ISSUED: February 14, 2011 **AR-01-40-11**

THE UNITED STATES VIRGIN ISLANDS

OFFICE OF THE VIRGIN ISLANDS INSPECTOR GENERAL

AUDIT REPORT

AUDIT OF THE EDUCATION INITIATIVE FUND

ILLEGAL OR WASTEFUL ACTIVITIES SHOULD BE REPORTED TO THE OFFICE OF THE VIRGIN ISLANDS INSPECTOR GENERAL BY:

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EXECUTIVE SUMMARY

The following summarizes the major findings resulting from the Audit of the Education Initiative Fund (AR-01-40-11).

Finding 1: Funding (pages 6 to 18)

- ✓ Funds were not evenly distributed between the schools.
- ✓ Public schools were underfunded by at least $4,636,332 during the audit scope period.
- ✓ No documentation was provided to show that 16 schools had received $378,827 in fiscal year allocations that had been set aside for them.
- ✓ Funds were generally disbursed to schools late with schools receiving their funding as many as 48 months after the beginning of the fiscal year and the allotment releases by the Office of Management and Budget.
- ✓ The Virgin Islands Lottery owed at least $726,903 to the Fund from private contractor lottery gaming revenues received over the audit scope period.

Finding 2: Expenditures (pages 19 to 29)

- ✓ Schools did not expend and account for the uses of Education Initiative Fund monetary resources in accordance with the law.
- ✓ Of the estimated $1,275,857 in school expenditures, $257,802 was not allowable under the law, $429,436 was not adequately supported, and at least $220,246 was not properly authorized.

Finding 3: Internal Controls (pages 30 to 36)

- ✓ Finance and Education did not effectively monitor schools' uses of awarded funds to ensure proper accountability and compliance with the law.
- ✓ Finance did not review the expenditures for an estimated $2,979,285 in Fund monies disbursed to the schools, and did not consistently provide compliance reports to Education, as required by law.

- ✓ Education did not properly monitor the schools' uses of Fund monies through the review and reporting processes.

Finding 4: Law (pages 37 to 38)

- ✓ The Virgin Islands Code contains ambiguous and contradictory statutes addressing the Fund.
- ✓ These ambiguities and contradictions were impediments to clearly understanding the rules and regulations governing the Fund.

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February 14, 2011

Honorable John P. de Jongh, Jr.
Governor of the Virgin Islands
Government House
Kongens Gade
Charlotte Amalie, St. Thomas, V. I. 00802

Honorable Ronald E. Russell
President
29th Legislature
Capitol Building
Charlotte Amalie, St. Thomas, V. I. 00802

Dear Governor de Jongh and Senator Russell:

This report contains the results of our audit of the Education Initiative Fund (Fund). The objective of our audit was to determine if the resources of the Fund were allotted, expended, and accounted for in accordance with applicable laws and regulations. The audit objective included the identification of inadequacies in the funding process; the use, management, and accounting of funds; construct of the law; and recommendations to address the inadequacies found.

The Fund was administered in a substandard internal control environment that resulted in inadequate stewardship and accountability of Fund resources by the Department of Finance (Finance) and the Department of Education (Education). Report deficiency findings relating to funding, expenditures, reporting, and monitoring were due to the poor internal control conditions. Specifically, we found that: (i) funds were not evenly distributed between the schools; (ii) the public schools were underfunded by at least $4,636,332 during the audit scope period; (iii) no documentation was provided to show that 16 schools had received $378,827 in fiscal year allocations that had been set aside for them; (iv) funds were generally disbursed to schools late with schools receiving their funding as many as 48 months after the beginning of the fiscal year and the allotment releases by the Office of Management and Budget; (v) the Virgin Islands Lottery owed at least $726,903 to the Fund from private contractor lottery gaming revenues received over the audit scope period; (vi) of the estimated $1,275,857 in school expenditures audited, $257,802 was not allowable under the law, $429,436 was not adequately supported, and at least $220,246 was not properly authorized; (vii) Finance did not review expenditure reports for an estimated $2,979,285 in funds disbursed to the schools, and did not consistently provide compliance reports to Education as required by law; (viii) Education did not effectively monitor schools' uses of awarded funds to ensure proper accountability and compliance with the law; and, (ix) the Virgin Islands Code contained ambiguous and contradictory statutes addressing the Fund.

We attributed these conditions to: (i) the Code's funding formula; (ii) insufficient contributions made to the Fund from General Fund appropriations and the V.I. Lottery; (iii) Education's irregular and late reporting practices of schools' fiscal year expenditures; (iv) the Lottery's failure to submit, to Finance, required monthly revenue reports; (v) Finance, as the administrator of the Fund, not taking steps to routinely verify that Lottery revenue payments to the Fund equaled the required payment percentage of gaming revenue stipulated in the Code; (vi) the failure of Finance and Education to provide adequate guidance to the schools regarding the uses and limitations of the Fund; and, (vii) the failure of Finance and Education to follow established policies and procedures governing the Fund and to implement good internal control practices.

As a result: (i) some schools received an unfair advantage over others in their yearly funding allocation amounts; (ii) undistributed school allocations contributed to an unreconciled Fund balance of $18,424,689, as of December 31, 2008; (iii) public school students, the ones for whom the Fund is intended to help, were deprived of the benefits of funds which reached schools late or are still outstanding; (iv) Fund resources were not used as intended due to the expenditure practices of the schools; (v) schools were not held accountable for the funding they had received during the audit scope period; and, (vi) the ambiguities and contradictions in the Code were impediments to clearly understanding the rules and regulations governing the Fund.

We made several recommendations to address the conditions and causes cited in the report. Our recommendations address the following areas: funding; expenditure and reporting requirements; internal controls; and, the construct of the law.

We have included a copy of the response to the report as Appendix I beginning on page 39. We have also included, as Appendix II beginning on page 59, the additional information need before the recommendations can be closed.

If you or your staff require additional information, please call me at 774-6426.

Sincerely,

Steven van Beverhoudt, CFE, CGFM
V. I. Inspector General

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INTRODUCTION

BACKGROUND

In 1995, the Virgin Islands Legislature (Legislature) passed Act 6088, which created the Education Initiative Fund (Fund). Prior to that act, the Fund was initially established as a two year pilot program under Act 5948 in 1994. The Fund was created to enable the acquisition of certain items of goods and services that are essential for the routine functioning of the public schools and the public adult education facilities.

According to Title 33, Section 3093, of the Virgin Islands Code (Code) the Fund consists of (i) a percentage of "the proceeds the Lottery derived from the games under each contract between the Virgin Islands Lottery and a private contractor of lottery games, including the proceeds under a contract with a contractor of video lottery games authorized under Title 32, Section 246(a)(1) of the Code"; (2) sums of money appropriated by the Legislature; and, (iii) all donations, gifts and bequests.

Title 33, Section 3093, of Code authorizes the Commissioner of Finance (Finance) to administer the Fund as a separate and distinct fund in the Treasury of the Virgin Islands Government, and to promulgate rules and regulations to guide the expenditure and the reporting of such expenditures by Fund custodians.

The Code provides the formula for determining the funding amount to each school; stipulates the time period in which funding must reach the schools; and provides guidelines for expending, managing, reporting and accounting for Fund monies.

In addition to Finance, funding of schools through the Fund requires the involvement of other facilitating agencies of the Virgin Islands Government. Those agencies include the Office of Management and Budget (OMB), the Virgin Islands Lottery (Lottery), and the Department of Education (Education).

OBJECTIVE, SCOPE AND METHODOLOGY

The objective of our audit was to determine if the resources of the Fund were allotted, expended, and accounted for in accordance with applicable laws and regulations. The audit objective included the identification of inadequacies in the funding process; the use, management, and accounting of funds; construct of the law; and recommendations to address the inadequacies found.

The audit scope covered deposit and disbursements processed through the Fund and the public schools' imprest fund checking accounts during Fiscal Years 2002 through 2007.

We reviewed applicable laws, regulations and procedures; examined all available Fund records provided by Finance, OMB, Lottery, Education, and the St. Thomas/St. John and St. Croix public schools pertaining to funding, expenditures, reporting, and monitoring; and interviewed key officials of the audited agencies. As part of our audit, we selected 14 of the territory's 37 public schools, 7 schools each from the St. Thomas/St. John and the St. Croix school districts for a more detailed analysis.[1] In addition, we reviewed and commented on Education procedures manual, "School Fund Management Manual," issued in 2009.

The audit was performed in accordance with generally accepted government auditing standards applicable to performance audits, contained in the "Government Auditing Standards" issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to provide a reasonable basis for our findings and conclusions. Accordingly, we performed such tests of records and performed other auditing procedures that were considered necessary under the circumstances.

As part of our audit, we evaluated the internal controls over the management of funds controlled by the audited agencies to the extent necessary to accomplish the audit objective. Weaknesses in internal controls are discussed in the Audit Results section of the report.

Based on the responses received from Education, Finance and the Lottery, we performed a limited follow-up review of Fund activities in fiscal years 2008 through 2010, maintained by Finance. This was done to verify the level of improvements claimed to have been made by the three entities involved. The results of our review are discussed after each finding under the sections entitled "Inspector General's Comments".

PRIOR AUDIT COVERAGE

There were no indications in the records we examined that the Fund had been audited within the past five (5) years. However, the Office of the Virgin Islands Inspector General audited and issued a report on the Fund in August 2003. The objectives of the audit were to determine if Fund resources were fairly allotted; distributed to the public school within the time period specified in the Code; and were used in accordance with the Code requirements. The audit scope period covered Fiscal Years 2000 and 2001.

The audit found that: (i) the amount and timing of OMB's initial releases to the Fund did not allow for schools to receive the required allotments within the time period stipulated in the Code; (ii) some schools received an unfair advantage over other schools in the amount of funding they received in each fiscal year; and, (iii) generally, custodians expended funds in accordance with Code guidelines. However, in those instances where custodians were determined by Education to be in default of the Code's expenditure reporting requirements, a penalty was imposed by withholding the schools' subsequent period's Fund allotment.

[1] The 37 public schools included 2 public day adult educational facilities, one each in the St. Thomas/St. John and the St. Croix districts.

The recommendations addressed areas dealing with: (i) reforming the distribution allotment method to facilitate funding to the schools in the amount and time period stipulated by the Code; (ii) ensuring that schools received their fair share of funding each year; and, (iii) implementing provisions of the Code to safeguard Fund resources.

AUDIT RESULTS

CONCLUSIONS

The Fund was administered in a substandard internal control environment that resulted in inadequate stewardship and accountability of Fund resources by Finance and Education. Report deficiency findings relating to funding, expenditures, reporting, and monitoring were due to the poor internal control conditions. Specifically, we found that: (i) funds were not evenly distributed between the schools; (ii) the public schools were underfunded by at least $4,636,332 during the audit scope period; (iii) no documentation was provided to show that 16 schools had received $378,827 in fiscal year allocations that had been set aside for them; (iv) funds were generally disbursed to schools late with schools receiving their funding as many as 48 months after the beginning of the fiscal year and the allotment releases by OMB; (v) the Virgin Islands Lottery owed at least $726,903 to the Fund from private contractor lottery gaming revenues received over the audit scope period; (vi) of the estimated $1,275,857 in school expenditures audited, $257,802 was not allowable under the law, $429,436 was not adequately supported, and at least $220,246 was not properly authorized; (vii) Finance did not review expenditure reports for an estimated $2,979,285 in Initiative funds disbursed to the schools, and did not consistently provide compliance reports to Education as required by law; (viii) Education did not effectively monitor schools' uses of awarded funds to ensure proper accountability and compliance with the law; and, (ix) the Virgin Islands Code contained ambiguous and contradictory statutes addressing the Fund.

We attributed these conditions to: (i) the Code's funding formula; (ii) insufficient contributions made to the Fund from General Fund appropriations and the V.I. Lottery; (iii) Education's irregular and late reporting practices of schools' fiscal year expenditures; (iv) the Lottery's failure to submit, to Finance, required monthly revenue reports; (v) Finance, as the administrator of the Fund, not taking steps to routinely verify that Lottery revenue payments to the Fund equaled the required payment percentage of gaming revenue stipulated in the Code; (vi) the failure of Finance and Education to provide adequate guidance to the schools regarding the uses and limitations of the Fund; and, (vii) the failure of Finance and Education to follow established policies and procedures governing the Fund and to implement good internal control practices.

As a result: (i) some schools received an unfair advantage over others in their yearly funding allocation amounts; (ii) undistributed school allocations contributed to an unreconciled Fund balance of $18,424,689, as of December 31, 2008; (iii) public school students, the ones for whom the Fund is intended to help, were deprived of the benefits of funds which reached schools late or are still outstanding; (iv) Fund resources were not used as intended due to the expenditure practices of the schools; (v) schools were not held accountable for the funding they had received during the audit scope period; and, (vi) the ambiguities and contradictions in the Code were impediments to clearly understanding the rules and regulations governing the Fund.

We made several recommendations to address the conditions and causes cited in the report. Our recommendations address the following areas: funding; expenditure and reporting requirements; internal controls; and, the construct of the law.

FINDING 1: FUNDING

Deficiencies existed in the administration of the Fund to the territory's schools. Specifically, we found that: (i) funds were not evenly distributed between the schools; (ii) the public schools were underfunded by at least $4,636,332 during the audit scope period; (iii) no documentation was provided to show that 16 schools had received $378,827 in fiscal year allocations that had been set aside for them; (iv) funds were generally disbursed to schools late with schools receiving their funding as many as 48 months after the beginning of the fiscal year and the allotment releases by OMB; and, (v) the Virgin Islands Lottery owed at least $726,903 to the Fund from private contractor lottery gaming revenues received over the audit scope period.

These conditions were attributable to: (i) the Code's funding formula; (ii) insufficient contributions made to the Fund from General Fund appropriations and the V.I. Lottery; (iii) the reporting practices of Education and Lottery; and, (iv) Finance, as the administrator of the Fund, not taking steps to routinely verify that Lottery revenue payments were made in accordance with Code requirements.

As a result: (i) some schools received an unfair advantage over others in their yearly funding allocation amounts; and (ii) public school students, the ones for whom the Fund is intended to help, were deprived of the benefits of funds which reached schools late or are still outstanding.

