



**CSIS** California School Information Services

# Alameda County Office of Education

Extraordinary Audit

of the

## American Indian Model Charter Schools

June 12, 2012

Joel D. Montero  
Chief Executive Officer







## CSIS California School Information Services

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June 12, 2012

Sheila Jordan, Superintendent  
Alameda County Superintendent of Schools  
313 W. Winton Ave.  
Hayward, CA 94544

Dear Superintendent Jordan:

In January 2012, the Fiscal Crisis and Management Assistance Team (FCMAT) entered into an agreement with the Alameda County Superintendent of Schools to provide an Assembly Bill 139 extraordinary audit of the American Indian Model Charter Schools. Specifically, the agreement states that FCMAT will perform the following:

1. Review the revenues and expenditures for the AIMS charter schools related to the After School Education and Safety (ASES) Federal Program Grant for the current and two prior fiscal years and determine if fraud, misappropriation of funds or other illegal activities have occurred. The ASES Program funds the establishment of local after school education and enrichment programs. These programs are created through partnerships between schools and local community resources to provide literacy, academic enrichment and safe constructive alternatives for students in kindergarten through ninth grade (K-9). Funding is designed to: (1) maintain existing before and after school program funding; and (2) provide eligibility to all elementary and middle schools that submit quality applications throughout the State of California.
2. Review the AIMS charter schools application for funds received from SB 740 Charter School Facility Grant Program and determine if fraud, misappropriation of funds or other illegal activities have occurred during the current and two prior fiscal years. The grant is a noncompetitive program that provides assistance with facilities rent and lease expenditures for charter schools that meet specific eligibility criteria. The grant program was enacted to reimburse charter schools for rental and lease costs in low-income areas. This program is targeted toward schools and communities with high proportions of economically disadvantaged students. Eligible applicants must have at least 70 percent of students enrolled at the charter school who are eligible for free or reduced-price meals or the charter school must be physically located in an elementary school attendance area where at least 70 percent of students enrolled are eligible for free or reduced-price meals. The charter schools must also give a preference in admissions to students who reside in the elementary school attendance area. The charter schools are funded \$750 per unit of classroom-based average daily attendance or 75 percent of its annual facilities rent and lease costs for the school, whichever is less.

### FCMAT

Joel D. Montero, Chief Executive Officer

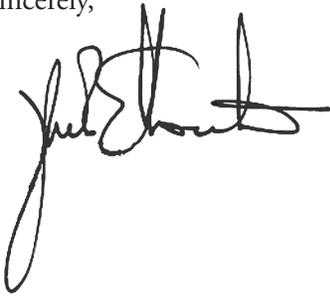
1300 17<sup>th</sup> Street - CITY CENTRE, Bakersfield, CA 93301-4533 • Telephone 661-636-4611 • Fax 661-636-4647  
422 Petaluma Blvd North, Suite. C, Petaluma, CA 94952 • Telephone: 707-775-2850 • Fax: 707-775-2854 • [www.fcmat.org](http://www.fcmat.org)  
Administrative Agent: Christine L. Frazier - Office of Kern County Superintendent of Schools

3. Determine if any of the AIMS charter schools violated any applicable conflict of interest disclosure requirements in accordance with the Political Reform Act of 1974 ("the Act") regarding California's conflict of interest laws for public officials. The Act requires certain "designated" public officials at all levels of government to publicly disclose their private economic interests and requires all public officials to disqualify themselves from participating in decisions in which they have a financial interest.

This report includes the study team's findings and recommendations.

FCMAT appreciates the opportunity to serve you and extends its thanks to all the staff of the Alameda County Office of Education in conjunction with the Oakland Unified School District for their assistance during fieldwork.

Sincerely,

A handwritten signature in black ink, appearing to read "Joel D. Montero". The signature is fluid and cursive, with a large initial "J" and "M".

Joel D. Montero

Chief Executive Officer

# Table of contents

About FCMAT .....	iii
Introduction .....	1
Background.....	3
Findings and Recommendations.....	7
Occupational Fraud.....	7
Related-Party Transactions and Significant Influence.....	11
Governing Board Oversight.....	29
Appendices.....	37



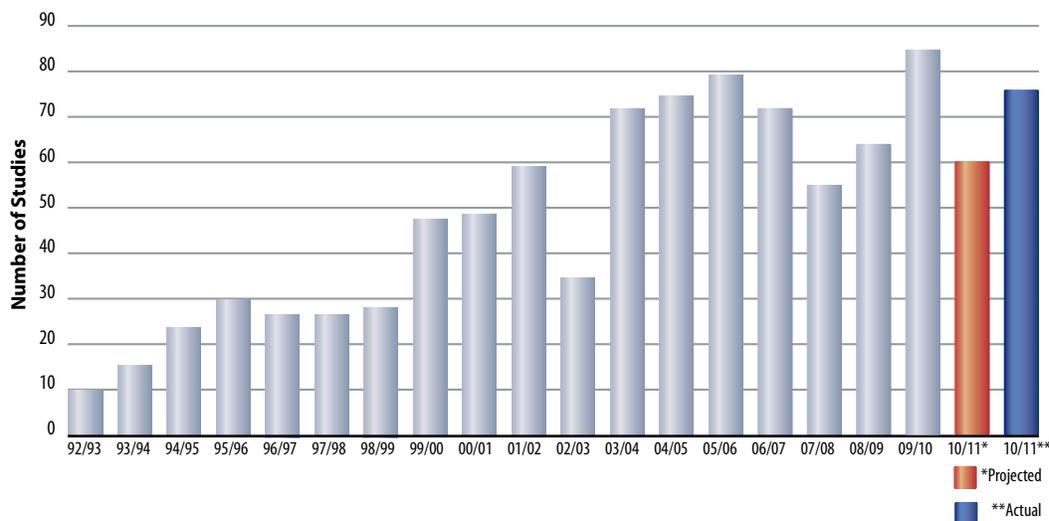
# About FCMAT

FCMAT’s primary mission is to assist California’s local K-14 educational agencies to identify, prevent, and resolve financial and data management challenges. FCMAT provides fiscal and data management assistance, professional development training, product development and other related school business and data services. FCMAT’s fiscal and management assistance services are used not just to help avert fiscal crisis, but to promote sound financial practices and efficient operations. FCMAT’s data management services are used to help local educational agencies (LEAs) meet state reporting responsibilities, improve data quality, and share information.

FCMAT may be requested to provide fiscal crisis or management assistance by a school district, charter school, community college, county office of education, the state Superintendent of Public Instruction, or the Legislature.

When a request or assignment is received, FCMAT assembles a study team that works closely with the local education agency to define the scope of work, conduct on-site fieldwork and provide a written report with findings and recommendations to help resolve issues, overcome challenges and plan for the future.

**Studies by Fiscal Year**



FCMAT also develops and provides numerous publications, software tools, workshops and professional development opportunities to help local educational agencies operate more effectively and fulfill their fiscal oversight and data management responsibilities. The California School Information Services (CSIS) arm of FCMAT assists the California Department of Education with the implementation of the California Longitudinal Pupil Achievement Data System (CALPADS) and also maintains DataGate, the FCMAT/CSIS software LEAs use for CSIS services. FCMAT was created by Assembly Bill 1200 in 1992 to assist LEAs to meet and sustain their financial obligations. Assembly Bill 107 in 1997 charged FCMAT with responsibility for CSIS and its statewide data management work. Assembly Bill 1115 in 1999 codified CSIS’ mission.

AB 1200 is also a statewide plan for county office of education and school districts to work together locally to improve fiscal procedures and accountability standards. Assembly Bill 2756 (2004) provides specific responsibilities to FCMAT with regard to districts that have received emergency state loans.

In January 2006, SB 430 (charter schools) and AB 1366 (community colleges) became law and expanded FCMAT's services to those types of LEAs.

Since 1992, FCMAT has been engaged to perform nearly 850 reviews for LEAs, including school districts, county offices of education, charter schools and community colleges. The Kern County Superintendent of Schools is the administrative agent for FCMAT. The team is led by Joel D. Montero, Chief Executive Officer, with funding derived through appropriations in the state budget and a modest fee schedule for charges to requesting agencies.

# Introduction

In December 2011, the Fiscal Crisis and Management Assistance Team (FCMAT) received a request from the Alameda County Office of Education for an Assembly Bill (AB) 139 extraordinary audit of the American Indian Model Schools (AIMS) charter schools. The county office had become aware that Oakland Unified School District Office of Charter Schools had received allegations of multiple fiscal irregularities, questionable expenditures and inappropriate related-party transactions at AIMS charter schools. Concerned that these allegations may have violated various government and education codes related to fraud and/or misappropriation of assets, the county superintendent initiated an investigation to determine whether sufficient evidence of criminal activity exists to report the matter to the local district attorney's office for further investigation. Under the provisions of Education Code (EC) section 1241, the Fiscal Crisis and Management Assistance Team (FCMAT) entered into a contract with the Alameda County Office of Education to conduct an AB 139 extraordinary audit.

FCMAT interviewed employee and reviewed documents to determine if instances of fraud, misappropriation of funds or other illegal practices occurred that would warrant further investigation by the local district attorney's office.

## Study Guidelines

FCMAT provides a variety of services to school districts and county offices of education upon request. Education Code Section 1241.5(c) permits a county superintendent of schools to review or audit the expenditures and internal controls of any school district in that county if he or she has reason to believe that fraud, misappropriation of funds, or other illegal fiscal practices have occurred that merit examination. According to the Education Code, the review or audit conducted by the county superintendent will focus on the alleged fraud, misappropriation of funds, or other illegal fiscal practices and is to be conducted in a timely and efficient manner. This is in accordance with Education Code Section 42638 (b), which states as follows:

If the county superintendent determines that there is evidence that fraud or misappropriation of funds has occurred, the county superintendent shall notify the governing board of the school district, the State Controller, the Superintendent of Public Instruction, and the local district attorney.

