

**Public School Capital Construction  
Assistance Program  
Department of Education**

**Performance Audit  
September 2013**



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is to improve government for the people of Colorado.*



September 17, 2013

Members of the Legislative Audit Committee:

This report contains the results of a performance audit of the Public School Capital Construction Assistance Program within the Department of Education. The audit was conducted pursuant to Section 22-43.7-111, C.R.S., which requires the Office of the State Auditor to conduct a performance audit of Public School Capital Construction Assistance Program by February 15, 2014. The report presents our findings, conclusions, and recommendations, and the responses of the Department of Education and the Public School Capital Construction Assistance Board.

A handwritten signature in cursive script, appearing to read "Dianne E. Ray".



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## *Glossary of Abbreviations*

**AIDS** – Acquired Immune Deficiency Syndrome

**Assistance Board** – Public School Capital Construction Assistance Board

**Assistance Fund** – Capital Construction Assistance Fund

**BEST Act** – Building Excellent Schools Today Act

**BOCES** – Boards of Cooperative Educational Services

**COPs** – Certificates of Participation

**Department** – Department of Education’s Division of Public School Capital Construction Assistance

**FCI** – Facility Condition Index

**FHWA** – Federal Highway Administration

**Historical Fund** – Colorado State Historical Fund

**HIV** – Human Immunodeficiency Virus

**Parsons** – Parsons Commercial Technology Group

**Priority Assessment** – Statewide Financial Assistance Priority Assessment

**Program** – Public School Capital Construction Assistance Program

**State Board** – State Board of Education

**Treasurer** – State Treasurer’s Office



# PUBLIC SCHOOL CAPITAL CONSTRUCTION ASSISTANCE PROGRAM

## Performance Audit, September 2013 Report Highlights



Dianne E. Ray, CPA  
State Auditor

Department of Education

### PURPOSE

Determine whether the Public School Capital Construction Assistance Board (the Assistance Board) and the Department of Education (the Department) have managed the Public School Capital Construction Assistance Program (the Program) in compliance with statutes and ensured the most equitable, efficient, and effective use of funds available to provide grants to Colorado school districts for school capital construction.

### BACKGROUND

- Statute created the Assistance Board to develop the Program to provide financial help to school districts that have difficulty financing projects to build, renovate, or maintain schools so that unsafe or overcrowded schools do not impair students' abilities to learn.
- The Assistance Board was required by statute to assess and prioritize public school capital construction needs statewide and spent \$12 million for a statewide financial assistance priority assessment (Priority Assessment) that identified approximately \$13.9 billion in school capital construction needs in Colorado.
- In Fiscal Years 2009 through 2014 the Assistance Board awarded about \$1.1 billion to fund 211 school capital construction projects, including about \$759 million in state funds and about \$330 million in district matching funds.

### OUR RECOMMENDATIONS

- Identify and prioritize critical school capital construction needs in the state based on statutory criteria and use the results as a basis for providing grants to school districts.
- Improve grant decision making processes to ensure transparency and adherence to statutory direction.
- Improve policies to prevent conflicts of interest for Assistance Board members.
- Establish written policies and procedures to strengthen management of grant contract budgets and monitoring of grant projects.

The Assistance Board and Department agreed with all of our recommendations.

### AUDIT CONCERN

**The Assistance Board has awarded over \$1 billion in state and local funds as part of the Program without identifying critical public school capital construction needs and prioritizing those needs throughout the state. As a result, it is unclear how well the Assistance Board is accomplishing the statutory intents of ensuring that public schools are safe and uncrowded and that public funds are used equitably, efficiently, and effectively to improve public schools.**

### KEY FACTS AND FINDINGS

- The Assistance Board has not prioritized public school capital construction needs throughout the state or identified school districts with critical capital construction needs and helped those districts apply for grants, as required by statute.
- Schools with critical needs may not be receiving grants. To identify critical needs, one indicator we used is an industry standard index that indicates that a facility has significant deficiencies and likely needs to be replaced. Of the 70 schools with critical needs, only about half have applied for grants to address their needs and only one-quarter have been awarded grants. Further, the Assistance Board funded projects that were classified as low importance while denying projects that were high importance and awarded cash grants for projects that did not address deficiencies rated as high-priority.
- The Assistance Board does not have adequate methods to determine and consider a school district's ability to finance capital construction projects, as required by statute. First, the Assistance Board's calculations of school district matching fund requirements do not accurately reflect the relative financial capacity of the districts to provide matching funds. Second, the Assistance Board does not have a tool to evaluate matching fund waiver requests and granted waivers to districts that appear to have greater capacity to fund their own projects while denying waivers to other districts with less capacity.
- The Assistance Board's conflict of interest policies do not comply with the Colorado Code of Ethics and we found two board members had voted on grant applications with which they had conflicts, in violation of both the Assistance Board's policies and statute.
- Of five projects we reviewed, we identified \$1.7 million in expenditures that appear questionable, including \$877,000 for 1,364 laptops and iPads for one school, over half of which were used by other schools in the district. These funds could have been made available to address other health and safety projects that did not receive funding.

For further information about this report, contact the Office of the State Auditor  
303.869.2800 - [www.state.co.us/auditor](http://www.state.co.us/auditor)

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## RECOMMENDATION LOCATOR

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Rec. No.	Page No.	Recommendation Summary	Agency Addressed	Agency Response	Implementation Date
1	28	Identify and prioritize the critical public school capital construction needs in the state and use the results as the basis for providing grants to school districts. This should include: (a) determining if adjustments can be made to the Priority Assessment data to prioritize capital construction needs and add health and safety data, (b) working with school districts to update Priority Assessment data, and (c) using the Priority Assessment data and other factors to identify school districts with critical needs that have not applied for funds and targeting outreach to those districts.	Public School Capital Construction Assistance Board  Department of Education	a. Agree b. Agree c. Agree  a. Agree b. Agree c. Agree	a. August 2014 b. June 2014 c. December 2013  a. August 2014 b. June 2014 c. December 2013
2	39	Improve grant decision making processes to ensure they are transparent and adhere to statutory direction by: (a) developing a standardized tool to evaluate grant applications based on objective criteria from the Priority Assessment, statutory requirements, and district financial capacity; (b) communicating evaluation criteria to potential applicants; (c) retaining documentation of completed application scoring documents; and (d) providing documentation of the application evaluation methodology to the State Board of Education.	Public School Capital Construction Assistance Board	a. Agree b. Agree c. Agree d. Agree	a. December 2013 b. December 2013 c. May 2014 d. June 2014

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## RECOMMENDATION LOCATOR

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Rec. No.	Page No.	Recommendation Summary	Agency Addressed	Agency Response	Implementation Date
3	51	Ensure matching fund requirements reflect the financial capacity of the school district and ensure equity in the process by: (a) evaluating whether statutory change is needed to use remaining bonded indebtedness or adjust other statutory factors for determining district match, (b) developing a methodology to calculate matching funds that correlates to districts' financial capacity to provide matching funds, (c) obtaining documentation that supports each waiver request, and (d) developing a tool to evaluate matching fund waiver requests and document the reasons for approval or denial of each request.	Public School Capital Construction Assistance Board	a. Agree b. Agree c. Agree d. Agree	a. May 2014 b. May 2014 c. December 2013 d. December 2013
4	59	Maximize the safeguards in place to prevent actual and apparent conflicts of interest by: (a) implementing rules that align with the Colorado Code of Ethics to ensure members do not evaluate or vote on projects in which they may have a financial interest; (b) establishing rules for handling conflicts of interest, including enforcement measures if members do not comply with the rules; and (c) documenting and retaining Assistance Board member conflicts of interest disclosures.	Public School Capital Construction Assistance Board	a. Agree b. Agree c. Agree	a. May 2014 b. May 2014 c. February 2014

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## RECOMMENDATION LOCATOR

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Rec. No.	Page No.	Recommendation Summary	Agency Addressed	Agency Response	Implementation Date
5	70	Establish written policies and procedures to strengthen management of grant contract budgets, including: (a) obtaining finalized, line-item budgets for each grant contract that serve as the basis for the Department's monitoring of grant expenditures; (b) requiring grant recipients to submit funding requests that align with the finalized line-item budgets; (c) providing direction to Department project consultants on conducting detailed monitoring of grant expenditures against final line-item budgets; (d) including definitions of allowable expenditures in grant contracts; and (e) including requirements in grant contracts for districts to manage project expenditures to the approved budget and revert funds not needed for delivering the project.	Department of Education	a. Agree b. Agree c. Agree d. Agree e. Agree	a. December 2013 b. December 2013 c. December 2013 d. December 2013 e. December 2013
6	78	Implement a more robust system for monitoring grant projects by: (a) establishing standardized contract provisions requiring grant recipients to provide the Department with standardized written progress reports and documentation demonstrating key quality processes have been completed, (b) establishing policies and procedures to provide direction to Department staff on monitoring contracts and evaluating grant recipient performance, and (c) developing requirements for how Department staff should document their contract monitoring activities.	Department of Education	a. Agree b. Agree c. Agree	a. December 2013 b. December 2013 c. December 2013
7	82	Improve the ability to hold cash grant recipients legally responsible for delivering the project covered by the grant by: (a) revising cash grant contracts to incorporate exhibits describing the project scope, timeline, and deliverables; and (b) amending any active cash grant contracts that are not substantially complete to incorporate the exhibits into the contracts.	Department of Education	a. Agree b. Agree	a. Implemented b. December 2013

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# Overview of the Public School Capital Construction Assistance Program

## Chapter 1

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In 2008 the Building Excellent Schools Today Act (BEST Act) [Section 22-43.7-102, C.R.S., et seq.] established the Public School Capital Construction Assistance Program (the Program) to help Colorado school districts, Boards of Cooperative Educational Services (BOCES), charter schools, and the Colorado School for the Deaf and Blind, build new public schools and renovate or maintain existing public schools, so that unsafe, deteriorating, or overcrowded facilities do not impair students' abilities to learn. Throughout the report we refer to school districts, charter schools, and BOCES collectively as "school districts". The primary purpose of the BEST Act is "to provide financial assistance to school districts ... throughout the state that have difficulty financing new capital construction projects and renovating and maintaining existing facilities." Statute [Section 22-43.7-105 and 106, C.R.S.] established the Public School Capital Construction Assistance Board (the Assistance Board) to oversee the Program with the support of the Department of Education's Division of Public School Capital Construction Assistance (the Department).

Statute [Section 22-43.7-108, C.R.S.] requires the Assistance Board to conduct, or contract for, a statewide financial assistance priority assessment (Priority Assessment) to determine the overall school capital construction needs at public schools in the state. In March 2010, Parsons Commercial Technology Group (Parsons), a national company that specializes in school facility assessment, design, and construction management, completed the Priority Assessment. The total cost of the assessment was \$12 million, and it provided the Department and Assistance Board with an evaluation of the condition, air and water quality, space requirements, ability to accommodate education technology, site requirements, and demographics for 8,419 school facilities in Colorado (including teaching and learning facilities, administrative buildings, and other support facilities and buildings). The Priority Assessment identified about \$13.9 billion in school capital construction needs over the time period of 2010 through 2013 for the approximately 1,687 schools in the state.

Based on the parameters established in law, the Assistance Board developed a statewide competitive grant program to provide financial assistance to school

districts for capital construction projects. The grant program operates on an annual cycle in which the Assistance Board accepts applications for financial assistance from school districts each spring. School districts can apply for any type of school capital construction project, such as a new roof, boiler repair, facility renovation, or new school facility.

In addition, the Program has a matching fund requirement for applicants. Section 22-43.7-109(9), C.R.S., details the method by which the Department and Assistance Board must determine the local matching percentage a district must contribute to each project. It is based on several factors related to the applicants' financial capacity. Statute also allows school districts to request a waiver for all or part of the matching fund requirement.

Statute [Sections 22-43.7-109 and 110, C.R.S.] establishes three types of grants to provide financial assistance to school districts:

**Lease-purchase grants**—typically awarded to fund larger projects such as new school construction, major renovations, and additions to buildings. For lease-purchase grants, the Assistance Board instructs the State Treasurer's Office (the Treasurer) to enter into lease-purchase agreements with a trustee on behalf of the State to finance specific public school facility capital construction projects. Essentially, a lease-purchase agreement means that the Treasurer works with a trustee who issues certificates of participation (COPs) for projects funded by lease-purchase grants. The trustee sells the COPs to investors and uses revenues generated to pay for projects funded through the lease-purchase grants awarded. In return, the trustee pays principal and interest to the investor, and the State makes lease payments to the trustee to cover the trustee's payment of principal and interest. All property financed with COPs funding is held "in trust" by the trustee until the COPs are paid in full (after approximately 20 years). If, for any reason, the lease payments cannot be made, the trustee can liquidate the assets in the trust to make the payments on the COPs.

The BEST Act caps the amount of lease-purchase grant agreements that can be entered into by limiting the amount of annual lease payments the State may make in any fiscal year. For Fiscal Year 2012 and beyond, the maximum State share for lease payments each year is \$40 million. The State may reach this \$40 million mark in the Fiscal Year 2014 grant cycle. Consequently, unless new legislation is passed to grant authority for additional annual lease-purchase payments, lease-purchase grants may not be available until the existing lease-purchase grant agreements begin to expire in 2029. For the Fiscal Year 2009 through 2014 grant cycles, the Assistance Board has funded a total of \$884 million in lease-purchase grants, including \$636 million in state and \$248 million in school district matching funds. We refer to all grant

awards as “funded,” however, funding for the nearly \$110.4 million in grants awarded in the Fiscal Year 2014 grant cycle will not be finalized until December 2013 after school district bond elections are completed and matching funds are made available.

**Cash grants**—typically used to fund smaller projects such as roofs, boiler replacements, and heating and cooling systems. These project budgets are most often less than \$1 million. However, in the Fiscal Year 2013 grant cycle, the Department created a large cash grant category, from which 11 cash grants were approved to fund larger projects, ranging from \$1.4 million for a high school boiler replacement and heating and cooling system upgrades to \$13.6 million to replace an elementary school. For the Fiscal Year 2009 through 2014 grant cycles, the Assistance Board has awarded a total of \$123 million in state funds for cash grants and required grant recipients to provide about \$82 million in matching funds.

**Emergency grants**—grants made for an unanticipated event that makes all or a significant portion of the building unusable for educational purposes or threatens the health or safety of the people using the facility. Statute [Section 22-43.7-104(4), C.R.S.] requires a \$1 million reserve to be maintained in the Capital Construction Assistance Fund (Assistance Fund) for the purposes of funding emergency grants. For the Fiscal Years 2009 through 2014 grant cycles, the Assistance Board has awarded a total of about \$927,000 for three emergency grants.

## Grant Awards

The Program began operations in July 2008 and awarded its sixth cycle of grant awards in May 2013. For the Fiscal Year 2009 through 2014 grant cycles, the Department received 475 grant applications, requesting a total of about \$1.7 billion in state funds and requiring about \$768 million in local matching funds. As shown in the table below, for the Fiscal Year 2009 through 2014 grant cycles, the Assistance Board has awarded about \$759 million in state funds to 211 projects and required matching funds totaling about \$330 million. Thus, in total, the Program has approved about \$1.1 billion for school capital construction projects over the past 6 years. The following table illustrates the grant award totals by fiscal year and type of grant.

<b>Public School Capital Construction Assistance Program Grant Totals</b>							
<b>Fiscal Year 2009 through 2014 Grant Cycles</b>							
<b>Dollars in Thousands</b>							
	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014<sup>3</sup></b>	<b>Total</b>
<b>State Funds</b>							
Cash Grants	\$ 14,124	\$ 14,112	\$ 11,350	\$ 26,318	\$ 47,637 <sup>2</sup>	\$ 9,063	\$ 122,604
Lease-purchase Grants	66,354	79,160	158,601	116,428	151,108	64,114	635,765
Emergency Grants	573	23	163	0	0	0	759
<b>Total State Funds</b>	<b>\$ 81,051</b>	<b>\$ 93,295</b>	<b>\$170,114</b>	<b>\$142,746</b>	<b>\$198,745</b>	<b>\$ 73,177</b>	<b>\$ 759,128</b>
District Matching Funds <sup>1</sup>	22,937	52,402	71,517	42,560	103,867	37,202	330,485
<b>Total</b>	<b>\$103,988</b>	<b>\$145,697</b>	<b>\$241,631</b>	<b>\$185,306</b>	<b>\$302,612</b>	<b>\$110,379</b>	<b>\$1,089,613</b>
<b>Source:</b> Office of the State Auditor's analysis of data provided by the Department's Division of Public School Capital Construction Assistance.							
<sup>1</sup> Combined district matching contributions for cash, lease-purchase, and emergency grants.							
<sup>2</sup> The Assistance Board decided to greatly increase the amount of cash grants funded in Fiscal Year 2013.							
<sup>3</sup> Grant awards from the Fiscal Year 2014 grant cycle have been approved by the State Board of Education and the Capital Development Committee; however, local matching funds for some districts will be secured through bond elections in November 2013, making these grants "awarded" but not yet "funded".							

The grants awarded during the Fiscal Year 2009 through 2014 grant cycles have impacted an average of about 53 schools and 21,000 students each year, as shown in the table below.

<b>Impact of Public School Capital Construction Assistance Program Grants</b>							
<b>Fiscal Year 2009 through 2014 Grant Cycles</b>							
	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014<sup>1</sup></b>	<b>Average Per Year<sup>2</sup></b>
<b>Number of Schools Receiving Grants</b>	53	72	75	37	49	33	53
<b>Number of Students Attending Schools that Received Grants</b>	22,410	26,506	29,728	14,283	20,895	13,645	21,245
<b>Source:</b> Data provided by the Department's Division of Public School Capital Construction Assistance based on information provided in grant applications and the Department's yearly pupil count.							
<sup>1</sup> Data on schools and students impacted by the Program for the Fiscal Year 2014 grant cycle are preliminary until financing is complete for the lease-purchase grants in December 2013.							
<sup>2</sup> Because some schools received grants in multiple grant cycles, the number of schools and number of students cannot be totaled across all years.							