Background

From its inception until 2003, the Fund primarily consisted of monies appropriated by the Legislature of the Virgin Islands. The approval of Act 6590 in August 2003 provided, through the Lottery, an additional funding source. This initiative was in response to a July 5, 2002 funding mandate that increased the base funding to the schools from $10,000 to $50,000. Lottery contributions to the Fund are based on a percentage of the proceeds the Lottery receives from games under contracts it has with private contractors of lottery games, to include contractors of video lottery games. The Code contains conflicting requirements regarding the percentage amount the Lottery must pay into the Fund from private contractor gaming revenues. Title 33, Section 3093(b) specifies that Lottery must pay 35% of those revenues into the Fund while Title 32, Section 246(iv) specifies that Lottery must pay only 25%. Lottery contributions to the Fund have been based on the 25% revenue payment requirement. Lottery officials said that they were not aware of the contradictions in the Code. This matter is discussed in further detail under Finding 4.

Title 32, Section 247(i) of the Code requires that the Director of Lottery "certify monthly to the Commissioner of Finance and the (Lottery) Commission a full and complete statement of lottery revenues…for the preceding month."

In reference to monies appropriated by the Legislature, OMB is required to "allocate all monies due to schools and educational facilities…within 15 days following the beginning of each fiscal year." Monies from Lottery are not processed through OMB, but paid directly from Lottery to Finance for deposit into the Fund. Finance is then responsible for obligating the funds for the schools. The Code does not stipulate when Lottery is required to transfer money to the Fund.

As part of its responsibilities, Education coordinates funding to the public schools and public adult educational facilities by determining the amount of each school's and facility's Fund allocation and arranging for its distribution through Finance. Funding determinations are based on the following formula as prescribed in the Code.

Stage 1. Each school is awarded a base amount of $50,000. Prior to June 22, 2002, the base amount was $10,000.

Stage 2. Each School receives an additional sum of $15 for every enrolled student over 500, as determined by the fall school population report generated by Education's Office of Testing, Planning and Evaluation.

Stage 3. If one district receives a larger sum than the other, the district receiving the smaller sum is awarded an additional sum equaling the difference in funding received between the two districts. The additional sum is shared between the district's schools and facilities proportionately to the number of students enrolled in each. The Code stipulates that the purpose for awarding the additional sum is to ensure that the two districts receive equivalent sums of funding.

Uneven Funding

Monies from the Fund were not evenly distributed between the public schools. Specifically, we found that schools in the district receiving the additional funding sum, as per the third stage of the formula, had an advantage over schools in the other district. For instance, the St. Croix district had been consistently awarded the additional sum every year in the audit scope period. This was done to ensure that the two districts received equal funding. This, however, resulted in more monies being awarded to schools in the St. Croix district even if their student enrollments approximated or were lower than the student enrollments of schools in St. Thomas/St. John district. The funding inequities were actually caused by a combination of the formula and insufficient levels of funding which prevented schools from receiving allocations in amounts required by law. As a result, these factors influenced certain discretionary decisions made by Education in apportioning monies to the schools. For instance, for Fiscal Year 2004, funding to the territory's public schools, from the General Fund and the V.I. Lottery, totaled only $453,290 and $49,070, respectively. These amounts were insufficient to fund the public schools at the increased base amount of $50,000. As a result, Education apportioned the $453,290 to the schools using the obsolete base formula amount of $10,000, and shared the $49,070 among the territory's high schools and vocational school.

The following exhibits show Education's allocation determinations for the public schools for Fiscal Years 2004 and 2007. They show the disparity in funding between the schools in the St. Thomas/St. John and the St. Croix districts. In the two fiscal years shown, schools in the St. Croix district with individual enrollments up to 500 students were awarded more funds than schools in the St. Thomas district with the same enrollment statistics. For instance, in Fiscal Year 2004 (Exhibit A), the Elena Christian Junior High School on St. Croix and the Peace Corps/Bowsky Elementary School on St. Thomas received varying award amounts of $10,402 and $10,000, respectively, even though they each had 396 students.

The exhibits point out more disparities in the funding between schools in the two districts. For instance, in Fiscal Year 2004 (Exhibit A), St. Croix Educational Complex-Vocational School, which had a student enrollment of 593 and had been awarded $17,593, received more funding than three St. Thomas schools which had higher student enrollments. The St. Thomas schools Addelita Cancryn Junior High, Bertha Boschulte Middle School, and Joseph Gomez Elementary School had enrollments of 845, 770, and 629, but only received $15,175, $14,050, and $11,935, respectively. In Fiscal Year 2007 (Exhibit C), St. Croix Educational Complex-Vocational School, with an enrollment of 704, received $53,350 when Addelita Cancryn and Bertha Boschulte, with enrollments of 723 and 718, received $53,270 and $53,345, respectively.

Exhibit A – Fiscal Year 2004

Schools	Enrollment	Allocation	Schools	Enrollment	Allocation
St. Thomas/St. John District			**St. Croix District**		
Charlotte Amalie H.S.	1,616	$40,516	Central High	1,471	$37,430
Kean High	897	23,835	STX Ed. Complex-Aca	1,315	34,021
Cancryn Jr. High	845	15,175	Arthur Richards	675	13,313
Bertha Boschulte	770	14,050	John Woodson	650	12,913
Joseph Gomez	629	11,935	Alexander Henderson	602	12,144
Lockhart Elementary	608	11,620	STX Ed. Complex-Voc	593	17,593
Benjamin Oliver	578	11,170	Pearl Larsen	586	11,866
Muller	425	10,000	Ricardo Richards	503	10,558
Peace Corps/Bowsky	396	10,000	Lew Muckle	501	10,526
Adult Ed. – STT	369	10,000	Charles Emanuel	498	10,506
Kirwan/Abraham	328	10,000	Eulalie Rivera	488	10,496
Julius E. Sprauve	264	10,000	Juanita Gardine	471	10,479
Jarvis	245	10,000	Evelyn Williams	465	10,474
Sibilly	237	10,000	Claude Markoe	460	10,468
Marcelli	200	10,000	Alfredo Andrews	439	10,466
Dober	171	10,000	Elena Christian Jr. High	396	10,402
Edith Williams	110	10,000	Adult Ed.-STX	349	10,354
Jane E. Tuitt	97	10,000	Positive Alternative Ed.	50	10,050
Guy Benjamin	67	10,000			

Exhibit B – Fiscal Year 2007

Schools	Enrollment	Allocation	Schools	Enrollment	Allocation
St. Thomas/St. John District			**St. Croix District**		
Charlotte Amalie H.S.	1,652	$67,280	STX Ed. Complex-Aca	1,240	$61,612
Kean High	951	56,765	Central High	1,197	60,949
Cancryn Jr. High	723	53,345	STX Ed. Complex-Voc	704	53,350
Bertha Boschulte	718	53,270	Adult Ed.-STX	600	51,746
Lockhart Elementary	582	51,230	Woodson Alexander	598	51,715
Joseph Gomez	551	50,765	Arthur Richard	592	51,623
Benjamin Oliver	523	50,345	Henderson	504	50,267
Muller	415	50,000	Pearl Larsen	493	50,202
Peace Corps/Bowsky	412	50,000	Ricardo Richards Lew	486	50,199
Adult Ed. – STT	345	50,000	Evelyn Williams	457	50,187
Kirwan/Abraham	339	50,000	Muckle	444	50,182
Sibilly	234	50,000	Elena Christian Jr. High	424	50,174
Jarvis	222	50,000	Charles Emanuel	418	50,171
Dober	173	50,000	Eulalie Rivera	409	50,168
Julius E. Sprauve	161	50,000	Claude Markoe	365	50,150
Marcelli	141	50,000	Alfredo Andrews	346	50,142
Guy Benjamin	130	50,000	Juanita Gardine	334	50,137
Jane E. Tuitt	75	50,000	Positive Alternative Ed.	63	50,026

Funding Formula

The funding unevenness was in part due to the formula. It gives schools in the district receiving the additional sum a funding advantage over schools in the other district. The difference specifically occurs at the third stage of the formula, where the district with the smaller sum – determined after having applied stage two of the formula – receives an additional sum so that both districts will be funded equally. This creates unevenness in funding the public schools because the additional sum is shared only among the schools in the recipient district. Consequently, the legislative decision to ensure equal funding to the districts, through the required application of the third stage of the formula, has resulted in disproportionate funding between the public schools.

Recognizing the unevenness in funding caused by the formula, Education, in Fiscal Year 2006, proposed that the formula be amended. The proposal, presented in a document addressed to OMB, included revising the construct of the formula to consist only of stages one and two. Apart from a written reply by OMB requesting additional information, no other documentation was presented to auditors documenting the outcome of Education's attempt to reform the funding method to the schools.

Funding Levels

Based on documentation provided by Finance and Education, public schools were collectively underfunded by at least $4,636,332 during the audit scope period. Monies distributed to public schools for those years were not sufficient to meet the base funding requirements of the Code. In contrast to the underfunding, some schools were collectively overfunded by an estimated $125,698. However, the overfunding only occurred in Fiscal Year 2002.

Using the information in Exhibit A (see p.11), we illustrate how individual schools were impacted by the underfunding. For instance, payment documents confirmed that St. Thomas/St. John schools Kean High, Bertha Boschulte, and Julius Sprauve did receive their Fiscal Year 2004 allocations of $23,835, $14,050, and $10,000. However, based on the Code's funding requirements, they should have received $55,955, $54,050, and $50,000, respectively. Together, they were underfunded by $112,120. The following exhibit shows the estimated combined overages and shortages in payments to both district schools by fiscal years.

Exhibit C

Fiscal Year	Overages	Shortages
2002	$125,698	$46,997
2003		1,381,169
2004		1,451,426
2005		1,087,939
2006		575,456
2007		93,345
Total	**$125,698**	**$4,636,332**

Education attributed the funding shortages to insufficient contributions made to the Fund from General Fund appropriations and the V.I. Lottery. The limited contributions presented challenges in applying the formula as required. As a result, Education used its discretion in allocating monies to the public schools based on available Fund resources. For instance, for Fiscal Year 2003, the 37 public schools received only $603,780, which was provided from the General Fund, the primary funding source at the time. The V.I. Lottery had not yet been identified as a funding source to help fund the schools at the increased base amount of $50,000. For Fiscal Year 2004, total contributions to the Fund from the General Fund and the V.I. Lottery totaled only $453,290 and $49,070, respectively. Working within these funding constraints, for Fiscal Years 2003 and 2004, Education allocated the General Fund monies to the public schools, using as the standard, the obsolete base formula amount of $10,000. However, it shared the $49,070, which was subsidized by the Lottery for Fiscal Year 2004, only among the territory's four high schools and vocational school. Of this amount, $13,776 was awarded to Charlotte Amalie High School, $7,880 to Ivanna Eudora Kean High School, $11,365 to Central High School, $10,445 to Educational Complex-Academic High School, and $5,594 to Educational Complex-Vocational School.

Undistributed Allocations

Finance and Education provided no documentation to show that $378,827 in allocations made to 16 schools from General Fund allotments were distributed to those schools. The allocations comprised funding that had already been set aside specifically for those schools from OMB released monies, but no evidence existed that checks had been processed or distributed. For instance, based on provided documents, St. Croix's Ricardo Richards did not receive $30,551 in funding that had been set aside for Fiscal Years 2005 through 2007. Over the same

period, St. Croix Central High did not receive allocated funds totaling $64,765. Since Finance records did not provide confirmation that the 16 schools had been distributed their allocations, we sought confirmation from Education on selected schools, but received no response.

In response to our inquiries about the unconfirmed distributions, Finance said that General Fund subsidized checks were not processed for schools that had not submitted expenditure reports. For instance, Finance had no records of Positive Alternative Education School submitting expenditure reports for 4 consecutive years, Fiscal Years 2004 – 2007. As a result, the school did not receive $40,106 in funding that had been set aside for it. We found that while schools did not receive General Fund funding disbursements, they did receive V.I. Lottery funding disbursements. This anomaly was linked to internal control weaknesses related to how expenditure reports were reviewed by Finance. More is discussed on this matter in the section entitled Finding 3: Internal Controls.

Fund Balance

The $378,827 in undistributed school funds contributed to an unreconciled Fund balance of $18,424,689, as of December 31, 2008. We found that the high Fund balance was caused by the funds received from the Lottery's contributions and the use of the Fund by Finance as a depository for monies unrelated to the Fund's intended purpose. Unrelated monetary deposits over the audit scope period included approximately $4 million earmarked for maintaining schools' accreditation status and paying substitute teachers. We did not audit the specific funding transactions constituting the $18.5 million Fund balance.

Funding Distributions

Funding distributions to the public schools were not timely. Results from our sample review of 14 schools showed that the elapsed time from the beginning of the fiscal year to the date of the distribution or deposit of checks ranged from 2 to 48 months. In some instances, schools did not receive their funding. General Fund and Lottery contributions to the Fund were distributed separately to the public schools; with funding checks from Lottery contributions consistently reaching schools from 9 to 15 months after the fiscal year had begun.

General Fund Contributions. Despite the funding checks distribution delays, we found that OMB allotments were generally timely and that Education's Budget Control Office, the division tasked with determining the funding allocable to each school, was prompt in notifying Education officials and schools of the available funding. Delays in the distributions stemmed partly from Education's expenditure report submission practices. The timing of Education's school expenditure report submissions to Finance for one fiscal year determined when schools received their funding distributions for the next – making inconsequential any timely allotments by OMB. As stated, Finance required the previous fiscal year's expenditure reports to initiate check processing for the schools, at least as it related to General Fund monies.

The Code requires that Education compile, for submission to Finance, an Annual Financial Report of the schools' fiscal year expenditure activities by the 30th of the month following the end of the fiscal year. Education does not compile an Annual Financial Report of fiscal year expenditure activities. The system of reporting used by Education – and allowed by Finance – consisted mainly of Education submitting the individual expenditure reports to Finance when received from the schools.

We found that Finance had not received school expenditure activities for monies that had been funded by the Lottery. This did not prevent the schools from receiving their yearly Lottery funding. Finance and Education treated General Fund monies and Lottery monies as belonging to two distinct "Funds," instead of funding sources for the Fund. Findings 2 and 3 discuss the accounting treatment given these funding sources and the review practices of Finance.