Therefore, FCMAT focused on the allegations of misappropriation of assets, misuse of grant funds and conflict of interest to determine whether AIMS Charter Schools and/or its personnel were involved in or committed fraudulent activities.

## Audit Fieldwork

Investigating allegations of fraud requires a number of steps that include interviewing potential witnesses and assembling evidence from internal and external sources. The FCMAT study team visited the charter schools and district office in December 2011, January and February 2012 to conduct interviews, collect data and review documents. Specifically, FCMAT reviewed, analyzed and tested records that included audited financial statements, financial records, grant documents, board minutes, the charter petitions and other documentation from independent third party sources. The review also included interviews with board members, the former director, manage-

ment personnel, business office staff, current and former charter school employees to evaluate information concerning any alleged mismanagement, fraud, or abuse.

The fieldwork focused on determining whether there is sufficient information to ascertain fraud, the mismanagement of grant proceeds, misuse of state funds and conflict of interest particularly related-party and intercompany transactions. Although there are many different types of fraud, a conflict of interest exists when officers or employees of the organization have a personal financial interest in a contract or transaction and is considered to be a form of misappropriation of assets.

All fraud has common elements including the following:

- Intent, or knowingly committing a wrongful act
- Misrepresentation to accomplish the act
- Reliance on weaknesses in the internal control structure
- Concealment of the act

This report is the result of that investigation and is divided into the following sections:

- I. Introduction
- II. Background
- III. Scope and Procedures
- IV. Findings and Recommendations
  - Occupational Fraud
  - Related-Party Transactions and Significant Influence
  - Governing Board Oversight
- V. Appendices

## Study Team

The FCMAT study team was composed of the following members:

Deborah Deal, CFE FCMAT Fiscal Intervention Specialist Los Angeles, California	Michelle Plumbtree FCMAT Chief Management Analyst Petaluma, CA
John Von Flue FCMAT Fiscal Intervention Specialist Bakersfield, CA	Leonel Martínez FCMAT Technical Writer Bakersfield, CA

# Background

The Oakland Unified School District granted the first American Indian Public Charter School (AIPCS) a charter in 1996. The first campus, AIPCS, is a middle school campus serving sixth-through eighth-grade students, located in the Laurel area of Oakland. In September 2006, American Indian Public High School (AIPHS) opened and shared the same campus housing students in grades nine through 12. A year later, a second middle school, American Indian Public Charter School II (AIPCS II), opened in the Chinatown area in the city of Oakland serving grades five-eight. Total student enrollment for all three schools reported to the California Department of Education (CDE) for 2009-2010 was 471, and 493 in 2010-11.

In 1999, California Legislature passed the Public Schools Accountability Act. A primary component of this act is Academic Performance Index (API), which is used to determine adequate yearly progress for federal Title One funding and identifies schools that are underperforming and are in need of state intervention. API is a numeric score ranging from 200 to 1,000 designed to measure an individual schools' performance target from year to year. Statewide, this target is 800.

All three schools operated by American Indian Model Schools (AIMS) rank in the top decile of comparable schools statewide. In 2009- 2010, AIPCS had an API of 988, which was the highest in the state, the AIPCH II API of 974 was sixth highest in the state, and the AIPHS API of 976 was fourth highest in the state. The U.S. Department of Education awarded both middle schools Blue Ribbon Awards issued to only 200 schools each year across the nation. The student race and ethnicity reported to the California Department of Education for the 2010-2011 fiscal year was 68.5% Asian, 18% Hispanic, 1% American Indian and 12.5% other.

Originally hired in 2000 as the director of the single AIPCS school existing at that time, the director thereafter participated in the opening of two additional AIPCS schools, and was frequently referred to as "the founder." At the June 21, 2007 AIPCS board meeting, the founder resigned as director after allegedly making racist comments and the board reassigned him as "CEO of the AIPCS network." From 2007 through July 2011, the founder served as CEO from his farm in North Carolina, and continued to exercise significant control over AIPCS's operations and financial decisions, many of which benefitted him directly. According to an interview with the current board president and board minutes of July 14, 2011, at the board's request, the founder returned to California in August 2011 "to work with the board and school administration..." and to provide a written report to the board by September 1, 2011. According to interviews, on October 31, 2011, the board elected the founder as a board member, a position he resigned on December 14, 2011.

The schools have received praise for outstanding achievements in academic performance, but criticism of their founder for his unconventional methodology and rigorous discipline. Several former employees have reported multiple incidences of financial irregularities by the founder and his spouse. The AIMS governing board is responsible for fiscal accountability and proper governance over all financial transactions but has limited involvement in the schools' financial affairs. The lack of due diligence and internal controls by the governing board has effectively granted the founder and his spouse unrestricted access to the assets of the organization and implied authority to enter into a variety of business arrangements for personal gain.

The involvement of the founder, his spouse, business associates, former board members and numerous businesses owned by the founder or his spouse has raised questions regarding potential conflict of interest, significant influence over financial transactions, control over fiscal management and related party transactions in violation of government and education codes.

During the summer of 2011, the Oakland Unified School District Office of Charter Schools learned of several irregularities and possible misappropriation of funds in the AIMS charter school organization that oversees three charter schools. Several purported fraud allegations involved the mismanagement of charter school funds related to facility grants, after school funding and related-party transactions between the founder (who is also a former director and board member) who owns several private businesses that conduct business with the charter schools including the building rented by one school and a sub-lease for the other two schools. Additional complaints involved the founder's spouse, who performed bookkeeping services and general back office accounting for all three schools.

Based on these allegations, the Oakland Unified School District Office of Charter Schools conducted a preliminary investigation, and based on the results of their initial findings, requested assistance from the Alameda County Office of Education in October 2011.

Upon review of the allegations, the county office requested the Fiscal Crisis & Management Assistance Team (FCMAT) to provide for the assignment of professionals to study specific aspects of alleged fraud, misappropriation of funds and possible criminal activity in the AIMS Charter Schools organization.

Education Code Section 42638(b) requires action by the county superintendent to include the following:

If the county superintendent determines that there is evidence that fraud or misappropriation of funds has occurred, the county superintendent shall notify the governing board of the school district, the State Controller, the Superintendent of Public Instruction and the local district attorney.

## Scope and Procedures

The fraud investigation consisted of gathering adequate information regarding specific allegations, establishing an audit plan, and performing various audit test procedures to determine whether fraud occurred, and if so, evaluate the loss, determine who was involved, and determine how it occurred. During the interviews, FCMAT study team members asked questions pertaining to levels of authority to enter into contracts, governing board oversight, financial management policies and procedures, job duties and responsibilities, and questions related specifically to the After School Education and Safety Program Grant (ASES) after school program, SB 740 Charter Schools Facilities Grant and the Charter Schools Financing Authority Charter School Lease/Purchase Grant.

The primary focus of this review is to provide the Alameda County Office of Education and the district with reasonable assurances based on the testing performed that adequate management controls are in place regarding the charter schools reporting and monitoring of financial transactions and that fraud, misappropriation of funds or other illegal activities have not occurred. Management controls include the processes for planning, organizing, directing, and controlling program operations, including systems for measuring, reporting, and monitoring performance.

The FCMAT Team conducted sample tests of financial transactions and data to determine if fraud, misappropriation of funds or other illegal activities have occurred. Testing associated with this review is based upon sample selection and does not include the testing of the complete list of all transactions and records for this period. Sample testing and review results are intended to provide reasonable, but not absolute assurance as to the accuracy of the district's transactions and financial activity.

To accomplish the objectives of this audit, a number of audit test procedures were developed to provide an in-depth analysis and understanding of the allegations and potential outcomes. The team had access to the general ledger records from July 1, 2009 through December 31, 2011 but supporting documentation for many of the transactions was reportedly missing, including several construction contracts. Specifically, FCMAT performed audit tests related general ledger transactions, check disbursements, construction expenditures and facility lease agreements, including the following:

- Review the general ledger records from July 1, 2009 through December 31, 2011 for the three AIMS charter schools.
- Extrapolate records pertaining to the ASES program, facility grants, leases, rents, financial recordkeeping charges, wages, and other records that are deemed questionable.
- Compile check disbursements entries consisting of approximately 600 individual records.
- Review the available supporting documentation.
- Extrapolate credit card payments relating to 34 credit card statements.
- Compile approximately 100 individual credit card transactions.
- Analyze supporting documentation for credit card transactions.
- Compile Federal Form 1099 and federal Form 1096 over the audit period.
- Review the charter schools' fiscal policies and procedures.
- Review the charter schools' petition documents and assurances.
- Review the governing board minutes.
- Analyze the charter schools' compliance with laws and regulations relating to conflict of interest and the Political Reform Act.
- Review the charter school's internal control process and procedures to determine possible weaknesses in prevention and detection of fraud, misappropriation and/or criminal activity.

The following findings and recommendations are the result of the audit procedures and review performed.



# Findings and Recommendations

## Occupational Fraud

The owners, executives, managers or employees of an organization may commit occupational fraud, which has three primary classifications: schemes related to asset misappropriation, corruption, and financial statements.

Asset misappropriation frauds include cash skimming, falsifying expense reports and/or forging company checks. Corruption schemes involve an employee(s) using his or her influence in business transactions to obtain a personal benefit that violates that employee’s duty to the employer or the organization; conflicts of interest fall into this category. Financial statement fraud includes the intentional misstatement or omission of material information in the financial reports.

Occupational fraud is one of the most difficult types of fraud and abuse to detect; however, the most common method of detection is receiving tips, which accounts for three times the number of any other fraud prevention method for this type of scheme. According to the “2010 Report to the Nations” conducted by the Association of Certified Fraud Examiners (ACFE), corruption schemes accounted for 21.9% of the 1,843 reported cases with a median loss of \$485,000. There is a direct correlation between the perpetrator’s position and authority in the organization and the losses incurred. Owners and/or executives losses are three times higher than those from managers and nine times higher than losses incurred by the employees within the organization.