## Program Oversight

The BEST Act places the majority of responsibility for the Program with the Assistance Board and created the Department to act in a supporting role to the Assistance Board. The roles and responsibilities for the entities charged with overseeing the Program are described below.

- **Public School Capital Construction Assistance Board:** Statute [Section 22-43.7-106, C.R.S.] establishes the Assistance Board as a Type 1 board as defined in Article 1, Title 24 of Colorado Revised Statutes, and consists of nine appointed members, including one public school board member, one public school superintendent, two school facilities planners or managers, one architect, one engineer, one construction manager, one school technology expert, and one public school finance expert. The State Board of Education (State Board) is responsible for appointing three members representing different areas of the State (rural, urban, and suburban), the Governor is responsible for appointing three members, and the General Assembly is responsible for appointing three members. Assistance Board members serve 2-year terms, with a maximum of three consecutive terms, and they may not hold a state elective office. Statute gives the appointing authority of a member the authority to remove that member for any cause that renders the member incapable of discharging or unfit to discharge his or her duties.

According to statute [Section 22-43.7-106(2), C.R.S.], the broad function of the Assistance Board is to protect the health and safety of students, teachers, and other persons who use public school facilities and to maximize student achievement by ensuring that the public school facilities provide a safe and uncrowded environment that is conducive to students' learning. Statute specifically requires the Assistance Board to provide financial assistance to school districts to improve the condition of their facilities to accomplish this broad purpose. The Assistance Board is granted rulemaking authority for the Program.

- **Department of Education:** The Department's responsibilities include implementing state and federal education laws, disbursing state and federal funds, and holding schools and districts accountable for their performance. The Department is charged with providing technical and professional support to the Assistance Board for the administration of the Program. The Department has eight professional staff dedicated to the Public School Capital Construction Assistance Program. According to statute [Section 22-43.7-105(2), C.R.S.], the Department is responsible for providing professional and technical support to the Assistance Board.

Department staff also provide professional and technical support to districts in preparing their grant applications and conduct monitoring and oversight of awarded projects.

- **State Board of Education:** The State Board, charged by the Colorado Constitution with the general supervision of the public schools in the state, promulgates and adopts policies, rules, and regulations concerning general supervision of the public schools, the Department of Education, and educational programs maintained and operated by state agencies. Under the BEST Act [Section 22-43.7-109(7), C.R.S.], the State Board approves funding for school capital construction projects recommended to them by the Assistance Board. The State Board also promulgates proposed Assistance Board rules and regulations.
- **Capital Development Committee of the General Assembly:** The Capital Development Committee is a statutory committee responsible for reviewing funding requests for capital projects from all state agencies and making prioritized recommendations to the Joint Budget Committee. Senate Bill 13-214, effective in June 2013, requires the Capital Development Committee to give final review and approval for all recommended lease-purchase grants from the Program. Prior to June 2013, the Capital Development Committee did not have a role in the review of Program grants.

## Fiscal Overview

Program revenues are required to be placed in the Assistance Fund and include State Land Board revenue, school district matching funds, interest earned on the Assistance Fund, and lottery proceeds from “spillover” funds. Spillover funds are lottery proceeds that remain after lottery proceeds satisfy several other obligations established by the Constitution. Program revenue and expenditures are shown in the table on the next page.

**Public School Capital Construction Assistance Program  
Revenue, Expenditures, and Fund Balance, By Source  
Fiscal Years 2009 Through 2013  
Dollars in Thousands**

	Fiscal Year				
	2009	2010	2011	2012	2013
<b>Beginning Fund Balance</b>	\$0 <sup>6</sup>	\$61,032	\$ 77,018	\$117,481	\$143,365
<b>Revenue</b>					
State Land Board Proceeds	35,195	33,196	60,261	72,357	61,663
COPs Proceeds <sup>1</sup>	0	41,101	82,354	162,907	167,118
Lottery Proceeds	5,535	89	662	4,559	8,644
Interest, Transfers, and Reimbursement <sup>2</sup>	45,321	2,604	1,722	1,670	1,662
School District Matching Funds	0	801	3,729	7,233	10,313
<b>Total Revenue</b>	<b>\$86,051</b>	<b>\$77,791</b>	<b>\$148,728</b>	<b>\$248,726</b>	<b>\$249,400</b>
<b>Expenditures</b>					
Lease-purchase Project Expenditures	0	33,036	79,888	177,291	167,172
Cash Grant Payments	20,052	16,943	15,809	9,521	21,352
Personal Services Contracts <sup>3</sup>	4,456	7,649	76	58	47
Lease-purchase Debt Payments	0	3,535	11,817	35,184	34,269
Administrative <sup>4</sup>	511	642	675	788	813
<b>Total Expenditures</b>	<b>\$25,019</b>	<b>\$61,805</b>	<b>\$108,265</b>	<b>\$222,842</b>	<b>\$223,653</b>
<b>Ending Fund Balance</b>	<b>\$61,032</b>	<b>\$77,018</b>	<b>\$117,481</b>	<b>\$143,365</b>	<b>\$169,112</b>
<b>Obligations<sup>5</sup></b>	<b>\$ 1,000</b>	<b>\$19,751</b>	<b>\$ 39,036</b>	<b>\$ 58,527</b>	<b>\$104,690</b>
<b>Fund Balance Less Obligations</b>	<b>\$60,032</b>	<b>\$57,267</b>	<b>\$ 78,445</b>	<b>\$ 84,838</b>	<b>\$ 64,422</b>

**Source:** Office of the State Auditor's analysis of information from the Colorado Financial Reporting System (COFRS) and Department Financial Statements dated May 31, 2013 and June 30, 2013.

<sup>1</sup>The first bond offering for the Program was issued in August 2009, which is Fiscal Year 2010. Thus, no bond proceeds were received by the State until Fiscal Year 2010.

<sup>2</sup>This line includes interest on the Capital Construction Assistance Fund, a transfer from another fund in Fiscal Year 2009, and reimbursement of prior year expenses in Fiscal Year 2010. In Fiscal Year 2009, there was a transfer of \$44 million in funds remaining from the prior public school capital construction assistance program to the BEST program as required by statute [Section 22-43.7-104, C.R.S].

<sup>3</sup>Personal Services Contracts include the Parsons contract for \$4,450,000 in Fiscal Year 2009 and \$7,596,000 in Fiscal Year 2010, for a total of \$12,046,000, and all other personal services contracts issued by the Department for the Program.

<sup>4</sup>Administrative expenses include salary and benefits for staff, travel costs, operating expenses, capital complex rent, and workers compensation costs.

<sup>5</sup>Obligations include the statutory emergency set aside, upcoming bond obligation payments, district cash match set asides, cash grant encumbrances as set forth in the Department's May 31, 2013 and June 30, 2013 Financial Position for the program.

<sup>6</sup>The Assistance Fund was established during Fiscal Year 2009 as a result of the BEST Act.

## Audit Purpose, Scope, and Methodology

Section 22-43.7-111, C.R.S., requires the Office of the State Auditor to conduct a performance audit of the financial assistance grant and lease-purchase program for the Public School Capital Construction Assistance Program by February 15, 2014. Audit work was performed from December 2012 through September 2013. We acknowledge the cooperation and assistance provided by the Department of Education's Division of Public School Capital Construction Assistance staff.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The primary objective of our audit was to determine whether the Assistance Board and the Department have managed the Program in compliance with statutes and in a manner that ensures the most equitable, efficient, and effective use of funds available to provide financial assistance to school districts for school capital construction projects. Specifically, we evaluated whether:

- The Assistance Board and Department have complied with the statutory mandate to develop construction guidelines and conduct a Priority Assessment and used them to identify the critical public school capital construction needs throughout the State.
- The Assistance Board is complying with its statutory mandate to provide recommendations for funding, based on objective criteria and using the Priority Assessment to prioritize applications based on statutory criteria.
- The Assistance Board uses an objective, measurable, and documented grant evaluation and award process to provide a prioritized list of projects recommended for funding to the State Board.
- The Assistance Board follows statutory criteria in determining district matching fund requirements and approving matching fund waivers or reductions, and whether the Assistance Board's matching requirements appear equitable.
- The Department has adequate controls in place to ensure that districts provide high-quality projects, on time, and within budget, and that districts

spend grant funds on items that are reasonable, necessary, and allowable under the terms of the grant award contract.

- The Department has sufficient terms and conditions in its cash grant contracts to ensure that the grant recipient completes the project, as described in the grant application, on time, and within budget, and that the Department has sufficient remedies available to enforce the contract.
- The Assistance Board has sufficient policies and procedures to prevent conflicts of interest while carrying out its duties.

We assessed the effectiveness of internal controls that are significant to the audit objectives described above. Our conclusions on the effectiveness of those controls are described in the audit findings and recommendations.

To accomplish our audit objectives we:

- Reviewed relevant state laws, rules, regulations, policies, procedures, and Attorney General's Office guidance related to the Program; Fiscal Year 2013 grant cycle applications and grant denial letters; all 25 matching fund waiver requests submitted by school districts, charter schools, and BOCES with funded applications in the Fiscal Year 2011 through 2013 grant cycles; and the Department's cash and lease-purchase grant contract templates. We did not find problems with the contract provisions for the lease-purchase grants.
- Interviewed Department management and staff, Assistance Board members, State Board members, individuals involved in drafting the BEST Act legislation, and a representative from the contractor that completed the Priority Assessment.
- Conducted a survey of all nine Assistance Board members, of whom seven responded, to determine the Assistance Board's policies, procedures, and practices related to grant decision making and waiver request approval.
- Reviewed Assistance Board meeting minutes for the period January through December 2012; July, August, and October 2009 (the Assistance Board did not meet in September 2009); and June 2010; and attended and observed Assistance Board meetings, including the May 2013 meetings in which grant award decisions for the Fiscal Year 2014 grant cycle were made.

- Compared Priority Assessment data with Department data on the school districts that applied for grants in the Fiscal Year 2009 through 2014 grant cycles.
- Interviewed staff and reviewed grant application evaluation and award processes used at several other grant programs in Colorado to identify grant programs that might serve as best practices for the Program in evaluating and selecting grant applications for funding.
- Reviewed the Assistance Board's processes for determining district matching fund requirements and reviewing and approving matching fund waivers or reductions to determine whether their processes comply with statute, appear equitable to school districts, and are documented.
- Reviewed the Department's contract administration processes for a nonstatistical judgmental sample of five lease-purchase grant awards from the Fiscal Year 2011 through 2012 grant cycles, including:
  - Reviewing Department and school district documentation related to the grant project budget and expenditures, quality control processes, and reimbursement requests.
  - Visiting two of the five school districts in our sample that received grant awards and contacting the remainder of the districts in our sample by phone to conduct interviews.

We relied on sampling techniques to support our audit work as follows:

- We selected a nonstatistical judgmental sample of seven of the 178 school districts and 21 of the 122 eligible charter schools in the state, as of Fiscal Year 2013. We designed our sample to provide sufficient, appropriate evidence for evaluation of the Department's calculation of matching fund requirements.
- We selected a nonstatistical judgmental sample of five of the 19 lease-purchase grant awards issued during the Fiscal Year 2011 through 2012 grant cycles. We designed our sample to provide sufficient, appropriate evidence for our evaluation of the Department's contract administration practices.

## **Information Prohibited from Public Disclosure**

The Department provided us with two memoranda from the Attorney General's Office to the Assistance Board regarding conflicts of interest. However, the memoranda are subject to attorney-client privilege and the Assistance Board did not agree to waive the privilege. Section 7.39 of Government Auditing Standards states that, "If certain pertinent information is prohibited from public disclosure or is excluded from a report due to the confidential or sensitive nature of the information, auditors should disclose in the report that certain information has been omitted and the reason or other circumstances that make the omission necessary." As a result, although pertinent to this audit, information contained in the two memoranda from the Attorney General's Office to the Assistance Board has been omitted from this report.

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# Program Oversight

## Chapter 2

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Statute [Section 22-43.7-106(2), C.R.S.] created the Public School Capital Construction Assistance Board (the Assistance Board) to develop the Public School Capital Construction Assistance Program (the Program), for the purpose of protecting the health and safety of students, teachers, and others who use public school facilities and to maximize student achievement by ensuring that the condition and capacity of public school facilities are sufficient to provide a safe and uncrowded environment that is conducive to students' learning. The Assistance Board consists of nine members who bring various expertise to the Program. Under statute [Section 22-43.7-106(1)(a), C.R.S.], the Assistance Board includes representatives of urban, suburban, and rural school districts, as well as experts in school facility planning, architecture, engineering, construction management, technology, and school finance. Statute requires the Assistance Board to ensure the most equitable, efficient, and effective use of Program funds when providing financial assistance to school districts that have difficulty financing new capital construction, renovation, and maintenance projects. Statute specifically requires the Board to assess public school capital construction needs throughout the state and to provide recommendations based on objective criteria to the State Board of Education (State Board) regarding the appropriate prioritization and allocation of such financial assistance. Statute further requires the Assistance Board to consider the financial capacity of each applicant in carrying out the Assistance Board's responsibilities to provide financial assistance to school districts.

The Assistance Board developed a competitive grant process, available to all public school districts, to provide financial assistance to public schools in Colorado.

We reviewed the Assistance Board's implementation of the Program, including the Assistance Board's processes and procedures for prioritizing public school facility needs, reviewing grant applications and waiver requests, and ensuring that the Assistance Board operates in accordance with the Colorado Code of Ethics and found that the Assistance Board could make improvements in four key areas: (1) prioritization of need, (2) grant decision making, (3) determining financial capacity, and (4) preventing conflicts of interest.

## Prioritization of Need

Sections 22-43.7-107 and 108, C.R.S., require the Department of Education's Division of Public School Capital Construction Assistance (the Department) and the Assistance Board to conduct, or contract for, a statewide financial assistance priority assessment (Priority Assessment) of public school facilities to identify and prioritize the overall school capital construction needs in the state. The Department and Assistance Board paid more than \$12 million to Parsons Commercial Technology Group (Parsons), a national company that specializes in school priority assessment, design, and construction management, to conduct an assessment of all public school facilities in Colorado. Parsons completed the Priority Assessment of the State's nearly 1,700 public schools as well as more than 6,700 other school facilities (such as modular classrooms, building additions, storage sheds, administrative buildings, and concession stands) and issued a final report in March 2010.

The Priority Assessment report estimated approximately \$13.9 billion in statewide school facility deficiencies in the following three categories:

- \$9.4 billion to address condition needs (needs related to the physical condition of the school)
- \$4.5 billion to address suitability needs (needs related to how well the facility supports its educational program)
- \$19.1 million to address energy needs (needs based on facility energy costs, usage, and other utility data)

Every school had current facility deficiencies identified in one or more of the three categories and the total amount of funds needed to address the facility needs varied by school.

Public school capital construction needs are significant, but the amount of funding available to meet those needs is limited. Although the Priority Assessment estimated the total cost to address school facility construction needs in the state to be almost \$14 billion, in the 6 years since the Program began, the Assistance Board has funded a total of over \$1 billion in Program grants, including \$759 million in State funding and \$330 million in school district matching funds.

### **What audit work was performed and what was its purpose?**

The purpose of our audit work in this area was to determine whether the Assistance Board and Department have complied with the statutory direction to

conduct a priority assessment of public school capital construction needs throughout the state and to identify the critical public school capital construction needs using the public school facility construction guidelines. We interviewed Department staff, the Assistance Board, and a Parsons representative to find out how the Assistance Board uses the facility construction guidelines and Priority Assessment to identify and prioritize the capital construction needs throughout the state and what processes the Assistance Board or Department have implemented to help districts with critical needs submit quality applications for funding to address those needs.

Statute does not define critical need. The Assistance Board has generally identified critical need to mean health and safety needs, however, the Assistance Board has not developed a methodology to identify health safety needs and prioritize those needs statewide. As a result, we used one of the indices in the Priority Assessment report to identify districts with critical needs and determine if they applied for grants. As will be discussed more fully later, we compared the list of needs identified based on the Facility Condition Index (FCI), as identified in the Priority Assessment, with the large facility replacement grants applied for during the Fiscal Year 2009 through 2013 grant cycles. FCI is an industry-standard measurement of a facility's condition that is the ratio of the cost to correct a facility's deficiencies to the current replacement value of the facility.

### **How were the results of the audit work measured?**

Statute assigns responsibility to the Assistance Board and the Department to identify and prioritize the critical public school capital construction needs throughout the state as a basis for providing financial assistance to school districts, thereby ensuring that the condition and capacity of public school facilities are sufficient to provide a safe and uncrowded environment that is conducive to students' learning. This responsibility includes the following key steps.