Lottery Contributions. Education attributed delays in the issuance of Lottery checks to the schools to receiving Lottery contributions late in the fiscal year. We found that problems related to the timeliness of the funding were partly linked to the small levels of contributions initially received from the Lottery, which for Fiscal Year 2004 was only $49,070. The funding, however, increased substantially over the audit scope period. By the end of Fiscal Year 2007, the Lottery had contributed $6,425,316, more than enough to the meet the funding requirements of the Code. As a result, Education officials said the decision was made to fund the schools solely from Lottery contributions starting in Fiscal Year 2008. The increased funding should facilitate the timely processing and issuance of check disbursements to the schools. Finance and Education must ensure that Funds are promptly disbursed to the schools at the beginning of each fiscal year.

The following exhibit shows the time delay in months that it took for selected schools to receive their funding disbursements after the beginning of each of Fiscal Years 2004 through 2006. Time delay measurements were determined based on the month in which schools received or deposited checks rather than on a 30 day duration period.

Exhibit D

Schools	Fiscal Year 2004*		Fiscal Year 2005		Fiscal Year 2006	
	Time Delay in Months to Receive Checks Funded by the *General Fund*	Time Delay in Months to Receive Checks Funded by the *Lottery*	Time Delay in Months to Receive Checks Funded by the *General Fund*	Time Delay in Months to Receive Checks Funded by the *Lottery*	Time Delay in Months to Receive Checks Funded by the *General Fund*	Time Delay in Months to Receive Checks Funded by the *Lottery*
Sibilly	2		2	14	7	10
Kirwan/Abraham	2		6	14	6	10
Charlotte Amalie	8	15	7	14	8	12
Kean High	14	13	21	14	N/A	12
Bertha Boschulte	9		N/A	14	N/A	10
Julius Sprauve	2		3	14	9	10
Guy Benjamin	2		3	14	8	12
Henderson	9		6	13	16	11
Claude Markoe	2		3	16	7	16
Central High	48	12	N/A	12	N/A	13
Ricardo Richards	42		N/A	15	N/A	13
Eulalie Rivera	3		3	14	5	13
Arthur Richards	2		3	14	4	9
Positive Alt. Ed.	N/A		N/A	N/A	N/A	N/A

* For Fiscal Year 2004, only five of the Territory's schools received funding from Lottery contributions. Three are in our sample of schools.
N/A Based on provided documents, we could not determine when or if these schools had received their allocations.

Lottery Contributions Due the Fund

The V.I. Lottery owed a minimum of $726,903 in contributions to the Fund from private contractor gaming revenues received over the audit scope period. Payment documents and audited financial statements showed that the V.I. Lottery paid $6,425,316 to the Fund from $28,608,873 in compensatory revenue received from private contractors beginning in the fourth quarter of Fiscal Year 2003 to the end of the fourth quarter of Fiscal Year 2007. Based on applying the lower of the Code's two contradictory revenue percentage payment requirements (25% instead 35%), we found that the V.I. Lottery should have paid at least $7,152,219 to the Fund. Its contributions, however, totaled only a little over 22% of the collected private contractor revenue.

Our audit found that neither Finance nor Lottery was aware that Lottery had not met its revenue payment obligations to the Fund. For instance, during our review of payment documents, we discovered that Lottery was unaware that it had missed an August 2007 payment. In response to our inquiry, the Lottery Director said that the Agency had "inadvertently omitted that month's payment," of which he informed us totaled $207,875. As of the issuance of this report, the missed August payment was still outstanding.

Finance, as the administrator of the Fund, had not taken steps to routinely verify that revenue payments to the Fund were in accordance with even the 25% revenue payment requirement stipulated in the Code. As a result, it was also unaware of the outstanding payments. The Code includes provision which enables Finance to verify if payments to the Fund are complete and current. The Lottery Director is required to submit certified monthly reports of lottery revenues to the Commissioner of Finance and the Lottery Commission. Our audit found that this reporting requirement had not been met by the V.I. Lottery for Fiscal Years 2002 through 2007, nor was there any evidence that Finance had required the revenue reports.

Recommendations

We recommend that the Commissioner of Education:

1. Revisit and consider resubmitting the proposal recommending that the Code's formula be amended to allow for the equitable distribution of funding to the schools.
2. Propose that the Code be amended to stipulate a time period in which Lottery contributions must be paid to the Fund.
3. Ensure that schools expenditure reports are submitted to Finance in accordance with the law. This will facilitate the timely disbursement of funding to the schools.

We recommend that the Commissioner of Finance:

1. Ensure, in partnership with Education, that schools receive the funding that has been set aside for them.

2. Ensure, in partnership with Education, that funding checks are timely distributed to schools each fiscal year.

3. Verify, on a routine basis, that Lottery payments to the Fund equal the required payment percentage of private contractor gaming revenue stipulated in the Code.

We recommend that the Virgin Islands Lottery Commission direct the Virgin Islands Lottery to:

1. Pay the outstanding revenue contributions owed the Fund.

2. Submit certified monthly reports of lottery revenues to the Commissioner of Finance as required by law.

Department of Education's Response

The Governor of the Virgin Islands, on January 26, 2011, submitted a consolidated response to the audit recommendations made in the report. Included as a part of the response were comments made by Education, Finance and the Virgin Islands Lottery Commission as they related to recommendations applicable to each. It was noted in the response that the audit scope period covered Fiscal Years 2002 through 2007, and that Finance and Education had already implemented a majority of the corrective measures proposed in the report. It was also noted that, "Although the auditor was privy to this information, there was no substantial reference made to the already instituted corrective actions in the relevant parts of the draft report."

For recommendation one, Education agreed that the funding formula, as written, does not allow for the equitable distribution of funds to the schools in proportion to their enrollment populations. It allows schools with lower student populations to be awarded larger sums than schools within the other district with more or equal student populations. The department indicated that it will submit recommendations to amend the contradictory language in the formula.

Education deferred to Finance for the issuance of a response to recommendation two. It chose not to respond stating that the recommendation and its corresponding finding were not applicable to the department. Finance issued a response which acknowledged that there is no time stipulated in the Code for the payment of V.I. Lottery contributions to the Fund. The department also stated that the V.I. Lottery already has been making quarterly contribution payments to the Fund. In light of this, it will submit a recommendation providing for quarterly contribution payments from the V.I. Lottery.

Education concurred with recommendation three, acknowledging noncompliance as it related to submitting expenditure reports to Finance during the period covered by the audit. The department indicated that it corrected the reporting delinquencies by issuing, in June 2008, a memorandum to the district Insular Superintendents which stipulated quarterly reporting due dates and explained the action to be taken against noncompliant schools. Funds are withheld from schools until quarterly reports are submitted. In addition, the Superintendents are required to hold school administrators accountable for noncompliance.

V.I. Inspector General's Comments

Regarding the comment that substantial reference was not made in the draft report concerning corrective measures taken by the departments after the audit scope period (Fiscal Year 2002 – 2007), the departments, in responding to the report recommendations, did not specify which corrective actions the V. I. Inspector General's Office should have made "substantial" reference to in the draft report, a rather subjective proposition. During the course of the audit, Education officials provided auditors with a copy of the School Fund Management Manual, which was published by Education and distributed to school administrators after the audit scope period. The manual represents a key corrective measure taken by the department to provide guidance to school administrators regarding three government funds, which include the Fund. The draft report specifically addressed this manual, referencing its confusing and problematic aspect. As noted in the report, we found that the manual does not clearly outline allowable and unallowable costs relative to the Fund, leaving it up to the schools to differentiate such costs (see Finding 2: Expenditures). The inclusion of discussions on the manual in the draft report, which included alerting the departments to its deficiencies, was intended to improve existing internal controls over the management and use of Fund resources. We believe that the manual and all other issues relevant to the audit were amply covered in the draft report.

The responses to recommendations one and two from Education and Finance, respectively, are sufficient for us to consider them resolved. Appendix II of this report details the additional information needed before the recommendations can be considered closed and fully implemented.

We, however, consider Education's decision not to respond to recommendation two as evasive. Its position on the inapplicability of the recommendation to the department is unfounded. Education has the most to gain by proposing, through established protocols, that the Code be amended to stipulate a time period in which Lottery contributions must be paid to the Fund. This is especially true since the decision was made in Fiscal Year 2008 to fund the schools solely from Lottery contributions. We understand that Education does not have the final say on this matter, but neither does Finance. We are advocating that Education take the same initiative in proposing that a time period be established for Lottery contribution payments as it did in proposing that the Code's funding formula be amended.

Although Education concurred with recommendation three, we consider this recommendation unresolved. Based on our recent follow-up review, we found that schools were not submitting quarterly reports as required by the June 2008 memorandum. In addition, we also

found that schools were not even submitting reports in accordance with the reporting requirements of the Code. For 20 of the 21 schools in our review, submission delinquencies ranged from 10 to 13 months to not at all for Fiscal Years 2008 and 2009 funding. The one exception was St. Croix school Positive Alternative Education which was closed after the end of Fiscal Year 2007. As of the conclusion of the follow-up review on December 8, 2010, none of the active St. Croix schools in the review had submitted expenditure reports accounting for the use of Fiscal Year 2009 funds and none of the schools in the review had submitted reports for funding related to Fiscal year 2010. Although we acknowledge the department's efforts to correct the schools' delinquent reporting, the instituted corrective action is not either being enforced or followed.

Department of Finance's Response

Finance indicated general agreement with recommendation one and a section of the Inspector General's draft report that stated that substantial increases in V.I. Lottery contributions facilitated schools receiving the funding that has been set aside for them. Finance provided the following excerpt from the draft report.

> The funding, however, increased substantially over the audit scope period. By the end of Fiscal Year 2007, the Lottery had contributed $6,425,316, more than enough to meet the funding requirements of the Code. As a result, Education officials said the decision was made to fund the schools solely from Lottery contributions starting in Fiscal Year 2008. The increased funding should facilitate the timely processing and issuance of check disbursements to the schools.

In support of its corrective action plan, Finance noted that as of the beginning of 2008 schools have been receiving all their funding as a result of the substantial increase in V.I. Lottery contributions. In addition, the department stated that it will work with Education to devise procedural measures for ensuring that schools receive their set aside funding.

Finance concurred with recommendation two. In its response, Finance made reference to a section of the draft report which partly linked delays in the distribution of checks to the timing of expenditure report submissions by Education. Finance provided an excerpt from the section which notes that Finance needed the previous fiscal year's expenditure reports to initiate check processing for the schools…as it related to General Fund monies. It also provided the following quote from the report, "We found that Finance had not received school expenditure activities for monies that had been funded by the Lottery. This did not prevent the schools from receiving their yearly Lottery funding."

Finance stated that since the V.I. Lottery became the primary funding source for the Fund, beginning in Fiscal Years 2008, Finance disburses funds to compliant schools based on funding determinations made by Education at the beginning of the school year. As part of its action plan, Finance indicated that it "will continue to monitor fund disbursements to compliant schools to ensure timely distribution of checks." Also, it will work together with Education to develop ways of ensuring timely distribution of checks to schools through initiatives which include possibly placing sanctions on schools for noncompliant and delinquent reporting.

Finance concurred with recommendation three. Finance stated that beginning in March 2011 and with the next quarterly remittance from the V.I. Lottery, the department will implement a "verification process to ensure Code compliance."

V.I. Inspector General's Comments

Regarding recommendation one, our recent follow-up review disclosed that all schools in our review that had submitted expenditure reports had received the funds set aside for them for Fiscal Years 2008 through 2010. As of the close of the review (on December 8, 2010), none of the reviewed St. Croix schools had received their 2010 funds due to expenditure reports not having been submitted. While we acknowledge that the substantial increase in V.I. Lottery contribution allows for schools to finally receive their allocations in amounts required by law, this in itself does not necessarily guarantee that schools will receive their allocations. There must be meaningful monitoring and intervention by the responsible departments. As explained during the exit conference and a subsequent meeting on September 29, 2010, and January 11, 2011, respectively, the recommendation specifically addresses the 16 schools that had not received $378,827 in funding that had already been set aside for them. The monies or funding had been allotted and allocated, yet there was no evidence that checks had been processed and distributed to the schools.

While we acknowledge that schools may not have received their funding due to non-reporting, for schools to have gone as many as four consecutive years without receiving funds that had been set aside for them was unacceptable. As it related to certain schools not consistently receiving their yearly allocations, we saw no evidence of intervention by either Finance or Education to remedy the problem. Obviously, we are encouraged that Finance will partner with Education to devise procedural measure for ensuring that schools will receive the funding set aside for them.

In addressing Finance's response to recommendation two, our recent follow-up review revealed that funding checks are still not being distributed to schools in a timely manner. Funds designated for distribution in one fiscal year are being distributed in the next. Funds related to Fiscal Years 2008, 2009 and 2010 were distributed to the reviewed schools in Fiscal Years 2009, 2010 and 2011, respectively. As of the follow-up review, the active St. Croix schools in our review had not received any funding for Fiscal Year 2010. For the schools that had received checks, Finance notified them that their checks were ready for pickup from 12 to 16 months after the fiscal year had begun for the three fiscal years reviewed. We support Finance's plan to work together with Education to develop ways of ensuring timely distribution of checks to schools. We are aware that Finance cannot implement the recommendation by itself; it needs the cooperation of Education.

Regarding recommendation three, we consider the response to be sufficient for us to close the recommendation. However, we require documentation of verification procedures performed to ensure Code compliance (Appendix II).

Virgin Islands Lottery Commission's Response

The V.I. Lottery Commission agreed with both recommendations. Regarding recommendation one, the Commission recognized that the V.I. Lottery missed an August 2007 payment to the Fund totaling $207,875. The Commission stated that it authorized the Director to pay the outstanding contributions in quarterly payment amounts totaling $51,968.75 through the end of Fiscal Year 2011 (September 30, 2011). Regarding recommendation two, the Commission stated that the V.I. Lottery started implementing the submission of certified monthly reports to Finance beginning in Fiscal Year 2007.

V.I. Inspector General's Comments

The V. I. Lottery Commission's responses to recommendations one and two are sufficient for us to consider these recommendations resolved. However, we do require documentation of the quarterly payments made against the total outstanding $207,285 amount owed the Fund for August 2007.

