation for those items chosen for testing. Analyzed documentation to verify the accuracy of amounts posted to the general ledger, determine whether appropriate account number(s) were used to post revenue, and check the reasonableness of amounts posted based on the number of students served by the charter school.
- General Ledger Journal Entries – Selected journal entries from the general ledger and requested backup documentation for those items chosen for testing. Evaluated backup documents for adequate support and/or explanation for the journal posting, including amount and account number verification and appropriateness of the posting.
- Cash Flow Statement – Evaluated operating activities for reasonableness based on expected revenue streams for charter schools and the number of students served. Verified whether cash

flow statement amounts matched the general ledger and income statement, and whether receivables, liabilities, and the beginning and ending cash balances matched the general ledger and balance sheet.

- Income Statement – Evaluated reasonableness of amounts based on expected cash flow and the number of students served. Reviewed whether amounts matched applicable categories in the general ledger.
- Balance Sheet – Reviewed reasonableness of balance sheet and whether amounts matched applicable categories in the general ledger.
- Budget to Actuals – These documents were not provided for May 2016.

FCMAT found the following anomalies in the items sampled and reviewed:

- General – Payments made to the charter management organization (referred to as MERF or the home office) are made via a cash transfer between the home office bank account and the charter school's bank account. This process does not provide for appropriate checks and balances.
- General – MERF does not provide sufficient backup documentation when billing the charter schools for items or when making loans between itself and the charters. Sufficient documentation for expenses paid by MERF on behalf of the charter schools should have a signed and dated invoice sheet showing expenses to be repaid and how expenses were allocated to each charter, copies of the invoices paid by MERF, a charter approved purchase order with the account codes to be charged, and when applicable, an excerpt showing the board approval date. Documentation for loans between MERF and its charters should include a board approved loan agreement signed by both parties, the approved repayment schedule, a purchase order with the appropriate account code and a notation as to which payment is being made. If a payment schedule is revised – for example, when a charter has insufficient cash to make the scheduled payment – the backup documents should clearly show that change.
- MSA 6
 - Uncategorized revenue from April was still not cleared by the end of May.
 - Unable to verify monthly budget to actual data by object because information was not provided.
 - Unable to read signatures on several documents, and there was no printed name and/or signature date on them. For example: MSA61226 shows the same illegible signature used in place of both Terri Boatman and Oswaldo Diaz. One printed name was crossed out, the other said "for Terri Boatman," and the signer did not print their name. On the second page of this journal entry, Terri Boatman signed but there was no signature for Oswaldo Diaz. Documents MSA61231 and MSA61232 were signed but no printed names were noted, only titles. There were no written dates showing when these documents were signed.

- MSA 7
 - Unable to verify monthly budget to actual data by object because information was not provided.
 - Unable to read signatures on several documents, and there was no printed name and/or signature date on them. For example: Document #58369 included a deposit log that was unsigned. MSA71225, MSA71226 and MSA71227 were signed but no printed names were noted, only titles. There were no written dates showing when these documents were signed.
- MSA 8
 - Unable to verify monthly budget to actual data by object because information was not provided.
 - Unable to read signatures on several documents, and there was no printed name and/or signature date on them. For example: MSA81242, MSA81246 and MSA81259 were signed but no printed names were noted, only titles. There were no written dates showing when these documents were signed.

Recommendations

The charter schools should:

1. Make payments to the charter management organization (MERF/home office) using the accounts payable process with appropriate documentation and approvals, rather than through a cash transfer between the applicable bank accounts.
2. Ensure interschool loans and loans between a charter school and MERF are sufficiently documented, accounted for accurately and timely, and paid back via the accounts payable process.
3. Process transactions with the appropriate account code rather than as uncategorized.
4. Prepare monthly budget to actual data by object for ongoing review and analysis.
5. Ensure that signed documents include the printed name of the signor and date signed.

June 2016

Payroll

Payroll Registers

Magnolia had three payroll cycles during the month of June 2016. Two payroll cycles mirrored those in other months, encompassing June 1 through June 15 and June 16 through June 30 for all employee classifications. FCMAT's review of Magnolia's general ledger also revealed a significant payroll event on June 10. Magnolia stated this was due to payroll processing for involuntarily terminated employees as of the last day of school. Magnolia did not provide FCMAT with documentation of the June 10 payroll or

additional information regarding why a separate payroll was necessary and could not be combined with the June 15 payroll. Consequently, FCMAT was unable to perform testing on the June 10 payroll.

FCMAT received copies of payroll registers for the June 1-15 and June 16-30, 2016 payroll cycles and found that those for the June 30 payroll were missing the dates of the signatures from the people who prepared the payroll and the person who approved the payroll.

FCMAT inquiries of Magnolia revealed that this was an error in their process/procedures and that they have taken steps to ensure that the payroll registers will be signed and dated by the preparer as well as the CFO on an ongoing basis.