**First, the Assistance Board is responsible for establishing public school facility construction guidelines.** The guidelines must identify and describe the capital construction, renovation, and equipment needs in public school facilities in the state, and the means of addressing those needs [Section 22-43.7-107(2), C.R.S.]. Statute [Section 22-43.7-107(1), C.R.S.] also states that the guidelines are required to be used by the Assistance Board for “assessing and *prioritizing public school capital construction needs throughout the state.*” [*Emphasis added*] The guidelines are required to address the following items [Section 22-43.7-107(1) and (2), C.R.S.]:

- Health and safety issues, including security needs
- Technology
- Building site requirements
- Building performance standards and guidelines
- Functionality of existing and planned school facilities for core educational programs
- Capacity of existing and planned public school facilities
- Public school facility accessibility
- The historic significance of existing public school facilities and the potential to meet current programming needs by rehabilitating such facilities

**Second, the Assistance Board is responsible for conducting a Priority Assessment of the public school capital construction needs throughout the state.** Statutes [Sections 22-43.7-106(2)(b) and 22-43.7-108(1)(a) and (3), C.R.S.] require the Assistance Board to conduct or contract for a Priority Assessment of the public school capital construction needs throughout the state using the public school facility construction guidelines, as noted above. Statute [Section 22-43.7-108(2)(a), C.R.S.] requires the Priority Assessment to be based on the following additional factors:

- The condition of the public school facility
- Air and water quality in the public school facility
- Public school facility space requirements
- The ability to accommodate educational technology, including but not limited to technology for individual student learning and classroom instruction
- Site requirements for the public school facility
- Public school facility demographics, including a 5-year projection of substantial changes in the pupil count of individual public school facilities

The word “priority” (as related to the Priority Assessment) is not defined in statute, but a plain reading would seem to indicate that it means giving something precedence, preference, or superiority over other things. Definitions for “priority” in *Merriam-Webster’s Collegiate Dictionary* (11th edition) include “superiority in rank, position, or privilege;” “a preferential rating, especially one that allocates rights to goods and services usually in limited supply;” and “something given or meriting attention before competing alternatives.” In addition, statute [Section 22-43.7-107(1) and (2), C.R.S.] requires the Assistance Board to establish public school facility construction guidelines to be used for “assessing and prioritizing public school capital construction needs throughout the state” and to conduct the Priority Assessment using those guidelines. The plain definition of “priority” along with the statutory language that the Assistance Board should be prioritizing

public school capital construction needs indicate that the requirement to conduct a priority assessment means that the assessment should identify the school capital construction needs that should have a preferential ranking over others, in other words, which needs should be prioritized over others. Our analysis during the audit is based on this interpretation. However, the Assistance Board has indicated that it does not interpret the word “priority” in the statute to mean that the assessment should establish a prioritized list of public school capital construction needs, but rather that the assessment should be done before other things, as a priority, such as awarding grants.

**Third, the Assistance Board and Department have statutory responsibilities to identify critical capital construction needs.** Specifically:

- Section 22-43.7-105(2)(d), C.R.S., states that the Department, subject to Assistance Board direction, has the power or duty to assist applicants and potential applicants in identifying critical capital construction needs using the public school facility construction guidelines.
- Section 22-43.7-106(2)(d), C.R.S., states that to further the performance of its function, the Assistance Board has the power or duty to establish guidelines for the Department to follow when assisting potential applicants in identifying critical capital construction needs and preparing financial assistance applications.

### **What problem did the audit work identify?**

We found the Assistance Board and the Department have taken some of the steps outlined in statute but have not fully carried out their responsibilities for identifying and prioritizing public school capital construction needs throughout the State as a basis for providing financial assistance to school districts.

We found the Assistance Board has:

- Established public school facility construction guidelines that address the considerations in statute (health and safety issues, technology, building site requirements, building performance standards and guidelines, functionality of existing and planned school facilities for core educational programs, capacity of existing and planned school facilities, accessibility, and the historic significance of existing public school facilities).
- Conducted an assessment of the public school capital construction needs throughout the state.

However, we found the Assistance Board has not:

- **Prioritized public school capital construction needs throughout the state.** The Priority Assessment database does not provide the Assistance Board with a prioritized list of projects; however, it has a wealth of data available to help the Assistance Board prioritize public school capital construction needs in the state, with one exception. The Priority Assessment was not conducted in a manner that clearly identified all health-and-safety related deficiencies and therefore cannot be used to generate a comprehensive list of all health-and-safety related needs at public school facilities. For example, as part of each school's assessment, Parsons flagged some deficiencies as "critical repairs". However, Department staff stated that they are not confident that all deficiencies flagged as "critical repairs" are indeed health or safety deficiencies, or that all actual health and safety deficiencies were identified. Health and safety needs at schools are key factors that statute requires the Assistance Board to use when prioritizing applications for funding. Further, having the ability to use the Priority Assessment to create a comprehensive, prioritized list of health and safety needs would help the Assistance Board and Department identify the critical school capital construction needs in the state.
- **Identify districts with critical needs and assist those districts to submit quality applications for financial assistance.** The Department provides general outreach to schools throughout the state by offering webinars, making presentations at statewide school district meetings, posting information about the grant program on its website, and responding to school district requests for assistance in preparing grant applications. However, Department staff do not systematically use the Priority Assessment, or any other mechanism, to identify schools with critical needs, perform targeted outreach to those schools, and then assist them to develop high-quality applications for funding. Given the fact that funding is limited and cannot address all the needs in the state, developing techniques to identify critical needs and help the schools with those needs compete for funding would help ensure the effectiveness of the program.

### **Why did the problem occur?**

Although the Priority Assessment report indicates that the Priority Assessment was conducted in accordance with the construction guidelines, the Department and the Assistance Board did not ensure that the Priority Assessment data could be queried specifically to identify health and safety needs at schools, or to prioritize those needs as required by statute. Additionally, the RFP issued by the

Department to contract for the Priority Assessment required that the contractor provide a software application that is “able to produce a three year forecast of school district wide recommended projects along with associated costs estimates.” Parsons’ bid proposal stated that in its final report it would provide a 5-year project list that “will be provided in order of priority along with associated cost estimates.” However, Parsons did not provide a list that prioritized all public school capital construction projects in the State and the Department did not use the assessment to develop a prioritized list of projects.

The Priority Assessment data are now nearly 4 years old, and the assessment database has not been fully updated, making it difficult for the Department to complete a meaningful prioritization of capital construction needs across the state or to demonstrate overall improvements in the condition of public schools. The ages of systems in the Priority Assessment database are automatically updated annually, and districts can submit updates for the Department’s review and input into the Priority Assessment database. However, being able to maintain an accurate database of public school capital construction needs throughout the State is challenging because the Department and Assistance Board do not have mechanisms to routinely and comprehensively update the assessment. Districts are not required to provide updates to the system when deficiencies are corrected (either through projects funded with Program grants or through other financing sources) or when new deficiencies are identified. Further, Department staff do not update the system based on the grants the Assistance Board has awarded (e.g., by removing schools that have been replaced with BEST grant funds, adding newly built schools or systems, or updating information on priority one and two deficiencies as systems age). Some options the Department could consider to ensure that the Priority Assessment database is updated include: (1) seeking statutory requirements for schools to verify existing information in the database on an annual basis and submit updated information as deficiencies arise or improvements are made, (2) establishing a requirement that schools submit updated information each year as a condition of eligibility for funding, and/or (3) establishing a process for the Department to update the Priority Assessment data based on grant awards.

As discussed, the Assistance Board lacks a methodology to prioritize school construction needs throughout the state. As a result, we worked with Parsons to determine if there is information in the Priority Assessment that could provide some indication of the schools with the most critical needs. For purposes of the audit, we used one of the indices in the Priority Assessment report as an indicator of the criticality of a public school’s construction needs. Specifically, we used the Facility Condition Index (FCI) to evaluate the extent to which the Program has addressed critical needs at schools in the state. FCI is an industry-standard measurement of a facility's current condition compared with what it would cost to replace the facility. FCI is represented as a percentage and is calculated by

dividing the amount it would cost to repair the deficiencies at the facility by the amount that it would cost to replace the facility with one of similar use and size. The higher the FCI percentage, the more likely the building has significant deficiencies and needs to be replaced rather than repaired. We recognize that this index is a single indicator and that other factors or indices, in combination with the FCI, may provide a more comprehensive guideline to identifying the schools with the most critical capital construction needs. However, in the absence of criteria or guidance developed by the Assistance Board or the Department to prioritize capital construction needs statewide, we selected the FCI for the following reasons:

- According to the Priority Assessment report, “The higher the FCI, the poorer the condition of a facility. After an FCI is established for all buildings within a portfolio, a building’s condition can be ranked relative to other buildings.” The report also states that the Priority Assessment used benchmark indices, including the FCI, “to establish a hierarchy of facility needs as a guide for the [Assistance Board] in its determination of financial priority assistance.”
- When interviewed, Parsons told us that an FCI of 70 percent or higher could serve as a rough indicator of critical need.
- We conducted research on capital management programs and the use of FCI and found that it is common practice for entities to use FCI as a means of prioritizing facility capital needs and directing limited resources to address the most critical needs. Colleges and universities and the National Park Service, for example, use FCI to identify which buildings are most in need of repair or maintenance and prioritize funding accordingly. The United States Government Accountability Office’s 2007 report titled *U.S. Postal Service Facilities* tasked the United States Postal Service with assessing its facilities and using FCI to prioritize its capital maintenance and repair projects.

As shown in the table on the next page, only about half of the schools with FCI scores of 70 percent or greater applied for funding, and less than one-quarter of schools with FCI scores of 70 percent or greater were awarded funding. Therefore, using the FCI as an indicator, it appears that the majority of schools with critical needs have not received grants through the Program.



<b>Number of Schools with a Facility Condition Index (FCI) of 70 Percent or Higher<sup>1</sup> That Applied for and Received Funding Fiscal Year 2009 through 2013 Grant Cycles<sup>2</sup></b>	
Total Number of Schools in the State with FCI > 70%	70
Schools with FCI > 70% for which Districts Applied for Grants	36 (51%)
Schools in the State with FCI > 70% That Were Funded	17 (24%)

**Source:** Office of the State Auditor's analysis of Priority Assessment data, grant applications, and grant awards.

<sup>1</sup>The original Priority Assessment database was created in 2010. According to the Department, there is no mechanism for the Priority Assessment database to be regularly and comprehensively updated to reflect either improvements in school facility conditions due to improvement projects or new deficiencies that have occurred since the Priority Assessment was conducted. As a result, the data in the Priority Assessment database may not accurately reflect the conditions of all school facilities as of the 2013 grant cycle. In the absence of other data, we used the Priority Assessment database for this analysis because these are the same data the Department and Assistance Board have available to help prioritize school improvement needs.

<sup>2</sup>Based on all schools that are eligible to receive funding, (e.g., excludes schools that are vacant or not owned by the school district or charter school).

The Assistance Board and Department also stated that, because of the history of local control of schools in Colorado, it is not their role to take a proactive approach to prioritize or identify critical public school capital construction needs throughout the State. They believe it is their role to evaluate applications they receive to make recommendations for funding to the State Board. As discussed previously, the Department has not systematically identified critical needs projects and has not conducted specific targeted outreach to the schools with the highest needs. Further, the Assistance Board has not developed any guidelines for the Department to follow to assist potential applicants in identifying critical capital construction needs and preparing financial assistance applications.

### **Why does the problem matter?**

As a State entity responsible for the Program, the Assistance Board is in an ideal position to take a statewide perspective on addressing public school capital construction needs and to award limited monies to address those needs that are most critical. We recognize that local control is a vital concept in Colorado's K-12 education system, but individual school districts do not have the information or combined expertise of the Assistance Board to determine where limited funds should be awarded. As such, statutes imply the Program was established so that the Assistance Board would take a statewide view of public school capital construction needs and not rely solely on local school districts to determine what projects are critical and what projects should receive funding to improve the overall condition of the State's public school facilities.

Additionally, the Assistance Board spent more than \$12 million for an assessment of public school capital construction needs in the state that does not provide

enough information to prioritize all those needs. The Priority Assessment assigned a priority of 1 through 5 to each deficiency noted within a school facility, with priority 1 and 2 ratings indicating that the deficiency should be corrected immediately or within one year. The Priority Assessment report identifies nearly \$123.5 million in deficiencies rated as priority 1 or priority 2 deficiencies and the Assistance Board has not attempted to identify which priority 1 deficiencies should be considered for funding prior to other priority 1 deficiencies. Further, there are no indicators to show whether the deficiencies are specifically related to health, safety, or security issues, and as a result, the Assistance Board cannot use the priority ratings alone to develop a prioritized list of public school capital construction needs. Finally, the Assistance Board has awarded more than \$759 million in state funds but does not have information on the extent to which the grants have addressed the critical needs in the state.

Overall, it is not clear the extent to which the Assistance Board is accomplishing the statutory intents of:

- Protecting the health and safety of students, teachers, and other persons who use public school facilities and maximizing student achievement by ensuring that the condition and capacity of public school facilities are sufficient to provide a safe and uncrowded environment that is conducive to students' learning [Section 22-43.7-106(2), C.R.S.].
- Ensuring the most equitable, efficient, and effective use of state revenues dedicated to provide financial assistance for capital construction projects through this program. [Section 22-43.7-106(2), C.R.S.].

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## **Recommendation No. 1:**

The Public School Capital Construction Assistance Board (the Assistance Board), with the assistance of the Department of Education's Division of Public School Capital Construction Assistance (the Department), should take steps to identify, in a prioritized manner, the critical public school capital construction needs in the state, taking into account all factors required by statute, and use the results as a primary basis for providing financial assistance to school districts in priority order to the extent possible. This should include:

- a. Working with Parsons Commercial Technology Group (Parsons) to determine if adjustments can be made to the statewide financial assistance priority assessment (Priority Assessment) data to prioritize capital construction needs and add health and safety data across the State in accordance with statutory requirements.

- b. Working with school districts to identify a means of maintaining updated information in the Priority Assessment database.
- c. Systematically using the Priority Assessment data, in conjunction with other factors as appropriate, to identify school districts that have not applied for funds for their schools with critical needs and that do not have the financial ability to help themselves, and targeting outreach to those districts to help them prepare quality applications for funding.

### **Public School Capital Construction Assistance Board Response:**

- a. Agree. Implementation date: August 2014.

The Assistance Board, with the assistance of the Department, will work with Parsons to identify potential updates and adjustments to the Priority Assessment data, including the addition of health and safety data that would allow the Assistance Board to develop a prioritized list of the critical public school capital construction needs statewide, based on statutory criteria. Depending upon the specific scope of work, Parsons has indicated the cost to make the recommended updates and adjustments to the Priority Assessment data could be significant. The Assistance Board will work with Parsons to determine the appropriate scope of work, develop and estimate costs, and work with the Department and the State Board of Education on a potential funding request.

- b. Agree. Implementation date: June 2014.

The Assistance Board will work with school districts to determine a method to maintain updated information in the Priority Assessment database and to identify the associated impact upon district resources.

- c. Agree. Implementation date: December 2013.

The Assistance Board will use available data, including the Priority Assessment data, and any future enhancements to the data, to identify and conduct targeted outreach to districts with critical capital construction needs including those that do not have the financial ability to help themselves. The Assistance Board will consider approaches to identify school districts with critical needs based upon currently available data and direct the Department staff to perform targeted outreach to those districts. The Assistance Board will revise

the direction to Department staff as additional data, including enhancement to the Priority Assessment data, become available and new approaches are identified.

### **Department of Education Response:**

- a. Agree. Implementation date: August 2014.

The Department will provide assistance to the Assistance Board in working with Parsons, including determining the estimated costs of updating the Priority Assessment database and developing funding requests as appropriate.

- b. Agree. Implementation date: June 2014.

The Department will support the Assistance Board in working with school districts to determine a method to maintain updated information in the Priority Assessment database and to identify the associated impact upon school district resources.

- c. Agree. Implementation date: December 2013.

The Department will support the Assistance Board's efforts to identify districts with critical capital construction needs and conduct targeted outreach. As part of this effort, the Department is developing various approaches to recommend to the Assistance Board in order to identify school districts with critical needs based upon currently available data. The Department will revise these recommended approaches as additional data, including enhancements to the Priority Assessment data, become available.

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## **Grant Award Decision Making**

The Assistance Board's grant application review and grant decision making processes are based on an annual cycle as illustrated in the table on the next page.

<b>Public School Capital Construction Assistance Program Grant Cycle Time Line</b>	
<b>September</b>	The Department sends out notification of the upcoming grant cycle to schools.
<b>October</b>	
<b>November - February</b>	The online grant application is open to applicants. The Department helps applicants prepare their applications.
<b>March</b>	Department staff review all grant applications and compile key data from each application into a summary book for the Assistance Board members. The summaries include a description of the project; amount of funding requested and proposed amount of matching funds; data from the Priority Assessment database, including the facility's FCI and Colorado Index (a score that assesses the condition as well as the programmatic adequacy of a facility) scores and the facility deficiencies; and several indicators from Department staff as to whether the project: (1) is a health or safety project, an overcrowding project, or a technology project; (2) is of low, medium, or high urgency and importance; (3) addresses identified deficiencies; (4) has reasonable costs per square foot; and (5) has any negative financial indicators (e.g., the district's annual revenues are consistently below its annual debt payments for each of the past 3 years).
<b>April</b>	
<b>May</b>	The Assistance Board reviews the summary book and holds a 2-day public meeting to discuss the grant applications and create a prioritized list of recommended grants for the State Board's approval. The Assistance Board begins the meeting by having Department staff and applicants make a brief presentation for each grant application. After the presentations, each Assistance Board member individually creates a ranked list of projects that he or she believes should be funded. The Department averages the members' rankings to develop a final list of prioritized projects. The Assistance Board then preliminarily awards funding, in priority order, until the Program runs out of available funding for the year. The prioritized list contains the amount and type of grant to be provided and may have a list of backup projects that should be funded if a higher-priority project becomes ineligible for funding.
<b>June</b>	The Assistance Board submits the prioritized list to the State Board for approval. The State Board can approve or disapprove the entire list or individual projects on the list submitted by the Assistance Board. The State Board must then provide the final prioritized list of projects recommended for funding to the Capital Development Committee of the General Assembly, which reviews and approves or disapproves the final list.
<b>July</b>	The Department sends out notices of non-awards to applicants that were not awarded funds.
<b>August</b>	The Department sends contracts to applicants that were awarded funds.
<b>Source:</b> Office of the State Auditor's analysis of the Department's Division of Public School Capital Construction Assistance's grant application and award cycle information.	

## **What audit work was performed and how were the results of the work measured?**

We reviewed the Assistance Board and Department policies and procedures related to evaluating grant applications and making grant award decisions. The purpose of our audit work was to determine whether the Assistance Board is complying with its statutory mandate to provide recommendations for funding, based on objective criteria [Section 22-43.7-106(2), C.R.S.] and using the Priority Assessment to prioritize applications based on statutory criteria. Specifically, statute [Section 22-43.7-109(5), C.R.S.] requires the Assistance Board, while taking the results of the Priority Assessment into consideration, to prioritize applications based on the following criteria in descending order of importance: (1) projects that address safety hazards or health concerns at existing facilities; (2) projects that relieve overcrowding, including those that move students from temporary facilities into permanent ones; (3) projects that incorporate technology into the education environment; then (4) all other projects.