Regarding recommendation two, during the audit and our recent follow-up review, we found no evidence to show that the V.I. Lottery had submitted certified monthly reports of lottery revenues to Finance since Fiscal Year 2007. During the audit, in a written response dated October 15, 2009, the V.I. Lottery Director informed the V. I. Inspector General's Office that there was no documentary evidence showing that certified monthly reports had been submitted to Finance during Fiscal Years 2002 through 2007. In addition, our recent review found that the earliest record of a report submission was November 30, 2009, for October 2009 revenue activity. We found that reports were submitted after that through July 28, 2010, for June 2010 revenue activity.

FINDING 2: EXPENDITURES

Schools did not expend and account for the uses of Fund monetary resources in accordance with the law. Of the estimated $1,275,857 in school expenditures we audited, $257,802 was not allowable under the law, $429,436 was not adequately supported, and at least $220,246 was not properly authorized. This was attributable to Finance and Education's failure to provide adequate guidance to the schools regarding the uses and limitations of the Fund. As a result, Fund resources were not used as intended due to the expenditure practices of the schools.

Background

In an interview, the primary sponsor of the bill creating the Fund explained that Fund resources were intended to help schools deal with immediate needs and emergencies in a timely manner. A motivating factor for sponsorship was to help prevent the frequent closure of schools due to urgent situations such as water shortage emergencies. The sponsor added that the Fund was never intended to supplant Education's acquisition of goods and services through the regular budget and procurement processes, as required by law.

Title 33, Section 3093 of the Code stipulates that monies from the Fund are not to be used to purchase the following:

- Entertainment items, goods, or services;
- More than $3,500 worth per year of equipment and supplies for administrative offices;
- Donations, raffles, tickets, or other related expenditures;
- More than $2,500 for personal services per person, legal entity, employee, or representative thereof, and not more than 50% of the school's total allocation on personal services;
- Vehicles; or
- Travel.

The Code stipulates, "Principals will consult with the School Based Management Team at their respective sites prior to making any expenditure over $500 except that Principals may make expenditures prior to seeking approval in cases of emergency. Such emergency expenditures over $500 must be reported to the School Based Management Team at the next meeting of the body."

The Code requires that each school establishes an imprest fund checking account (Fund checking account) specifically for the deposit of monies from the Fund. The school principal and the next ranking assistant principal in the absence of the principal serve as the custodians of the account. Custodians must submit reports to the Commission of Education and district Insular Superintendent detailing the amount, nature, and the justification of expenditures. Original receipts and other supporting documentation must accompany the reports.

Expenditures Review Results

Our review of $1,275,857 in public school expenditures disclosed that $257,802 was unallowable under provisions of the Code, and $429,436 was not adequately supported. In addition, at least $220,246 in expenditures was not properly authorized. These expenditures were discovered by reviewing the accounting records and other supporting documents for the 14 public schools comprising our sample. The extent of our expenditure review was largely dependent on the availability of files and records housed at Education's main offices on St. Thomas and St. Croix, and at the schools. The reviewed $1,275,857 in expenditures did not represent the total expenditures incurred by the sampled schools who had received $2,174,113 in Initiative funding over the audit scope period. Our review was limited to the $1,275,857 because of the unavailability of school expenditure reports for certain reporting periods and the commingling of funds.

Availability of School Expenditure Reports. Our audit found that 9 of the 14 public schools could not provide any documentation to support expenditures incurred in some fiscal years. The expenditure reports were also not available at Education's main offices on St. Thomas and St. Croix. Each of the 9 schools had no reports to account for expenditures incurred over 1 to 5 fiscal years. Additionally, reports for 5 of the 9 schools were not available for expenditures made in Fiscal Years 2006 and/or 2007, the two most recent years in the audit scope period. The general explanation we received was that the reports could not be found. Custodians of schools' Fund checking accounts indicated that they did not know where their predecessors had filed the expenditure reports because they had received no briefing when custodianship was assumed. Consequently, due to the unavailability of the records, we were unable to verify that certain schools' fiscal years expenditures were made in accordance with applicable guidelines and the law.

Commingling of Funds. Our expenditures review was also limited because of the commingling of funds by four schools. Fund custodians for the schools commingled Initiative funds totaling $142,222 with non-Initiative funds. The custodians deposited the Fund monies, which were received from Fiscal Years 2006 and 2007 funding disbursements, into either the schools' general or substitute teacher checking accounts. The inadequacy of the recordkeeping by the custodians did not allow auditors to clearly and fully identify expenditures related to Fund monies.

Unallowable Expenditures

The public schools comprising our sample expended Fund monies totaling $257,802 for goods and services not allowed under provisions of the Code. The unallowable expenditures included $39,765 for substitute teacher payments, $35,244 for entertainment and gift items, $29,654 for travel expenses, and $1,475 for donations. In addition, payments to vendors for personal services or labor costs exceeded the $2,500 limit that could be paid to each vendor, per year, by $84,379. This was based on personal services expenditures totaling $184,379. We also found that of $21,782 in expenditures made for administrative offices equipment, $7,782 was in excess of the $3,500 amount allowed, per year, for such expenditure for each school.

In addition, schools accumulated $59,503 in other unallowable expenditures, which included expenditures incurred for issuing loans; conducting teacher training and professional development conferences; opening prepaid vendor accounts at various retail establishments; paying stipends; paying accreditation association dues and fees; paying late fees and delinquent prior obligations; and paying bank fees assessed against the schools' Fund checking accounts. According to Finance guidelines, bank fees should not be charged to the accounts. At the time of a checking account's establishment, the custodian is required to present a letter to the banking institution, from the Commissioner of Finance, to ensure that fees are not assessed against the account. Our interviews with the custodians revealed that some of them were not aware of this provision.

The following exhibits show the unallowable expenditures incurred by each of the 14 schools in our sample by the schools' respective districts.

Exhibit E
St. Thomas/St. John District

Schools	Total Expenditures Reviewed	Total Unallowable Expenditures	Unallowable Expenditures by Classification						
			Substitute Teacher	Travel	Entertainment/ Gifts	Donations	Over $2,500 Limit for Personal Services	Over $3,500 Limit for Admin. Equip.	Other
Sibilly	$106,596	$19,819			$4,722		$8,142		$6,955
Kirwan/ Abraham	82,846	10,908			936		5,163		4, 809
CAHS	186,737	14,882	$3,616	$9,890					1,376
Kean H.S.	154,243	54,940	24,380	7,350	$9,145	$1,000	2,140		10,925
Bertha Boschulte	90,928	32,526				175	21,502	$3,874	6,975
Julius Sprauve	119,304	17,353	1,560	922	4,245		1,975		8,651
Guy Benjamin	121,056	30,795	9,049	5,809	2,696		9,241		4,000
Totals	$861,710	$181,223	$38,605	$23,971	$21,744	$1,175	$48,163	$3,874	$43,691

Exhibit F
St. Croix District

Schools	Total Expenditures Reviewed	Total Unallowable Expenditures	Unallowable Expenditure by Classification						
			Substitute Teacher	Travel	Entertainment/ Gifts	Donations	Over $2,500 Limit for Personal Services	Over $3,500 Limit for Admin. Equip.	Other
Central High	$86,409	$22,859	$584	$417	$2,700		$19,158		
Alexander Henderson	47,300	4,226	576		2,585			$1,065	
Arthur Richards	64,379	2,566			1,266	$300	500	500	
Claude O. Markoe	67,170	16,687		5,266	5,736		4,965		$720
Eulalie Rivera	57,983	4,636					4,636		
Positive Alternative	16,416	6,089					1,890		4,199
Ricardo Richards	74,490	19,516			1,213		5,067	2,343	10,893
Totals	$414,147	$76,579	$1,160	$5,683	$13,500	$300	$36,216	$3,908	$15,812

Exhibit G
Combined Totals St. Thomas/St. John and St. Croix Districts

Schools	Total Expenditures Reviewed	Total Unallowable Expenditures	Unallowable Expenditure by Classification						
			Substitute Teacher	Travel	Entertainment/ Gifts	Donations	Over $2,500 Limit for Personal Services	Over $3,500 Limit for Admin. Equip.	Other
St. Thomas Schools	$861,710	$181,223	$38,605	$23,971	$21,744	$1,175	$48,163	$3,874	$43,691
St. Croix Schools	414,147	76,579	1,160	5,683	13,500	300	36,216	3,908	15,812
Totals	$1,275,857	$257,802	$39,765	$29,654	$35,244	$1475	$84,379	$7,782	$59,503

Entertainment/Gifts. In the above schedules, we treated schools' hiring of catering services and purchasing of food items for recognition luncheon and dinners, teacher training conferences, faculty meetings, parties, and similar functions under entertainment. These represented the bulk of expenditures under this classification. Other entertainment expenditures included, for example, the purchase of $3,130 in movie tickets for students to attend a movie cinema, the payment of $497 for a music band's engagement at a school function, and the payment of $509 to cover expenses related to a school troop's participation in the 2002 Carnival Children's Parade. Expenditures classified as gifts consisted of plaques and trophies for teachers and students and assortments of novelty items such as balloons, clocks, t-shirts, books, flowers, teacher mugs, and gift cards and certificates. Our review of submitted documents confirmed that schools had reimbursed $6,436 of the $35,244 expended for entertainments and gifts. The reimbursement amount included $2,750 of the $3,130 paid for the purchase of the movie tickets.
Travel. The schools' use of Fund monies totaling $29,654 to cover travel expenses included funding staff and student interisland and United States mainland travel to conferences, workshops, sporting and other events. The travel expenses encompassed costs related to fares,

accommodations, allowances, and event and conference fees. The travel expenses also included the cost of commutes between St. John and St. Thomas by a principal of the Guy Benjamin Elementary School on St. John. The principal paid barge fares totaling $4,297 for the interisland commutes which occurred over Fiscal Years 2003 through 2006. The principal had requested in writing approval from Finance to use Fund checking account monies for the commutes. Provided documents did not indicate if Finance had approved the request. However, regardless if approval was granted, Finance has no authority to grant such approval under provisions of the Code.

The Charlotte Amalie High School (CAHS) also shared a similar situation related to the alleged granting of approval by government officials to use Fund monies for travel. A compliance review conducted by Finance, for school year 2004–2005, found CAHS to be in violation of the Code for incurring travel and vehicle rental expenditures totaling $9,890. The entire questionable amount was used to fund travel for students to participate in the Penn Relays, a track and field event, in Pennsylvania. In a written response addressing the finding, the school's principal noted that the violation occurred because permission had been granted by the Commissioner and the Insular Superintendent of Education to use Initiative funds for the travel. The principal added that the understanding was that the Fund checking account would be reimbursed. Again, regardless if approval was given, Government officials and agencies have no authority to override provisions of the Code.

Substitute Teacher Payments. Schools issued $39,765 in payroll checks to substitute teachers from Fund checking accounts even though the Substitute Teacher Pool had been established as a funding source for that purpose. School officials informed us that the payroll payments were made from the Fund checking accounts because they had not received Substitute Teacher Pool monies in time to meet payroll obligations to the teachers. Based on provided documents, we confirmed the reimbursement of $18,032 of the $39,765.

Personal Services. Schools used Fund monies to pay recurring casual labor costs and fund construction and repair projects that should have been acquisitioned through the regular budget and procurement processes. These practices resulted in the sampled schools' labor cost payments to vendors exceeding the allowable amount of $2,500 per vendor, per year, by $84,379. For instance, one school paid $15,853 to 3 vendors for recurring landscaping and cleaning services which resulted in combined excess personal services payments of $8,353. In addition, the same school, over the same year, paid another vendor $4,280 on an $8,405 invoice for labor costs associated with electrical service repairs to classrooms and office facilities. Personal services expenditures represented 72% of the $27,945 in total allocation the school received that year. As stated, the Code stipulates that no more than 50% of a school's total allocation must be used on personal services. Although we do not question the validity of the needs for these expenditures, we do emphasize the public schools' responsibility to follow Code provisions governing expenditures. The Government should examine whether the expenditure ceilings need to be raised to better accommodate the needs of the schools, and amend the law accordingly, if such action is required.

Unsupported Expenditures

Our audit found that $429,436 or 34% of the $1,275,388 in reviewed expenditures was either unsupported or inadequately supported by receipts, invoices, timesheets, and/or canceled checks. As a result, the validity of these expenditures could not be properly verified. The $429,436 in unsupported and inadequately supported expenditures consisted of $319,573 for the St. Thomas schools and $109,863 for the St. Croix schools. The St. Thomas schools amount represented 37% of their $861,710 in reviewed expenditures and the St. Croix schools amount represented 27% of their $414,147 in reviewed expenditures. The assessed unsupported amount of $429,436 was determined by auditing school expenditure reports. In some instances, when available, schools' check registers and files were the primary audited documents if expenditure reports had not been submitted to Education or could not be produced by either Education or the schools.

Authorization of Expenditures

The sampled schools expended at least $220,246 in Fund monies without proper authorization. The specific breach involved the schools making expenditures over $500 each without first consulting with their respective School Based Management Teams as stipulated by the Code. Based on interviews with the principals and Education officials, we found that the schools' non-adherence was primarily due to their unawareness of this requirement. In addition, some principals could not definitively state whether their schools had a functioning School Based Management Team. Others had never heard of such a management body. An Education official said that steps would be taken to immediately implement the Code's requirements. However, the schools would be reporting to a body called the School Improvement Team.

The breakdown in expending Fund monies was reflected in the high expenditures made by some schools without proper authorization. Single expenditures were as high as $14,200. Additionally, some schools entered into maintenance contracts for office equipment with vendors for as high as $6,600. These contracts should have been planned for through the budget process. A memorandum of agreement, dated February 21, 2003, between Education and the Virgin Islands public high schools required that three bids be taken for any purchase over $1,000. None of the schools in our sample provided documentary evidence of adhering to this requirement for Fund checking account expenditures.

The Code provides exceptions regarding the schools' reporting requirements. First, in cases of emergencies, principals do not have to report to their respective management teams prior to making any expenditure over $500. However, their management teams must be informed of the expenditure at the next scheduled meeting of the body. Second, the Code states that, "The requirements of this section shall not apply to any school whose School Based Management Team has not met in 30 days prior to the time of expenditure." Although the latter does provide, under special circumstances, some degree of autonomy in the schools' reporting obligations to their respective School Based Management Teams, it certainly does not allow for neglecting the responsibility of fully implementing the section's requirements.