The integral relationship and common management between the founder, his wife, their private businesses and the AIMS charter schools create an environment that allowed access, opportunity and motivation for occupational fraud to occur.

## Internal Control Elements

Internal controls are the principal mechanism for preventing and/or deterring fraud or illegal acts. Illegal acts, misappropriation of assets or other fraudulent activities can include an array of irregularities characterized by intentional deception and misrepresentation of material facts. Effective internal control processes provide reasonable assurance that a charter school’s operations are effective and efficient, that the financial information produced is reliable, and that the organization operates in compliance with all applicable laws and regulations.

Internal control elements provide the framework for an effective fraud prevention program. An effective internal control structure includes the policies and procedures used by staff, adequate accounting and information systems, the work environment and the professionalism of employees. An effective internal control structure includes the five interrelated components of the control environment, fraud risk assessment, control activities, information and communication, and monitoring.

<b>Internal Control Element</b>	
<b>Control Environment</b>	Commonly referred to as “the moral tone of the organization,” the control environment includes a code of ethical conduct; policies for ethics, hiring and promotion guidelines; proper assignment of authority and responsibility; oversight by management, the board or an audit committee; investigation of reported concerns; and effective disciplinary action for violations.
<b>Fraud Risk Assessment</b>	Identification and assessment of organization’s objectives to establish and develop a strategy to react timely.
<b>Control Activities</b>	The development of policies and procedures to enforce the governing board’s directives. These include the actions by management to prevent and identify misuse of the district’s assets, including the prevention of override of controls in the system by any employee.
<b>Information and Communication</b>	The establishment of effective fraud communication. This includes ensuring that employees receive information regarding policies and opportunities to discuss ethical dilemmas. Establishing clear lines of communication in an organization to report suspected violations.
<b>Monitoring</b>	Ongoing monitoring that includes periodic performance assessments for fraud deterrence by managers and employees.

Examples of improper internal controls include, but are not limited to, the following:

- Failure to adequately segregate the duties and responsibilities of authorization.
- Failure to limit access to assets or sensitive data.
- Not recording transactions, resulting in lack of accountability and the possibility of theft.
- Unauthorized transactions, resulting in skimming, embezzlement or larceny.
- Lack of monitoring or implementing internal controls by the governing board and management.
- Collusion among employees where little or no supervision exists.

A system of internal controls consists of policies and procedures designed to provide the governing board and management with reasonable assurance that the organization achieves its objectives and goals. Traditionally referred to as hard controls, these include segregation of duties, limiting access to cash, management review and approval, and reconciliations. Other types of internal controls include soft controls such as management tone, performance evaluations, training programs, and maintaining established policies, procedures and standards of conduct.

The internal control environment is a critical component since it establishes the organization's moral tone, commonly referred to as "the tone at the top." The tone at the top is an intangible internal control element that consists of the perception of an organization's employees in regarding the ethical conduct displayed by the governing board and executive management.

A strong system of internal controls that consists of all five elements can provide reasonable, but not absolute assurance that the organization will succeed in achieving its goals and objectives. The failure to establish adequate internal controls limiting the founder's ability to access assets coupled with a lack of accountability to the governing board created an environment for fraud and misappropriation to occur.

## Conflict of Interest

A conflict of interest exists when an individual who has a private financial interest in the outcome of a contract or a public decision and does either of the following:

1. Participates in the decision-making process, or
2. Influences, or attempts to influence, others making a contract or decision.

Statutes that govern conflicts of interest include the Political Reform Act, Government Code 1090, Government Code 87100, and Corporations Code Section 5233 for nonprofit organizations. Governing board members and administrators should abstain from all discussions, negotiations and votes that are related to a contract in which they have a personal financial interest by removing themselves from the meeting and ensuring that abstention and departure are recorded in the board minutes. A conflict of interest can still exist with subsequent action on the contract, such as authorizing payment under a contract, negotiating disputes or contract terms; therefore, the governing board member or administrator should abstain from all discussions, negotiations and/or votes related to the contract in which he or she has a personal interest.

The report will demonstrate that conflict of interest in multiple transactions allowed the founder and his spouse to gain financially.

## Political Reform Act – Disclosure, Conflicts of Interest and Enforcement

The Political Reform Act (PRA), Government Code Sections 81000 -91014, was enacted by Proposition 9 in June 1974. The stated intent of the act was to establish a process for most state and local officials as well as certain designated employees to publicly disclose their personal income and assets as follows:

[a]ssets and income of public officials which may be materially affected by their official actions...[are] disclosed and in appropriate circumstances the officials...[are] disqualified from acting in order that conflicts of interest may be avoided.

The PRA provisions are enforced by the Fair Political Practices Commission (FPPC) and require every state and local governmental agency to adopt a conflict-of-interest code. The commission is the state agency responsible for interpreting the provisions of the law and issuing California Form 700 – Statement of Economic Interests. Because charter school governing board members are considered “public officials” and governing boards are considered “legislative bodies,” board members and certain designated individuals must file Form 700 annually, or upon taking office/position. Additionally, some consultants to the organization “who makes, participates in making, or acts in a staff capacity for making governmental decisions” may be required to complete Form 700.

PRA provides an eight-step process to determine whether a conflict of interest exists as follows:

1. Is the individual a public official?
2. Is the public official making, participating in making, or influencing a governmental decision?
3. Does the public official have one of the six qualifying types of economic interests? (An economic interest will be discussed more fully in the next section of this report.)
4. Is the economic interest directly or indirectly involved in the governmental decision?
5. Will the governmental decision have a material financial effect on the public official’s economic interests?
6. Is it reasonably foreseeable that the economic interest will be materially affected?
7. Is the potential effect of the governmental decision on the public official’s economic interests distinguishable from its effect on the general public?
8. Despite a disqualifying conflict of interest, is the public official’s participation legally required?

Until most recently, the AIMS governing board members, charter school officials, designated employees and certain consultants had never filed Form 700, and designated employees as well as consultants that meet the conditions previously identified have not filed them to date. Although the charter petition contains a conflict-of-interest-policy, it is not technically in effect because the code must go through several steps including a 45-day public review and approval by the county board of supervisors.

## **Government Code 1090 – Financial Interest of Public Officials, Officers and Employees**

Simply stated, the intent of Government Code 1090 (section 1090) is to prohibit a public official, officers and employees from engaging in a contract in which he or she has a financial interest in both a governmental and personal capacity.

Section 1090 has broad implications, applies to school districts and can also apply to charter schools if included in the charter petition or the memorandum of understanding. Section 1090 provides as follows:

Members of the Legislature, state, county, district, judicial district, and city officers or employees shall not be financially interested in any contract made by them in their official capacity, or by any body or board of which they are members. Nor shall state, county, district, judicial district, and city officers or employees be purchasers at any sale or vendors at any purchase made by them in their official capacity.

As used in this article, “district” means any agency of the state formed pursuant to general law or special act, for the local performance of governmental or proprietary functions within limited boundaries.

The AIMS charter petition states the governing board’s intent to abide by Oakland Unified School District’s policies and regulations regarding ethics and conflicts of interest and in addition has adopted its own conflict-of-interest policy.

This report will establish that a business relationship exists between the founder and the AIMS schools as evidenced by contracts, lease agreements and consulting arrangements. There is conclusive documentation to support that the founder and his spouse have significant personal involvement and financial interest, violating the conflict of interest statutes.

# Related-Party Transactions and Significant Influence

## After School Education and Safety Program Grant

Proposition 49 passed in 2002 and authorized the After School Education and Safety program (ASES). ASES is a before- and after-school program that provides tutoring, homework assistance and educational enrichment for elementary and middle school students grades K through nine. The program's intent is to provide additional academic assistance to children in a safe and educational environment during nonschool hours, and promote partnerships and collaboration between students, parents, educational agencies, local public agencies, community-based organizations, and the private sector. The grant funds are intended to supplement, not supplant, existing levels of service for students.

Beginning with the 2004-05 school fiscal year, the ASES program expanded eligibility and created several operational requirements, including minimum staff qualifications, pupil-to-staff ratio maximums, a nutritious snack provided daily, and minimum operational hours. Highlights of these requirements include the following:

- Staff members who supervise pupils must meet minimum qualifications; hiring requirements; health and fingerprint clearances.
- The pupil-to-staff ratio must be no more than 20-to-1 (EC 8483.)
- A nutritious snack must be provided daily to students in the program and must meet standards in EC 49430.
- The program is to operate a minimum of 15 hours per week and until at least 6 p.m. daily. The program must begin immediately following the end of the school day and operate every school day during the regular school year for at least five days per week and three hours per day.

The program requires the grantee to provide a safe environment that consists of literacy and educational enrichment components that reinforce and expand the content of the regular school day. The literacy component must provide tutoring and/or homework assistance for at least one of the core academic subjects of math, language arts, history, social sciences, or science. The educational enrichment component must offer activities that support and complement the school's programs. Activities to satisfy this component can include arts, physical activity, recreation, community service-learning, work preparation, career awareness, or other youth development activities.

ASES grants are renewable and funded for three years. The allocation for after-school programs is \$7.50 per student per day with a legislation-established annual funding cap of \$112,500 for elementary schools and \$150,000 for middle schools/junior high. Therefore, full funding is achieved at 15,000 student attendance days for elementary and 20,000 student attendance days for middle school/junior high.

At a minimum, 85% of the funds must be allocated to direct services, and up to 15% of the grant can be used on administrative costs. Administrative costs include indirect cost (maximum 5%), teacher training and program administration.

EC 8483.75 requires each program to provide a local matching contribution of cash or in-kind services equivalent to \$1 matching for every \$2 in total grant funding. No more than 25% of the local match contribution can be from facilities. The following website has useful suggestions in making the match and program compliance: <http://76.12.61.196/publications/MakingTheMatch.pdf>.