Recommendation

The charter schools should:

1. Carefully review payroll registers prior to submittal for processing to ensure that the signatures of both the person who prepared the payroll and the person who approved the payroll are contained on the documents.

New Employees

FCMAT compared payroll registers from the May 31, 2016 payroll to the June 15, 2016 payroll as well as the June 15, 2016 payroll to the June 30, 2016 payroll to attempt to identify newly hired employees. No new employees were identified. Consequently, no additional testing was performed.

Payroll Transactions

FCMAT reviewed Magnolia's MPS Employee Pay Raise Scale, adopted on May 2, 2014, to determine the process by which the charter determines employees' pay. Based on the date the scale was adopted, board minutes were reviewed to determine if there had been board approved changes to salary schedules. On March 25, 2015, the board approved a 1.5% increase to both base pay and employee qualifications pay (EQP). FCMAT's review of the board agenda item provided in support of the salary increase found that its stated budget implications were related to the 2015-16 fiscal year, but it lacked a specific date of implementation and information regarding to which specific employee group(s) the salary increase applied. A 2015-16 Pay Raise Salary Scale was presented to the board on April 15, 2015 to reflect revisions generated by the increases approved on March 25, 2015.

FCMAT reviewed the April 11, 2015 MPS Pay Raise Scale spreadsheets to determine if employees' salaries conformed to the amounts in the 2015-16 Pay Raise Salary Scale and found the following:

- Multiple employees continued to have EQP that did not conform to Magnolia's formula amounts provided in the 2015-16 Pay Raise Salary Scale. Those increases, as presented to the board, were to be valued at \$508 per point for prior experience for both certificated and classified employees. Magnolia Public Schools experience was to be valued at \$1,015 and \$761 per point for certificated and classified employees, respectively. However, the April 11, 2015 MPS Pay Raise Scale spreadsheets use a \$507.50 value for prior experience for both classes of employees and \$761.25 for MPS experience for classified employees. Rounding after the calculation is made for each employee further complicates the situation. While the differences between the amounts provided to the board and those listed in the April 11, 2015 MPS Pay Raise Scale spreadsheets are minimal, and in most cases less than \$2 in a pay period, this condition allows for employees'

payroll to be inaccurate and does not provide a consistent methodology across all schools and employees.

- There also continues to be no standardized schedule of hourly rates to ensure consistent pay to employees in the same job classification.

FCMAT randomly selected four employees per school per payroll cycle for testing, a total of 24 employees in Magnolia's June payroll. The testing process included comparing the wages/salaries as listed in the Paycom payroll registers to Magnolia's April 11, 2015 MPS Pay Raise Scale spreadsheets and 2014-15 or 2015-16 Offer of At-Will Employment to identify any discrepancies. FCMAT recalculated payroll benefit amounts based on the gross pay listed in the Paycom payroll registers to ensure accuracy and then traced the amounts shown on the registers to Magnolia's general ledger. FCMAT found the following anomalies in the payroll items sampled:

- Two hourly employees' timesheets failed to reflect the supervisor's approval.
- One hourly employee's timesheet did not reflect the employee's signature.
- Magnolia supplied supporting documentation for two hourly employees that contradicts itself as to the number of hours the employees worked:
 - The payroll register for one employee shows payment for 35 hours on June 30, 2016. Magnolia initially provided FCMAT with a timesheet showing 11 hours worked (Monday through Wednesday, 3 hours per day; and 2 hours on Thursday) for the period June 6-9, 2016. FCMAT requested documentation to support the remaining 24 hours paid and was then provided with a timesheet that shows 35 hours worked (7 hours per day Monday through Friday) for the period June 6-10, 2016. Given the disparity between these two documents and the fact that neither contains the date of the employee's signature nor a signature/date of a supervisor, FCMAT is uncertain which document is the correct timesheet representing the actual time that the employee worked for the week of June 6-10, 2016.
 - The payroll register for the second employee shows payment for 25 hours on June 30, 2016. Magnolia initially provided FCMAT with a timesheet showing 14 hours worked (Monday through Wednesday, 4 hours per day; and 2 hours on Thursday) for the period June 6-9, 2016. FCMAT requested documentation to support the remaining 11 hours paid and was then provided with a timesheet that shows 25 hours worked (5 hours per day Monday through Friday) for the period June 6-10, 2016. Given the disparity between these two documents and the fact that neither contains the date of the employee's signature nor a signature/date of a supervisor, FCMAT is uncertain which document is the correct timesheet representing the actual time that the employee worked for the week of June 6-10, 2016.
- Two employees' timesheets reflected their work hours but did not reflect a start and stop time for a meal period as required by Labor Code Section 512 and the California Industrial Welfare Commission Wage Orders. Magnolia did not have a consistent timesheet form during the period being tested. Some simply record the start/stop time for each day, others include a column for overtime hours and yet another form includes start/end time for meal periods. Having a consistent form for all schools ensures that meal times are recorded and lessens calculation errors in payroll processing. Magnolia reported to FCMAT that not all timesheets for the period

reviewed contained recorded start/stop times for meal/rest periods and that, beginning in 2016-17, employees are required to track their meal periods.