Guidance

Finance and Education failed to provide adequate guidance to the schools regarding the uses and limitations of the Fund. Reviewed documents revealed that agency officials did not have a thorough understanding of the statutes establishing and governing the Fund. They treated General Fund monies and Lottery monies as belonging to two distinct "Funds," instead of funding sources for the Fund. Guidelines and other documentation originating from both agencies linked General Fund monies to the Fund and Lottery monies to a "Lottery Fund." This resulted in the dissemination of inaccurate information to the schools. For instance, Finance issued a compliance report for school year 2005 that incorrectly found a school to be in noncompliance for commingling funds. In the report, Finance stated that the school had commingled funds by depositing Lottery received monies into its Fund checking account. On the contrary, the school did not commingle funds, for schools are required by law to deposit Lottery monies (a funding source for the Fund) into their Fund checking accounts. The Finance report findings were perpetuated in compliance reports and guidelines produced by Education for the schools. We found that some schools were allowed to unnecessarily open two checking accounts for the deposit of Fund monies: one for General Fund monies, and the other for Lottery monies.

The difference in treatment given to General Fund and Lottery contributions were highlighted in Fiscal Year 2008 guidelines disseminated to the schools by Education. The guidelines erroneously classified the contributions under two different Funds even though the contributions are funding sources for the Fund. The named Funds under which the contributions were classified were "Initiative" and "Lottery."

Ambiguous Guidelines. Guidelines distributed to the schools by Education did not clearly identify allowable or unallowable costs. The ambiguity of the guidelines was reflected in a 2003 memorandum of agreement which existed between Education and the high schools. The memorandum was established to set forth the policies and procedures for administering funds for the Accreditation Fund, the Substitute Teacher Pool, and the Fund. The memorandum made reference to an addendum that listed the allowable and unallowable costs for the three funds. However, the addendum consisted merely of a general list of acceptable and unacceptable costs which were not linked to their respective Fund. This format left it up to the schools to decipher what costs were applicable (or not applicable) to the Fund. The memorandum also failed to list certain prohibited costs and explain restrictions placed on certain allowable ones. For instance, no detail existed explaining that casual labor cost was limited to $2,500 per vendor, per year, and could not exceed more than 50% of a school's total allocation.

Subsequent to the 2003 memorandum of agreement, Education produced two sets of guidelines for the schools. The first was the 2008 guidelines (discussed in the previous subsection) and the second was a School Fund Management Manual, which had a revised copy date of February 27, 2009. As stated, the 2008 guidelines classified General Fund monies under the Fund and Lottery monies under a "Lottery Fund." This form of classification for funding sources of the Fund was ambiguous. We found that the "Funds" under which General Fund and Lottery contributions were classified had varying sets of allowable and unallowable costs. For example, travel was listed as an unallowable expenditure under the (Initiative) Fund, but an

allowable expenditure under the "Lottery Fund." In another example, construction of facilities was listed as unallowable under the Fund, but was not prohibited under the "Lottery Fund."

The School Fund Management Manual addressed the policies and procedures governing the Accreditation Fund, Substitute Teacher Pool, and the Fund. Although more comprehensive than previously issued guidelines, its presentation format of allowable and unallowable costs did not link these costs to their respective Fund. Consequently, as with the 2003 memorandum, this left it up to the schools to discern which costs were applicable (or not applicable) to the Fund.

Education Guidelines Departures. We considered certain costs, listed as allowable, in Education guidelines outside the intended purpose of the Fund. The following are examples of these costs.

- Professional Training and Development
- Registration fees for seminars/conferences
- Room deposit for persons attending seminars/conferences outside the Virgin Islands
- Utility services for offices outside the Virgin Islands, as needed
- Subscriptions to publications
- Advertising in media, to include newspaper, magazines, radio, and television

A 1994 policy memorandum, issued by the Commissioner of Education, informed key Education officials and school principals that the rationale for establishing Fund checking accounts was to provide materials, supplies, equipment and other related goods to the schools in a timely manner. Also, as noted, the sponsor of the bill creating the Fund related to auditors that the Fund was established to help schools deal with immediate needs and emergencies. These criteria suggest that Fund resources should directly impact the students and schools. Consequently, expenditures for professional training and development, and registration fees and room deposits for staff to attend seminars and conferences are outside the scope of the Fund's purpose. These expenditures should be paid for through the regular budget process or another funding source.

Recommendations

We recommend that the Commissioners of Education and Finance:

1. Communicate to the schools, accurately, clearly and consistently, the provisions of the Code regarding expenditures as they relate to uses and limitations, documentation support, and authorization.
2. Implement and enforce the provisions of the Code governing expenditures.

Department of Education's Response

Education agreed with our recommendations in this section of the report. Regarding recommendation one, the department acknowledged that during the audit scope period all schools may not have received informational guidance regarding Fund expenditures as set in the Code. Education further stated that in 2008 the department created the Fiscal and Administrative Services School Fund Management Manual to provide guidance to the schools. The manual was given to the V. I. Inspector General's Office for the purpose of evaluating the department's current procedures and including the results of the review in the audit report. Education stated, "The manual provides rules, regulations, and the operating procedures for the Education Initiative Fund; as well as, it includes the provisions of the Virgin Islands Code regarding the uses and limitations of the Initiative Fund, documentation required, and the authorizations needed." In addition to the manual, the department said that both districts have hired Financial Control Officers and School Accountants to assist schools in managing their financial accounts. Education presented the manual as part of its corrective action initiative and stated that in partnership with Finance it will work to revise the manual.

Regarding Recommendation two, Education acknowledged that the department did not implement and enforce the provisions of the Code governing expenditures during the audit scope period. In the response the department made reference to its implementation of the Fiscal and Administrative Services School Fund Management Manual and its hiring of the Financial Control Officers and School Accountants as corrective measures to ensure proper management and use of Fund resources. It also stated that the Insular Superintendents are tasked with monitoring and taking action, which includes issuing warnings and reprimanding school administrators, to address departures from the procedures outlined in the manual.

V.I. Inspector General's Comments

We consider Education's response to recommendations one sufficient to consider this recommendation resolved. However, we require a copy of the revised School Fund Management Manual.

Regarding recommendation two, we will discuss the results of our recent follow-up review of expenditures incurred by the Territory's schools during Fiscal Years 2008 through 2010. Although the review was limited, we looked at records maintained by Finance for 21 schools, and found that schools were still not using Fund monetary resources in accordance with the law. Specifically, we found that schools had expended more than $82,974 in unallowable expenditures for travel, substitute teacher payroll payments, vendor services and entertainment. In addition, except for one transaction totaling $13,300, we saw no documentation to show that other transactions totaling more than $500 were properly authorized. We note that these infractions also occurred in Fiscal Year 2010.

As it pertains to travel related expenditures, we found that they totaled $30,539. Of that amount, we were able to document reimbursements totaling only $9,735. Education's Financial Control Officers did not note on their review sheets that schools were not in compliance with the

Code for $16,525 of the travel related expenditures. For an additional $14,014 the officers did note noncompliance, but for $4,274 of that amount indicated that it was because the schools had not received preapproval for the travel. In addition, during our meeting on January 11, 2011, Education officials were under the wrong impression that travel was an allowable use of the Fund. It was emphasized then and reiterated again that travel is unallowable – no exceptions.

Regarding the substitute teacher payroll payments, expenditures totaled $33,804. School records show that the payments originated as loans to substitute teacher pool checking accounts. However, we were able to verify reimbursements totaling only $18,750. Loans cannot be used as justification to override provisions of the Code. We note that $15,000 or 44.38% of the $33,804 in substitute teacher payments occurred in Fiscal Year 2010.

Vendor services payments, which were linked to two schools, exceeded the allowable amount for such services by as much as $18,200. As noted in the report, we do not question the validity of the need for such expenditures. However, we do emphasize the schools responsibility to follow Code provisions. If changes need to be made to better accommodate the needs of the schools, the Government should do so and amend the Code accordingly.

As noted, we agree with Education's decision to revise the manual in partnership with Finance. We believe that there is a correlation between our review findings and the existing manual's presentation format. As indicated in the report, the manual, as published is ineffective and confusing. Though not the intent of the department, the manual contradicts the Code and allows for the misuse of Fund resources by schools. It addresses three government funds: The Accreditation Fund, the Substitute Teacher Pool, and the Fund. The section entitled "Fund Usage" is problematic in that it provides a general list of allowable and unallowable costs without linking these costs to their respective government funds. For instance, travel and substitute teacher payroll payments are listed as allowable costs, but the section does not indicate to which funds these costs apply. The section's presentation format leaves it up to the schools to determine which costs are applicable (or not applicable) to the Fund.

Department of Finance's Response

Finance concurred with our recommendations in this section of the report. For recommendation one, the department indicated that it already provides a copy of the Code's section governing the uses and management of Fund resources when disbursement checks are distributed to school administrators. In addition, the department referenced Education's School Fund Management Manual as a guidance tool which outlines rules, regulations and operating procedures for the Fund. By August 2011, the department plans to include a signature line on copies of the relevant Code criteria that is provided to school administrators when checks are distributed. In addition, working with Education, it will revise and reissue the School Fund Management Manual as a joint document.

Regarding recommendation two, Finance stated that the recommendation has already been addressed through the department's issuance of the "Education Initiative Fund – Findings and Exception Reports" to the Commissioner of Education. The issuance of the Findings and Exceptions Reports is part of Finance's Annual Compliance Review.

V.I. Inspector General's Comments

In addressing Finance's response to recommendation one, we are pleased that the department will reissue the School Fund Management Manual as a joint document with Education. As noted in the report and in our above comments to Education, the manual, as published, is flawed. It contradicts the Code by providing loopholes for schools to misuse and abuse Fund monetary resources. In reissuing the manual Finance and Education should communicate to the schools, the provisions of the Code accurately, clearly and consistently. To close this recommendation, we do require a copy of the reissued School Fund Management Manual for our review.

In reference to Finance's response to recommendation two, our follow-up review confirmed that the department is now issuing Education Initiative Fund – Findings and Exceptions Reports. However, we note that the recommendation calls for Finance and Education to implement and enforce provisions of the Code governing expenditures. Despite the now issuance of the Findings and Exceptions Report, we cannot at this time vouch for the degree of effectiveness of the implementation and enforcement of relevant provisions of the Code. Based on our follow-up review, there are dominant issues that still need to be addressed regarding schools' usage of Fund monies (see our above comments to Education). We agree that the Findings and Exception Report is a great tool in helping to accomplish implementation and enforcement objectives. This is why, in "Finding 3 – Internal Controls," we recommended that Finance prepare and provide them to Education as required by law. However, it is mandatory that Finance and Education meaningfully and accurately interact with the schools to ensure compliance.

FINDING 3: INTERNAL CONTROLS

Finance and Education did not effectively monitor schools' uses of awarded funds to ensure proper accountability and compliance with the law. We found that Finance did not review the expenditures for an estimated $2,979,285 in Fund monies disbursed to the schools, and did not consistently provide compliance reports to Education, as required by law. As the agency responsible for administering the Fund, Finance did not demonstrate that it had control over the Fund. We also found that Education did not properly monitor the schools' uses of Fund monies through the review and reporting processes.

These conditions were attributable to the failure of Finance and Education to follow the law governing the Fund and to implement good internal control practices. As a result, schools were not properly held accountable for the funding they had received.

Background

Title 33, Sections 3093 and 3100i of the Code, establishes the reporting protocols and procedures for accounting for and monitoring the uses of Fund monies. Principals are required to submit their expenditure reports to the Commissioner of Education and their respective Insular Superintendents. From the expenditure reports, Education then compiles and presents to Finance and the Legislature an Annual Financial Report of the fiscal year's activity by the 30th day of the month following the end of the fiscal year. Finance reviews the annual report submitted by Education for compliance with the Fund guidelines and provides a Findings and Exception Report within 30 days after the submission of the report. Finance's system of review entails preparing the Findings and Exception Reports from schools' submitted expenditure reports.

Lottery Monies Not Reviewed By Finance

The Department of Finance did not review expenditures for an estimated $2,979,285 in Lottery monies disbursed to the schools during the audit scope period. As noted, Finance accounted for Lottery monies and General Fund monies differently, even though they are both funding sources for the Fund. For instance, from Fiscal Years 2004 through 2007, Finance routinely disbursed Lottery monies to the schools without accounting for the use of the schools' previous year's Lottery funding disbursements. This occurred because it did not require or review schools' "Lottery" expenditure reports. In contrast, Finance required that Education submit schools' General Fund monies expenditure reports in order to replenish the schools' Fund checking accounts. Finance officials, from the General Ledger Division responsible for doing the compliance reviews, said that it was their understanding that General Ledger was responsible for reviewing only expenditure reports accounting for the use of General Fund monies, not Lottery monies. The officials said that Education had not submitted, to General Ledger, any expenditure reports for the $2,979,285 in funding schools had received from the Lottery beginning in Fiscal Years 2004 through 2007. The officials also said that had General Ledger received the "Lottery" reports, they would have reviewed them, even though they were unaware of their responsibility to do so.

In response, Education officials said that General Ledger would not have processed checks for the schools had Education not submitted reports accounting for the use of the previous year's Lottery funding. We, however, found that documents provided by Education either supported submission of reports accounting for only a small percentage of the total Lottery funding disbursement or did not clearly document the submission of reports to Finance. For instance, documents supplied by Education's St. Thomas/St. John Business office showed that the number of reports submitted by Education on behalf of St. Thomas/St. John district schools totaled only two. These reports represented only $20,000 of the estimated $1,497,941 in Lottery funds disbursed to the St. Thomas and St. John schools over Fiscal Years 2004 through 2007. For the St. Croix district schools, we were unable to clearly document, through the St. Croix Business Office, the submission of Lottery reports to Finance.

Based on the Code, Finance is ultimately responsible for administering the Fund. A key duty assigned the agency is the reviewing of school expenditures to ensure that all Fund monies – regardless of the funding source – are used in accordance with the requirements of the Code. Consequently, the failure of Finance to monitor the territory schools' uses of $2,979,285 in Lottery funding resulted in those funds not being accounted for.