The Legislature intended that elementary students attend the program daily and middle school/junior high student a minimum of nine hours and three days per week. Enrollment priority is to be given to students who attend daily. To be counted for a day's attendance, students must attend at minimum half the day's program hours. The grantee must develop an early release policy for students who are unable to attend the program until the end of the day and a policy for late arrival to the program.

Grantees are required to submit an annual budget, quarterly expenditure reports, semiannual attendance reports, and an annual evaluation report to the California Department of Education (CDE). These reports are used to monitor compliance and in the consideration for grant renewal.

Expenditure reports are required to be submitted quarterly. The CDE warns that untimely submission will delay future payments and possible invoicing for unexpended funds, and these must be returned to the CDE.

Attendance reports are required to be submitted semiannually. Untimely submission of the report may be cause for withholding of grant payments. Daily sign-in and -out sheets must be maintained to provide records for compliance auditing. These records should be reconciled with monthly attendance and must be maintained for five years after the end of the grant.

If the CDE determines that the program does not comply with the reporting requirements as established, the grant may be terminated.

As the fiscal agent for three charter schools, American Indian Public Charter School II applied for three ASES grants of \$150,000 each: AIPCS II, East Oakland Leadership Academy (EOLA) and Conservatory for Vocal/Instrumental Arts Charter School (COVA.) EOLA and COVA are partnership charter schools also located in the Oakland area authorized by the Oakland Unified School District. OASES, a private company owned by the founder, provides the oversight for the EOLA and COVA programs in exchange for the 15% oversight fee although there are no board minutes available authorizing OASES to provide this service in behalf of AIPCS II.

AIPCS II received a notification dated September 27, 2010 of the award totaling \$450,000 for July 1, 2010 through June 30, 2011. As a condition of the funding release, AIPCS II agreed to the grant terms and conditions, including 11 that were noted on the grant award letter and 45 assurances as certified on the ASES application. However, FCMAT found numerous violations.

Program requirements mandate that the program operate at a minimum of 15 hours per week and stay open until 6 p.m. each regular school day. However through documentation and interviews with staff, FCMAT found several discrepancies and conflicting information regarding the hours of operation, including the following:

- A survey memo dated July 7, 2011 from the AIPCS II site coordinator to parents offered the after-school program at AIPCS II from 3:30 p.m. to 6 p.m. Monday through Thursday, and from 12:20 p.m. to 4 p.m. Friday, a total of 13 hours and 40 minutes per week.

- An October 12, 2011 memo from the ASES site coordinator to parents stated the ASES program runs from 2:30 p.m. to 6 p.m. Monday to Thursday and from noon until 6 p.m. on Friday. These meet the hours per week required by the grant.
- Another memorandum dated October 25, 2011 stated that beginning October 31, 2011, hours of operation would be 3:15 p.m. to 5:45 p.m. Monday through Thursday and 1 p.m. to 3:15 p.m. on Friday.
- Student rosters identified “time out” between 3:50 p.m. and 5:45 p.m. Monday to Thursday and 1:30 p.m. to 3 p.m. on Friday.
- Student sign-in sheets show “out” times between 4:15 p.m. and 5:45 p.m. Monday through Thursday and 12:40 p.m. and 3:15 p.m.

The ASES site coordinator should ensure that the hours of operation meet the grant requirements and are consistent with memorandums sent to parents.

On October 12, 2011, the ASES site coordinator sent a survey memo to parents of students in the After School Nutrition Program inquiring about program participation and requesting information about food allergies. The memo stated that “food will be provided free of charge to any student participating in the After School Program after (emphasis added) 5:00 PM.” This is clearly against grant regulations. EC 8482.3(d) requires the after school program to provide a daily nutritious snack to all program participants, yet expenditures for supplies including food are not sufficient to support students being provided with a nutritious snack. Records show that \$1,903.65 was expended in 2010-2011, and \$1,368.86 has been expended for seven months in the current fiscal year. The ASES site coordinator should ensure that all students are offered a free nutritious snack in accordance with the Education Code, and OASES should provide proper oversight that all programs requirements and assurances are followed at each site.

December 17, 2009 board meeting minutes for after school programs report activities such as a Math Counts competition, TechBridge, a spelling bee, music and choir. These programs existed before the ASES award; therefore, any expenditure for activities from these programs charged to the ASES program is considered supplanting. In May 2011, the ASES program recorded an expenditure of \$13,500 to Tech Bridge. Specific expenditures classified as music are also questionable and should be reversed and charged to the appropriate cost center.

As of February 28, 2012, the CDE reports that AIPCS II had not submitted its second quarter 2011-12 expenditure report, which was due by January 31, 2012. As stated previously, the untimely submission of expenditure reports may delay payments and be cause for invoicing for unexpended funds.

EOLA and COVA are subrecipients to the ASES grant administered by AIPCS II; however, the founder operated the subrecipient programs from his personal business, OASES, on behalf of AIPCS II and collected the administrative fee as part of the arrangement.

The term of the contract between AIPCS II and EOLA was from October 6, 2010 to July 31, 2011 and provided for after-school educational programs and services to 115 students. The hours of operation for this program are 2:30 p.m. to 6 p.m. on regular school days. The contract outlines program requirements that align with the ASES grant provisions, including supplanting and administrative cost considerations. The contract states that AIPCS II will pay EOLA the total not to exceed \$93,000 for services related to the ASES; however, 85% of the grant is required to be spent on direct services; therefore, the correct amount of the contract should have been \$127,500. According to the founder, the error was caught during the summer of 2011,

but the refund of \$34,500 was not made until January 12, 2012, more than 15 months after the original award.

Similarly, the agreement with COVA stipulated the amount to be paid as \$105,000 when a total of \$127,500 was due. The founder again claims that the error was not discovered until the summer of 2012 and the refund of \$22,500 was not made until January 28, 2012, more than 15 months after the original award.

The founder concurs that a total of \$105,000 was originally paid to his private company, OASES, for the administrative functions and oversight for the EOLA and COVA programs totaling 35% of the grant proceeds, \$60,000 more than the maximum 15% allowable.

As previously mentioned, EC 8483.75 requires a local match equivalent to one-third of the grant award. For AIPCS II, the total grant was \$150,000 for 2010-2011; therefore, the required match is \$50,000. Of this amount, only 25% (or \$12,500 for this grant) can be attributed to in-kind facilities. The team requested information on the local match and received the following response:

The ASES program's local match requirement is, in part, met by AIPCS II's facilities donation, whereby all facilities needs are provided free of charge from 2:30 pm to 6:00 pm Mondays through Thursdays and 12:30pm to 6:00pm on Fridays. The value of this in-kind contribution easily exceeds the 25% (\$12,500) maximum allowed by the program each year.

No further local match supporting documentation was provided or is identified in the accounting records. Absent further document to support the local match other than the \$12,500 listed above, the program is out of compliance.

FCMAT found no evidence of program oversight by OASES to ensure that the terms, conditions and assurances were followed in accordance with the grant provisions. Attempts to verify program compliance with EOLA and COVA for hours of operation by the new AIMS coordinator were unsuccessful as of March 20, 2012.

Memos to parents, attendance rosters, planning sheets, and discussion with the site staff lead FCMAT to believe that the hours of operation do not meet the requirements of the grant. These documents show that snacks were provided based on attendance but only to a minority of the students. Expenditures for food items were not enough to provide snacks for all students as required. AIPCS II is not current on its reporting to the CDE. Expenditures do not reflect the required 85% direct services and 15% maximum administration expense. Lastly, there is no evidence that AIPCS II has met the local match requirements.

A series of interviews, observations and document reviews indicated that the program coordinator and founder are aware of the requirements and assurances confirmed with the acceptance of the grant. However, FCMAT found numerous incidences where practices did not meet the program assurances. AIMS administration of the ASES program is inadequate and, absent further clarification and support, out of compliance.

The founder exercised significant influence over program decisions and information that was shared with the board. The decision to allow the founder to receive the 15% oversight fee was never clearly communicated to the governing board. According to the founder, board minutes and agendas are missing and presumed to have been stolen. The FCMAT study team obtained some board minutes from the charter schools office and other outside sources, and those regarding the ASES grants indicate there was little discussion about programs requirements,

terms, conditions, assurances or alternatives methods to oversee the program by the existing AIMS staff. The founder stated in his interview with FCMAT that during the grant period, he spent much of his time working on his farm in North Carolina and was “completely removed” from the AIMS organization but acting as an advisor emeritus.

The governing board has a fiduciary responsibility and duty to oversee the AIMS charter schools’ operations. The board, however, did not establish and maintain proper internal controls, policies and procedures, which allowed the founder to engage in contractual arrangements subject to conflict-of-interest prohibitions and misappropriation of assets. The founder had a separate fiduciary duty to abstain from entering into a self-dealing and for-profit arrangement. Instead, in contracts with EOLA and COVA, the founder positioned himself to make \$45,000 through AIPCS II as the “fiscal agent,” having exercised considerable influence by negotiating and executing a public contract in direct violation of Government Code Section 1090 conflict-of-interest laws. As evidenced with the management of these grants, there was no functional separation between the public and private interests as several businesses owned by the founder and/or his spouse conduct business with AIMS charter schools. These two individuals managed the finances, signed commercial warrants, authorized purchases and executed binding contracts without effective board oversight that eventually blurred the distinction between the public and private functions and interests.

### **Stanford Academy Institute of Learning Summer Math Institute**

The Stanford Academic Institute of Learning Summer Mathematics Institute (SAIL) is a privately operated three-week accelerated math, language arts, and physical fitness program owned by the founder and operated by a former board member. The purpose of the SAIL program is to ensure that all students are confident in their academic skills when they begin the math curriculum. Students spend six hours a day enhancing their algebra, geometry, algebra II, and language arts skills, allowing them ample time to master the material. They are also enrolled in a physical education course, in which they train for the national physical fitness test to develop anaerobic and aerobic fitness ability.