- Five employees tested, or 20.8%, had rounding or keying entry errors between what was contained in the employee's final offer letter and what was entered into the payroll system, ranging from overpayments of \$0.01 to \$0.25 per pay period. Beginning with the 2016-17 fiscal year, Magnolia reported that it has instituted a policy to reconcile the amount paid and the amount contained in the employees' final offer letters. Overpayments will be deducted from the employees' June 30 payroll and any underpayment will be added to the June 30 payroll.
- Three certificated employees at MSA 8 were paid stipends ranging from \$1,200 - \$1,300. Magnolia allows each school to set its own stipend schedule, and FCMAT was provided with Auxiliary Pay Components 2015-16 schedule and the 2015-16 Academic Support Stipend Program agreement for MSA 8. All three certificated employees received a \$1,200 After School Education and Safety Program (ASES) stipend and one employee had an additional \$100 paid. However, FCMAT noted the following issues for these payments:
 - Neither the Auxiliary Pay Components 2015-16 schedule nor the 2015-16 Academic Support Stipend Program agreement and its terms reflect approval by Magnolia's governing board.
 - None of the certificated employees receiving a \$1,200 ASES stipend had that amount recorded on their ASES timesheets provided to support this payment.
 - The 2015-16 Academic Support Stipend Program agreement provides that staff members are to host two tutoring sessions per week but are allowed four non-qualifying/missed sessions. At the point that the fifth non-qualifying/missed session is recorded, "the employee will be ineligible to receive the stipend payout." Review of the three timesheets submitted shows that all three employees missed at least one session and there is no notation as to where in the continuum of the four non-qualifying/missed sessions these fall or whether Magnolia is tracking them.
 - The timesheet of the certificated employee receiving the \$100 additional stipend appears to tie the payment to the employee's work regarding a talent show and parent meeting; however, the Auxiliary Pay Components schedule provides for \$50 per occurrence for home visits and class coverage. FCMAT was not provided with documentation that would tie a stipend payment to either a talent show or parent meeting.
- Three employees' employer contributions for PERS were calculated incorrectly in the Paycom payroll registers. Instead of using PERS' employer contribution rate of 11.847%, that number was rounded up to 11.85%. FCMAT inquired regarding which percentage was paid to PERS and Magnolia provided an Excel spreadsheet that was used for their calculation and payment of the PERS contribution. However, based on the documentation provided, FCMAT was unable to determine the exact amount that was paid to PERS. While Magnolia may not use the Paycom payroll register to remit the PERS contribution, the Paycom payroll register is used to post the PERS payroll expense to Magnolia's general ledger, and those same amounts are used in Magnolia's income statements. FCMAT reviewed the general ledger and balanced the Paycom payroll register to the entries in the general ledger. No adjustments to the general ledger were made to decrease the PERS expense to 11.847%. Consequently, the PERS expense in Magnolia's general ledger is overstated.

- One employee's bimonthly payroll reflected a deduction for health and welfare insurance; however, the amount deducted was the full monthly employee portion of the insurance premium. This resulted in the employee having paid double the amount necessary for health care coverage. Magnolia indicated it had conducted a review of benefit deductions for all employees to ensure that proper amounts were deducted and reported, and that any amounts due to employees had been included in their November 30, 2016 paycheck.
- One employee's bimonthly payroll reflected a \$24.15 deduction for health and welfare insurance. Multiplying this amount by two does not equal the \$48.31 monthly employee cost of the insurance pursuant to Magnolia's 2015-16 Employee Benefits booklet, resulting in an overpayment to the employee of \$0.01 per month.
- One employee's payroll did not reflect withholding for state disability insurance, which would result in an overpayment to this employee. Magnolia did not provide FCMAT with an explanation for this discrepancy.
- One certificated employee, who had begun their career as a classified employee and remained in PERS, had no Social Security taxes withheld from their paycheck, which would result in an overpayment to this employee. Magnolia provided FCMAT with a statement to explain the discrepancy that said, "the employee was a PERS employee and should have been contributing to STRS." There appears to be some confusion as to which retirement system this employee belongs. If it is determined that the employee wishes to remain in PERS, which is allowed if required documentation is completed and submitted timely, Social Security taxes would be due. Failure to withhold Social Security taxes can obligate Magnolia for payment of both the employer and employee portions of amounts due.
- One school's payroll Excel sheet did not tie to the gross payroll reflected in the Paycom payroll register by \$7,465.00. Magnolia explained that the excess amount on the Excel spreadsheet was due to the contract buyout of an employee; however, FCMAT's review of the June 30, 2016 payroll register failed to find the named employee in the report. FCMAT requested copies of the documentation authorizing the buyout; however, Magnolia did not provide them. Consequently, it is unknown if the payment had been made and whether appropriate taxes were applied and/or withheld for this payment. It is also unknown if the board approved the buyout. These documents should be kept with the original spreadsheet and payroll register in the file for the payroll period to provide a complete payroll file. This is especially significant given the personnel turnover that Magnolia has experienced to ensure that a record is kept to support financial transactions.
- MSA 7
 - FCMAT was unable to trace the employer's/employees' STRS expense/liability from the June 30, 2016 Paycom payroll register to the general ledger due to amounts differing for these items between the payroll register and the general ledger. Through consultation with EdTec, it was determined that \$616.55 of STRS expense was neither reported as STRS expense nor liability, causing MSA 7's expenses to be understated. FCMAT did not receive information on when an adjusting entry would be made to correct this error. EdTec reported it would be adjusting its procedures to include full reconciliation between the payroll register, tax report and cash report. The general ledger should also be included in the reconciliation process.