Compliance Reports

Finance failed to consistently provide Findings and Exception Reports to Education as required by the Code. These reports are generated from General Ledger's compliance reviews of schools' expenditure reports and provide written feedback of review findings. We found that from Fiscal Years 2002 through 2007 Finance had provided Education with Finding and Exception Reports for a limited number of schools for only Fiscal Years 2004 and 2005. The issued reports documented review findings addressing the use and disposition of $342,242 in funding disbursements made to 27 of the 37 active schools over those two fiscal years. This amount represented only about 6.3% of the $5,475,640 in Fund monies disbursed to the schools over the audit scope period. The failure of Finance to provide the reports demonstrated that breakdowns in the monitoring process extended beyond the unreviewed $2,979,285 in Lottery monies. It included an additional $2,154,113 for which expenditure reports were received, but were not thoroughly reviewed.

1099-MISC Statement Reporting

Finance did not ensure that schools provided summaries of personal services payments, from Fund checking accounts, to non-employees or unincorporated vendors for the preparation of IRS FORM 1099-MISC. Policy memorandums issued by the Commissioner of Finance require schools to provide this information to Finance to ensure that income paid to vendors are reported to local and federal tax agencies. No school was found to have adhered to this requirement.

Education

Education did not properly monitor the schools' uses of Fund monies through the review and reporting processes. It did not provide consistent and timely feedback to the schools in direct response to their submitted expenditure reports. Other than two compliance reports Education had issued to the schools in Fiscal Years 2006 and 2007, no other reports or records were provided documenting the results of Education's internal reviews of schools' report submissions over the audit scope period. The two issued reports documented review findings addressing the use and disposition of $245,889 in funding disbursements made to 18 schools over Fiscal Years 2004 and 2005. This amount represented only about 4.5% of the $5,475,640 in Fund monies disbursed to the schools over the audit scope period. An Education official said that Education's internal compliance reports are directly based on the Findings and Exception Reports generated by Finance.

We found that transitioning principals had limited or no knowledge of the rules and regulations governing the uses and limitations of the Fund and were not briefed by their predecessors when assuming custodianship. Rules and regulations did not clearly and consistently appear in management directives, administrative policies or operating manuals to ensure that the Fund was properly administered. Except for a 2003 memorandum of Agreement between Education and the high schools, insufficient documentary evidence existed to show that Fund guidelines were properly disseminated to all schools over Fiscal Years 2002 through 2007.

Education had lost management control over the schools' reporting. Reports were generally not submitted to Education's Business Offices on St. Thomas and St. Croix in time for submission to Finance by the 30th of the month following the end of the fiscal year. In some instances, due to the inadequate maintenance of records, we could not determine when or if Education had received, from the schools, expenditure reports for certain funding periods.

Internal Control Weaknesses

Finance and Education's failure to adequately monitor Fund monetary resources resulted in lost opportunities to address and correct internal control weaknesses over schools' management and uses of awarded funds. Certain transactions and practices of the schools clearly violated good internal controls. For instance, the following summarizes key control weaknesses we found from our audit of the 14 sampled schools.

- Four schools issued checks payable to cash totaling $22,211. Custodians should be prohibited from writing checks payable to cash.

- Four schools commingled Initiative funds totaling $142,222 with non initiative funds. The Fund monies, which were part of Fiscal Years 2006 and 2007 funding disbursements, were deposited into either the schools' general or substitute teacher checking accounts.

- Bank reconciliations were not being completed by some schools, although a 1994 Policy Memorandum from the Commissioner of Finance requires monthly reconciliations be performed in order to monitor and control cash flow. As a result of checking accounts not being reconciled, monitored, or maintained, schools lost control over assets. For instance, one school could not explain or trace the source of a $10,000 credit applied to its checking account by the bank. We requested information to verify the source of the funds but the principal, bank representatives, Education and Finance officials could provide no source documents to account for the credit.

Recommendations

We recommend that the Commissioner of Education:

1. Monitor the schools' uses of Fund monies through the review process by providing consistent and timely feedback to the schools in response to their report submissions.

2. Ensure that transitioning principals are given sufficient guidance to properly administer Fund monies.

3. Maintain proper records and files of schools' report submissions.

4. Ensure that schools submit their expenditure reports in time for Education to forward them to Finance in accordance with the law.

We recommend that the Commissioner of Finance:

1. Review and monitor the expenditures for all Fund monies disbursed to the schools, which include disbursements funded by the Lottery.

2. Prepare and Provide Findings and Exception Reports to Education as required by the Code.

3. Ensure that Education provides summaries of personal services payments, from the Fund, for the submission of reportable income to local and federal tax agencies via IRS Form 1099-MISC.

Department of Education's Response

Education in its response agreed with all the recommendations in this section except recommendation three. For recommendation one, two, and four the department acknowledged that during the audit scope period it did not: (i) provide consistent and timely feedback to the schools pertaining to their use of Fund monies; (ii) ensure that transitional principals were given sufficient guidance to properly administer Fund monies; and, (iii) ensure that school expenditure reports were submitted to Finance in accordance with the law.

In addressing these issues, the department stated that in 2008 it hired Financial Control Officers and School Accountants in both districts who monitor the schools' uses of Fund monies based on submitted expenditure reports. In addition, the departments authorized the district Insular Superintendents to hold school administrators accountable for noncompliance with established criteria. It was stated that additional initiatives included providing training, starting in September 2009, to school administrators at the beginning of the school year regarding Code requirements governing the Fund. At the trainings, School administrators are provided a copy of the School Fund Management Manual which ensures that schools' uses of funds are in accordance with prescribed regulations.

Regarding recommendation three, Education stated the following: "The Department…maintains proper records and files of the school report submission for the Education Initiative Fund. Records are maintained by the Business Office, the district Superintendents, the Accountants, and the Financial Control Officers." In its response, the department informed the V. I. Inspector General's Office that records are available for any follow-up review.

V.I. Inspector General's Comments

Our immediate comments will address Education's responses to recommendations one, two and four. The responsibilities assigned to the Insular Superintendents and Financial Control Officers are good starts. However, in light of our audit and follow-up review results, Education needs to improve its monitoring of the public schools. For instance, we found that Financial Control Officers did not consistently inform schools of violations to Code provisions governing expenditures. We saw this as it related to travel, substitute teacher payments and excessive vendor services payments.

As we noted in a January 11, 2011, meeting, our follow-up review revealed a transaction which was improper in the way that it was processed. The transaction involved the payment of a $3,500 personal check from a private citizen to a school for travel expenses. The memo of the check stated the following, "Loan for air trip." Several months after the check was written, the school repaid the private citizen the total amount of the loan from its Fund checking account. However, based on our review of bank documents and interview with the school administrator, we found that the private citizen's check payment was not deposited in the school's Fund checking account from which it was repaid months later. It was deposited into one of the school's other accounts. In addition, the supporting documents in the school's submitted report did not provide an adequate account of transactions related to the deposit and use of the loan proceeds.

Due to the nature of the transaction, Finance should have been involved in its processing and at the very least Education should have had prior knowledge of it through its accountants. As it relates to monitoring, Education did not inform the school that it was in violation of Code expenditure guidelines, neither did it detect or address the unusual nature of the transaction. On the other hand, in its Findings and Exception Report to Education, Finance did note that the travel is prohibited; however, it did not address the unusual nature of the transaction.

In its response, Education spoke about the distribution of the existing version of the School Fund Management Manual to the schools as a viable corrective measure taken by the department. In view of our previous discussions on the manual, we will simply reiterate our position that the manual, as published, is ineffective and misleading because of its confusing presentation format of allowable and unallowable costs for the Fund.

Regarding recommendation three, Education's claim that auditors did not contact department personnel regarding the maintenance of files or missing documentation is incorrect. As indicated in our report, our audit was hampered by the unavailability of files and documentation we had requested but did not receive. For instance in emails dated August 26, 2009, which were addressed to officials in charge of Education's business offices in the St. Thomas/St. John and the St. Croix districts, we requested specific documents needed for our audit. The officials who were either notified about the email requests before their sending or had emailed an acknowledgment of receipt after receiving them never provided the requested documents. In view of the manner in which we conducted the audit, we stand by our finding and recommendation.

Department of Finance's Response

Finance concurred with all the recommendations in this section of the report. In responding to the recommendations, Finance said that it: (i) already monitors schools' uses of Fund monies through the schools' submission of Imprest Fund Reports which are part of Finance's annual compliance review; (ii) already provides Findings and Exceptions Reports to the Commissioner of Education for further action as part of Finance's Annual Compliance review; and, (iii) provided guidance to Education regarding IRS Form 1099-MISC reporting through distribution of the V.I. Finance instructional document "Overview of 1099 Reporting for Unincorporated Vendors." The department indicated that the document was initially provided to Education in October 2008. It will be reissued to Education, "as a refresher," by February 2011. The stated implementation date for above items 1 and 2 was Fiscal Year 2008.

V.I. Inspector General's Comments

Regarding recommendation one, our previous comments in this and other finding sections to Education and Finance's responses have already addressed issues concerning the effectiveness of monitoring as they relate to schools' management and use of Fund resources. Based on our audit and follow-up review findings, we do not agree with Finance that further action is not needed by the department at this time.

For recommendation two, we consider the response to be sufficient for us to close this recommendation. However, as indicated in our comments to Finance under Finding 2, although the Finding and Exception Report is a great tool for monitoring, it will be ineffective if it is essentially used only to collect information and there is no meaningful and accurate interaction with Education.

We consider Finance's response to recommendation three to be sufficient to close this recommendation. However, we do require documentation showing that IRS 1099 forms were being prepared for unincorporated vendors as required by law after notification of the requirement to Education in October 2008.

FINDING 4: LAW

The Virgin Islands Code contains ambiguous and contradictory statutes addressing the Fund. These statutes contain unclear and conflicting language regarding the (i) reporting requirements of Finance, Education, and the schools; (ii) the amount remaining from a school's allocation that should be returned to the Fund for redistribution the next fiscal year; and, (iii) the percentage of private contractor gaming revenues that Lottery must transfer to the Fund. These ambiguities and contradictions were impediments to clearly understanding the rules and regulations governing the Fund.

Sections 3093 and 3100i

Title 33 of the Code contains two sections, 3093 and 3100i, which set forth rules and regulations for the administration of the Fund. These sections, however, contain ambiguous and contradictory language regarding its administration. Section 3093 was established as a result of Act 6088, which was passed by the Legislature in 1995. As noted, this act created the Fund. To address changes in how the Fund was to be administered, the Legislature in July 2002 established 3100i as a separate section in the Code, instead of amending Section 3093 to reflect the changes. A confusing aspect in the construct of the law is that although 3093 precedes 3100i, it has been amended through 2005. As a result, both sections can create confusion in interpreting the law because they remain active and enforceable.

The contradictions presented in both include the following:

- Section 3093 requires that principals submit their expenditure reports to the Commissioner of Education and their respective insular Superintendent of the respective school district on a quarterly basis. However, Section 3100i requires that reports be submitted monthly and does not specify to whom the reports should be given.

- Section 3093 states, "The Commissioner of Education shall maintain a record of all monies deposited into and disbursed from the Fund and shall annually report to the Governor and the Legislature the status of the Fund." Section 3100i, on the other hand, assigns these responsibilities to the Commissioner of Finance.

- Section 3093 states, "All monies in excess of $100 remaining from a school's allocation at the end of the fiscal year shall be returned to the Fund for redistribution in the next fiscal year." Section 3100i stipulates that any sum remaining from the school's allocation must be returned.

Lottery Allocation Amount

Title 33, Section 3093, and Title 32, Section 246 contradict each other in that the former requires the Lottery to transfer 35% of the proceeds it derives from contractor gaming revenues to the Fund. The latter, however, sets the transfer amount at 25%. Both sections of the code are linked to Act 6590, which was approved on August 1, 2003.

Recommendations

We recommend that the Commissioner of Education:

1. Propose that the contents of Title 33, Sections 3093 and 3100i of the Code be merged under one section and the contradictory and ambiguous language be removed.

2. Propose that the Code be amended to specify whether the Lottery is required to transfer either 25% or 35% of the proceeds it derives from contractor gaming revenues to the Fund.

Department of Education's response

Education agreed with both recommendations in this section of the report. The department indicated that its "legal Counsel will review and make the necessary recommendations to address the contradictory and ambiguous language in the Virgin Islands Code."

V.I. Inspector General's Comments

Education's responses adequately address recommendations one and two; therefore, we consider them resolved.

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

THE UNITED STATES VIRGIN ISLANDS
OFFICE OF THE GOVERNOR
GOVERNMENT HOUSE
Charlotte Amalie, V.I. 00802
340-774-0001

January 26, 2011

Mr. Steven van Beverhoudt
Inspector General
Office of the Inspector General
2315 Kronprindsens Gade #75
St. Thomas, Virgin Islands 00802

Re: Response by the Government of the Virgin Islands to Draft Audit Report, Audit of the Education Initiative Fund for the Fiscal Years 2002 to 2007 (Report No. AR 01-40-11)

Dear Inspector General van Beverhoudt:

This letter acknowledges receipt of the above-referenced draft audit report, which was transmitted with correspondence dated September 30, 2010, to the Departments of Education (DOE) and Finance (DOF). The Government of the Virgin Islands (GVI) recognizes the importance of the audit work and underlying procedures conducted by the Office of the V. I. Inspector General (OIG). The efforts and continued commitment of your office serve to foster strengthening existing internal controls, government-wide.

The focus of the audit entailed a review of the manner in which specific government departments and entities were allotting, expending, and accounting for the financial resources that sustained the Education Initiative Fund ("the Fund"). Specifically, the roles of DOE and DOF in administering the Fund were revisited, coupled with that of the Virgin Islands Lottery which is a key source of funds for educational purposes.

Overall, the aforementioned entities concurred with most of the recommendations proffered by the Inspector General; however, the exceptions or areas of non-concurrence are specifically noted in the attached audit response (Exhibit I) to the draft report. It should be noted for the record that the audit covered the period of Fiscal Years 2002 to 2007, and that the majority of the corrective measures suggested in the audit report had already been implemented from Fiscal Year 2008 by Education (DOE) and/or Finance (DOF). Although the auditor was

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

privy to this information, there was no substantial reference made to the already instituted corrective actions in relevant parts of the draft report.