In reviewing various sources of information, FCMAT found that the SAIL program is inappropriately promoted and supported. In addition, the program establishes fees for nonattendance, which is a violation of the California Code of Regulations, Title 5, Section 350, which states the following: “A pupil enrolled in a school shall not be required to pay any fee, deposit, or other charge not specifically authorized by law.” (Article IX, Section 5 of the California Constitution. Fiscal Management Advisory 11-01, November 9, 2011.) While charter schools are exempt from most laws governing school district (Ed. Code Section 47610), a free school guarantee by the California Constitution applies to all schools including charter schools. According to the staff handbook, it is mandatory for students going into sixth and eighth grades to attend SAIL or an alternative math program approved by the site administrator. Several references throughout the AIMS family handbook include language about summer programs that, according to Education Codes 47605(d) and 37252.2, should be voluntary with limited exceptions:

*We require* (emphasis added) participation in an approved summer school program or course of study.

Summer School: Students *must successfully complete mandatory* (emphasis added) summer school. The school has the ability to approve particular programs.

Students *must attend school* (emphasis added) each day on time. This includes summer school and required summer intensive programs like SAIL.

In a memorandum to families from the executive director (edited by the founder) dated May 23, 2011, parents/guardians were notified that their student was “awarded a scholarship” to attend the SAIL program. The program operated from July 18 to August 5, 2011 and parents/guardians notified that a fee of \$50 per day would be assessed for any absences. The telephone number listed on the memorandum for any questions is registered to the founder in North Carolina.

Board meeting minutes support the promotion of SAIL through board action, communication, and scholarships. The following are excerpts and references from AIMS board minutes:

March 24, 2011: “Sending all 8th graders and bottom 2 low 6th grades to SAIL.”

December 2009: “The SAIL program was very effective at AIPCS” and that the program was being extended to AIPCS II.

January 12, 2010, Emergency board meeting: “board approve AIPCS, AIPCS II, and AIPHS spending of \$500 for each student to attend SAIL Summer Program.”

Mandatory attendance in SAIL is illegal. Ed Code 47605(d) states that supplemental programs such as SAIL can be required only for a student that has been retained. Outside of this requirement, the charter school “shall provide a mechanism for a parent or guardian to decline to enroll his or her child in the program.”

The charge that would be assessed for missing a day at SAIL is also not allowable. The California Code of Regulations Title V section 350 states: “A pupil enrolled in a school shall not be required to pay any fee, deposit, or other charge not specifically authorized by law” and there is no statute that authorizes charging for missed attendance.

Additionally, FCMAT found that other summer program choices were not actively promoted or supported financially similarly to the SAIL program. This gives the perception that the SAIL summer program is promoted for personal gain and to funnel money from the school accounts to support scholarships. The founder told the FCMAT study team that former students teach the SAIL program. Instead of wages, these students receive scholarship money to attend college as several are undocumented and cannot apply for financial aid.

The SAIL program charged the AIMS charter schools \$500 per student. According to the federal form 1099 and the general ledgers the following amounts were paid to SAIL:

### **AIMS Charter Schools**

#### **Payment to SAIL Summer Programs**

#### **Fiscal Year 2009-2010 through December 31, 2011**

<b>Year</b>	<b>Amount Paid To SAIL</b>
<b>2009</b>	\$136,500
<b>2010</b>	\$177,000
<b>2011</b>	\$144,500
<b>Total</b>	\$355,000

Because the founder and his spouse serve in many different capacities that have significant influence over financial transactions, there is a lack of functional separation between the public and private interests. The integral relationship and common management between the founder, his wife, their private businesses and the AIMS charter schools create an environment that allowed access, opportunity and motivation for occupational fraud to occur. Lack of oversight, internal controls, policies and procedures greatly enhance the possibility that conflicts of interest and fraud may have occurred and will continue to occur.

The governing board should implement appropriate internal control systems that include proper separation of duties and limits access to the school's assets; creates and monitors policies and procedures for all employees to follow. Additionally, the board should require completion of Form 700 with the full disclosure of business interests annually and retain from entering into agreements with designated employees, former directors and other individuals that may have a personal financial interests.

## Facility Grant Programs

### SB740 and Facilities Incentive Grant

FCMAT reviewed the AIMS charter schools application for funds received from the California Department of Education's Charter School Facility Grant Program (SB 740) to determine if fraud, misappropriation of funds or other illegal activities have occurred during the current and subsequent two fiscal years. During this review, the FCMAT study team discovered that AIMS also receives facility funding from federal grant program called the Charter School Facilities Incentive Grant Program. FCMAT reviewed both funding sources as part of this specific scope item.

It is common for these two grant programs, one federal and the other state, to complement each other if a charter school is eligible to receive both. While it is permissible for charter schools to apply and receive funds from both programs, charter schools that receive grant funds authorized under either may not receive funding that is more than 75 percent of annual lease costs for any one school year.

SB 740 is a noncompetitive grant enacted in 2002 and codified in EC 47614.5 that provides assistance to charter schools with facility rent and lease expenditures in low-income areas if they meet specific eligibility criteria. This program is specifically targeted toward schools and communities with high proportions of economically disadvantaged students. To qualify they must meet the following criteria:

1. Eligible applicants must have at least 70 percent of students enrolled at the charter school who are eligible for free or reduced-price meals, or
2. The charter school must be physically located in an elementary school attendance area where at least 70 percent of students enrolled are eligible for free or reduced-price meals, and
3. The charter school must give a preference in admissions to students who reside in the elementary school attendance area.

The maximum annual grant award is based on "lesser of the two" calculations, as follows:

**Calculation Test #1** A per-pupil grant of \$750 for lease or rent per unit of average daily attendance as certified at the second principal apportionment by CDE, or

**Calculation Test #2** An amount up to, but not more than 75% of a school's annual facilities costs for lease or rent.

The program funds were historically used to reimburse eligible charter schools for their prior-year facilities rent and lease expenditures; however, beginning with fiscal year 2009-10, the state superintendent of public instruction allocates the facilities grants to eligible charter schools on a current-year basis. Funding appropriated in fiscal year 2010-11 is first required to be used to reimburse eligible charter schools for 2009-10 rent or lease costs, and then to fund eligible charter schools for fiscal year 2010-11.

FCMAT verified the grant amounts were awarded to the three AIMS charter schools from the actual funding source for the years 2009-2010 through 201-2012. For 2011-2012, the final allocation is not listed on the website; only the advanced funding allocations. FCMAT verified the grant amounts received to the charter schools' general ledger for years 2009-10 through 2011-2012 through December 31, 2011 and found no variances except that the amount received for the current fiscal year and recorded in the charter schools' general ledger was more than reflected on the website for the advance apportionment. This often means that the most current allocations have not yet been posted on the state's website. The table below lists the grant awards received in the prior two fiscal years and advanced apportionment for the current fiscal year.

### **AIMS Charter Schools**

#### **SB 740 Funding Allocations Received**

##### **July 1, 2009 through December 31, 2011**

<b>Fiscal Year</b>	<b>2009-2010</b>	<b>2010-2011</b>	<b>2011-2012</b>
<b>AIPCS</b>	\$96,698	\$140,798	\$65,538
<b>AIPCS II</b>	\$113,715	\$104,056	\$87,128
<b>AIPHS</b>	\$88,628	\$78,908	\$90,276

#### **Charter School Facilities Incentive Grants Program**

The Charter School Facilities Incentive Grants program started in 2001 under the U.S. Department of Education, State Charter School Facilities Incentive Grants Program (CFDA Number: 84.282D). These are federal grants administered through the California School Finance Authority based on preference points for eligible applicants. Approximately 20 to 25 competitive grants are issued annually to California charter schools. The authority was created in 1985 to oversee the statewide system for the sale of revenue bonds for the acquisition of new school sites and buildings and the reconstruction, remodeling, and replacement of existing facilities. The authority also assists school districts, community college districts, county offices, and charter schools by providing access to financing for working capital and capital improvements. Since its inception, the authority has developed a number of school facilities financing programs and most recently focused on assisting charter schools to meet their facility needs.

The purpose is to assist charter schools by providing facility funding for rents, leases, renovation, leasehold improvements and facility purchase. These grants provide an incentive for states to share in the costs of funding charter school facilities as they often do in funding the capital costs of regular public schools.

The grant period is a maximum term of five years. The maximum federal share of the cost of establishing, or expanding, and administering the program decreases each fiscal year of the program, starting at no more than 90% in the first year; no more than 80% in the second year; 60% in the third; 40% in the fourth; and no more than 20% in the fifth year. States may reserve up to 5% of grant funds for administrative expenses, including indirect costs, to carry out evaluations, provide technical assistance and disseminate information. Priority is given to states with charter authorizers that conduct a periodic review and evaluations of charter schools at least once every five years, as well as perform all the following:

- Demonstrate progress in increasing the number of high-quality charter schools.
- Provide for a charter authorizer that is not a local educational agency (LEA), or, if LEAs are the only authorized public chartering agencies.
- Allow for an appeals process.

- Ensure that charter schools have a high degree of autonomy over their budgets and expenditures.

In addition, states receive priority based on the capacity of charter schools to offer public school choice to communities most in need of educational options with the following factors considered:

- The extent to which the applicant would target services to geographic areas in which a large proportion or number of public schools have been identified for improvement, corrective action or restructuring under Title I of ESEA, as amended;
- The extent to which the applicant would target services to geographic areas in which a large proportion of students perform poorly on state academic assessments; and
- The extent to which the applicant would target services to communities with large proportions of low-income students.