- MSA 8
 - June 15, 2016 Payroll: FCMAT was originally provided a Paycom payroll register for June 15, 2016 but was unable to balance 10 of the 11 lines of that report to Magnolia's general ledger. In EdTec's research of FCMAT's questions on this journal entry, EdTec provided FCMAT with a payroll check register for the June 15, 2016 payroll that eliminated one employee from the payroll. Using the amounts from the payroll check register, FCMAT was able to reconcile all but four lines of the journal entry:
 - Object 3100 – STRS: There appears to be \$1,297.81 of expense that had not yet been recorded in Magnolia's general ledger.
 - Object 3200 – PERS: There appears to be \$146.77 of expense that had not yet been recorded in Magnolia's general ledger.
 - Object 9550 – PERS Liability: There appears to be a \$146.77 understatement of Magnolia's liability.
 - Object 9555 – STRS Liability: There appears to be a \$1,297.81 understatement of Magnolia's liability.
 - June 30, 2016 Payroll: FCMAT was unable to trace three lines of the journal entry used to record the June 30, 2016 Paycom payroll register in the general ledger as follows:
 - Object 3100 – STRS: No STRS expense was recorded in Magnolia's general ledger. In EdTec's research on FCMAT's question, it was discovered that \$5,008.13 was erroneously coded to object 3300 – OASDI (Social Security)-Medicare expense. It was also found that this amount should be adjusted to reflect an additional \$36.10 of STRS expense, bringing the total STRS expense to \$5,044.23.
 - Object 9555 – STRS Liability: There appears to be a \$36.10 understatement of Magnolia's liability.
 - FCMAT did not receive information on when adjusting entries would be made to correct these errors. EdTec reported it would be adjusting its procedures to include full reconciliation between the payroll register, tax report and cash report. The general ledger should also be included in the reconciliation process.
- All Schools
 - The employer's expense for workers compensation insurance is not included in the monthly payroll calculations and deductions completed by Paycom. Instead, monthly payments are made to the insurance carrier, CharterSafe, and then reconciled after the end of the fiscal year. Due to this practice, FCMAT is unable to test this aspect of payroll.
 - FCMAT's review of the June payroll registers revealed that state unemployment insurance had not been paid for any employee. Magnolia reported that this should have been reported and paid quarterly on form DE-9423. However, because of mistakes made during the implementation of its new payroll/hours system, payments had not been made. Magnolia further reported to FCMAT that processes and procedures had been corrected and implemented and payments were being brought current. FCMAT's inquiries regarding further details about how processes/procedures were changed, when past due payments were made and whether penalties were assessed were not answered.

Recommendations

The charter schools should:

1. Include a specific implementation date and language to identify the positions/classifications affected on all board agenda items related to payroll increases.
2. Carefully review base salaries to ensure against over- and underpayments.
3. Carefully review its application of the points associated with employee qualifications pay to ensure that the final calculation complies with the formula approved by its board in the 2015-16 Pay Raise Salary Scale.
4. Develop a salary schedule for positions with hourly rates of pay.
5. Ensure that both the employee and their supervisor execute all timesheets.
6. Carefully review, verify and math check all timesheets to ensure proper payment to employees. If employees submit an adjusted timesheet, mark the previous submission as having been superseded.
7. Develop a timesheet/time keeping system to track employees' start/stop times for meal/rest periods.
8. Reconcile the amounts paid to employees with the amounts contained in the employees' final offer letters to resolve rounding and keying errors in gross wages. Ensure payment shortfalls are returned and overpayments are collected from employees.
9. Review timesheets associated with stipends to ensure that the functions listed are those that qualify for stipends and that the employee has provided all of the required sessions associated with the ASES stipends. Implement tracking mechanisms so that, should an employee reach a fifth non-qualifying/missed session, their stipend is withheld and Magnolia does not have to recapture payment.
10. Reconcile and adjust the general ledger PERS expense to the amounts actually paid.
11. Conduct a thorough audit of all employees to ensure proper enrollment in the applicable retirement system, and be prepared to pay the employer and employee share of contributions to date as well as any interest and penalties levied by PERS.
12. Review all health and welfare benefits deductions made to employee payroll to ensure that proper amounts were withheld, and return any overages to employees immediately.
13. Ensure that supporting documentation exists for all elements of a payroll transaction including gross pay whether that is salary, stipends or timesheet/hourly pay, payroll increases/changes, PERS/STRS, declination of health insurance, vacation pay and stipends. Keep such items in individual payroll files. Reflect approval by the governing board for items associated with rates of pay such as salary or stipend schedules and hourly pay rates.