Additionally, we obtained a memorandum from the Attorney General's Office to the Assistance Board regarding the use of the Priority Assessment in grant decision making. However, the memorandum is subject to the attorney-client privilege and the Assistance Board did not agree to waive the privilege. Section 7.39 of Government Auditing Standards states that, "If certain pertinent information is prohibited from public disclosure or is excluded from a report due to the confidential or sensitive nature of the information, auditors should disclose in the report that certain information has been omitted and the reason or other circumstances that make the omission necessary." As a result, although pertinent to this audit, information contained in the memorandum from the Attorney General's Office to the Assistance Board has been omitted from this report.

As discussed in Recommendation No. 1, because the Assistance Board has not developed a prioritized list of capital construction projects in the state or a methodology for identifying the most critical needs, for purposes of the audit, we used indices in the Priority Assessment report as indicators of the criticality of a public school's construction needs. First, we used an FCI score of 70 percent or higher to identify schools that have critical needs, because the higher the FCI score, the poorer the condition of the facility. In addition, we used the priority one and two rankings of various system deficiencies (e.g., roofing systems, boilers, heating and cooling systems) as defined in the Priority Assessment, to determine which schools have deficiencies that have been identified as needing to be corrected immediately or within 1 year. We used the FCI to evaluate grants awarded and denied during the Fiscal Year 2009 through 2013 grant cycles and we used the Priority 1 and 2 rankings to evaluate the grants awarded in the Fiscal Year 2014 grant cycle.

We also looked at grant application evaluation and award processes at several other grant programs in Colorado, including the Energy and Mineral Impact Assistance Program, the Limited Gaming Impact Program, the Grant Program for Historical Preservation, and the Colorado HIV and AIDS Prevention Grant Program to identify grant processes that might serve as best practices for the Assistance Board and Department. We specifically inquired as to the extent to which these programs use standardized tools to evaluate and select grant applications for funding and the extent to which these programs document the reasons for approving or denying grant funding and how the various factors used in evaluation relate to the grant award or denial decisions.

### **What problem did the audit work identify?**

It is unclear the extent to which the Assistance Board is using the Priority Assessment to prioritize recommended grant awards according to the statutory criteria. As discussed more in the next segment of this comment, this is primarily because the Assistance Board has not developed a formal written evaluation tool for reviewing grant applications that documents the factors from the Priority Assessment, as well as statutory factors, that the Assistance Board considers to prioritize the applications for funding. Further, without a documented evaluation tool, the Assistance Board cannot demonstrate the rationale for approving or denying each grant application.

We conducted a number of analyses to evaluate whether the Assistance Board's prioritization of projects for financial assistance appears to adhere to the statutory requirements. The results of our analyses indicate that the Assistance Board may not always be following the statutes, as described below. We recognize that a variety of factors may have driven the Assistance Board's decisions when prioritizing projects in our examples below. For example, the Assistance Board may have ranked some health safety projects or projects assigned a priority one or two ranking as lower priority for funding because the proposed project did not appear to address the facility needs or the applicant had not prepared a comprehensive application. However, due to the limited documentation regarding the reasoning for the Assistance Board's funding decisions, we were unable to evaluate the impact of such factors on the Assistance Board's decision making processes. The following examples raise concerns about whether the Assistance Board's funding decisions prioritized financial assistance to projects in accordance with statutory directives.

- **The Assistance Board funded projects that were classified as low importance while denying projects classified as high importance.** At the direction of the Assistance Board, the Department created criteria to review all applications and assign a ranking of low, medium, or high

importance. According to the criteria, applications that address problems that have a high risk of injury or property loss should be rated as “high importance.” Of the 30 lease purchase and cash projects recommended for funding in the Fiscal Year 2014 grant cycle, 2 were rated as “high importance,” 17 were rated as “medium importance,” and 11 were rated as “low importance.” The Assistance Board chose to award almost \$27 million to the 11 projects rated as “low importance” and denied funding for three grant applications rated as “high importance.” The Department reports that the importance rankings are a guide for the Assistance Board, but these rankings are not the sole factor that Assistance Board members rely on in evaluating grant applications. However, because the Assistance Board does not formally score each application, we could not determine how any of the factors the Assistance Board reportedly uses are weighted in the process of deciding whether to award or deny funding for a given application.

- **The Assistance Board awarded cash grants for projects that did not address a priority one or two deficiency.** During the Fiscal Year 2014 grant cycle, the Assistance Board awarded 24 cash grants totaling \$15.7 million. Of these, 18 cash grants totaling \$10.4 million were awarded for projects that did not address a priority one or two deficiency (as listed in the database as of March 2013). Specifically, for 12 (67 percent) of the 18 grants, the district had *no* priority one or two deficiencies listed in the Priority Assessment, indicating that the schools in that district did not have any systems that needed to be replaced immediately, or within 1 year. For the remaining six awards, the district had priority one and two deficiencies listed in the Priority Assessment that were not addressed by the grant award, indicating that the grant fixed a facility system deficiency that is lower-priority than other deficiencies identified in the Priority Assessment for that district. For example, one district had 32 deficiencies classified as priority one or two, including cracking in walls that could indicate structural problems, fire alarm systems that were not up to code, and fire sprinkler systems that were missing. The grant application submitted by the district did not address any of these 32 high-priority deficiencies, but the Assistance Board awarded the district funds to repair a boiler system that was not identified as a priority one or two deficiency in the Priority Assessment database. Although the school districts have control over which deficiencies they wish to request grant funding to correct, the Assistance Board has the authority to prioritize funding to address the most critical deficiencies with the limited funds available.
- **The Assistance Board funded projects with low FCI scores while denying funding for projects with high FCI scores.** The Assistance



Board awarded districts \$404 million to replace 31 schools with FCI scores of less than 50 percent during the Fiscal Year 2009 through 2014 grant cycles. Of the 31 schools that were awarded grants, nine were not funded, typically because the districts were unable to reach their matching fund goals and did not receive their grants, resulting in a total of \$295 million in grant awards actually being provided to 22 schools with FCI scores of less than 50 percent. An FCI score of 50 percent is well below the 70 percent threshold Parsons identified for replacing a school. Of the 22 schools, four had FCI scores of less than 30 percent and 18 had FCI scores between 30 and 50 percent. During these same grant cycles, the Assistance Board denied funding to five school districts that applied for \$90 million to replace schools with FCI scores greater than 70 percent. We recognize that FCI is only a rough estimate of critical need, and the Department indicated that the schools with low FCI scores had important and urgent needs. However, because the Assistance Board did not document its decision making processes, it cannot demonstrate that the schools selected had more critical needs or why one grant was prioritized over another for allocating the limited funding available.

We also noted specific examples of grant decisions made by the Assistance Board for which using an evaluation tool that documented the reasons for the decisions would have helped prevent the appearance of inconsistency. In one example, the Assistance Board denied a \$5.5 million grant application where the Assistance Board Chair told the applicant that it was against the Assistance Board's policy to fund grant applications requesting larger schools based on predicted student population increases. However, during the same grant cycle, the Assistance Board awarded a \$21.9 million grant to a school district asking for a new school to replace two existing schools. However, the Assistance Board meeting minutes reflect that the Assistance Board chair praised this school district for planning for future growth in their proposed solution. There was nothing in the documentation provided to the Assistance Board or in the Assistance Board meeting minutes to demonstrate why the Assistance Board chose to fund one school for growth and not fund the other school for future growth. In the second example, the Assistance Board held \$13 million in awarded funds for more than 21 months after the award and changed the type of grant awarded from a lease purchase to a cash grant, to allow more time for the school district to secure land needed for the project. In the subsequent year, the Assistance Board rescinded a \$12.8 million grant to a school district that also needed more time to secure land for the grant project. The Department reports that in all of these cases there were other circumstances taken into account by the Assistance Board in making its decisions. However, the circumstances were not adequately captured in the documentation that is made available to the Assistance Board or in the Assistance Board meeting minutes.

## **Why did the problem occur?**

The Assistance Board does not have a uniform, documented tool or guidelines for evaluating grant applications that incorporate the statutory requirements and priorities for awarding grants and that documents that applications have been evaluated in a consistent manner. Overall, the Assistance Board cannot demonstrate the specific rationale, either by individual member or for the Assistance Board as a whole, for its prioritization of each application for funding. Further, the Assistance Board cannot demonstrate that it is complying with statute because it cannot show that factors from the Priority Assessment and facility construction guidelines are used or how those factors are weighted in the grant decision making process and cannot demonstrate that projects are prioritized and limited funds are used to address the most critical needs first.

Assistance Board members indicated that they use statutory criteria when evaluating the grants, but the members do not use an evaluation form to assess grant applications. However, the Assistance Board has not identified the information in the Priority Assessment (e.g., FCI or priority score) or the facility capital construction guidelines (such as facility components that are necessary to ensure the health and safety of a facility) that will be used to guide its evaluation and prioritize grant requests. When we surveyed the Assistance Board members, the five that responded reported using somewhat different criteria when evaluating applications. Specifically, of the five Assistance Board members who responded to our survey question about the most important criterion for making grant award decisions, two reported it is the FCI score, one reported it is the importance of the project as assessed by Department staff, one reported it is the Colorado Facility Index (an indicator in the Priority Assessment of a facility's condition and programmatic needs), and one reported it is the summary information provided by Department staff, such as whether the project addresses the deficiencies in the Priority Assessment or any red flags identified by staff for the project. From these responses, it seems clear that Assistance Board members are not using consistent criteria in evaluating and prioritizing grant applications and that the Assistance Board has not agreed on how to use the information in the Priority Assessment in the evaluation process.

During the Fiscal Year 2012 grant cycle, with the approval of the Assistance Board, the Department used a grant application scoring tool to score and prioritize applications based on statutory criteria. The Department then provided the Assistance Board with a prioritized list of projects based on the scoring; the Assistance Board reviewed the list and chose to fund some projects that were not the top priorities based on the Department's scoring process and to deny funding to applications that had received higher scores. The Assistance Board did not document either the criteria it used to review the prioritized list or its reasoning for awarding grants to lower priority projects. According to Department staff,

districts complained that this process potentially reduced the chances of the Assistance Board funding projects that the Department staff had scored as lower priority. Applicants also complained that the Assistance Board chose to fund lower-priority projects in lieu of high-priority projects. Because of these complaints, the Assistance Board decided not to use a documented evaluation process in the Fiscal Year 2013 or 2014 grant cycles.

At the March 2013 Assistance Board meeting, Department staff recommended a proposed scoring rubric for the upcoming grant cycle to assist the Assistance Board in its application review. Assistance Board members stated they did not want to use a scoring rubric because each member uses his or her unique expertise and the review process is enhanced by the collaboration of the different types of expertise represented on the Assistance Board.

We found examples of other competitive grant programs in Colorado that have expert boards or committees that evaluate applications and make funding recommendations or decisions with a standardized tool to guide and document the evaluations. These programs have made the process of awarding funds consistent and transparent through a clearly documented evaluation process. One of these examples is the Colorado HIV and AIDS Prevention Grant Program which is overseen by a board of experts in the area of providing care for individuals with HIV and AIDS. This board, in its evaluation of grant applications, uses a standardized tool that scores applications based on several factors. A second example is the Department of Local Affairs' Energy and Mineral Impact Assistance Program, which is overseen by an advisory committee, including representatives from areas impacted by energy conversion and mineral resource development. The advisory committee evaluates and scores energy and mineral grant applications with a standard set of criteria and a weighted scoring sheet. In both examples, allowing each board or committee member to score applications individually enables board members to use discretion in awarding higher scores in areas that they view as important based on their individual expertise while maintaining a standardized, documented process for selecting successful applications. If the Assistance Board's application evaluation and scoring processes were more formalized, the Department could improve the consistency of its application review process, better demonstrate compliance with statutory directives for prioritizing grant applications for funding, and also inform applicants about the criteria against which their applications will be scored, leading to higher-quality applications and a more transparent process.

### **Why does the problem matter?**

It is important for the Assistance Board to have a consistent, documented process for evaluating grant applications for several reasons. First, the Assistance Board's

policies and procedures could provide more guidance to individual Board members on the criteria for evaluating grant applications and better demonstrate that Board members are adhering to the statutory intent and direction for the Program by using a standardized evaluation tool. As noted above, we could not determine the extent to which the Assistance Board's decisions to award or deny funding were consistent with the statutory intent expressed in Section 22-43.7-102(1), C.R.S., where the General Assembly, in establishing this program, declared that Colorado school districts have differing financial abilities to meet needs for new public schools, renovations, and maintenance, so that unsafe, deteriorating, or overcrowded facilities do not impair students' abilities to learn. The statute also states that establishing a program to provide financial assistance to school districts throughout the state that have difficulty financing new capital construction projects and renovating and maintaining existing facilities will help such districts to meet students' fundamental educational needs. Additionally, we could not determine whether the Assistance Board was applying the priorities established in statute. Statutes address the importance of prioritizing projects to ensure that the limited funding available to provide financial assistance to schools be used to address those schools with critical needs and the least financial ability to address their needs. Each dollar spent on one project is a dollar that is not available to help another school to provide a safe, healthy, uncrowded environment for the students, teachers, and members of the public who use those facilities.

Second, the Assistance Board could improve the amount of detail it provides to the State Board and better demonstrate the methodology it used to identify the projects recommended for funding if it used a documented evaluation process. According to statute [Section 22-43.7-109(7), C.R.S.], if the State Board concludes that the Assistance Board misinterpreted the results of the Priority Assessment or misapplied the statutory priority criteria (e.g., it did not recommend funding health and safety projects before overcrowding projects), the State Board can vote to disapprove the Assistance Board's funding recommendations. However, the Assistance Board does not have any detailed documentation to provide the State Board that demonstrates how the statutory priorities were applied or information from the Priority Assessment was used to determine which grant applications were recommended for funding. Therefore, the State Board does not have the information it needs to evaluate the extent to which the Assistance Board has applied the prioritization criteria and Priority Assessment data properly. The State Board has never overturned any of the Assistance Board's grant recommendations.

Third, the Assistance Board could improve school districts' understanding of the basis for the grant decisions by using a documented evaluation tool. We found that some grant applicants do not understand what criteria are used to evaluate and prioritize grant applications. The Assistance Board, with the support of the

Department, conducted surveys of grant applicants after each of the Fiscal Year 2012 and 2013 grant cycles. In both surveys, some applicants included comments stating that they were unclear what specific criteria the Assistance Board used to score or evaluate their applications and that they had concerns about how grants were prioritized for funding. Because of the way the Department tabulated the survey data, we could not determine how many unique individuals made these comments. However, using a documented scoring tool for evaluating grants would enable the Assistance Board to provide additional transparency in the evaluation and selection process.

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## **Recommendation No. 2:**

The Public School Capital Construction Assistance Board (the Assistance Board) should improve its grant decision making processes to ensure that the process is transparent and adheres to statutory direction by:

- a. Developing a standardized evaluation tool to evaluate grant applications that includes criteria based on the statewide financial assistance priority assessment (Priority Assessment) data and statutory priorities and requirements. Additionally, the scoring criteria should evaluate the adequacy of the proposed solution to address the school's needs and the district's financial capacity to address problems outside of a grant program.
- b. Communicating to potential applicants in the solicitation for grant applications the evaluation and review criteria developed in part "a" above.
- c. Retaining documentation of all completed scoring documents for each grant application.
- d. Providing documentation demonstrating the methodology it used to select the projects for funding to the State Board of Education.

## **Public School Capital Construction Assistance Board Response:**

- a. Agree. Implementation date: December 2013.

The Assistance Board will develop a standardized evaluation tool to evaluate grant applications that includes criteria based on the Priority

Assessment data, statutory priorities and requirements, factors that evaluate the adequacy of the district's proposed solution, the district's financial capacity to address the problems identified, and any other relevant factors. The Assistance Board will document the application evaluation and prioritization processes.

- b. Agree. Implementation date: December 2013.

The Assistance Board will provide the standardized evaluation and prioritization criteria, developed as a result of implementing part "a" above, to grant applicants during the grant solicitation process.

- c. Agree. Implementation date: May 2014.

The Assistance Board will incorporate the use of a more comprehensive evaluation tool and will retain the documentation produced during the evaluation and prioritization process.

- d. Agree. Implementation date: June 2014.

The Assistance Board will provide documentation of the methodology used to select projects for funding to the State Board of Education.

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## Determining Financial Capacity

Statute [Section 22-43.7-109(11), C.R.S.] requires the Assistance Board to consider the financial capacity (the ability to finance a capital construction project) of an applicant when making decisions about the amount of grant funds to award, the amount of any matching funds to require from the applicant, and whether to reduce or waive the matching fund requirements. Statute [Section 22-43.7-109(9), C.R.S.] also authorizes the Assistance Board to (1) determine the amount of matching funds a school district must provide for a grant project based on specified factors related to the district's financial capacity, and (2) reduce or waive the matching fund requirement. Since the Program's inception, the Assistance Board has completed six grant cycles, one in each of Fiscal Years 2009 through 2014. The Assistance Board has funded 211 projects, totaling about \$1.1 billion. State funds made up about \$759 million (70 percent) of this total, and the school districts contributed about \$330 million (30 percent) in matching funds. During this time frame, the Assistance Board waived the matching requirement for 37 grants. These 37 waivers totaled about \$52 million.

## What audit work was performed and what was the purpose?

We reviewed the Assistance Board's processes for considering the financial capacity of school districts when evaluating and making recommendations for grant awards, determining district matching fund requirements, and approving matching fund waivers or reductions to determine if the methodology and related policies comply with statute, appear equitable to school districts, and are documented. Specifically, we reviewed:

- The calculation of the matching fund requirements for a judgmentally selected, non-statistically valid sample of 7 of the 178 school districts and 21 of the 122 eligible charter schools in the state. The Assistance Board has delegated the responsibility for calculating the matching fund requirements to the Department.
- The Assistance Board's process for approving or denying matching fund waiver requests in the Fiscal Year 2011 through 2013 grant cycles.
- All 25 waiver requests submitted by school districts with funded applications in the Fiscal Year 2011 through 2013 grant cycles.