In the 2004 fiscal year, the program awarded \$18.7 million in first-year funding for the first cohort of grantees, including California, Minnesota, Utah and the District of Columbia. Ongoing annual awards were made to these four grantees through the 2008 fiscal year, with aggregate awards totaling \$78 million over the five-year period. In the 2008 fiscal year, the program awarded \$12.7 million in first-year funding for a second cohort of grantees, including California and Indiana. Ongoing annual awards will be made to these two grantees through the 2013 fiscal year, bringing the program's award totals to \$139 million.

Charter schools that receive these federal grant funds through their state are required to use them to pay for current and future facilities costs for up to three years. Allowable expenditures include the following:

- Paying rent or lease costs,
- Purchasing or acquisition of a school building,
- Purchasing land if the land is included in an allowable building purchase or if the charter school has immediate plans to construct a building on the land,\*
- Design and/or constructing a school building,
- Renovating an existing school facility,
- Making leasehold improvements,
- Paying debt service or a mortgage on a new or existing school facility (unless restricted by state or local law. They may also be paid into the account of a third party or trustee who in turn makes debt service payments for facilities on behalf of charter schools),
- Paying Proposition 39 pro-rata payments for existing or new facilities.

*\*Because charter schools are permitted to use these grant funds for acquiring facilities, a charter school may use grant funds to purchase a building and the land on which it is located. However, charter schools may not use these grant funds for purchasing land when they have no immediate plans to construct a building on that land because land alone does not meet a charter school's building infrastructure needs. 34 CFR 226.21(b).*

Awards may not be used to reimburse a charter school for costs incurred before the date the grant is awarded and may not be used toward the same debt or project (purchase, construction or renovation) related to a project designated in a prior grant award. In addition to documented evidence of an existing lease, rent, mortgage or debt obligation annual ongoing costs associated

with a charter school facility, the authority reserves the right to evaluate prior year's facilities costs to determine eligibility for the current funding round.

Grant funds may also not be used to perform the following:

- Supplement a new construction project funded through the Charter School Facilities Program, or
- Make Charter School Facilities Program payments to the state, or
- Satisfy a Charter School Facilities Program recipient's local matching share.

When funds from this program are used for construction-related activities costing more than \$2,000, such as constructing a school building, renovating an existing school facility, or making leasehold improvements, any laborers and mechanics employed by contractors or subcontractors on the projects assisted with these federal funds are required to be paid in accordance with prevailing wage requirements as determined by the secretary of labor in accordance with subchapter IV of chapter 31 of title 40 of the United States Code (commonly called "Davis-Bacon and related acts"). All charter schools that receive an award of these grant funds are also required to meet all applicable federal, state, and local health and safety requirements.

Additionally, subgrantees must abide by CSFA Section 10190, Audits and Conflicts of Interest, which states the following:

subgrantees must avoid apparent and actual conflicts of interest when administering grants from the U.S. Department of Education. Department regulations at 34 CFR 75.525(a) *prohibit a person from participating in an administrative decision regarding a project if (a) the decision is likely to benefit that person or his or her immediate family members* (emphasis added); and (b) the person is a public official or has a family or business relationship with the subgrantee. Section 75.525(b) provides further that a subgrantee may not permit *any person participating in a project to use his or her position for a purpose that is – or gives the appearance of being – motivated by a desire for a private or financial gain for that person or for others* (emphasis added).

The founder owns one building and is the lessor to AIMS schools on the other building. A conflict of interest exists as the founder has participated in the administrative decision to enter into rental/lease agreements and used his position for private and financial gain. In addition, these agreements clearly give the "appearance" of a conflict of interest in violation of CSFA Section 10190 and 34 CFR 75.525(a).

FCMAT reviewed applicable websites to obtain grant amounts for the charter school. The state website includes information on how the different grant recipients were scored, and what the grant can be used for, but does not contain specific grant information on the amount awarded. Therefore, the amounts in the table below are those recorded in the charter schools' general ledger and have not been verified through CSFA independently.

The amounts received by individual charter school, per the general ledger, for the three years requested in the study agreement are as follows:

Fiscal Year	AIPCS	AIPCS II	AIPHS
2009-10	\$23,436	\$98,120	\$76,870
2010-11	\$120,620	\$117,744	\$92,244
July 1, 2011 through December 31, 11	\$60,310	\$49,060	\$46,122

The charter school's application requested the grant funds for rent, lease, mortgage or debt service payments. The application agreement and certification signed as part of the application states that the applicant may be required to return all or a portion of the grant funds including any investment earnings if the applicant fails to use the funds as approved and/or fails to meet grant regulations. CSFA Section 10186 states that: "Grant funds shall only be used in the manner prescribed in the application, unless the Authority, pursuant to Section 10186, approves a change in writing." Applicants also certify that interest will not be earned on these federal funds and that they will comply with A-133 audit requirements, with a single or program specific audit to be provided to the authority.

Because these funds supplement the lease costs for each site and the lease payments are paid to the founder's companies the governing board should ensure that all grant regulations, particularly CSFA 10190, are followed.

## Credit Card Transactions

FCMAT observed general ledger charges for credit card transactions and requested supporting documentation based on detailed credit card statements. The team reviewed a sample of 34 credit card statements from 2009-2010 through December 31, 2011 that revealed numerous expenditures lacking support documentation or board authorization. Several different credit cards are used, and all credit cards are in the founder's name. The founder's personal and unrelated business expenses are comingled with purchases for the AIMS schools.

The team examined credit card statements showing that charges between the founder's personal business and that of the AIMS schools were sporadically itemized before the payment was prepared by the bookkeeper, the founder's spouse. Some charges are initialed by site administrators authorizing the charges to a particular school site; however, numerous charges to schools are not signed by a site administrator and have no support documentation, according to the business office (see table below.) FCMAT found one occasion where a limited number of expenditures in the prior month were listed in the board minutes.

Many purchases were questionable. The listing below shows that several purchases are charged to school accounts that originated from Lumberton, North Carolina where the founder has a farm. For example, a North Carolina Farm Bureau Insurance premium for \$298 was charged to AIPCS. Many other charges to school accounts include airfare and car rental; hotels, restaurants; and general merchandise stores from locations in Washington, DC; Myrtle Beach, South Carolina; Arizona; and Lumberton, North Carolina. Many of these charges were made during a period of time that the founder was not employed by AIMS or member of the board and "had nothing to do with the school."

Other examples include charges for San Francisco Giants tickets, DIRECTV and Amazon purchases. The current administration claims that many of the Amazon charges are for textbooks, but that the supporting documentation for many for these expenditures is missing.

Several charges were incurred in Arizona where the founder, business associates, and board members have petitioned to open and operate a charter school. Several expenses related to this endeavor have been charged to AIMS school accounts. Expenditures for a start-up school in a different state should not be charged to AIMS school account since only expenditures that have a tangible benefit to the school are considered legitimate school charges once authorized by the governing boards, or a designee. Admission fees to universities for students totaling \$7,707 were paid from school funds even though these expenditures have no benefit to the school itself and

lack any authorization from the governing board. Subsequent to the FCMAT fieldwork, staff redirected these charges appropriately to the scholarship fund.

The FCMAT study team requested supporting documentation for the credit card transactions totaling \$72,602.28. The table below represents approximately 35% of the total requested transactions that lacked supporting documentation and therefore were inappropriate or lack proper authorization.

### AIMS Charter Schools

#### Credit Card Transactions Lacking Support Documentation

#### For the Fiscal Year 2009-2010 through December 31, 2011

Payee	Amount Paid From School Funds Lacking Support Documentation
Agri Supply Inc. – Lumberton, NC	\$ 30.68
AIRTRANAIR – Atlanta, GA	1,505.40
Amazon	5,889.99
Bank A Count Corp.	42.63
Becky's Chinese Restaurant	203.00
Ben & Jerry	128.78
Car rental to North Carolina	134.20
Delta Onboard	2.00
Diamond Shamrock - Tucson, AZ	20.45
Dollar General – Lumberton, NC	31.56
Domino's Pizza	39.78
DirecTV Service	359.46
Home Depot	758.06
Hotels.com	124.70
House of Produce	54.00
Jimmy's Seafood House - Lumberton NC	37.42
Lakeshore Natural Foods	24.69
Landmark Resort, Myrtle Beach, SC	279.11
Lou's Plumbing Supply - Tucson, AZ	686.63
Lowe's Foods - Lumberton NC	35.21
Not Identified - Missing pages from the credit card statement.	3,022.39
Outback - Lumberton NC	63.98
PayPal	52.01
Phnom Penh House	51.00
Pizza Hut	232.64
Sequel House Korean Restaurant	23.00
Smart & Final	1,450.15
Sundo Magnolia – Lumberton, NC	130.49
Take Sushi	17.51
TNT Deals	144.00
US AIRWAYS Chavis/Ben One way IAD/OAK	119.60
Waffle House, Lumberton, NC	27.00

Wal-Mart	249.31
Microtel Inn & Suites -Raleigh, NC	48.86
Virgin America	40.00
US Airways One way PHX/OAK	220.00
North Carolina Farm Bureau Insurance Premium	298.00
Lucky	92.06
OYA Restaurant - Washington, DC	71.00
Paper Moon	130.00
Ruby Tuesday - Washington, DC	73.00
Renaissance - Washington, DC	62.06
Advantage - Tucson, AZ	139.95
Not Identified - Breakdown not legible	6,975.53
Jet Blue - Chavis to Salt Lake, UT	109.70
Uncle Georges Restaurant – North Carolina	64.11
San Francisco Giants Tickets	295.00
Sports Scene - Atlanta, GA	11.62
Southwest Airlines TUS/OAK & LAX/OAK	7.50
Hertz Rent-a-car - Tucson, AZ	127.88
SCI Supply	21.40
Sears	26.64
Balance Transfer – (From Unknown Credit Card)	757.85
Pump It Up of Oakland	259.00
Grand Total – Charges to AIMS Schools	\$ 25,748.09

The above list clearly demonstrates that school funds were utilized for personal reasons and/or expenditures that do not benefit the school and may be in violation of the constitutional ban on gifts of public funds. The founder claims that he made several donations to the school scholarship fund account, but this does not negate the improper spending of school funds. Several of these expenditures were redirected to the scholarship fund subsequent to FCMAT's fieldwork. The founder has an agreement signed by the acting chair dated June 24, 2004 that specifically authorizes the use of these funds for student financial aid; maintenance or purchase of property; student incentives and family support.