14. Carefully review the payroll registers to ensure that all required statutory benefits are paid and that proper percentages are used in their calculation.
15. Ensure payroll report files include documentation of any corrections made to provide a complete record of the transaction.
16. Review the payroll registers in conjunction with the journal entries made by EdTec to ensure that payroll information has been correctly recorded in the general ledger.

Accounts Payable

FCMAT reviewed June 2016 financial system reports provided by Magnolia and performed the following procedures:

- Analyzed data in the general ledger reports and selected a sample of individual transactions for review, including checks issued for accounts payable transactions, journal entries, and Automated Clearing House (ACH) electronic transactions. The general ledger has the following types of accounts payable document numbers:
 - Check – used for an ACH or electronic payment.
 - Bill Payment – used for a paper check.
 - Journal – used for a journal entry.
- Requested from Magnolia all supporting documentation for each selected transaction.
- Reviewed documentation received for each transaction to determine whether:
 - Authorization was obtained and documented in advance of the expenditure.
 - Goods or services were received and an obligation was incurred.
 - Invoices and/or agreements were reviewed and approved for payment.
 - Transactions were processed timely, accurately and properly recorded.

A combined sample of 71 transactions was tested for MSA 6, MSA 7, and MSA 8: 18 checks/ACH, 45 bill payments, and eight journals. FCMAT tested the transactions for the following attributes and found exceptions as indicated below for each school:

1. No signed requisition was used to start the purchase.
2. No purchase order was attached.
3. The purchase order was dated after receipt of the item/service.
4. The service contract was not signed by both parties (charter signatory and consultant).
5. A signed contract for ongoing services was not present and signed by an authorized Magnolia Science Academy signatory.
6. The invoice or detailed receipt was not attached.

7. The invoice was not initialed or signed to approve payment or a receiving document was not attached.
8. The invoice or detailed receipt was not stamped “paid.”
9. The invoice was not paid timely.
10. Other, not described above.

Of the 71 transactions tested, all (100%) had one or more exceptions per transaction.

MSA 6

Twenty-seven transactions were selected, including 13 checks/ACH, 12 bill payments, and two journals. All of the 27 transactions included one or more of exceptions 1, 2, 3, 4, 5, 6, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- MERF loan transfers did not have board approval attached.
- One transaction included payment for \$2.00 more than the invoice.
- Two transactions had no proof of employee payment for classes being reimbursed.
- One reimbursement was made to an individual for the purchase of student awards. FCMAT was unable to locate a board policy for student awards.
- One payment was made for an invoice that was to the Magnolia Foundation.

MSA 7

Twenty transactions were selected, including three checks/ACH, 13 bill payments, and four journals. All of the 20 transactions included one or more of exceptions 1, 2, 3, 4, 5, 6, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- One transaction had no proof of employee payment for items being reimbursed.
- One employee’s life insurance cancellation request took nine months to resolve.
- Backup documentation provided to FCMAT for one payment to an individual did not include a W-9 form.
- One check was voided due to an error; it took a year to resolve this issue.

MSA 8

Twenty-four transactions were selected, including two checks/ACH, 20 bill payments, and two journals. All of the 24 transactions included one or more of exceptions 1, 2, 3, 6, 7, 8, 9 as enumerated above, and/or the following Other exceptions:

- One transaction had no proof of employee payment for items being reimbursed.
- Backup documentation for reimbursement to one individual indicated that the expenditures had been approved by the parent-teacher foundation. It is unclear why the charter school paid this expenditure, and no proof of the foundation’s approval was attached.
- Two loan transfers to MERF did not have board approval attached.

The charter schools' accounts payable process begins with a request entered in the purchasing system (COOLSSIS) and electronically routed for approval. Once the purchase is approved the items are ordered. When items are received a check request is prepared and approved electronically, and then payment is processed in the EdTec financial system. The purchasing system tracks each step of the process and provides an opportunity for comments and notations. The invoice is not signed by the receiving party but is attached to the check request. Some of the charter schools do not require a wet signature on the check request, but rely instead on electronic approvals. Invoices are not stamped "paid" at the time payment is made to the vendor.