## How were results of the audit work measured?

The BEST Act [Section 22-43.7-101, C.R.S., et seq.] established the Program to “provide financial assistance to school districts, boards of cooperative services (BOCES), and charter schools throughout the State *that have difficulty financing* new capital construction projects and renovating and maintaining existing facilities” [emphasis added]. Statute [Section 22-43.7-109(11), C.R.S.] requires the Assistance Board to be as equitable as possible in determining the amount of grant awards by considering the total financial capacity of each applicant. One of the primary mechanisms the Assistance Board uses to account for the varying financial capacity of applicants is the determination of a matching funds requirement.

We evaluated the Assistance Board's policies and procedures for considering the financial capacity of applicants when determining matching fund requirements and approving waivers of the matching funds requirements against the statutory provisions below.

**Calculation of the Matching Fund Requirements.** Statute [Section 22-43.7-109(9), C.R.S.] requires the Assistance Board to determine the amount of matching moneys a school district must provide for a project “after consideration of the applicant's financial capacity as determined by the following factors:”

- The school district's assessed value per pupil relative to the state average.
- The school district's median household income relative to the state average.
- The school district's mill levy relative to the state average.
- The percentage of pupils in the school district who are eligible for free or reduced-cost lunch.
- The effort put forth by the school district to obtain bonded indebtedness in the 10 years prior to submitting a grant application. This factor may only be used to reduce the percentage of matching funds required from a district that has made such an effort.

In addition to the above factors for school districts, statute provides some additional factors that the Assistance Board should consider when determining the financial capacity of a charter school for the purposes of determining matching fund requirements. Specifically, statute requires the Assistance Board to consider whether the authorizer of a charter school has more than 10 percent of its remaining bonding capacity available as well as take into consideration the amount of the charter school's unreserved fund balance.

Statute also prohibits the Assistance Board from imposing a matching requirement that would cause a school district to exceed its remaining bonded indebtedness capacity. Specifically, Section 22-43.7-109(10)(a), C.R.S., states: "A school district shall not be required to provide any amount of matching monies in excess of the difference between the school district's limit of bonded indebtedness...and the total amount of outstanding bonded indebtedness already incurred." School districts are generally limited by statute [Section 22-42-104, C.R.S.] to issuing bonds for no more than 20 percent of the assessed value of the taxable property in the district.

**Approval of Waivers.** Statute allows the Assistance Board to waive or reduce the matching funds requirement if it determines that: (1) a waiver or reduction would significantly enhance educational opportunity and quality in the school district, (2) complying with the matching requirement would significantly limit educational opportunities in the school district, or (3) there are extenuating circumstances deemed significant by the Assistance Board that make a waiver appropriate [Section 22-43.7-109(10)(b), C.R.S.]. Statute also gives the Assistance Board the power and duty to promulgate rules establishing evaluation criteria for requests for waivers of matching fund requirements [Section 22-43.7-106(2)(i)(I)(b), C.R.S.].



When a school district applies for a waiver of its matching fund requirements, the district can apply for a full waiver or a partial waiver. School districts typically request a partial waiver of their matching fund requirements. The Assistance Board also has the discretion to grant as much of a waiver as it deems appropriate. The Assistance Board typically approves the full amount that the school district requested to be waived.

We also looked at the practices that several other states and other Colorado grant programs use to evaluate waivers for grant matching requirements. We found that New Mexico’s public school construction grant program requires documentary support for any hardship that school districts cite in their request for a waiver of required matching funds. We also identified two Colorado programs—the State Historical Fund grant program and the Energy and Mineral Impact Assistance Program—that provide competitive grants to fund capital construction projects. Both programs also allow applicant matching fund requirements to be waived or reduced and require the applicant to provide documentation of the circumstances that justify a waiver. Both programs use a standardized tool to evaluate the waiver request and make a determination about whether to deny or approve the grant and waiver request.

### **What problem did the audit work identify and why did the problem occur?**

Our review of the Department and Assistance Board’s calculation of matching fund requirements and waiver requests identified problems in two areas: (1) matching fund formula, and (2) matching fund waivers.

#### **Matching Fund Formula**

Each year, the Department calculates the required matching funds percentage for every school district by ranking each district from “poorest” (having the least financial capacity) to “wealthiest” (having the greatest financial capacity) in each of four factor areas:

- **Median Household Income:** Districts are ranked from 1 to 178 with the district with the lowest median household income having a ranking of 1.
- **Free and Reduced Lunch:** Districts are ranked from 1 to 178 with the district with the highest percentage of students eligible for free and reduced lunch having a ranking of 1.
- **Per Pupil Assessed Value:** Districts are ranked from 1 to 178 with the district with the lowest per pupil assessed value having a ranking of 1.

- **Mill Levy:** Districts are ranked from 1 to 130 with the district with the highest mill levy rate having a ranking of 1. The district with the highest mill levy is considered to be the “poorest” because a high mill levy signifies that a district has gone to taxpayers many times to obtain funding for schools and taxpayers are paying higher taxes for school expenses than taxpayers in other areas. There are only 130 rankings for the 178 districts because 49 districts do not have any mill levy. Therefore all 49 districts without a mill levy are ranked as the highest possible ranking of 130, and the other 129 districts are ranked from 1 through 129.

The Department then determines an overall rank for each district based on the average of the district’s rank from each of the four factors and uses the average rank of each school district to determine each district’s matching rate. Each factor is given equal weight when determining the overall rank of the districts.

We compared the matching fund requirements for districts based on the Department’s ranking of the districts in each of the four factors areas and found that the Assistance Board’s method for calculating the matching fund requirements comply with statute in that the formula used by the Assistance Board is based on the factors identified in statute and the calculation is applied consistently across all school districts. However, we found the formula used to calculate the percentage of matching funds a school district must provide for a grant project does not appear to generate results that accurately reflect the relative financial capacity of the State’s school districts to provide matching funds. As shown in the table on the next page, we found significant differences in the matching rate requirements among the poorest districts and among the wealthiest districts, indicating that the current matching funds formula does not correlate the overall wealth of a district with the district’s matching requirements.

<b>Comparison of Composite Matching Rates Among the Poorest and Wealthiest Districts Based on Individual Rankings<sup>1</sup> As of Fiscal Year 2013</b>								
	Median Household Income		Percentage of Students Eligible for Free and Reduced Lunch		Per Pupil Assessed Value		Mill Levy	
	Match Percentage		Match Percentage		Match Percentage		Match Percentage	
	Range	Average	Range	Average	Range	Average	Range	Average
<b>18 Poorest Districts<sup>2</sup></b> <i>(Poorest 10%)</i>	4 to 67%	32%	4 to 56%	30%	4 to 47%	26%	4 to 57%	33%
<b>18 Wealthiest Districts</b> <i>(Wealthiest 10%)</i>	53 to 90%	69%	47 to 90%	66%	56 to 90%	70%	21 to 90%	52%

**Source:** Office of the State Auditor’s analysis of the Department’s Division of Public School Capital Construction Assistance’s matching rate calculations.

<sup>1</sup> Match percentages range from 4 to 90 percent across all 178 districts. Match percentages shown above are based on the district’s composite match rate based on the average of all four factor rankings.

<sup>2</sup> For mill levy, the match percentage is for the poorest and wealthiest 7 percent of school districts because rankings for mill levy range from 1 to 130, with 129 of the 178 districts having mill levy rankings ranging from 1 to 129 and the other 49 districts having the same mill levy ranking of 130. Districts ranked as 130 have no mill levy, therefore they are all ranked the same.

As shown, the 18 school districts (10 percent) with the lowest median household income have matching rate requirements ranging from 4 to 67 percent. We further analyzed the 18 wealthiest and poorest districts to identify how many have match rates in the 53 to 67 percent range (the range where the match percentage overlaps for the wealthiest and poorest districts). We found that two of the poorest districts have match rates of 66 and 67 percent, respectively, and that nine of the wealthiest districts have match rates between 53 and 67 percent. Similar variances in match requirements are seen in each of the other four factors used in the matching funds formula.

The Department and the Assistance Board reported they recognize that the matching funds formula does not consistently generate results that reflect a school district’s financial capacity. The Department and the Assistance Board believe that some of the statutory factors in the matching funds formula do not necessarily reflect a district’s ability to raise capital and contribute matching funds. For example, the percentage of students that qualify for free and reduced lunch and the median household income reflect the wealth of the individuals living in the

district but do not necessarily indicate the financial resources available to the district. Department staff expressed particular concern about the per pupil assessed value, because a district with a large number of students could have a very low per pupil assessed value while a district with a small number of students may have a high per pupil assessed value, but those values may reflect the number of students more than the wealth of the district. For example, the Vilas RE-5 school district in Baca County and the Littleton 6 school district in Arapahoe County have the same per pupil assessed value of about \$86,000. Vilas RE-5 has a total assessed value of \$5.2 million and 61 students while Littleton 6 has a total assessed value of nearly \$1.3 billion and about 14,700 students. While the Littleton 6 school district has almost 250 times the total assessed value of the Vilas Re-5 district, the current matching funds formula ranks these two districts very similarly based on the per pupil assessed value.

According to the Department and the Assistance Board, a district's ability to provide matching funds is primarily a function of the district's available financial reserves and the district's remaining bonded indebtedness. Bonded indebtedness limits are determined by the districts' total assessed value, and districts are allowed to issue bonds up to 20 percent of their assessed value. Remaining bonded indebtedness is the proportion of a district's total limit that has not been used. According to Department staff, the amount of available bonded indebtedness serves as an indicator of both the school district's overall wealth and its ability to incur debt to pay for school improvements.

The Department and the Assistance Board believe a change in statute is needed to include bonded indebtedness as one of the factors used in determining matching fund requirements for school districts and to exclude the per pupil assessed value. Due to similar concerns with the matching fund requirements for charter schools, the Department and the Assistance Board successfully sought statutory change during the 2012 Legislative Session, which allowed the Department and Assistance Board to consider the amount of remaining bonded indebtedness available to charter schools when determining charter school matching fund requirements. To date, the Department and the Assistance Board have not sought changes to the statutes that address the matching rate for school districts, to either eliminate the factors they believe are not suitable or add factors they believe are more representative of financial capacity.

The table below highlights several comparisons of school districts for which the formula generates similar matching funds requirements (within 10 percentage points), but the amount of capital available to the district to pay for matching funds (as measured by remaining bonded indebtedness) is very dissimilar. Not all of the school districts listed in the table below have applied for grants through the Program.

<b>Financial Capacity and Matching Funds Requirements Comparison Sorted from Smallest Match Rate to Largest for Select Schools Districts for Fiscal Year 2013 Grants</b>		
<b>School District</b>	<b>Required Match Percentage</b>	<b>District's Remaining Bonded Indebtedness Capacity<sup>1</sup></b>
Adams 14	14%	\$24,528,710
Holly RE-3	15%	3,520,200
Greeley 6	27%	95,279,810
Cheraw 31	28%	863,390
Pritchett RE-3	44%	2,010,720
Denver 1	44%	1,136,720,800
Jefferson R-1	55%	772,149,110
Lone Star 101	59%	1,039,540
Creede 1	73%	6,683,330
Boulder RE 2	73%	549,374,880
Hinsdale RE 1	85%	9,742,450
Aspen 1	90%	\$387,878,020

**Source:** Office of the State Auditor's analysis of the Department's Division of Public School Capital Construction Assistance's matching fund calculations.  
<sup>1</sup> As of November 2012.

The table below provides an example of the effect of the current matching funds formula on two school districts that received grants in Fiscal Year 2013.

<b>Comparison of Matching Fund Requirements for Two Projects Funded During the Fiscal Year 2013 Grant Cycle</b>					
<b>District</b>	<b>Amount of Grant Award</b>	<b>Remaining Bonded Indebtedness Capacity</b>	<b>Required Match Percentage</b>	<b>Total Matching Funds Required</b>	<b>Percentage of Remaining Bonded Indebtedness Used for Match</b>
Denver 1	\$6.8 Million	\$1.1 Billion	44%	\$3 Million	0.27%
Dolores RE 4A	\$6.1 Million	\$10 Million	57%	\$3.5 Million	35%

**Source:** Office of the State Auditor's Analysis of Fiscal Year 2013 Grant Cycle Information.

As shown, for the Dolores RE 4A school district to obtain a \$6.1 million grant, the district had to use 35 percent of its remaining bonded indebtedness capacity to provide matching funds, whereas Denver 1 only had to use 0.27 percent of its

remaining financial capacity to obtain slightly more funding. Therefore, the formula does not generate results that accurately reflect school districts' relative financial capacity to provide matching funds.

## Matching Fund Waivers

We identified problems with matching funds waivers in two areas.

- **Evaluating Matching Fund Waivers.** The Assistance Board has not established a formal tool to evaluate waiver requests to determine whether they should be approved. Instead, during the grant decision making meetings, the Assistance Board members review the waiver requests individually and then vote on whether to grant each request. The Assistance Board's approval and denial of matching fund waivers does not appear to consistently generate results that accurately reflect the relative financial capacity of the State's school districts. Of the 25 waivers submitted for projects awarded funding during the Fiscal Year 2011 through 2013 grant cycles, only 13 were for projects funded at school districts, and the remaining 12 were for charter schools or BOCES, which do not have independent bonding authority. Therefore, we could not analyze their remaining bonded indebtedness. We analyzed data on the 13 school district waiver requests submitted to the Assistance Board for approved projects in the Fiscal Year 2011 through 2013 grant cycles and found that the Assistance Board approved one waiver request for a school district that has a high amount of available bonded indebtedness and denied 11 waiver requests for school districts with lower available amounts of bonded indebtedness. For example, we found that the Assistance Board waived about \$159,300 in matching fund requirements for a school district with \$75.1 million in remaining bonded indebtedness capacity and a match rate of 41 percent, while denying a request for waiver of \$79,400 from a school district that had only \$2.7 million in remaining bonding capacity and a match rate of 66 percent. The final waiver request was approved for a school with a low amount of available bonded indebtedness.

Because the Assistance Board does not use an evaluation tool or otherwise document its reasoning for approving or denying waiver requests, we could not evaluate whether the decisions appeared consistent with the statutory provisions, including that: (1) the waiver or reduction would significantly enhance educational opportunity and quality in the school district, (2) complying with the matching requirement would significantly limit educational opportunities in the school district, or (3) there are extenuating circumstances deemed significant by the Assistance Board

that make a waiver appropriate. At the March 2013 Assistance Board meeting we attended, Department staff asked the Assistance Board to consider standardizing and documenting its decisions on waiver requests. Some Assistance Board members stated that they use their own criteria in reviewing waiver applications and do not feel a standardized scoring tool is necessary. The Assistance Board voted to continue evaluating and approving waiver requests in the same way it has in the past.

- **Support for waiver requests.** Program rules [Section 4.2, 1 CCR 303-3] require districts requesting a waiver to submit a detailed explanation of the basis for the request and the amount of the waiver requested. However, program rules do not require school districts to provide documentation supporting the basis for their waiver requests. The Department reports that it does not ask school districts to submit any financial information with their waiver requests because the Department already collects some information, such as district financial statements and how often school districts have attempted and been successful at issuing bonds to raise capital for school projects. However, financial statements do not necessarily provide all information needed to support the need for a waiver, and the financial documentation collected is not provided to the Assistance Board for consideration while assessing waiver requests. For example, school districts stated that a waiver was needed to avoid budget cuts or because the district has had to deplete its reserves. We reviewed the 25 waiver requests submitted for projects that were awarded funds during the Fiscal Year 2011 through 2013 grant cycles and found they included the reasons for requesting a waiver, such as budget cuts, a perception that local voters would be unwilling to support a bond measure, or extenuating circumstances that have depleted the school district's reserves. However, the requests were not accompanied by any documentation as evidence to support their statements, such as minutes that indicate what categories would need to be cut from a district's budget as discussed and approved at a school board meeting or evidence that the district had researched the likely success of a bond issue or had tried a bond issue and failed.

### **Why does the problem matter?**

When the calculation of the matching funds requirements and decisions on waivers do not accurately reflect the financial capacity of the school district, there is a risk that the Program is not fulfilling its intent of addressing the critical needs in districts that do not have the financial capacity to meet those needs. Specifically:

- **High-priority school improvement projects may not be funded.** School districts that have a high matching fund requirement relative to their ability to provide matching funds (e.g., their available financial reserves and remaining bonded indebtedness) may not be able to provide the match and consequently, may not apply for funding. Lack of funding may, in turn, result in poor school conditions persisting or increasing, particularly in districts with limited capacity to fund their own projects. We identified three school districts with schools that had FCI scores of 70 percent or greater (indicating that the schools have significant capital construction needs) that reported they had not applied for funding due to their high matching fund requirements.
- **State funds may not be effectively leveraged.** The State portion of a grant project may be larger than necessary if a school district has access to sufficient financial capital and can afford to pay a higher match than the matching fund formula requires. Districts a match percentage that is too low would result in the Program having less funding available to support other projects than if the match percentage accurately reflected the district's financial capacity. Matching funds are not only a way to ensure local "buy-in" and ownership of funded projects, but also the primary way the Assistance Board can leverage State funds to maximize the number of school improvement projects funded.
- **Lack of documentation may impede the Assistance Board's ability to defend its decisions, if challenged.** The current methods used to calculate the matching funds percentage and approve waiver requests appear to result in inequitable requirements in some cases. As a result, school districts may believe that the Program is unfair and, at a minimum, may complain to the State Board and seek to have the Assistance Board's decisions overturned. In an extreme case, a district may choose to seek reparations through the courts for inequitable treatment. If complaints or legal actions occur, the lack of documentation of how waivers are evaluated may hamper the Assistance Board's ability to show that it conforms to statutory guidance, and does so in a consistent manner, in approving waivers.