Also listed in the agreement is a provision for payment of the founder's credit card expenditures. The governing board should clarify this provision of the agreement, which could violate IRS regulations if the tax deductible donation was used to pay the donor's personal expenses.

The governing board should develop policies and procedures that establish spending authority and ensure that all credit cards are in the name of the school. All transactions should be signed by authorized personnel and have supporting documentation that includes invoices and bills of lading.

## Prepaid Escrow

The FCMAT study team questioned a deposit of \$160,000 recorded in the general ledger that was classified as a "Pre-paid" expense refund and requested information regarding this transaction.

According to the current administration, Lumbee Holdings and AIPCS entered into a joint real estate transaction to purchase property located at 3050 International Boulevard, Oakland, CA. On January 7, 2009, a commercial warrant for \$190,000 was deposited in the Fidelity National Title escrow account and recorded in the books of account as “Pre-paid Escrow” and in the audit report as a “Security Deposit.”

On August 7, 2009, a \$160,000 check was deposited in the AIPCS account, and on August 31, 2009, an offsetting entry to a “Miscellaneous” expense account was charged \$30,000. The refund check to AIPCS from Fidelity National Title lists Lumbee Holdings LLC as the “buyer.”

The only supporting documentation provided for this transaction was an unsigned statement by LOH Real Estate Holding dated September 29, 2009 stating that the \$30,000 was a non-refundable deposit. Despite several requests for escrow instructions to support this transaction, including the original agreement between Lumbee Holdings LLC and AICPA, FCMAT has not received these documents.

Additionally, no evidence was provided to the FCMAT study team to support that a fully executed contract between Lumbee Holding LLC and AIPCS existed, or that the AIMS governing board was aware of this joint venture where the school lost \$30,000.

Using his position in the organization coupled with access to the checking accounts and a total lack of internal controls, the founder was able to circumvent the formal authorization process for personal financial gain. The governing board should ensure proper procedures and internal controls exist for all formal agreements and contracts to be authorized exclusively by the governing board and that federal procurement regulations are followed.

## Construction/Modernization Transactions

The FCMAT study team examined the general ledger entries for the AIMS schools construction activity covering the 2009-2010 fiscal year through December 31, 2011. During fieldwork, the team was unable to verify that the governing board had knowledge of the executed contracts or determine whether the board authorized the construction contracts because the board minutes and agendas were missing, according to the founder. Subsequent to the fieldwork, FCMAT received board minutes from third-party sources, but was unable to verify their authenticity.

Tracing construction transactions through the general ledgers provided evidence that the founder exercises significant influence over the schools’ transactions involving inter- and related-party transactions through a series of agreements and contracts in which he had a direct financial interest in violation of conflict-of-interest laws.

On June 22, 2006, two board members signed a modernization-project proposal from ADS for the AIPCS campus, the founder’s private business to upgrade restroom facilities totaling \$115,000. The founder signed this agreement on behalf of ADS and during this time, also acted as the director of AIMS schools. A review of the board minutes for April 21, 2006, August 17, 2006 and December 21, 2006 does not include any reference to this proposal or approval for a contract to the founder. Furthermore, the board minutes do not reflect that a disclosure was made declaring the founder’s personal financial interest and financial gain due his position as director and owner of ADS and as required by the conflict-of-interest statutes. As a result, violations of the conflict-of-interest statutes have occurred. The founder signed three commercial warrants relating to these projects totaling \$104,000 from the AIPCS checking account made payable to Lumbee Properties and/or ADS.

A second modernization proposal dated April 22, 2007 between AIPCS II and Lumbee Holdings to upgrade restroom facilities at 171 12th Street, Oakland, CA was signed by a representative of Lumbee Holdings, and two board members and totaled \$195,500. During this time, the founder was the director of AIMS schools. A review of the board minutes dated March 15, 2007, June 21, 2007 and September 20, 2007 does not include any reference to approval of a contract to Lumbee Holdings for this proposal. Furthermore, the board minutes do not show that a disclosure was made declaring the founder's personal financial interest and financial gain due to his position at the time as director and owner of Lumbee Holdings and as required by the conflict-of-interest statutes. As a result, violations of the conflict of interest statutes occurred.

FCMAT requested the construction contract(s) to support the transactions for these construction expenditures, but was informed that all the contracts related to these expenditures were missing. The team requested, but did not receive, contracts from the founder's personal business to support the commercial warrants paid to his companies. Instead, some sketch drawings and one permit application worksheet (attached as part of Appendix A to this report) were provided for FCMAT's review. Without proper supporting documentation and board approval, these expenditures are considered unauthorized.

AIMS schools provided check copies to support payments totaling \$348,500 made to the founder's private companies, ADS and Lumbee Holdings from September 2007 through March 2008:

#### AIMS Schools

#### Construction/Modernization Projects Paid to ADS and Lumbee Holdings

#### September 2007 through March 2008

Payee	Date	Check Number	Total Amount Paid
ADS	August 30, 2007	1009**	\$38,000
ADS	August 31, 2007	476**	\$31,000
ADS	September 19, 2007	480**	\$38,000
ADS	December 13, 2007	1041*	\$38,000
ADS	March 30, 2008	5072	\$46,000
Lumbee Holdings	September 13, 2007	1010*	\$35,000
Lumbee Holdings	January 26, 2008	1051*	\$75,000
Lumbee Holdings	March 25, 2008	1071*	\$47,500
<b>Total</b>			<b>\$348,500</b>

\*Checks are copies with some check number difficult to verify the last digit.

\*\*Checks signed by the founder.

Many of these transactions involve hundreds of thousands of dollars payable to the founder's personal businesses for construction improvements on his building with public funds not supported by formal contracts, competitive bidding or authorization by the governing board. Additionally, several checks written from the AIPCS bank account made payable to his personal companies were signed by the founder. Government Code 1090 is a prohibition against self-dealing. The intent is to prohibit public officials, which includes designated employees, from having a financial interest in any contract made by them in their official capacity. The founder in his position as director had a fiduciary responsibility to AIMS schools, but used his position to advance his own personal financial interests in direct violation of Government Code 1090.

FCMAT requested supporting documentation for payments for the construction expenditures listed above such as the contract document, architectural drawings and/or city permits and received a single page invoice for each project. For example, one statement for \$75,000 dated October 15, 2007 offered the following supporting documentation:

## Description

171 12st Street Suite #102

Complete design and build two classrooms at \$37,500 each

**TOTAL \$75,000**

FCMAT was able to obtain board minutes from January 12, 2010 to support that the governing board authorized a maximum of \$500,000 to be spent on “the architecture and contractor at 171 12th Street.” The board minutes do not authorize a specific vendor(s), request competitive bids or provide any discussion regarding the various projects to be completed. FCMAT received four AIA document agreements signed by the founder as the “owner” of the project on behalf of American Indian Public Charter Schools dated between June 16, 2010 through October 20, 2011 and totaling \$792,780 for construction improvements located at 171 12th Street, Oakland, CA which is property owned by the founder.

General ledger transactions support that an additional \$710,533.86 was spent on construction and modernization activities during the 2009-2010 fiscal year through December 31, 2011. Because AIMS schools participate in federal program funding opportunities, federal procurement regulations require that they abide by the federal procurement regulations for competitive bidding according to the conditions and assurances for receipt of federal funds. When asked by the FCMAT study team whether AIMS schools requested formal bids or quotations for the construction projects, the founder stated that AIMS charter schools did not formally request competitive bids or quotations. The table below shows the various construction projects as well as the three projects that exceed the \$100,000 bidding threshold:

**AIMS Schools****Construction Expenditures Analysis****For the Fiscal Years 2009-10 through December 31, 2011**

Vendor	Amount Paid	Description	Supporting Documentation	Exceed Federal Procurement Threshold
Lung HWA Architect's	\$8,000.00	Architectural Services	Yes	No
MT Szeto Construction	\$169,686.63	Bathroom Remodel – Phase I	Yes	Yes
MT Szeto Construction	\$305,634.00	Structural Upgrade – Phase II	Yes	Yes
MT Szeto Construction	\$128,764.90	Second Floor Renovation – Phase III	Yes	Yes
MT Szeto Construction	\$17,765.00	Sprinkler Project – Phase IV	Yes	No
MT Szeto Construction	\$42,682.33	Multiple Projects	Yes	No
ADS	\$38,000.00	Stage	No	No
<b>Total</b>	<b>\$710,533.86</b>			

FCMAT requested and received fully executed contracts to support projects completed by MT Szeto Construction, but was told the ADS contract was missing.

Several construction projects of more than \$100,000 were subject to competitive bidding and therefore may be in violation of federal procurement regulations, which could result in a loss of all federal funding to the AIMS schools.

**Administrative Services and Wages**

The founder's spouse provides financial administrative services for all three schools through a private company she owns under the names A & A Business Solutions LLC and AAFS. Services include general accounting for the day-to-day business of the schools, processing accounts payable; compliance reporting to various local, state and federal entities; interacting with the charter authorizer, attending board meetings and assisting with the annual audit.

From July 1, 2009 through December 31, 2011, the founder's spouse charged each school a fee for her services. The records for AICPS show that she and the founder were recorded on the payroll earnings PERS credit.

In addition to the normal CalPERS contribution from payroll, the founder's company, Lumbee Holdings, sent checks each month for "CalPERS retirement." In a memorandum dated March 27, 2012 to CalPERS, the new administration claims that these additional CalPERS payments were in error and it is attempting to correct these contributions.

