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November 16, 2009

MEMORANDUM

TO: Legislative Education Study Committee

FR: David Peña *DP*

**RE: LESC STAFF OVERVIEW: LEGISLATIVE FINANCE COMMITTEE
PROGRAM EVALUATION OF THE FEDERAL FUND REIMBURSEMENT
PROCESS AT THE PUBLIC EDUCATION DEPARTMENT**

During the 2009 legislative session, a senate joint memorial was introduced requesting the Public Education Department (PED) to work with the Office of Education Accountability, the Legislative Education Study Committee (LESC), and the Legislative Finance Committee (LFC) to examine and recommend appropriate procedures for timely reimbursement of funds to school districts and charter schools.

Although the joint memorial did not pass, the LFC included a review of the reimbursement process in its 2009 interim program evaluation workplan. According to the final LFC report, the objective of the review was to examine issues related to the reimbursement of funds, primarily federal flow-through funds, by PED to school districts, charter schools, and the state's nine Regional Education Cooperatives (RECs) and to suggest procedures to make the PED reimbursement process timely and efficient.

This LESC staff brief summarizes a number of the LFC report sections, including the:

- issues that prompted the review;
- selected review activities;
- findings;
- recommendations; and
- PED's response.

The LESC staff brief also outlines the LESC involvement with the LFC review (see Background).

Issues

- Prior to FY 06, PED distributed federal funds to school districts, charter schools, and RECs on a quarterly cash-advance basis. An audit of this practice, however, determined that the entities were maintaining cash balances from federal dollars in violation of federal requirements, primarily the federal *Cash Management Improvement Act*, that requires a state education agency (in this case PED) to certify that federal funds are being expended within three business days of being drawn down from the federal government.
- Beginning in FY 06, PED transitioned into a reimbursement basis based on the advice of outside counsel and the Department of Finance and Administration (DFA). As a result, school districts, charter schools, and RECs are required to expend their own operational funds, request reimbursement from PED, and have sufficient cash on hand to address other operational needs.
- With specific reference to RECs, a 2007 LFC review identified cash flow issues attributed to processing delays, software implementation, and incorrect or incomplete reimbursement submissions.
- In an effort to mitigate REC cash flow issues, beginning in FY 07, the Legislature has appropriated nonrecurring funds to PED to provide cash advances to RECs. For FY 07 and FY 08, the cash advances were to be returned to PED at the end of each fiscal year. For FY 09, language in the *General Appropriation Act of 2008* allowed RECs with a justified need to retain cash advances and required undistributed funds to revert to the General Fund at the end of the fiscal year.

Selected Review Activities

According to the LFC report, in order to gain a perspective on the timeliness of the PED reimbursement process, LFC staff developed a number of documents included in the appendix of the report, including:

- *Appendix A: Average Processing Time:* This spreadsheet outlines, the total reimbursement time in working days by school district, charter school, and REC;
- *Appendix B: Reimbursement Submissions by Month for FY 09:* This graph summarizes the number of reimbursements submitted to PED for each month in FY 09; and
- *Appendix C: REC, District and State Chartered Charter Process* and *Appendix D: Locally Chartered Charter Process:* These charts outline the required work flow steps from the submission of a reimbursement request to PED to the issuance of a wire transfer or check by DFA.

The LFC report also indicates that LFC staff conducted a statewide survey of school districts, charter schools, and RECs to identify cash flow issues relating to the PED reimbursement process. While eight out of the nine RECs, or 89 percent, responded to the survey; the response rate for school districts and charter schools was 30 percent since only 49 out of 112 of these entities responded to the survey.