Best accounting practices require a signature of the person reviewing the receiver document and/or the invoice to indicate it has been verified for accuracy and the goods/services have been received. It is then forwarded to accounts payable for payment. When payment is generated the invoice is stamped "paid."

Magnolia Public School Accounting Policies, Procedures and Forms, SOP#PUR104 Revision:2 states, "All accounts payable and cash disbursements will have documented pre-approval" and "Approvals for reimbursement requests must be obtained prior to purchase." The standard operating procedure (SOP) also states, "The quantities shown shipped or delivered on the invoice will be compared to the packing slip and/or receiving reports if items have been received by the designee of each site." The SOP further states that accounts payable invoices should normally be paid within seven days or sooner of the payment term and invoices are to be stamped "paid" once processed. The sampling of transactions shows that the SOP and best accounting practices are not consistently followed. For example, invoices are not signed indicating they have been compared to the receiving document, some check requests do not have hard signatures, and invoices are not stamped "paid."

Magnolia allows the use of debit cards, and numerous debit card transactions are used for online purchases including, but not limited to, Amazon, Wal-Mart, and Lakeshore Learning. According to Magnolia's SOP, all accounts payable and cash disbursement will be preapproved. However, the use of debit cards does not follow this procedure. For example, MSA 6 made 12 debit card transactions without prior approval.

Electronic transfers/ACH are processed for monthly ongoing expenses as well as one-time payments. These expenses do not have prior approval. Contracts or agreements for these expenses should be renewed annually, or as applicable, if the service is to continue, and purchase orders should be created and approved annually. Payments can then be referenced to the purchase order when posted to the general ledger.

The charter schools use a temporary clearing account for posting some general ledger entries, and ACH activities for each week are entered as one journal number. The amounts recorded represent actual cash transactions that have occurred in the bank per retrieval of cash activities from the online banking portal. EdTec staff indicated the entry is done so the most accurate depiction of cash balances in the accounting system is available while awaiting the details from the school. These entries are later moved without detail to expense accounts, making it challenging to follow the trail of entries. Staff indicated that DB manual check cover sheets are created; however, these cover sheets were not attached to the transaction.

The process of posting journal entries to the general ledger based on information directly from the bank account poses concerns. Without prior approval for the purchase and a reported delay of up to seven days prior to reversing the original entry, reviewing each transaction and posting them to the correct expense accounts, there is an increased opportunity for fraud. In addition, when the reversal of the journal entry occurs in the following month, it is more challenging to balance the bank statement to the general ledger and complete the reconciliation.

Some school expenses are coded to “uncategorized expense.” When the correct account is determined, the expense is transferred. If expense reports are run prior to moving the transactions to the correct account, the account totals are inaccurate. All purchases should be preapproved with the correct account code to eliminate the need to post transactions as uncategorized.

FCMAT’s review of the sampled transactions indicates that some payments were not made timely. Best practices provide for the payment of undisputed invoices within 30 days of the invoice date.

Recommendations

The charter schools should:

1. Ensure that all purchases and disbursements, including debit card transactions and employee travel requests, have documented preapproval, which includes a purchase order and/or contract.
2. Ensure that the person approving an invoice for payment signs it stating it is accurate and has been verified.
3. Ensure invoices are paid for the correct amount, and total all invoices being paid with the invoice batch total to verify.
4. Stamp invoices “paid” once processed.
5. Include the board approval date and/or excerpt from the board meeting minutes as backup documentation for those items that require board approval.
6. Renew contracts, as applicable, and complete purchase orders annually for monthly ongoing expenses, including ACH transfers.
7. Pay invoices timely.
8. Use separate and distinct transaction type names in the general ledger for ACH transfers and paper checks.
9. Process check requests only with authorizing signatures.
10. When making reimbursements, attach documents that show the employee has paid for the item for which reimbursement is being requested.
11. Require legible itemized receipts or invoices for transactions, and not make payments based on bank statements.
12. Not pay invoices that are for another entity, such as the Magnolia Foundation.
13. Adopt a board policy regarding if and when student awards will be allowed.
14. Ensure that a copy of the W-9 form for applicable individuals is included in backup documentation for payments made to them.
15. Research and clear outstanding items, such as voided checks, timely.

Bank Statements and Reconciliations

FCMAT reviewed June 2016 bank statements, reconciliation detail reports and general ledgers provided by Magnolia. Each bank statement was compared to the general ledger to match each transaction. Each reconciliation detail report was also compared to the bank statement and general ledger to match transactions, identify outstanding transactions, and determine whether the reconciliation detail report balanced to the general ledger. FCMAT found the following anomalies in the items reviewed:

MSA 6

- Four journal entries were made debiting object 7998 Temporary JE Clearing and crediting object 9121 Cash. Shortly after, another journal entry was made to reverse each entry. The descriptions on these journals state they were done as a “Temporary DB manual check entry.” Examples include journal entries MSA61266 dated 6/16/16 and MSA61267 dated 6/24/16, both totaling \$10,057.95. Journal entries posted to cash do not show on the bank statement; therefore, this practice makes it more difficult to reconcile the general ledger to the bank statement.