To reiterate, as already indicated in my response (Exhibit I) to the draft report, both the Departments of Education and Finance have already taken measures, since Fiscal Year 2008, to solidify their internal controls relative to their administration of the Education Initiative Fund. Further, the heads of these departments emphatically share my vision of and commitment to ensuring that public school students in the territory of the United States Virgin Islands receive the greatest benefit possible from available funds derived from lottery gaming in the Territory.

Thank you for the opportunity provided to the Office of the Governor to comment on this OIG draft audit report.

Sincerely,

John P. de Jongh, Jr.
Governor

Attachments

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Exhibit I

GOVERNMENT OF THE VIRGIN ISLANDS

Response to Office of the Virgin Islands Inspector General's Draft Letter Audit Report

Audit of the Education Initiative Fund (Fiscal Years 2002 to 2007)

(AR-01-40-11, September 30, 2010)

FINDING 1: FUNDING

RECOMMENDATIONS – DEPARTMENT OF EDUCATION

1. Revisit and consider resubmitting the proposal recommending that the Code's formula be amended to allow for the equitable distribution of funding to the schools.

2. Propose that the Code be amended to stipulate a time period in which Lottery contributions must be paid to the Fund.

3. Ensure that schools expenditure reports are submitted to Finance in accordance with the law. This will facilitate the timely disbursement of funding to the schools.

Government's Response – Department of Education (DOE)

DOE concurs with Recommendation # 1 (re: Funding)

The Department of Education concurs with the recommendation of equitable distribution to schools with enrollment being the primary base to allow all schools funds to be proportioned to the populations with larger schools receiving the larger amount and smaller schools receiving the lower amount, irrespective of which district the school is located in. DOE recognizes that the current legislation is contradictory as it speaks to distribution by formula in one instance and also speaks to even distribution by district/school; which allows for schools with lower enrollment to be awarded larger sums than a school within the other district with the same or equal amount of students.

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Corrective Action Plan

The department (DOE) will submit recommendations to change the contradictory language in the legislation.

Due Date: April 2011

Responsible Party: Commissioner of Education; Legal Counsel, DOE

DOE does not proffer comments with respect to Recommendation #2 (re: Funding)

This finding is not applicable to the Department of Education. The Department of Finance will respond to this recommendation.

DOF concurs with Recommendation #2 (re: Funding).

The Department of Finance recognizes that the V. I. Lottery is already currently making contributions quarterly, although there is no time stipulated in the Code.

Corrective Action Plan

The Department of Finance will submit a recommendation to provide for quarterly contributions from the V. I. Lottery.

Due Date: March 2011

Responsible Party: Commissioner of Finance

DOE concurs with Recommendation #3 (re: Funding)

The Department concurs with this recommendation. The Department of Education acknowledges that during the period of the audit, Fiscal Years 2002 - 2007, the expenditure reports were not submitted to the Department of Finance in accordance with the law. However, in June 2008, the department issued a memorandum to the Superintendents in both districts detailing when the expenditure reports are due. Schools that are not in compliance with this memorandum do not receive funds until the reports are received by the respective districts.

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GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Corrective Action Plan

The memorandum issued in June 2008 stipulates the deadlines for submission of the follow-up reports. Further, follow-up is conducted by the district Financial Control Officer who ensures that the district submits the information when required. **(See Attachment 1)** Further, the Department will require the Superintendents to hold Principals, who fail to comply with the reporting deadlines, accountable.

Implementation Date: June 2008

Due Date: September 2011

Responsible Party: Insular Superintendents – STT/STJ & STX Districts; Financial Control Officer

RECOMMENDATIONS – DEPARTMENT OF FINANCE

1. Ensure, in partnership with Education, that schools receive the funding that has been set aside for them.

2. Ensure, in partnership with Education, that funding checks are timely distributed to schools each fiscal year.

3. Verify, on a routine basis, that Lottery payments to the Fund equal the required payment percentage of private contractor gaming revenue stipulated in the Code.

Government's Response – Department of Finance (DOF)

DOF concurs with Recommendation #1 (re: Funding)

The Department of Finance agrees with this recommendation, in general, and the Inspector General's Draft Audit Report's suggestion that the issue of schools receiving the funding that has been set aside for them in the Virgin Islands Code is already being facilitated by a substantial increase in Virgin Islands Lottery contributions (see excerpt below). "The funding, however, increased substantially over the audit scope period. By the end of Fiscal Year 2007, the Lottery had contributed $6,425,316, more than enough to meet the funding requirements of the Code. As a result, Education officials said the decision was made to fund the schools solely from Lottery contributions starting in Fiscal Year 2008. The increased funding should facilitate the timely processing and issuance of check disbursements to the schools."

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APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Corrective Action Plan

It is important to note that the scope of the audit covered Fiscal Years 2002 through 2007, and that the substantial increase in Virgin Islands Lottery contributions is now facilitating schools receiving the funding that has been set aside for them in the Virgin Islands Code, beginning in Fiscal Year 2008.

The Department of Finance will partner with the Department of Education and meet to discuss the protocol/procedure for ensuring that schools receive the funding set aside for them.

Implementation Date: Fiscal Year 2008

Due Date: 2nd quarter of FY 2011

Responsible Party: Commissioner of Finance

DOF concurs with Recommendation #2 (re: Funding)

The Inspector General's Draft Audit Report notes that: "Delays in the distributions stemmed partly from Education's expenditure report submission practices. The timing of Education's school expenditure report submissions to Finance for one fiscal year determined when schools received their funding distributions for the next – making inconsequential any timely allotments by OMB. As stated, Finance required the previous fiscal year's expenditure reports to initiate check processing for the schools, at least as it related to General Fund monies."

The Report continues: "We found that Finance had not received school expenditure activities for monies that had been funded by the Lottery. This did not prevent the schools from receiving their yearly Lottery funding."

Now that the Education Initiative Fund is being funded solely by V.I. Lottery contributions since Fiscal Year 2008, the Department of Finance disburses funds to all *compliant* schools, based upon the amount calculated by the Department of Education, at the beginning of the school year. This ensures timely distributions of funding checks, as indicated in Recommendation # 2.

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Corrective Action Plan

The Department of Finance will continue to monitor fund disbursements/payments to compliant schools to ensure timely distribution of checks.

The Department of Finance will partner with the Department of Education and meet to discuss the protocol/procedure for ensuring timely disbursement of checks to schools, inclusive of possible sanctions for a school's failure to timely submit financial expenditure/activity reports.

Implementation Date: Fiscal Year 2008

Due Date: 2nd quarter of FY 2011

Responsible Party: Commissioner of Finance

DOF concurs with Recommendation #3 (re: Funding)

Corrective Action Plan

While the Virgin Islands Lottery has begun to promptly submit remittances and monthly reports to the Department of Finance for the Education Initiative Fund on a timely basis, the department will, effective with the next quarterly remittance, institute a verification process to ensure Code compliance.

Due Date: March 2011

Responsible Party: Commissioner of Finance; Director – Treasury Division, DOF

RECOMMENDATIONS – VIRGIN ISLANDS LOTTERY COMMISSION

1. Pay the outstanding revenue contributions owed the Fund.

2. Submit certified monthly reports of lottery revenues to the Commissioner of Finance as required by law.

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APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Government's Response – Virgin Islands Lottery Commission

The Virgin Islands Lottery Commission concurs with Recommendation #1 (re: Funding)

Corrective Action Plan

While the fiscal years under the scope of the audit have been closed, the Virgin Islands Lottery recognizes the missed payment in August 2007 in the amount of $207,875, and the Executive Director is authorized to make quarterly payments in the amount of $51,968.75 through the end of Fiscal Year 2011 (September 30, 2011) to satisfy the missed payment.

Due Date: September 30, 2011

Responsible Party: Chair, VI Lottery Commission; Executive Director – VI Lottery

The Virgin Islands Lottery Commission concurs with Recommendation #2 (re: Funding)

The submission of certified monthly reports of lottery revenues to the Commissioner of Finance has been implemented since Fiscal Year 2007.

Corrective Action Plan

No further corrective action is necessary.

Implementation Date: Fiscal Year 2007

Responsible Party: Chair, VI Lottery Commission; Executive Director – VI Lottery

FINDING 2: EXPENDITURES

Recommendations - Departments of Education and Finance

1. Communicate to the schools, accurately, clearly and consistently, the provisions of the Code regarding expenditures as they relate to uses and limitations, documentation support, and authorization.

2. Implement and enforce the provisions of the Code governing expenditures.

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Government's Response – Department of Education

DOE concurs with Recommendation #1 (re: Expenditures)

The Department of Education acknowledges that during the period of the audit, Fiscal Years 2002 – 2007, all schools may not have received information about the regulations prescribed in the Virgin Islands Code regarding expenditures. However, the Department implemented the Fiscal and Administrative Services School Fund Management Manual in 2008. During the audit, the department provided this manual to the auditors for their perusal so that they could evaluate the department's current procedures and incorporate the results in the audit report. This manual provides rules, regulations, and the operating procedures for the Education Initiative Fund; as well as, it includes the provisions of the Virgin Islands Code regarding the uses and limitations of the Initiative Fund, documentation required, and the authorizations needed. Also, the Department of Education will work with the Department of Finance to review the manual and make revisions, as necessary. Both districts have since hired Financial Control Officers and School Accountants who work in the schools to manage the various school accounts.

Corrective Action Plan

The Department of Education has implemented the Fiscal and Administrative Services School Fund Management Manual in 2008. This manual provides rules, regulations, and the operating procedures for the Education Initiative Fund. The Department of Education will work with the Department of Finance to make the necessary revisions to the manual.

Implementation Date: Fiscal Year 2008

Due Date: August, 2011

Responsible Party: Financial Control Officers – STT/STJ & STX Districts; School Accountants (STT/STX)

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GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Government's Response – Department of Finance

DOF concurs with Recommendation #1 (re: Expenditures)

The Department of Finance already provides a copy of Title 33 Virgin Islands Code Section 3093(g) to all School Principals along with the disbursement check for their respective share of the Education Initiative Fund ("EIF"). This section of the Code outlines items that Principals may not purchase with monies from the EIF. Additionally, the Department of Education has issued a "School Fund Management Manual" covering rules, regulations and operating procedures for the EIF.

Corrective Action Plan

To ensure accountability, the Department of Finance will be incorporating a signature line on the V.I. Code excerpt provided to all School Principals as part of its receipt procedure when EIF checks are disbursed. Additionally, the Department of Finance will work with the Department of Education to reissue the "School Fund Management Manual" as a joint document, since the Department of Finance has ultimate responsibility for all Virgin Islands Government funds, including the EIF.

Due Date: Addition of signature line: Immediately
Reissuance of Manual: August,, 2011

Responsible Party: Director of Financial Reporting & Audit (Addition of signature line)
Commissioner of Finance and Director of Financial Reporting & Audit (Manual)

Government's Response – Department of Education

DOE concurs with Recommendation #2 (re: Expenditures)

The Department of Education acknowledges that during the period of the audit, Fiscal Years 2002 – 2007, it did not implement and enforce the provisions of the Code governing expenditures. However, the department implemented the Fiscal and Administrative Services School Fund Management Manual in 2008. This manual provides the rules governing the expenditure of funds. Both districts have since hired Financial Control Officers and School Accountants who work in the schools giving guidance to the Administrators of the Fund accounts. These Accountants ensure the proper expenditure of funds. Additionally, the Insular

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GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Superintendent in each district monitors and take actions, as appropriate, including warnings and formal reprimands, when Principals fail to follow the procedures outlined in the Fiscal and Administrative Services School Fund Management Manual.

Corrective Action Plan

The Department of Education has implemented the Fiscal and Administrative Services School Fund Management Manual in 2008. The manual provides rules, regulations, and the operating procedures for the Education Initiative Fund. Further, the Insular Superintendent in each district monitors and take action, as appropriate, including warnings and formal reprimand, when Principals fail to follow the procedures outlined in the manual. The manual was implemented prior to issuance of the audit report, and will be updated occasionally to reflect revisions.

Implementation Date: Fiscal Year 2008

Due Date: August, 2011

Responsible Party: Financial Control Officers; School Accountants, Insular Superintendents

Government's Response – Department of Finance

DOF concurs with Recommendation #2 (re: Expenditures)

The Department of Finance has already addressed this issue through "Education Initiative Fund – Findings and Exceptions Reports", which are provided to the Commissioner of Education for further action as part of the Department of Finance's Annual Compliance Review. (See response to Recommendation # 2 under Finding 3: Internal Controls, below.)

Corrective Action Plan

Corrective action, per the above response, commenced in 2008.

Implementation Date: Fiscal Year 2008

Responsible Party: Commissioner of Finance and Director of Financial Reporting & Audit, DOF

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

FINDING 3: INTERNAL CONTROLS

Recommendations - Department of Education

1. Monitor the schools' uses of Fund monies through the review process by providing consistent and timely feedback to the schools in response to their report submissions.

2. Ensure that transitioning principals are given sufficient guidance to properly administer Fund monies.

3. Maintain proper records and files of schools' report submissions.

4. Ensure that schools submit their expenditure reports in time for Education to forward them to Finance in accordance with the law.

Government's Response – Department of Education

DOE concurs with Recommendation # 1 (re: Internal Controls)

The Department of Education acknowledges that during the period of the audit, Fiscal Years 2002 – 2007, it did not monitor the schools' use of fund monies through the review process by providing consistent and timely feedback to the schools. In 2008, both districts hired Financial Control Officers and School Accountants that work in the schools. These positions gave the department the ability to monitor the schools' use of fund monies and provided consistent and timely feedback to the schools in response to the expenditure reports submitted. Further, the department will require the Superintendents to hold Principals, who are not in compliance with the requirements, accountable.

Corrective Action Plan

The Department hired Financial Control Officers and School Accountants in both districts that work in the schools starting in 2008. These positions gave the department the ability to monitor the school's use of fund monies and to provide consistent and timely feedback to the schools in response to the expenditure reports submitted. Further, the department will require the Superintendents to hold Principals, who are not in compliance, accountable.