Findings

Findings cited in the review were presented to the LFC during the committee's September 2009 interim meeting, among them:

- In 2008, PED implemented an online request for reimbursement (RfR) system to effect “greater accountability, transparency and efficiency.” The system, however, is:
 - ▶ not integrated with other financial systems, such as the Statewide Human Resources, Accounting and Management Reporting System (SHARE) and the Operating Budget Management System (OBMS) and requires a manual interface to process reimbursements; and
 - ▶ incapable of directing resubmitted reimbursement requests to the point of denial. In other words, if a reimbursement request is denied approval by an analyst in a PED bureau, the resubmitted request must go through the entire review process again.
- Also in 2008, PED reported a reimbursement request approval time of six to seven working days, excluding payment processing time by the Department of Finance and Administration.
- In FY 09, PED did not meet the reported approval time. Among the reasons cited by PED for not meeting this target is the increase in the number of reimbursement request submitted to the department in the latter part of a fiscal year. For example, 32 percent of the FY 09 reimbursement requests were submitted to PED in May, June, and July.
- Despite the workload at the end of the fiscal year, in FY 09 PED managed to improve the average processing time to:
 - ▶ 17 working days (from 62 working days) for school districts and charter schools; and
 - ▶ 32 working days (from 94 working days) for REC reimbursement requests.
- There are no provisions within state law that requires PED to provide timely fund reimbursements.
- Each fiscal year, an intergovernmental agreement (I.A.) between an REC and each of its member school district must be approved in order for the REC to provide services and receive reimbursement. According to the LFC report, the average completion time for an I.A. is over 30 business days, however, some of the RECs reported an I.A. completion rate range of six to nine months.
- Also with regard to RECs, survey responses indicated that RECs submit reimbursement requests on a monthly or bi-monthly basis; however, data extracted from the reimbursement system at PED reveals that in FY 09, the majority of RECs did not.
- Finally, the LFC program evaluators reviewed the requirements for the distribution of the Legislature's appropriations to RECs in FY 07, FY 08, and FY 09. The report:
 - ▶ implies that letters to PED from RECs justifying a need for not returning cash advances were inadequate in that they “did not include cash-flow analysis, average monthly disbursements from flow-through funds, number and amount of monthly

outstanding reimbursement requests, etc. Also, many similarities between justification letters were observed, in most cases word for word.”; and

- ▶ states that despite legislative appropriations to provide REC cash advances, REC #9 continues to demonstrate financial difficulties, namely negative cash balances and fund deficits, and REC #2 has not submitted an audit to PED for FY 06 through FY 09.

Recommendations

Among their recommendations the program evaluators state that PED should:

- generate managerial performance reports from the reimbursement system at the department to identify reimbursement process delays to include improving the existing process for resubmittal of denied reimbursement requests;
- develop and implement guidelines that outline the scope of duties for PED program and fiscal staff;
- in collaboration with DFA and LFC, establish a performance measure in the *General Appropriation Act* that requires the department to report, on a quarterly and annual basis, the average number of working days required to process reimbursement requests;
- provide training for school districts, charter schools, and REC staff during PED’s spring budget workshop outlining the reimbursement process, the reimbursement timelines and common reasons for denial and delay of reimbursement requests;
- streamline I.A. approval process and consider the implementation of multi-year and multi-fund Intergovernmental Agreements;
- require the justification of an REC for not returning a cash advance to include a cash flow analysis and a document outlining average monthly cash balance from all sources; and
- require an audit of REC #2 and REC #9 to identify and resolve cash overdrafts, fund deficits and incomplete audits.

PED Response

On September 28, 2009, PED provided a response to the LFC review emphasizing that the department takes seriously its responsibility to administer federal education programs and welcomes the opportunity to work with the LFC to ensure its reimbursement process is timely and efficient. The response, however, noted that it is important to balance speed and efficiency against the need to fulfill certain federal requirements to:

- cover both financial and programmatic elements of federal grant programs;
- include both fiscal and program staff review;
- provide controls to ensure costs charged to federal funds are allowable; and
- include a variety of mechanisms to ensure major compliance requirements are monitored through the year.

Background

In the Executive Summary and in the Background Information, the LFC review report cites an LESC staff report, *Statutorily Created Funds*, that was presented to the LESC at its June 2008 interim meeting. The staff report, it is noted, identified “a pattern of delayed distributions from some of the funds examined, particularly those for which PED requires school districts to request funds on a reimbursement basis.” Among their recommendations, LESC staff recommended that PED, in collaboration with selected school entities, review statute, rule and internal policies, and implement administrative remedies to ensure a timely and efficient reimbursement process.

Finally, at several points during the evaluation process, LFC staff briefed LESC staff on the progress of the review. A few days before the report was to go to press, LFC staff invited LESC staff to review the draft report of the review.