MSA 7

- Journal MSA71023 dated 6/30/15, with a remaining balance of \$8,052.10, was still not cleared on the reconciliation detail report. Four additional items dated between 3/24/16 and 5/27/16 were also outstanding on the reconciliation. Journal entries posted to cash do not show on the bank statement, and therefore make it more difficult to reconcile the general ledger to the bank statement. Further, when these journal entries are not reversed timely it causes more confusion regarding what the entries were for and why they are considered an outstanding cash item.

MSA 8

- Five bill payments dated between 8/14/15 and 4/27/16 were still outstanding on the reconciliation detail report. Additionally, two journal entries dated 9/2/15 and 11/13/15 described as “Payroll #102” and “Payroll #90116” were outstanding. Journal entries posted to cash do not show on the bank statement, and therefore make it more difficult to reconcile the general ledger to the bank statement. Further, when these journal entries are not reversed timely it causes more confusion regarding what the entries were for and why they are considered an outstanding cash item.

Ed Tec staff indicated that the ACH activities for the week that cleared the bank but were not yet entered in the general ledger are entered as one lump sum temporary journal that is then reversed several days later. At the time of reversal the temporary journal is cleared and the expense objects are debited and cash is credited with a unique debit transaction number (DB). However, when the reversal is done in the following month, the total is listed as an outstanding debit on the reconciliation detail report to balance the general ledger to the bank statement. Therefore, it is difficult to reconcile the bank statement without substantial supporting documentation.

The reconciliation detail report should reflect actual deposits and expense transactions that directly affect cash, not journal entries, which usually do not affect cash. The total deposits on the reconciliation detail report should equal the total deposits on the bank statement, and the same for expenses. Adjusting journal entries posted to the general ledger such as “Temporary DB manual check entry” or “Payroll #102” or “Payroll #90116” should not be made unless they will be identified as deposits or expenditures on the bank statement.

EdTec prepares the monthly reconciliation detail reports. These reports are provided to Magnolia staff for review and comparison to the general ledger and bank statements for accuracy. The reports do not include staff signatures verifying they have been reviewed and that the totals agree with the general ledger and bank statements.

Recommendations

The charter schools should:

1. Only post items to the cash account if the amount will be reflected on the bank statement.
2. Post journals for manual checks only once, debit the appropriate expense object code and credit cash.
3. Post corrections to the general ledger using the same account code as the original transaction.
4. Ensure that the monthly bank statement is reconciled to the general ledger and that all transactions in the general ledger cash account will be reflected on the bank statement.
5. Research and clear outstanding items timely.
6. Include the signatures and printed names of the individual who prepared the bank statement reconciliation and the individual who reviewed/approved it, and the respective dates of same, on the reconciliation documents.

Revenue, Journal Entries and Financial Statements

FCMAT used the following processes in its review of June 2016 revenue and journal entry transactions and financial statements:

- General Ledger Revenue – Reviewed revenue transactions from the general ledger and requested supporting documentation for those items chosen for testing. Analyzed documentation to verify the accuracy of amounts posted to the general ledger, determine whether appropriate account number(s) were used to post revenue, and check the reasonableness of amounts posted based on the number of students served by the charter school.
- General Ledger Journal Entries – Selected journal entries from the general ledger and requested backup documentation for those items chosen for testing. Evaluated backup documents for adequate support and/or explanation for the journal posting, including amount and account number verification and appropriateness of the posting.
- Cash Flow Statement – Evaluated operating activities for reasonableness based on expected revenue streams for charter schools and the number of students served. Verified whether cash flow statement amounts matched the general ledger and income statement, and whether receivables, liabilities, and the beginning and ending cash balances matched the general ledger and balance sheet.

- Income Statement – Evaluated reasonableness of amounts based on expected cash flow and the number of students served. Reviewed whether amounts matched applicable categories in the general ledger.
- Balance Sheet – Reviewed reasonableness of balance sheet and whether amounts matched applicable categories in the general ledger.
- Budget to Actuals – Compared unaudited actuals from the general ledger to the applicable budget categories in the 2015-16 adopted budget. Reviewed whether expenses were within budget and revenues were appropriate based on expected cash flow and the number of students served.