Implementation Date: Fiscal Year 2008

Due Date: September 2011

Responsible Party: Financial Control Officers, School Accountants

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

DOE concurs with Recommendation # 2 (re: Internal Controls)

The Department of Education acknowledges that during the period of the audit, Fiscal Years 2002 – 2007, it did not ensure that transitioning Principals were given sufficient guidance to properly administer fund monies. However, in September 2009, the Department started providing training to the School Principals at the start of the school year on the requirements of the Education Initiative Fund. In addition, the department provides a copy of the Department of Education's Fiscal and Administrative Services School Fund Management Manual to all Principals at that meeting for their record and their usage. This helps to ensure that the Principals are utilizing the funds in accordance with the prescribed regulations.

Corrective Action Plan

The Department has already implemented corrective action and no further action is necessary.

Implementation Date: September 2009

Responsible Party: Commissioner of Education

DOE does not concur with Recommendation # 3 (re: Internal Controls)

The Department of Education maintains proper records and files of the school report submission for the Education Initiative Fund. Records are maintained by the Business Office, the district Superintendents, the Accountants, and the Financial Control Officers.

Corrective Action Plan

The records are available for any follow-up review by the auditors. Requests for follow-up information and access to files should be routed through the Office of the Commissioner for necessary action.

Due Date: N/A

Responsible Party: Commissioner of Education

DOE concurs with Recommendation # 4 (re: Internal Controls)

The Department of Education acknowledges that during the period of the audit, Fiscal Years 2002 – 2007, the expenditure reports were not submitted to the Department of Finance in accordance with the law. However, in June 2008, the department issues a memorandum to the

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Superintendents in both districts detailing when the expenditure reports are due. Schools that are not in compliance with this memorandum do not receive funds until the reports are received by the respective districts. The Insular Superintendent in each district monitors and take actions as appropriate, including warnings and formal reprimand, when Principals fail to follow the procedures outlined in the manual.

Corrective Action Plan

The Department of Education has implemented the Fiscal and Administrative Services School Fund Management Manual in 2008. This manual provides rules, regulations, and the operating procedures for the Education Initiative Fund. The department ensures that the schools submit their expenditure reports by requiring that the Insular Superintendent in each district monitor and take actions as appropriate, including warnings and formal reprimand, when Principals fail to follow the procedures outlined in the manual. Thus, the recommendation was implemented prior to the issuance of the audit report.

Implementation Date: June 2008

Responsible Party: Commissioner of Education; Insular Superintendents

Recommendations - Department of Finance

1. Review and monitor the expenditures for all Fund monies disbursed to the schools, which include disbursements funded by the Lottery.

2. Prepare and provide Findings and Exception Reports to Education as required b the Code.

3. Ensure that Education provides summaries of personal services payments, from the Fund, for the submission of reportable income to local and federal tax agencies via IRS Form 1099-MISC.

Government's Response – Department of Finance

DOF concurs with Recommendation # 1 (re: Internal Controls)

The Department of Finance already monitors the expenditure of all Education Initiative Fund monies disbursed to the schools by means of Imprest Fund Reports that are submitted as part of its annual compliance review.

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Corrective Action Plan

Corrective action, per the above response, commenced in 2008. No additional action on the part of the Department of Finance is indicated at this time.

Implementation Date: Fiscal Year 2008

Responsible Party: Commissioner of Finance and Director of Financial Reporting and Audit, DOF

DOF concurs with Recommendation # 2 (re: Internal Controls)

The Department of Finance has already addressed this issue through "Education Initiative Fund – Findings and Exceptions Reports", which are provided to the Commissioner of Education for further action as part of the Department of Finance's Annual Compliance Review. (Sample of report attached.) Items of non-compliance, on a per-school basis, are noted to the Commissioner of Education for further follow-up.

Corrective Action Plan

Corrective action, per the above response, commenced in 2008. No additional action on the part of the Department of Finance is indicated at this time.

Implementation Date: Fiscal Year 2008

Responsible Party: Commissioner of Finance and Director of Financial Reporting & Audit, DOF

DOF concurs with Recommendation # 3 (re: Internal Controls)

An "Overview of 1099 Reporting for Unincorporated Vendors" (attached) was provided as guidance by the Department of Finance to the Department of Education in October 2008.

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Corrective Action Plan

This document will be retransmitted to the Department of Education by February 2011, as a refresher.

Implementation Date: October 2008

Due Date: February 2011

Responsible Party: Commissioner of Finance and Director of Accounting, DOF

FINDING 4: LAW

Recommendations - Department of Education

1. Propose that the contents of Title 33, Sections 3093 and 3100i of the Code be merged under one section and the contradictory and ambiguous language be removed.

2. Propose that the Code be amended to specify whether the Lottery is required to transfer either 25% or 35% of the proceeds it derives from contractor gaming revenues to the Fund.

Government's Response – Department of Education

DOE concurs with Recommendation # 1 (re: Law)

Corrective Action Plan

The Department of Education's Legal Counsel will review and make the necessary recommendations to address the contradictory and ambiguous language in the Virgin Islands Code.

Due Date: April, 2011

Responsible Party: Commissioner of Education; Legal Counsel, DOE

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

DOE concurs with Recommendation # 2 (re: Law)

Corrective Action Plan

The Department's Legal Counsel will review and make the necessary recommendations to amend the conflicting language in the Virgin Islands Code.

Due Date: February 2011

Responsible Party: Commissioner of Education; Legal Counsel, DOE

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Government Of The United States Virgin Islands
DEPARTMENT OF EDUCATION
1834 Kongens Gade
St. Thomas, VI 00802-6746

Donna Frett-Gregory
Assistant Commissioner, Operations
Office of the Assistant Commissioner

Tel: (340)774-0100 X8009
Fax (340) 776-5687
Email: dgregory@doe.vi

MEMORANDUM

TO: Ms. Jeanette Smith-Barry, Insular Superintendent, STT
Mr. Garry Molloy, Insular Superintendent, STX

FROM: Ms. Donna Frett-Gregory
Assistant Commissioner, Operations

SUBJECT: ***Substitute Pool, Accreditation & Imprest Fund (Lottery Funds) Quarterly Reports***

DATE: June 20, 2008

Kindly be advised that all recipients of abovementioned funds will be required to submit quarterly reports effective Fiscal year 2009 (FY 2008-2009).

August - September	due	October 5th
October – December	due	January 5th
January – March	due	April 5th
April – June	due	June 5th

Non-adherence to the deadlines will preclude schools and activity centers from receiving funds until such time as the reports are submitted. All reports are to be forwarded to the Business Directors in your respective District.

CC: Dr. Laverne Terry, Ed. D, Commissioner
Ms. Beverly Jennings, Business Director STT
Ms. Mirrlees Duggins, Business Director STX

APPENDIX I

GOVERNOR OF THE VIRGIN ISLANDS' RESPONSE

Overview of 1099 Reporting for Unincorporated Vendors

Introduction

Agencies and departments often pay individuals who are not their employees for services rendered. If the Department of Education (DOE), through the use of Educational Initiative Funds (EIF), Accreditation Funds (AF), and Substitute Pool Funds (SPF) paid a non-corporate payee (the "unincorporated vendor") a total of $600 or more during a calendar year; the DOE must report the payment(s) via a "Summary by Vendor Listing" to the Department of Finance (DOF) by January 25th of each year. This report will only include the unincorporated vendors that were paid $600 or more through EIF, AF, and SPF inclusive of the payment(s) made to the same unincorporated vendor across other schools that utilize said funds during a calendar year period (i.e., January 1st to December 31st).

Now, as outlined below in the section entitled "Internal Procedures", the "Summary by Vendor Listing" is used by the DOF for reporting to the Virgin Islands Internal Revenue Bureau (IRB) Form 1099 Miscellaneous (MISC); with a duplicate Form 1099 sent to the unincorporated vendor. Note that, generally payments to corporations are not reportable. Form 1099 (MISC) is used by the DOF to report **non-employee payments** and serves two purposes:

- Individual payees use Form 1099 information to file their individual tax returns, and
- The IRS matches the Form 1099 to the payee's income tax return to ensure the income has been reported.

If more than one division or unit within the DOE is paying the same unincorporated vendor from EIF, the payments must be accumulated and/or consolidated by vendor.

Internal Policies

Independent contractors and other individuals who work for themselves will need to report their Social Security Number (SSN) or business Tax Identification Number (TIN) to the DOE when using EIF. This is done using Form W-9. Copies of Form W-9 should be kept at each school or can be downloaded at http://www.irs.gov.

All unincorporated vendors that are paid from EIF, AF, and SPF must complete this straightforward form, which requires the vendor to provide their name, address and Social Security Number. Conversely, contractors who have a separate business entity, must provide their name, address and Employer Identification Number (EIN) of their business. To ensure proper stewardship of EIF, AF, and SPF the DOE must ensure that a Form W-9 exists for each unincorporated vendor prior to providing any payments to said vendor. The DOE should track any changes to payee information (e.g., name, address and taxpayer identification number) to ensure successful mail delivery of 1099's.

Separately, the Form W-9 also asks whether the unincorporated vendor is subject to backup withholding. This is withholding at a flat rate of 28% on payments made to the unincorporated vendor or their business under certain circumstances. There are two common reasons for backup withholding: 1) the unincorporated vendor name and SSN as provided on Form W-9 don't match

the IRB's records, or **2)** the unincorporated vendor may have outstanding tax debts and the IRB has notified the DOF that the unincorporated vendor is subject to mandatory backup withholding until the taxes are paid in full. If any of these circumstances are revealed in advance by the unincorporated vendor please contact the DOF for further information.

Internal Procedures

To help the DOE comply with the requirement to properly report 1099's via imprest funds established per the EIF, AF, and SPF the accounting system(s) used at the school level should capture 1099 related data by generating a "Summary by Vendor Listing" that includes the following data elements:

Vendor name

Vendor address

- Vendor Tax Identification Number (TIN)
  - Social Security number (SSN), or
  - Employer Identification Number (EIN)
- Vendor telephone number
- Total amount paid to Vendor

The "Summary by Vendor Listing" **must** be submitted to the Department of Finance (DOF) by January 25th of each year. This report should only include the unincorporated vendors that were paid $600 or more through EIF; **inclusive** of the payment(s) made across other schools to the same unincorporated vendor that utilize EIF during a calendar year period (i.e., January 1st to December 31st).

APPENDIX II

ADDITIONAL INFORMATION NEEDED TO CLOSE RECOMMENDATIONS

Recommendation Number and Status	Additional Information Needed
Finding 1:	
To the Commissioner of Education:	
1-1 Resolved	Provide a copy of the submitted proposal recommending the amendment of the Code's formula.
1-2 Resolved	Provide a copy of submitted proposal recommending quarterly contribution payments to the Fund from the Lottery.
1-3 Unresolved	Provide documentation to show that schools' expenditure reporting is in accordance with the reporting requirements of the Code.
To the Commissioner of Finance:	
1-1 Resolved	Provide a copy of implemented procedures developed in partnership with Education for ensuring schools receive their allocations.
1-2 Resolved	Provide a copy of implemented procedures developed in partnership with Education for ensuring timely distribution of checks to schools.
1-3 Resolved	Provide a copy of the instituted verification process for ensuring that V.I. Lottery payments to the Fund equal the required payment percentage of private contractor gaming revenue stipulated in the Code.

APPENDIX II

ADDITIONAL INFORMATION NEEDED TO CLOSE RECOMMENDATIONS

Recommendation Number and Status	Additional Information Needed
To the Virgin Islands Lottery Commission:	
1-1 Resolved	Provide documentation showing the specified quarterly payments of $51,968.75 made to the Fund to satisfy the outstanding payment of $207,875 for August 2007.
1-2 Resolved	No further action needed.
Finding 2:	
To the Commissioner of Education:	
2-1 Resolved	Provide a copy of the revised and reissued School Fund Management Manual developed in collaboration with Finance.
2-2 Unresolved	In addition to providing a copy of the revised and reissued School Fund Management Manual, review of relevant documents and procedures must show evidence of Code provisions governing expenditures being implemented and enforced by responsible departments.
To the Commissioner of Finance:	
2-1 Resolved	Provide a copy of the revised and reissued School Fund Management Manual.
2-2 Resolved	Same as Recommendation 2-2 above.

APPENDIX II

ADDITIONAL INFORMATION NEEDED TO CLOSE RECOMMENDATIONS

Recommendation Number and Status	Additional Information Needed
Finding 3:	
To the Commissioner of Education:	
3-1 Unresolved	Review of relevant documents and procedures must show evidence of schools adequately being monitored and timely feedback being given in response to schools' expenditure report submissions.
3-2 Unresolved	Same as Recommendation 3-1 above.
3-3 Unresolved	Review of schools' expenditure report records and files must show that they are being properly maintained by the department.
3-4 Unresolved	Provide documentation showing that reports are being submitted to Finance in accordance with the reporting requirement of the Code.
To the Commissioner of Finance:	
3-1 Unresolved	Review of relevant documents and procedures must show evidence of schools adequately being monitored.
3-2 Resolved	No further action needed.
3-3 Resolved	Provide documentation showing that IRS forms were prepared for unincorporated vendors as required by law after notification of the requirement to Education in 2008.

APPENDIX II

ADDITIONAL INFORMATION NEEDED TO CLOSE RECOMMENDATIONS

Recommendation Number and Status	Additional Information Needed
Finding 4:	
To the Commissioner of Education:	
4-1 Resolved	Provide a copy of submitted proposal addressing the contradictory and ambiguous language in the Code.
4-2 Resolved	Same as Recommendation 4-1 above.

APPENDIX III

OFFICIAL REPORT DISTRIBUTION

Government of the Virgin Islands

Office of the Governor.....3

Office of the Lieutenant Governor.....1

Department of Education.....1

Department of Finance.....1

Virgin Islands Lottery.....1

Office of Management and Budget.....1

Department of Justice.....1

29th Legislature.....15

Office of the Legislative Post Auditor.....1

Delegate to Congress.....1

Government of the United States

Office of Inspector General, Department of the Interior.....1

Office of the United States Attorney, Department of Justice.....1

Federal Bureau of Investigation, Department of Justice.....1