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### **Recommendation No. 3:**

The Public School Capital Construction Assistance Board (the Assistance Board) should take steps to better ensure that matching fund requirements reflect the financial capacity of the district and to ensure equity in the process by:



- a. Evaluating whether statutory change is necessary to allow the Assistance Board to use the remaining bonded indebtedness capacity as a factor in determining the match percentage required from each district and whether adjustments are needed to the other statutory factors that should be considered when calculating the matching funds requirements.
- b. Developing a methodology to determine the matching funds required for each school district that correlates them with school districts' financial capacity to provide matching funds.
- c. Implementing a mechanism for the Assistance Board to obtain documentation that supports each waiver request. This should include the Department of Education's Division of Public School Capital Construction Assistance (the Department) providing information it maintains that is relevant to each waiver request to the Assistance Board and the Assistance Board requiring school districts to submit any additional information needed as part of their waiver requests.
- d. Developing and implementing an evaluation tool to guide the evaluation of each matching fund waiver request and to document the reasons for approval or denial of each request. As part of this process, the Assistance Board should review supporting documentation provided by the Department and districts to ensure that the need for a waiver is adequately documented.

### **Public School Capital Construction Assistance Board Response:**

- a. Agree. Implementation date: May 2014.

The Assistance Board believes it is advisable to incorporate bonded indebtedness limits as a factor into the statutory matching funds formula to better assess the financial capacity of applicants. The Assistance Board will also evaluate the appropriateness of other statutory factors and work with the General Assembly to make statutory changes.

- b. Agree. Implementation date: May 2014.

The Assistance Board will recommend appropriate statutory changes to the factors and/or weighting of those factors in order to ensure the match accurately reflects school district financial capacity.

- c. Agree. Implementation date: December 2013.

The Assistance Board will identify the types of documentation that will be required for waiver requests and will consider the documentation collected by the Department and received from the school districts when evaluating waiver requests.

- d. Agree. Implementation date: December 2013.

The Assistance Board will develop a formal evaluation tool for matching fund waiver requests and will review supporting documentation provided by the Department and the school districts in the evaluation of matching fund waiver requests.

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## Preventing Conflicts of Interest

The Assistance Board is a Type 1 board as defined in Article 1, Title 24 of Colorado Revised Statutes, and consists of nine members, appointed to use their expertise in school administration, facility planning and management, school finance, architecture, and construction to administer the Program. The Assistance Board includes one public school board member, one public school superintendent, two school facilities planners or managers, one architect, one engineer, one construction manager, one school technology expert, and one public school finance expert. The State Board is responsible for appointing three members representing different areas of the state (rural, urban, and suburban), the Governor is responsible for appointing three members, and the General Assembly is responsible for appointing three members. Assistance Board members serve 2-year terms, with a maximum of three consecutive terms, and they may not hold a state elective office.

Assistance Board members are often active professionals in their fields of expertise. If not properly handled, outside employment, as well as other activities of Assistance Board members, may create conflicts of interest with the members carrying out their duties on the Assistance Board. Because Assistance Board members are required by statute [Section 22-43.7-106, C.R.S.] to have expertise in areas related to school capital construction, administration, and finance, the Assistance Board should have adequate policies and procedures in place to protect against conflicts of interest and to instruct Assistance Board members on how to proceed should a conflict or potential conflict arise.

## What audit work was performed and what was the purpose?

The purpose of the audit work was to evaluate whether the Assistance Board has implemented adequate policies and procedures to prevent conflicts of interest while carrying out its duties. To do this, we reviewed the following:

- The conflict of interest rules developed by the Assistance Board.
- Memoranda the Assistance Board obtained from the Attorney General's Office in both August 2008 and May 2013 regarding conflicts of interest.
- The Assistance Board meeting minutes for January through December 2012, July, August, and October 2009, and June 2010. The Assistance Board did not meet in September 2009.

We also interviewed Assistance Board members and attended Assistance Board meetings.

## How were results of the audit work measured?

We evaluated the Assistance Board's rules and practices related to conflicts of interest against the following directives and guidance.

**The Colorado Code of Ethics.** Established in statute [Section 24-18-108.5(2), C.R.S.], the Colorado Code of Ethics provides that: "a member of a board, commission, council, or committee ... shall not perform an official act which may have a direct economic benefit on a business or other undertaking in which such member has a direct or substantial financial interest." The statute defines a "financial interest" as ownership, employment or prospective employment, debtor interest, or a directorship or officership in a business and an "official act" as including any vote, recommendation, approval, or other action that involves the use of discretionary authority. The statute also states that members of boards or commissions cannot perform official acts for private benefit without breaching their fiduciary responsibility to the State and the public trust. Thus, if an Assistance Board member violates this law, he or she has breached a fiduciary duty to the State.

**Memoranda from the Attorney General's Office.** The Department provided us with two memoranda from the Attorney General's Office to the Assistance Board regarding conflicts of interest. However, the memoranda are subject to attorney-client privilege and the Assistance Board did not agree to waive the privilege. Section 7.39 of Government Auditing Standards states that, "If certain pertinent information is prohibited from public disclosure or is excluded from a report due

to the confidential or sensitive nature of the information, auditors should disclose in the report that certain information has been omitted and the reason or other circumstances that make the omission necessary.” As a result, although pertinent to this audit, information contained in the two memoranda from the Attorney General’s Office to the Assistance Board has been omitted from this report.

### **What problem did the audit work identify and why did it occur?**

The Assistance Board rules do not provide maximum protection against members participating in situations that present either a real or perceived conflict of interest. During the audit, we were informed of an instance in which two construction firms that employed Assistance Board members unsuccessfully bid on a design-and-build construction contract for a project that later was awarded a grant by the Assistance Board. Both members voted on the project after losing a bid to perform work on the project. One member’s term expired in June 2012 and the other’s term expired in July 2013, so neither member involved in this incident is still on the Assistance Board. The table on the next page describes the time line of events for this situation.

<b>Time Line of Events For Conflict of Interest Involving Assistance Board Members</b>	
<b>Spring 2009</b>	A school district applied for a lease-purchase grant from the Program to fund a project. Before the application was reviewed by the Assistance Board, the school district held a meeting to select a construction and design firm. At this meeting, two Assistance Board members' firms bid to provide services. The school district selected a contractor but did not select the bid submitted by either of the Assistance Board member's firms.
<b>July 2009</b>	The Assistance Board held its meeting to select grantees. The minutes of that meeting show that the two Assistance Board members who bid on the project did not recuse themselves from the vote. The minutes do not indicate whether each member voted for or against funding for the project. Both Assistance Board members also participated in discussion about the grant and spoke negatively about the project. At the time they voted, the rules expressly prohibited members from voting on a project if they had "consulted with an applicant and [were] interested in bidding on the applicant's project". In addition, the grant recipient reported to the Department that it had felt pressured by the Assistance Board members to award the bid to the Assistance Board members' firms. In August 2009, the Assistance Board modified its conflict of interest rules to prohibit Board members from presenting "their position on the Board to school districts....as an advantage for using their firm over their firms' competition." The rules were also changed in November 2009 to state that "No Board members shall participate in the Board's evaluation process, including voting, for any application when the Board member's firm has had prior contact with the applicant regarding the project or application." The Assistance Board did not take any formal action against either member involved in this incident. The project was awarded a grant for \$51.3 million.
<b>November 2009</b>	The school district did not pass its bond issue. Therefore, the school district did not have the required matching money available to accept the grant and was unable to go forward with the project. The grant award was rescinded.
<b>Spring 2010</b>	The school district reapplied for a grant from the Program on the same project as in 2009.
<b>June 2010</b>	The Assistance Board voted on the new application. There is no indication in the Assistance Board minutes that the two Assistance Board members spoke about the project; however, the two members whose firms had unsuccessfully bid on the project in 2009 did not recuse themselves from voting. At the time they voted, the conflict of interest rules expressly prohibited members from voting on a grant application for a project for which they had previously had contact with the applicant. The Assistance Board did not take any formal action against either member. The Assistance Board awarded a grant for \$56.3 million.
<b>Source:</b> Office of the State Auditor's analysis of information provided in interviews and in Assistance Board meeting minutes.	

In the most recent meeting minutes we reviewed (January through December 2012), there were instances in which members did recuse themselves when they had involvement with an applicant or project. However, we were unable to determine whether members recuse themselves in all cases or if there were instances in which Assistance Board members either voted on projects that their firms subsequently bid on, or bid on projects that they subsequently voted on. The Assistance Board does not adequately document member conflict of interest disclosures or otherwise keep records of members who perform work on projects funded with grant funding. For example, the Assistance Board does not formally document conflicts of interest disclosed by Assistance Board members (e.g., members do not complete forms disclosing conflicts and there is no list of conflicts available for reference during grant decision making meetings to remind members to recuse themselves). Further, the Assistance Board does not track which members vote on which projects.

The Assistance Board is designed by statute to include members with significant experience in the fields of school capital construction and education. However, individuals actively participating in school construction or involved in public school administration have potential conflicts of interest. Further, the Assistance Board's rules originally closely aligned with statute to avoid conflicts of interest and ensure compliance with the Colorado Code of Ethics. However, the Assistance Board has weakened the rules over time and moved away from the more specific restrictions on member involvement in projects the Program funds, resulting in rules that are more general and therefore potentially more difficult to enforce. The table on the next page describes key elements of the rules related to Assistance Board members who work for or own firms that may have an interest in working on Program projects, how the rules changed over time, and the extent to which the rules align with applicable provisions of the Colorado Code of Ethics [Section 24-18-108.5, C.R.S.]

Public School Capital Construction Assistance Board Evaluation of Assistance Board Rules on Conflict of Interest			
Period Rule Applied	Rules on Members Evaluating and Voting On Projects	Rules on Member Participation on Projects the Member Voted On	Rule Aligns with Section 24-18-108.5
11/19/2008 to 8/19/2009	Assistance Board members shall not: - Participate in evaluating and voting on projects for any application that may be of interest to the member's firm. - Evaluate or vote on any project for which the member's firm consulted with the applicant.	Assistance Board members shall not: - Play any role in their firm's bid on the project. - Work on the project. - Participate in meetings or discussions about the project. - Review or approve documents connected with the firm's efforts to obtain the project award.	<b>Yes.</b> Statute states that board members should not vote on a project that <b>may</b> provide a financial benefit to the member. These rules expressly prohibited Assistance Board members from voting on projects in which they may have an interest and restricted a member's activities if the member's firm was performing work on the project.
8/19/09 to 11/13/2009	No changes.	All the restrictions on members' activities on projects, cited above, remained in place.  Added a prohibition on members presenting their position on the Assistance Board to districts as an advantage to select their firm over others.	<b>Yes.</b> These rules contained the same language as the prior version, which reflected the statutory restrictions and additional restrictions on Assistance Board members' activities.
11/13/09 to 11/12/2012	Eliminated the rule that Assistance Board members shall not evaluate or vote on any application that may be of interest to the member's firm.  Changed the rule on consulting to state that no members shall participate in the evaluation process, including voting, when the member's firm has had <b>prior contact</b> with the applicant regarding the project or application.	Eliminated all the specific prohibitions on Assistance Board members participating in their firm's bid on a project or work on a project. Added language specifically allowing members or their firms to respond to a competitive request for proposal or request for qualification, or to work on a project.  Added general language that members should exercise caution to avoid conflicts of interest or appearances of impropriety and inform the Assistance Board and Department of questionable situations.	<b>No.</b> These rules no longer contain language that reflects the statutory mandate that board members not vote on a project that <b>may</b> provide a financial benefit to them. Further, these rules no longer restrict Assistance Board members' activities on projects they voted on and specifically allow members to bid on projects they did vote on.
As of 11/12/2012	No changes.	Only change is the addition of language specifying that Assistance Board members may recuse themselves from any vote.	<b>No.</b> See concerns with rules enacted on 11/13/2009, described above.
<b>Source:</b> Office of the State Auditor's analysis of the Assistance Board's conflict of interest rules and how those rules have changed since the inception of the Program.			

During the 2012 Legislative Session, the General Assembly considered Senate Bill 12-179, which would have prohibited individuals from serving on the Assistance Board if they have a personal or corporate financial interest in a project that is being applied for or in a project that was funded through the Program. The Department reported to us that the Senate Education Committee looked at the Program rules and determined that they were adequate and that legislation was not necessary. Although members of the Assistance Board who testified in front of the Senate Education Committee provided the Committee with the Assistance Board's conflict of interest policies, the recording of the Senate Education Committee hearing does not indicate that the Committee comprehensively evaluated the adequacy of the policies or whether they aligned with the Colorado Code of Ethics.

Our concern is that the Assistance Board's rules have not provided adequate protection against conflicts of interest. As demonstrated in the above examples, the policies no longer align with the Colorado Code of Ethics; and Assistance Board rules do not contain any instructions as to how the Assistance Board should handle conflicts of interest that come to their attention. For example, the rules do not specify what action the Assistance Board or Department should take when an allegation of a conflict of interest is made or when a conflict of interest is observed. Additionally, the rules do not contain a description of what types of action, such as removal from the Assistance Board or disclosing the conflict to the member's appointing authority can be taken if a member violates the Assistance Board's conflict of interest rules.

### **Why does this problem matter?**

The Assistance Board is a Type 1 State Board that has fiduciary responsibilities for the operation of the Program. The Assistance Board is therefore responsible for acting in the best interests of the State and ensuring that the State's money is spent prudently and equitably. At the same time, the Assistance Board members are expected to have expertise in the area of public school construction and school operations. Allowing Assistance Board members to bid on design and construction contracts for projects funded with Program funds creates at least an appearance of conflict of interest and may lead to districts believing that the grant award process is unfair and inequitable.

Without adopting conflict of interest rules that (1) align with the Colorado Code of Ethics, (2) are sufficient to ensure that Assistance Board members do not financially benefit from grants they voted to approve, and (3) do not pressure districts to award projects to firms associated with an Assistance Board member, there is a risk that individual Assistance Board members could have undue influence in the grant-making process and use that influence to obtain financial gain for themselves or their employers.



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### **Recommendation No. 4:**

The Public School Capital Construction Assistance Board (the Assistance Board) should maximize the safeguards in place to prevent the appearance of, or actual conflicts of interest by:

- a. Implementing rules that align with the Colorado Code of Ethics to ensure that members do not evaluate or vote on projects in which they may have a financial interest. To maximize the safeguards against such conflicts, the Board should revise its rules to prohibit members from playing any active role in a grant-funded project that the member voted on or evaluated.
- b. Establishing in rules a clear process for handling conflicts of interest when they arise, including enforcement measures that can be used should members not comply with conflict of interest policies.
- c. Documenting Assistance Board member disclosures of conflicts of interest, including the date of the disclosure, the Assistance Board member involved, and the nature of the conflict. Documentation should be retained and made available at all Assistance Board meetings in which evaluation of applications or voting occurs to ensure that Assistance Board members comply with rules to recuse themselves from voting on a project if they have prior involvement with the applicant or project.

### **Public School Capital Construction Assistance Board Response:**

- a. Agree. Implementation date: May 2014.

The Assistance Board takes conflict of interest issues very seriously and will re-evaluate the conflict of interest rules, in consultation with the Office of the Attorney General to identify the changes that may be necessary to ensure alignment with the Colorado Code of Ethics and maximize safeguards to prevent perceived or actual conflicts of interest. The Assistance Board will make adjustments to the rules as appropriate. Given that the rule-making process takes approximately four months, the updated rules will be in effect about the same time as the upcoming grant review cycle. If the revised conflict of interest rules are not yet finalized at the time of the of the upcoming grant review cycle, it is the intent of the Assistance Board to follow the revised conflict of interest rules which will be in process.

- b. Agree. Implementation date: May 2014.

The Assistance Board will review and update the existing rules related to conflict of interest disclosure and enforcement and will develop a formalized process for documenting and acting upon potential conflicts of interest.

- c. Agree. Implementation date: February 2014.

The Assistance Board will document and retain conflict of interest disclosures and make those disclosures available at Assistance Board meetings to ensure that Assistance Board members recuse themselves appropriately and do not vote on action items related to projects in which the members have a real or apparent conflict of interest. The Assistance Board will immediately begin documenting and publicizing conflict of interest disclosures on the Capital Construction Assistance website and will subsequently develop a formal disclosure statement.

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# Grant Administration

## Chapter 3

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The Department of Education's Division of Public School Capital Construction Assistance (the Department) or the Public School Capital Construction Assistance Board (the Assistance Board) execute contracts with all grant recipients (school districts) that were awarded financial assistance for the capital construction, renovation or maintenance project described in the district's project application. As of March 2013, there were 77 active lease-purchase and cash grant contracts, totaling more than \$547 million in State grant funds. The contract amounts ranged from \$50,818 to more than \$34 million. The success of each grant project is the shared responsibility of the districts, which execute the day-to-day operations of project administration and will ultimately own the finished product, and the Department, which funds the project, issues the bonds to finance the lease-purchase grants, and, until the bonds expire, must ensure the school buildings used as collateral to back the bonds maintain their value. Currently, the Department has five project consultants, each of whom is assigned to a geographic region, who are responsible for overseeing all grant projects within their assigned regions. For large projects, grant recipients establish a district project manager, which is either one of their own staff or a contracted manager, to manage and oversee each grant project. The district project manager is responsible for facilitating the building, schematic, and construction designs; overseeing the general contractor and subcontractors; ensuring the project is completed on time; monitoring project quality; and developing and administering the master line-item budget for the project.

According to the State of Colorado Procurement Manual, signed contracts do not relieve the State of the ultimate responsibility for the quality of the goods or services provided. Monitoring contractor performance is a key function of proper contract administration. It verifies that contractors are performing in accordance with the terms of the contract, helps agencies identify and address problems in a timely manner, and ensures that quality goods or services are provided timely and within contract budgets. We reviewed the Department's contract administration practices for its contracts with school districts and found that the Department could make improvements in three key areas: (1) monitoring project budgets, (2) monitoring performance, and (3) cash grant contracts.