FCMAT found the following anomalies in the items sampled and reviewed:

- General – Payments made to the charter management organization (referred to as MERF or the home office), and loans between MERF and the charter schools, are made via a cash transfer between the home office bank account and the charter school's bank account. This process does not provide for appropriate checks and balances.
- General – MERF does not provide sufficient backup documentation when billing the charter schools for items or when making loans between itself and the charters. Board minutes indicate that the loans were approved; however, some changes were made to the approved repayment schedules (see further detail below for MSA 6 and MSA 8). Sufficient documentation for expenses paid by MERF on behalf of the charter schools should have a signed and dated invoice sheet showing expenses to be repaid and how expenses were allocated to each charter, copies of the invoices paid by MERF, a charter approved purchase order with the account codes to be charged, and when applicable, an excerpt showing the board approval date. Documentation for loans between MERF and its charters should include a board approved loan agreement signed by both parties, the approved repayment schedule, a purchase order with the appropriate account code and a notation as to which payment is being made. If a payment schedule is revised – for example, when a charter has insufficient cash to make the scheduled payment – the backup documents should clearly show that change.
- MSA 6
 - Net revenue of \$3,158 (document #60689) was posted to uncategorized revenue on 6/30/2016, yet information to correctly post this revenue was available via a Schools-in-Action letter dated 5/18/2016. This transaction included a set-up fee, so it should have been posted as \$4,158 to revenue and \$1,000 to expense.
 - There was insufficient documentation for journal entry MSA61273 dated 6/30/2016 for \$450,000. Backup documents included an unsigned spreadsheet and a partially signed transfer sheet from MERF titled "MPS CMO FEE LOAN/BANK TRANSFERS." The approval signature for the chief executive officer did not have a corresponding printed name, and there was no approval signature for the chief financial officer.
 - Documentation for a loan payoff from MSA 6 to MERF (MSA61272) had no approval signatures and was not dated. Backup documentation did not include a board approval date with the repayment schedule or an excerpt from the board meeting minutes.
 - Backup documentation for year-end accruals (MSA61307) did not match the actual accruals made on two accounts (objects 8220 and 8520).

- CMO fees were initially estimated at \$65,483; however, \$61,337.32 was charged on 6/30/2016 (MSA61309) and another \$40,955.51 was charged to the charter via MSA61370 dated 6/30/2016.
- The general ledger shows outstanding receivables from a prior year of \$5,649 in object 9251 and \$877 in object 9252 that should be researched and either followed up on or written off.
- There is a negative balance of \$669.38 in object 9310 (due from other funds). This should be researched and corrected as it is an over posting to this object.
- Backup documentation for journal entries did not include a listing of the account numbers and the applicable debit or credit amounts that were posted.
- There was \$13,282 of outstanding uncategorized expenses at 6/30/2016.
- MSA 7
 - Backup documentation for journal entries did not include a listing of the account numbers and the applicable debit or credit amounts that were posted.
- MSA 8
 - Backup documentation for journal entries did not include a listing of the account numbers and the applicable debit or credit amounts that were posted.
 - A loan to MERF (MSA81264 dated 6/7/2016) for \$300,000 had no purchase order or invoice, the accounts payable system was not used, and there were no printed signatures on the backup documentation provided, which makes it difficult to determine who approved the transfer. This cash transfer was done directly between the charter's and MERF's bank accounts.
 - Backup documentation for CMO fee loan (MSA81282 dated 6/30/2016) for \$1,800,000 only had one signature, and there were no printed names, no purchase order or invoice, and the accounts payable system was not used. This cash transfer was made directly between the charter's and MERF's bank accounts.
 - Backup documentation for home office expense (MSA81283 dated 6/30/2016) for \$72,758.59 only had one signature, no printed names, no date, no purchase order or invoice, and the accounts payable system was not used. This cash transfer was made directly between the charter's and MERF's bank accounts.
 - There was \$6,108 of outstanding uncategorized expenses at 6/30/2016.

Recommendations

The charter schools should:

1. Make payments to the charter management organization (MERF/home office) using the accounts payable process with appropriate documentation and approvals, rather than through a cash transfer between the applicable bank accounts.
2. Ensure interschool loans and loans between a charter school and MERF are sufficiently documented, signed by authorized approvers, accounted for accurately and timely, and paid back via the accounts payable process.

3. Process transactions with the appropriate account code rather than as uncategorized.
4. Prepare monthly budget to actual data by object for ongoing review and analysis.
5. Ensure that signed documents include the printed name of the signor and date signed.
6. Provide board approval dates as backup documentation for all items that require board approval.
7. Include a spreadsheet or similar backup documentation for journal entries, which shows all accounts affected, the amounts debited and credited to each account, and the reason for the entry.
8. Ensure backup documents are complete and accurate for each transaction.
9. Research and clear outstanding receivables and payables in a timely manner, and ensure there are no negative amounts in these object codes.
10. Update budgets throughout the fiscal year as factors such as changes in average daily attendance, grant funding, and staffing are known.

This concludes FCMAT's eighth and final management letter for Magnolia Public Schools.

Sincerely,



Diane Branham

Chief Management Analyst

C: Jose Cole-Gutierrez, Director, Charter Schools Division, LAUSD