## Monitoring Project Budgets

Grant applicants submit a detailed estimated budget, which contains line items, as part of their application for grant funds. However, this is a preliminary budget and how the project funds are allocated among the detailed line items and the line-item categories can change significantly once the project design is complete and construction is ready to begin. For each project, the district project manager is responsible for maintaining the master project line-item budget developed as a result of the completed design process and tracking all project expenditures.

The Department is also responsible for reviewing project expenditures to ensure they generally align with the project budget and fall within the scope of the approved project. Each month, grant recipients submit a funding request to the Department that details expenditures, by vendor, and attach invoices that support the requested amount. The Department's administrative staff person reviews funding requests to ensure that the invoices support the total request, that the expenditures are allowable under the terms of the grant award, and that there are sufficient remaining funds in the grant award to cover the expenses. Next, the consultant assigned to each project reviews the funding request to ensure the expenditures are within the project scope, are appropriate for the stage of the project (i.e., carpet should not be purchased while the contractor builds the foundation), and comply with the Department's furniture, fixture, and equipment guidelines. The Department's project consultants stated that they sometimes receive and review copies of the detailed line-item budgets, and they frequently ask grant recipients for more information about the project progress and the budget, but they generally only monitor project expenditures against the total amount of the grant award to ensure that expenditures do not exceed the total.

### **What audit work was performed and what was its purpose?**

Our audit objective was to review the Department's management of grant contracts and, specifically, the Department's controls over grant expenditures. We interviewed project consultants regarding their project monitoring activities related to grant awards, reviewed contract provisions, and reviewed the Department's draft policies and processes for monitoring grant contracts and reviewing and approving payment of funding requests. We reviewed the draft policies and procedures because the Department did not have finalized policies and procedures at the time of the audit.

Because the Department does not typically require grantees to submit a detailed budget that breaks down the grant award into specific cost categories, we expanded our testwork to review detailed budget documentation maintained by the district project manager for a sample of five grant projects. We identified three

categories of expenditures in the detailed budgets maintained by the district project manager that appeared to provide the greatest risk for misuse of funds because either the district had complete discretion on how to use that category of funds or the Department had designated that category of funds for a specific purpose but had not developed a process to monitor use of those funds to ensure the funds were used for the identified purpose. Specifically, for the five projects in our sample, we reviewed the following three categories of expenditures.

- **Owner’s contingency.** Consistent with industry best practice, applicants include a contingency budget to cover cost overruns (e.g., increased construction costs or unanticipated environmental remediation). The Department allows contingency funds to be used not only for unanticipated costs but also for additional items from an “add-alternates” list that is included for each project. (The add-alternates list is a list of items that the district would like to be included in the project, such as artwork or upgraded finishes, if funding is available). We reviewed approximately \$10.2 million in owner’s contingency line-item expenditures for the five projects in our sample.
- **Allowances.** This expense category is an allotment of funds for a specific purpose awarded as part of some grants. Some allowances are carved out of the original grant award amount, such as those for asbestos abatement and the purchase of land on which to build a new facility. However, one type of allowance is an allotment of state funding, in addition to the grant award amount, to pay for the increased cost of complying with the federal Davis-Bacon Act wage requirements. Specifically, for any lease-purchase project approved through the Public School Capital Construction Assistance Program (Program) that is funded with federal Qualified School Construction Bonds, the federal Davis-Bacon Act requires districts to pay individuals working on the project prevailing wages. For these projects, the Department provides a State-funded allowance to pay the increased wage costs. According to Department staff, regardless of the purpose of the allowance, any funds not spent for the specified purpose must be refunded to the Department. Within our sample of five projects, one project had a single allowance and another project had three allowances, and altogether, the four allowances totaled almost \$4.8 million in grant funds. The remaining three projects did not have allowances.
- **Project Reserves.** This expense category is a contingency added to each project by the Department to cover unforeseen circumstances. The project reserve is 10 percent of the total project cost for a facility renovation or repair project and 5 percent of the total cost for new building construction projects. The Department must approve a reserve request before the grant

recipient can access the funds. We reviewed approximately \$2 million in project reserves.

### **How was the audit work measured?**

Effective contract administration eliminates problems, potential claims and disputes and ensures that requirements are satisfied, goods and services are delivered in a timely manner, and the financial interests of the State are protected. According to the State of Colorado Procurement Manual, contract monitoring should include reviewing vendor invoices for accuracy and completeness, monitoring contractor performance to ensure conformance to budgets and work schedules, and verifying that the scope of work described in the contract is delivered and the work is satisfactory. For the Program, implementing controls over grant contract budgets and actual expenditures is key to ensuring that taxpayer dollars supporting the grants are used prudently and for the purposes intended and that any leftover funds can be redirected to other high-priority projects.

We evaluated the Department's monitoring of Program grant expenditures against State laws and rules, and authoritative guidance that provides a framework that the State and grant recipients must follow when managing grant awards. During the period of our audit this authoritative guidance included the following:

- Section 22-43.7-102, C.R.S., indicates that the overall intent of the Program is to help school districts address unsafe, deteriorating, and overcrowded schools, stating: "The General Assembly hereby finds and declares that Colorado school districts...have differing financial abilities to meet...the need for new public schools and renovations or controlled maintenance at existing schools so that unsafe, deteriorating, or overcrowded facilities do not impair students' abilities to learn."
- Section 22-43.7-109(5), C.R.S., indicates that the Assistance Board should award grants in descending order of priority to projects that will: (1) address safety or health concerns at existing facilities, (2) relieve overcrowding, (3) incorporate technology into the educational environment, and (4) address any other issues.
- The State of Colorado Procurement Manual establishes the components of a good contract monitoring program and establishes clear expectations for contract monitoring staff as to what will be monitored, the criteria that will be used to evaluate the contractor's performance, and how the contract monitor's activities will be documented. Specifically, the State of Colorado Procurement Manual recommends developing a comprehensive

contract monitoring checklist, policies on requirements for documenting ongoing monitoring activities, and requirements for the final written reports.

- Regulations (1 CCR 303-3, Section 8) require the Department to approve funding requests from grant recipients for project expenditures and require that payments will only be made to districts for work that is included in the project scope.

We also reviewed two other state grant programs to identify practices that could serve as models for the Program:

- The Colorado Department of Education's School Counselor Corps Grant Program provides funding to school districts to increase the availability of effective counseling within secondary schools to increase graduation rates and the number of students prepared for postsecondary education. The request for proposal for the School Counselor Corps Grant Program requires that grant recipients provide to the Department a final budget for approval, that the grant recipient seek approval from the Department for any changes to the project budget line items that exceed 10 percent, and that the grant recipient seek approval from the Department for any changes for two line items that the School Counselor Corps Grant Program identified as high risk.
- The State Historical Fund provides grant funding for historical preservation to local governments, including school districts and nonprofit organizations. The Historical Fund's grant manual sets forth several procedures that allow it to monitor the grant budget and aid it in linking project expenditures to the tasks identified in each project's scope of work, thus ensuring the project expenditures are allowable and appropriate. First, line-item project budgets are incorporated into every grant agreement. Second, the grant manual contains a list of allowable expenditures. Third, grant recipients must submit funding requests by budget line-item. Fourth, if a grant recipient wishes to reallocate grant funds among line-items, and the change will result in an increase or decrease in one line-item of more than 10 percent, the State Historical staff must approve the change prior to any expenditures. Further, any change of 25 percent or more to a single line-item will result in a contract amendment.

## **What problems did the audit work find and why do the problems matter?**

We reviewed Department practices for managing grant budgets and found the Department could improve its practices in two areas. First, the Department has not instituted sufficient controls to ensure that any owner's contingency funds that remain after unexpected conditions or cost overruns have been remedied are spent only on goods or services that are consistent with the overall program purpose of addressing unsafe, deteriorating, or overcrowded schools. Second, for reserve and allowance fund categories, the Department has not implemented a process to review budget-to-actual expenditures, by line item, even though the Department awards these fund categories for specified purposes. Our concerns are discussed in more detail below.

**Owner's Contingency.** The Department allows districts to spend any owner's contingency funds remaining near the end of a project on virtually any item within the broad project scope, with the exception of furniture, fixtures and equipment guidance discussed in the next section. We question whether this broad approach to defining allowable expenditures serves the best interest of the Program overall, because it may not return Program funds to the Department to provide financial assistance to other schools with unsafe, deteriorating, or overcrowded conditions. We reviewed \$10.2 million in owner's contingency funds across all five projects and identified approximately \$1.7 million (17 percent) in expenditures that appear questionable. Specifically:

- We found one case in which a district spent \$877,000 to purchase 1,364 laptops and iPads or approximately one portable computer device for almost every student at the school campus for which the grant was awarded. Of those devices, 62 percent were being used by other schools in the district. The district reported to us that it purchased the devices with the intent of sharing them with other schools in the district. Because the Department does not maintain add-alternates lists for grant projects, we were unable to determine whether the district planned to purchase 1,364 portable devices if the funds were available at the end of the project. However, this purchase of additional computers and other technology equipment nearly doubled the total amount requested for furniture, fixture, and technology expenses in its original grant application. It is possible these funds could have been reclaimed by the Department and directed to health safety projects in future grant cycles.
- We identified \$869,000 in contingency fund expenditures across all five projects, which we question in light of the outstanding need for projects that address unsafe, deteriorating, or overcrowding conditions at schools.



Some of the higher priced items included classroom projectors and AppleTVs for \$154,700, laptop storage/charging carts for \$42,300, upgrading flooring from linoleum to stained concrete floors for \$37,600, adding display cases and benches in the cafeteria and gym for \$29,900, a 3D color printer for \$29,900, upgrading the library circulation desk from a piece of furniture to an architecturally designed desk (because the library also serves as the public library) for \$27,200, adding a heritage wall (a wall commemorating the historic building demolished as part of the grant project) for \$26,600, and adding chair rails within classrooms for \$8,200. There were also numerous smaller items that appeared questionable, such as popcorn poppers and additional landscaping.

Every dollar spent on any project should be looked at as a dollar not available to another district that may have an unaddressed safety or overcrowding need. By not monitoring the use of the owner's contingency line item, the Department is not able to ensure that all funds are spent to achieve the statutory requirements that the Program provide financial assistance to schools to address health safety needs before addressing overcrowding, technology, or other needs. For example, 38 health and safety projects (totaling approximately \$72.8 million) applied for and did not receive funding during the Fiscal Year 2011 and 2012 grant cycles. The \$1.7 million in questionable owner's contingency fund expenditures, discussed above, could have funded 3 of those 38 projects.

**Allowances.** During our review of the district project manager's documentation for one of the five projects we reviewed, we identified approximately \$113,000 in allowance funds that may not have been used properly and have not yet been reverted to the Department. This grant recipient had an allowance for \$2,558,800 to pay for the additional wages required by the Davis-Bacon Act. The district's project manager's master budget showed that the full allowance had been spent, but the supporting documentation provided by the district project manager showed that as of April 2013, about \$113,000 of the allowance had not been spent. The district project manager explained that he had transferred the entire amount for the allowance into the general contractor's line-item in the budget and did not ensure that the general contractor only spent the funds on Davis-Bacon wages. Department staff did not identify that the district project manager was not tracking the allowance budget separately from his general contractor's budget.

**Reserves.** We could not determine whether reserve funds were spent only on items for which reserves were approved. For the five projects we reviewed, the Department approved the use of more than \$1.9 million in reserve funds. Grant recipients must submit a written request to the Department if something occurs on the project that requires the use of grant reserve funding. Once approved, the Department simply adds the reserve funds to the total available budget and does

not separately track or require the grant recipients to separately report the use of reserve funding in their monthly funding requests. As one district project manager explained, the documentation submitted to the Department with the funding requests often combines reserve and non-reserve expenditures as a single item. For example, a contractor's single expenditure for concrete may be for walls that are part of the original budget and foundation repairs that are part of the reserve. Further, for the five projects in our sample with reserve funds, only two district project managers included a budget line-item for the reserve funds. The other three district project managers added the reserve funds to existing line-items. Without tracking actual reserve expenditures, the Department cannot ensure that reserve funds are spent only for the items for which the reserve was approved.

By relying on district project managers to manage the expenditure of allowances and reserve funds without the Department monitoring line-item budgets, there is a risk that if any party involved in the project misappropriated project funds, the Department would not detect the misappropriation.

### **Why did the problem occur?**

We identified the following three areas in which we believe the Department's current policies and procedures do not provide maximum assurance that grant funds are spent only to complete the approved project scope or that funds not needed to complete contracted scope of work are returned to the Department for use in future grant rounds:

- **Finalized, detailed project budgets.** At the time of the grant award, most large projects are in a preliminary phase known as the concept phase. In the concept phase, the district has defined its needs, proposed a solution, and developed a preliminary budget for the project. For example, a district may know its elementary school is in such disrepair that it is more cost-effective to replace it than it is to repair it, and the district can provide a cost estimate for replacing the school. Preliminary budgets submitted in the application for funding may be quite detailed, but it is not until the subsequent design and construction phases occur that the district develops a more finalized line-item budget for the project.

Because the budget submitted with the application is preliminary and may change significantly after the design phase is completed, the Department cannot rely on it for the purposes of closely monitoring grant expenditures. However, the Department also does not require the district to provide its finalized line-item budget, which the district project manager uses to manage project expenditures. Moreover, the grant contracts do not contain a line-item budget; thus, the Department cannot manage expenditures

against the contract budget. Further, the Department does not require the district project managers to submit funding requests by budget line-item. In part due to the lack of a finalized budget and line-item funding requests, the Department does not monitor grant expenditures on a line item basis.

One way the Department and Assistance Board could obtain finalized, line-item budgets for grant projects would be to implement a two-phase application process whereby school districts could apply for funding to complete the planning and design phases of a project, then submit a subsequent application that would include the finalized line-item budget, for construction of the project. Another option would be for the Department and Assistance Board to require, as a part of the grant contract, that the grant recipient provide the finalized line-item budget to the Department when it has been prepared. Additionally, the contract with the districts should (1) require the district project manager to provide the Department with a monthly accounting of all expenditures, by line-item in the budget, and reconcile the budget to actual expenditures and (2) require districts and their project managers to explain and seek Department approval for any changes in line-item budgets.

Further, the Department has not developed written procedures for staff on documenting budget-monitoring activities. Currently, the Department staff document budget-monitoring activities related to the review of funding requests but we reviewed the project files, electronic and paper, maintained by staff and only one of five projects in our sample contained a master line-item budget for the project. There was also no evidence in any of the five project files we reviewed that Department staff were tracking the project budget by line item or that staff had routinely compared the expenditures to a project time line to ensure expenditures aligned with the percentage of the project that was completed.

- **Expectations on allowable expenditures and reversion of funds.** According to the four district project managers we interviewed, there is a lack of specific and consistent direction from the Department on what is allowable, which creates confusion and makes it difficult for grant recipients to properly budget for anticipated expenditures. First, although the Department has developed a list of allowable furniture, fixture, and equipment expenditures, the list was created to ensure project expenditures comply with the requirements of the federal bonds used to fund some lease-purchase projects. Thus, the Department's furniture, fixture, and equipment guidance is not sufficient to allow Department staff or districts to identify whether all grant expenditures are consistent with the Program's purpose of providing financial assistance to alleviate unsafe or

deteriorating conditions or overcrowding in schools. Second, according to three of the four project managers we interviewed, the Department has changed the criteria of what furniture, fixture, and equipment expenditures are allowable and applied the new criteria to all active grants, rather than just future grants. Therefore, if a recipient had budgeted to purchase something with grant funds and the Department later made that item unallowable, the recipient would have to find another source of funding for that purchase.

- **Contract provisions.** Currently, the Department's contracts do not contain performance standards specific to the project, reporting requirements, or monitoring requirements related to the project budget. Specifically, the contracts do not include a line-item budget or provisions that hold the grant recipient accountable for ensuring that grant funds are expended in compliance with Program guidance or that all funds not needed to accomplish the purposes of the approved grant are reverted to the Department.

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## **Recommendation No. 5:**

The Department of Education's Division of Public School Capital Construction Assistance (the Department) should establish written policies and procedures to strengthen its management of grant contract budgets. Specifically, these policies and procedures should include:

- a. Mechanisms to obtain finalized, line-item budgets for each grant contract that serve as a basis for the Department's monitoring of grant expenditures.
- b. A requirement that grant recipients submit funding requests that align with the finalized line-item budgets.
- c. Direction to the Department's project consultants on conducting detailed monitoring of grant expenditures against the finalized line-item budgets to ensure funds are spent according to the budget and are not transferred among line-items. The direction should also address the type and quantity of monitoring activities they are required to conduct and how the project consultants should document their monitoring activities.
- d. Definitions in the grant contracts of allowable expenditures that are tailored to meet the overall program purposes. If guidance on allowable

expenditures changes, it should be applied prospectively, except where federal bond requirements necessitate retroactive application.

- e. Additional performance expectations in the Department's contract with the districts requiring that districts manage project expenditures to the approved grant project and revert funds not needed for delivering the project, as approved in the grant award, to the Department for use on other projects.

### **Department of Education Response:**

- a. Agree. Implementation date: December 2013.

The Department currently requests and receives a preliminary line-item budget with all grant applications and, at times, finalized line-item budgets. In the future, the Department will include provisions in grant recipient contracts that require districts to provide the Department with a finalized line-item budget for all projects. The Department will review and approve the final line-item budget prior to approving payment of any funding requests.

- b. Agree. Implementation date: December 2013.

The Department will continue to perform a detailed review of each invoice prior to reimbursement to ensure compliance with the awarded project scope and will implement a process in which the school district aligns their requests for funds with a detailed line-item budget.

- c. Agree. Implementation date: December 2013.

The Department's new Standard Operating Procedure will document the expectations for the ongoing grant monitoring activities, including comparing expenditures against the finalized line-item budget, and outline standard documentation of these activities.

- d. Agree. Implementation date: December 2013.

The Department will review and clarify existing guidance on allowable expenditures as needed and incorporate this into a definition within the grant contracts.

- e. Agree. Implementation date: December 2013.

The Department will review and update our grant recipient contracts with school districts to further clarify the expectations of the school district in relation to management of the project budget and require districts to revert to the Department any monies not needed to deliver the project, as approved.

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## Performance Monitoring

In addition to monitoring adherence to the grant contract budget, it is also important for the Department to monitor the grant recipients' oversight of the contracted work and their quality control processes. Because the grant recipients have direct control over each project, it is important for them to have good procedures in place to ensure a high-quality finished project. Monitoring by the Department can also help to identify and address any significant problems before they become more serious and costly to correct. Ensuring quality in construction projects is a function of implementing both up-front controls and monitoring controls. Up-front controls include having a contractor selection process that ensures high-quality contractors are selected and contract requirements that hold contractors responsible for adhering to best practice quality assurance standards in conducting their work. Monitoring controls include reviewing documentation and conducting site-visits to ensure that work is progressing satisfactorily and that problems are identified and addressed before payment is made. As discussed earlier, the Department relies on the district to directly monitor the construction quality through its oversight of the district's project manager. The district's project manager is responsible for, among other duties, ensuring that all necessary material quality testing occurs, that the project is completed according to the plans and specifications, and that the project adheres to all building codes and standards.

The Department has implemented some guidance for districts to follow when procuring and selecting contractors, in an effort to ensure that districts select well-qualified contractors. Some of the guidance issued by the Department is discussed below and requests that school districts:

- Use a standard request for qualification template for district project managers, design-build contractors, architects, and construction managers/general contractors, which include job descriptions.

- Follow the Department's recommended competitive procurement process, as stated in the Department's Procurement Guidelines, or submit an alternative procurement plan to the Board for approval.
- Submit their project manager contracts, which should include requirements related to the project manager's oversight of and quality control processes for the project, to the Department for review prior to executing the contract.
- Include standard insurance requirements in all consultant and contractor contracts on projects.

### **What audit work was performed and what was its purpose?**

We conducted work to determine what controls the Department has in place to monitor grant recipient performance and ensure that grant recipients deliver high-quality projects. Specifically, we reviewed the Department's monitoring of a sample of five large lease-purchase projects (four new school projects and one school addition project) awarded funding in the Fiscal Year 2011 and 2012 grant cycles, totaling more than \$85 million in State funds. In the Fiscal Year 2011 and 2012 grant cycles, the Assistance Board funded 19 lease-purchase grants totaling approximately \$288 million. We focused our review on the controls and procedures the Department uses to oversee grant recipient performance. Because the Department has only limited draft-written procedures for monitoring its grant recipient contracts, in addition to reviewing those draft procedures we interviewed Department staff—including the Department's project consultants who are responsible for overseeing grant awards to districts, the Director of the Division of Public School Capital Construction Assistance, and grant recipients—to understand the Department's practices for ensuring that grant recipients provide quality projects. Finally, we examined project records to assess whether the Department adequately documented its oversight of grant recipient performance of contractual obligations.

### **How was the audit work measured?**

We evaluated the Department's monitoring of the Program's grant contracts against the State laws and rules and against authoritative guidance that provides a framework that the State and grant recipients should follow when managing grant awards. During the period of our audit this authoritative guidance included:

- Section 24-103.5-101, C.R.S., requires state contracts to include (1) performance measures and standards developed specifically for the contract that can be used to evaluate the performance of the contractor (or

in this case the grant recipient); (2) an accountability section that requires the contractor to report regularly on achievement of the performance measures until successful completion of all or part of the contract, and (3) monitoring requirements that specify how the grant recipient will be monitored.

- State Fiscal Rule 3-1, Section 11.2, requires that all agencies monitor contracts to ensure the contractor's compliance with requirements, standards, and measures of the contract, the time line of the contract, that the scope of work included in the contract is delivered satisfactorily, and the extent to which the grant recipient met or exceeded the budgetary requirements of the contract.
- The State of Colorado Procurement Manual states that the contract manager for a contract should monitor, among other things, the performance of the contractor to ensure conformance to the work schedule and verify that the scope of work in the contract is delivered satisfactorily.
- The State of Colorado Procurement Manual indicates that a good contract monitoring program establishes clear expectations for contract monitoring staff as to what will be monitored, the criteria that will be used to evaluate the contractor's performance, and how the contract monitor's activities will be documented. Specifically, the Procurement Manual recommends developing a comprehensive contract monitoring checklist, policies on requirements for documenting ongoing monitoring activities, and requirements for final written reports.
- The Department's contracts with districts allow the Department to monitor the project and ensure that the districts institute procedures to ensure a quality completed project. Additionally, all grant project contracts require districts to perform their obligations under the contract in accordance with the "highest standards of care, skill or diligence in the industry" and require districts to obtain all licenses, certifications, approvals, insurance and permits required by all to complete the grant project.

Finally, we reviewed two other government-run programs that provide funding for construction projects to identify practices that could serve as models for the Program. Specifically:

- The Federal Highway Administration (FHWA) provides federal aid and technical assistance to state highway departments to support the design, construction, and maintenance of federal highways. The FHWA developed construction management program guidelines to aid its regionally based



field offices in overseeing and evaluating the state-run agencies that implement the construction projects that receive federal aid. These guidelines state that the entity awarding the contract should: (1) create a formalized process to ensure that completed projects reasonably conform to the plans and specifications, (2) evaluate the quality of construction and promote appropriate improvements in construction quality, and (3) conduct frequent, thorough on-site reviews of the work in progress. According to FHWA guidance, the project manager for each project should, at a minimum, conduct three documented inspections: initial, intermediate, and final. The inspections must be sufficiently comprehensive to report the status and acceptability of ongoing work, planned future work, and the potential for delays or claims.

- The Colorado State Historical Fund (the Historical Fund) grant manual provides procedures for monitoring the quality of construction projects that require grant recipients to provide (1) documentation such as architectural plans, design specifications, and change orders to the Historical Fund, (2) engineering reports, and (3) progress reports every 2 to 4 months, depending on the scope and duration of the project, that include a narrative of the project's progress to date, the work the grant recipient plans to accomplish before the next progress report, and any assistance the grant recipient needs from the Historical Fund. Historical Fund staff report that they review the documents provided, follow up with grant recipients on any questions that arise, and perform on-site visits at construction project sites to monitor the progress on projects.

### **What problems did the audit work find and why did the problems occur?**

All Department staff interviewed reported that monitoring project quality is the responsibility of the district's project manager, not the responsibility of Department staff. We found that the Department has not developed and implemented a thorough system of controls to ensure that grant recipients have sufficient quality control processes in place to monitor whether district project managers have performed the tasks necessary to ensure project quality. We identified two key weaknesses in the Department's controls, as described below.

**Lacking grant contract provisions related to quality assurance.** We found that the Department's grant contracts do not contain requirements that are needed to enable the Department to oversee the performance of the contract. Specifically, the grant contracts do not:

- Include any provisions that require districts to follow the guidance described previously with respect to project quality (e.g., using a standard request for qualification template for district project managers, design-build contractors, architects, and construction managers/general contractors).
- Require that the grant recipient attest to the Department that the project manager (1) obtained and reviewed architectural plans, construction specifications, and quality testing reports to ensure that projects are designed in accordance with the requirements in the grant award and in compliance with accepted building code or (2) completed key steps in the construction process, including obtaining appropriate permits and inspections, and conducted site visits at the project at key points in the process.
- Require the grant recipient to submit standardized, comprehensive progress reports that provide detailed information on the progress of the project, including observations from routine site visits, information on any areas of concern and proposed solutions, updates on quality testing or inspections, or other indicators of the ongoing progress and quality of the project. Currently, the Department rules and grant contracts require only annual progress reports, rather than progress reports at key stages of the construction process, and the Department does not enforce the requirement; we found that none of the Department grant project files for the five grants in our sample contained any annual status reports. Additionally, the Department does not currently require the district or district project manager to conduct periodic site visits. Although the Department's project consultants reported receiving construction observation reports containing items such as the weather, number of people on site and project progress from the district's project manager, only one of the five projects we sampled contained construction observation reports.

**Lacking written policies and procedures for monitoring project performance.** The Department does not have a comprehensive process to guide project consultants with respect to what their monitoring efforts should include or how they should be documented. One of the project consultants we interviewed stated that it is not necessarily clear what is expected of them with respect to monitoring project quality. For example, there are no written policies directing what type of monitoring activities project consultants should conduct (e.g., site visits, documentation review, attendance at meetings between the districts and key contractors, etc.) or the frequency of site visits and what project consultants should observe and review on a site visit to evaluate the progress of the project and ensure the district is complying with contractual requirements for ensuring

the quality of the project. We reviewed the Department's site visit log for Fiscal Years 2012 and 2013. We found that for the five projects in our sample, the number of site visits varied, with one project receiving three site visits, three projects receiving two site visits each, and one project receiving only one site visit. However, the consultants do not prepare site visit reports, so we could not determine at what stage the visits occurred (e.g., beginning, middle, or end of the construction process) and what activities, if any, the consultant carried out to monitor the project. One way to facilitate the monitoring process is to develop a detailed contract monitoring checklist that instructs project consultants as to what they should monitor, how they should monitor those items (e.g., through review of reports and materials from the grant recipient, phone calls and emails, and on-site visits), how they should document their monitoring efforts, and the criteria that will be used to evaluate the grant recipient's performance.

Department management and the Assistance Board told us that the local control doctrine prevents them from imposing additional contractual requirements on the school districts in order to ensure school districts are adequately overseeing construction quality. Although the Colorado Constitution specifies that local school boards have control over instruction in their public schools (Colorado Constitution Art. IX, Section 15, known as the "Local Control Clause"), the Assistance Board, with the support of the Department, is statutorily responsible for operating the BEST Program. The Assistance Board is given the authority to establish rules and policies governing the grant application process and is responsible for signing grant contracts. As such, the Assistance Board should ensure that grant recipients deliver quality projects for the State's investment of funds. Implementing additional controls can help the Department ensure that the districts receive the finished construction project for which they received grant funds. Further, the Department and Assistance Board have included a number of specific requirements in contracts with grant recipients that have not been determined to violate the local control standards, including:

- All cash grant contracts require districts to adhere to specific conflict of interest provisions such as prohibiting district employees from working for a contractor awarded funding through the grant.
- All Program contracts require districts to ensure that contractors maintain identified types of insurance coverage.
- Contracts for projects involving the purchase of land have several specific requirements, such as districts must obtain Department approval of the purchase contract, the purchase price must be supported by an appraisal, the district must obtain a General Warranty deed to the property, and the

district must conduct an American Land Title Association survey of the property.

- Contracts for lease-purchase grants require the districts to obtain written Department approval of any changes to the project specifications.

### **Why do the problems matter?**

Without formalizing quality assurance requirements in contracts, the Department cannot adequately monitor projects to ensure that the scope of work is delivered satisfactorily and to protect the State's investment in the project. If a grant-funded project fails—in particular if the project was financed with lease-purchase funding—the State is ultimately responsible for ensuring that any problems are fixed so that the value of the project remains intact for the trustee until the lease-purchase payments are complete and the school district can take title to the building. The State's contracts with the districts allow it to pursue legal action against districts that fail to complete quality projects, but this ability does not eliminate the State's out-of-pocket legal defense costs if the trustee decides to pursue legal action. Further, the ability to pursue legal action against a noncompliant district does not ensure that the district has the financial means to correct the failing building, thus potentially leaving the State responsible for repair costs. Moreover, the first priority for the grant program is to improve health and safety conditions within Colorado's public schools. The Department should therefore ensure that public funds are achieving this purpose because construction quality defects may put students, teachers, and administrators at risk if safety concerns are identified.

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### **Recommendation No. 6:**

The Department of Education's Division of Public School Capital Construction Assistance (the Department) should implement a more robust system for monitoring grant projects by:

- a. Establishing standardized contract provisions that require grant recipients to adhere to standards and provide the Department with (1) standardized written progress reports detailing project progress, evidence of site visits, and areas of concern and proposed solutions; and (2) documentation demonstrating that key quality processes such as design review, inspections, and quality testing have been completed.
- b. Establishing policies and procedures to provide direction on what Department staff should monitor; what should be monitored through

various means such as review of reports and materials from the grant recipient, phone calls and emails, and on-site visits; and the criteria that will be used to evaluate the grant recipient's performance. Written policies should include standards for the frequency of site visits and what consultants should do on a site visit to evaluate the progress and ensure the district's project manager is adequately overseeing the quality of the project.

- c. Developing requirements for how Department staff should document their contract monitoring activities, including phone calls, emails, in-person contacts, and reviews of materials submitted by grant recipients.

### **Department of Education Response:**

- a. Agree. Implementation date: December 2013.

The Department will develop standardized contract provisions with customized information and timing that is correlated to the project type and scope. The elements listed in the recommendation will be included in the contracts with grant recipients. Department staff will review the required documentation as part of their ongoing grant monitoring activities.

- b. Agree. Implementation date: December 2013.

The Department's new Standard Operating Procedure will document the expectations for the ongoing grant monitoring activities performed by Department staff.

- c. Agree. Implementation date: December 2013.

As stated above, the Department's new Standard Operating Procedure will provide formalized guidance on the standard documentation for the ongoing grant monitoring activities performed by the Department staff.

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## **Cash Grant Contracts**

Once the Assistance Board awards a cash grant, the grant recipient and the Department, on behalf of the State, execute a grant contract. The cash grant contract contains the terms and conditions of the grant, including the grant award

and reserve amount, the termination date, a description of the funding request process, and the remedies available to the State in the event of a breach of contract. The cash grant contract also has two exhibits attached that are specifically used to (1) describe the details of the project (e.g., a roof replacement or new fire suppression system), including the scope of work, time line for the project, and the facility at which the project will occur, and (2) require that the district complete the project described in its application documents.

### **What audit work was performed and what was the purpose?**

For the Fiscal Year 2012 grant cycle, the Attorney General's Office began requiring the Department to use contracts, rather than an award letter for all cash grants awarded through the Program. The Attorney General's Office did not believe that the grant award letters (used previously by the Department to broadly describe the terms and conditions of the grant) were sufficient to protect the State's interests or ensure that funds were spent appropriately by the grant recipient. Because cash grant contracts are relatively new to the Department, we focused our audit work on the standard cash grant contracts for the Fiscal Year 2012 and 2013 grant cycles.

The purpose of the audit work was to assess whether the terms and conditions of the cash grant contracts are sufficiently detailed to ensure that the grant recipient completes the project, as described in the grant application, on time, and within budget, and that the Department has sufficient remedies available to enforce the contract.

### **How were the results of the audit work measured?**

After the grant award, the first step in effective grant monitoring is to create a clear and comprehensive statement of work that will be incorporated into the grant agreement or contract. A statement of work should identify the project deliverables and contract time frame, describe performance measures, and identify remedies for noncompliance. We compared the terms and conditions of the sample grant contract published by the Office of the State Controller with the terms and conditions contained in the Department's standard cash grant contract to determine whether the cash grant contract included all the required provisions from the State Controller's sample contract, including a sufficient description of the scope of work, deliverables, time line, grant award amount, and remedies for noncompliance.

### **What problem did the audit work identify?**

We found that the cash grant contracts do not contain a description of the project to be completed under the grant. The body of the cash grant contract contains the grant amount and grant reserve amount, but it does not identify the type of project (e.g., roof repair or boiler replacement) or the school building(s) that will be impacted by the project. Although a statement of work exhibit is attached to the cash grant contract and identifies the project type, time frame for completion, and the facility affected, we found that the contract is missing important language to specifically incorporate the exhibit into the contract. As a result, the exhibit containing the statement of work may not be part of the contract and may not be legally binding or enforceable by the Department. We discussed our concerns with the Attorney General's Office, which confirmed that the contract is missing key language.

### **Why did the problem occur?**

The Department worked with the Attorney General's Office to develop a contract for cash grants for the Fiscal Year 2012 grant cycle. However, language that is necessary to incorporate the contract exhibits, including exhibits describing the project scope and deliverables, was originally included in the standard contract template but then inadvertently taken out. Department staff are unsure at what point in the process the language was deleted and believe it was simply an oversight by all parties involved (i.e., the Department and the Attorney General's Office).

### **Why does the problem matter?**

Clear, comprehensive, and concise statements of work are important for avoiding disputes and possible litigation with grantees. The statement of work memorializes the terms of the agreement between the parties to the grant and prevents misunderstandings as memories fade or circumstance change. Further, statements of work are the roadmap for contract administration and, absent a defined project scope, it is difficult for Department staff to (1) identify whether an expenditure is allowable, which can lead to improper expenditures, or (2) hold the grant recipient accountable to a precise project scope and timely delivery of the project. Specifically, because the cash grant contracts do not legally incorporate the exhibits that define the detailed project scope, a grant recipient could spend the grant funds on something other than the project described in the application, and the Department could have limited legal recourse. The Department awarded about \$74 million in the Fiscal Year 2012 and 2013 grant cycles using the problematic contracts, and as a result, the Department may have limited legal

recourse if the funds are not spent in accordance with the grant application. The Department plans to correct the problems for the 2014 cash grant contracts.

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### **Recommendation No. 7:**

The Department of Education's Division of Public School Capital Construction Assistance (the Department) should improve its ability to hold cash grant recipients legally responsible for delivering the project covered by the grant by:

- a. Revising its cash grant contract form to specifically incorporate the exhibits describing the project scope, time line, and deliverables, or include the project scope, time line, and deliverables in the body of the contract.
- b. Amending any active cash grant contracts that are not substantially complete to incorporate the exhibits into the contracts.

### **Department of Education Response:**

- a. Agree. Implementation date: Implemented.

The Department has revised the cash grant contract form to include the missing words "incorporate by reference" to formally incorporate exhibits.

- b. Agree. Implementation date: December 2013.

The Department will perform a risk analysis on existing cash grant contracts and will amend any contracts deemed to be high-risk based upon factors including project completion status.

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