The FCMAT study team could not locate a formal agreement between AAFS and the governing board or any authorization to place the founder's spouse on the payroll during the same time she was paid as a subcontractor. The same individual cannot legally be an employee and a subcontractor simultaneously. These records should be corrected to reflect the correct classification and amend reports to the state and federal agencies accordingly.

The table below is a summary of administration services and wages reported through the general ledger accounts and federal forms for July 1, 2009 through December 2011.

### AIMS School

#### Administrative Services and Wages

#### For the Founder and Spouse

#### July 1, 2009 through December 31, 2011

Payee	Type of Service	Fiscal Year 2009-2010	Fiscal Year 2010-2011	Fiscal Year 2011-2012-(six months)	Total
AAFS	Financial Services	\$103,833.20	\$147,999.84	\$73,999.92	\$325,832.96
Spouse	Wages	\$12,000.00	\$12,000.00	\$6,000.00	\$30,000.00
Founder	Wages	\$107,083.29	\$0	\$23,181.81*	\$130,265.10
<b>Totals</b>		<b>\$229,966.49</b>	<b>\$159,999.84</b>	<b>\$103,181.73</b>	<b>\$486,098.06</b>

\*Board minutes dated July 14, 2011 state that the founder "will not accept pay for the position." FCMAT cannot locate a personnel contract or board minutes that authorize salary for the founder.

The founder operates several businesses that provide various services to the AIMS schools. According to his interview with FCMAT, the founder was a director for AIPCS beginning 2000 and resigned at the end of the 2007-2008 fiscal year and rejoined AIMS schools in the summer of 2011. Board minutes for March 15, 2007 state that "he will work part-time next year 2007-2008...his last year as director of American Indian Public Charter School." The June 21, 2007 board minutes state that the founder "will step down as of June 30, 2007 as principal of AIPCS" and work as CEO of the AIPCS network of schools and mentor each site administrator. The board minutes did not provide action to support that the CEO appointment was a paid position.

In addition to the wages and construction income listed above, the founder conducted business with the schools collecting rent through lease agreements, storage fees, additional construction projects and the summer SAIL program totaling \$2,769,060. The table below shows an itemization for each business entity reported on federal Form 1099:

### AIMS Schools

#### Businesses Owned by the Founder

#### Federal Form 1099 Data

#### For The Years 2009 through 2011

Recipient	2009	2010	2011	Total
ADS	\$491,571	\$273,302	\$344,622	\$1,109,495
Lumbee Holdings	\$259,200	\$586,979	\$491,886	\$1,138,065
SAIL		\$177,000	\$144,500	\$321,500
<b>Grand Total</b>	<b>\$750,771</b>	<b>\$1,037,281</b>	<b>\$981,008</b>	<b>\$2,769,060</b>

FCMAT verified these amounts through the general ledger for each year and found that a payment of \$136,500 for the SAIL program along with a payment of \$38,000 for construction work to ADS was not reported on federal form 1099 for earnings in 2009. AIMS schools should file a corrected federal form 1099 for each company.

Included in the rental/lease payments is \$1,900 per month charged to AIPCS II for storage beginning with the 2009-2010 fiscal year totaling \$57,000 that is not included in the lease agreements approved by the governing board. The AIMS governing board should review and approve all agreements.

The table below is a compilation of payments made through the school accounts to either the founder or his spouse from tables above:

### AIMS Charter Schools

#### Payments Made to Business Owned By the Founder and Spouse

##### For the Years 2007 through 2011

Payee	Source Data	Time Period	Amount	Type
ADS/Lumbee Holdings	Business Office	2007 – 2008	\$348,500	Construction
ADS	General Ledger	7/1/2009 through 12/31/2011	38,000	Construction
AAFS	General Ledger	7/1/2009 through 12/31/2011	325,833	Financial Services
Spouse	General Ledger	7/1/2009 through 12/31/2011	30,000	Wages
Founder	General Ledger	7/1/2009 through 12/31/2011	130,265	Wages
Lumbee Holdings	General Ledger	7/1/2009 through 12/31/2011	1,338,065	Rent/Storage
ADS	General Ledger	7/1/2009 through 12/31/2011	1,109,495	Rent/Storage
SAIL	General Ledger	7/1/2009 through 12/31/2011	458,000	Summer Math Program
<b>Total</b>			<b>\$3,778,158</b>	

# Governing Board Oversight

## Board Responsibility, Authority, and Control

In February 2005, the California Charter Schools Association published a brief that included “quality statements” that function as guidelines for charter school boards and administrators to ensure the strength and sustainability of the charter school movement. They cover the areas of student achievement, ethical leadership, and continuous focus on increasing quality, responsible governance, and fiscal accountability. The AIMS governing board should pay particular attention to the areas of responsible governance and fiscal accountability.

Responsible Governance: According to the brief, “Charter school boards and administrators establish and implement policies that are transparent and focused on student achievement. Charter school boards and administrators have a cogent understanding of and comply with the laws that govern charter schools.” This includes the following:

- The school administration and governing board are “well-versed in charter law.”
- “New board members are given formal orientation on the purpose and educational vision of the school and on their roles and legal responsibilities as a board member.”
- “The charter school governance follows a fully adopted set of bylaws which include policies that address conflicts of interest, meeting protocols and procedures....”
- “Conflicts of interest policies are comprehensive and address the disqualification of a board member or employees to act upon matters which may materially affect his/her assets and income.”

Fiscal Accountability: “A charter school fulfills its fiduciary responsibility for public funds and maintains publicly accessible fiscal records. The school engages in an annual financial audit, which is made public.” This includes the following:

- “Establishes clear fiscal policies to ensure that public funds are used appropriately and wisely.”
- “Fiscal policies include procedures for the authorization of purchases and release of funds, including signatories for checks or purchase orders over a specified threshold, and procedures related to credit cards ....”
- “Ensures financial resources are directly related to the school’s purpose: student attainment of learning goals.”

## Board Minutes

Charter school boards are responsible for providing governance to the charter. Within legal parameters, the board establishes how the charter will operate. It accomplishes this by establishing policies, approving procedures, delegating responsibilities, and maintaining its own level of oversight.

Charter schools must comply with the Ralph M. Brown Act, which requires every board to adopt a time and place for holding regular meetings. If the regular meeting location is rendered unsafe because of fire, flood, earthquake, or other emergency, meetings may be held elsewhere only if proper notice is given. In addition, the act requires agendas for regular meetings to be posted at

least 72 hours in advance, and items that are not listed on the agenda can be acted on in cases of exception. Actions taken in violation of the Brown Act may be declared invalid, including inadequate descriptions of posted items, action on items not posted for which no exception exists, and improper closed sessions.

Board meetings for the AIMS charter schools do not follow the schedule provided to the charter authorizing agency, the Oakland Unified School District. The limited number of board minutes available for review included dates that did not align with the meeting schedules provided to the district. Based on the board minutes provided, meetings were not held consistently or in accordance with the schedule.

Although board minutes are permanent records, the founder indicated that all the board minutes and agendas were removed presumably stolen from the business office. It is the responsibility of the board and administration to secure these records. The minutes received from outside sources demonstrated that information given to the governing board for action was vague and lacked sufficient detail to support the actions taken. For example, the board approved a maximum of \$500,000 to be spent on construction, but there was no discussion of the projects to be completed, timelines, funding sources or the selection of contractors. Bidding, quotations and requests for proposals were never discussed or considered.

The lack of consistency in meetings and the absence of board minutes to support the governing board's actions indicate a lack of board oversight, openness and the internal controls necessary to secure permanent records.

## **Fiscal Policies and Procedures**

AIMS governing board submitted fiscal policies and procedures to Oakland Unified with the original charter petition. These policies and procedures form a contractual agreement for fiscal oversight and accountability between the oversight agency and the charter. A selection of these policies is below:

Financial Reporting: The financial administrator shall prepare monthly financial reports for the AIM schools board.

Procedure: Statements of financial position and statements of activities shall include profit and loss, balance sheet, cash-flow, bank statements and shall be reviewed by the AIMS school board on a regular basis.

Bank Account Management: The financial administrator/site administrator shall adhere to the check signing procedures established by the AIM Schools Board.

Procedure: Secretary and treasurer of the board have check signing authority. The financial administrator is authorized by the board to stamp signatures for all check payments within the approved budget. The Board must approve the opening or closing of any bank accounts.

Purchasing: All purchases over \$10,000 must include documentation of a "good faith" effort to secure lowest possible cost for comparable goods or services.

Procedures: Documentation shall be attached to all checks and purchase order requests showing that at least three vendors were contacted and such documentation shall be maintained for three years. All purchases of more than \$20,000 must be bid by a board approved process.

Credit Cards: Credit card is issued to school for school related expenses.

Administrative assistant will use credit card for school related expenses. All charge must be supported by invoices and monthly log sheets detailing charge. Monthly credit card statements are reconciled to invoices and log sheets and are approved by the site administrator.

Included in the renewal petition dated December 14, 2010, an additional policy was added for check writing.

Writing Checks: Any checks over \$5,000.00 shall have board approval, except for vendors listed to include utilities, janitorial services, and landlords.

## **Noncompliance with Financial Policies and Procedures**

Financial Reporting: The financial administrator told FCMAT that board members are provided with financial statements monthly. FCMAT requested samples of the packets provided to board members, but did not receive them. The board minutes available make vague reference to budget documents, fiscal reports, and expenditures, but they provide little or no detail on what was reviewed, discussed or approved. The board members interviewed said they review a profit and loss statement at the quarterly board meetings and do not review transactional detail.

The charter school's governing board does not comply with its own financial reporting policy. It should maintain board minutes as permanent records, and hold regularly scheduled board meetings that include a complete and descriptive record of the board's discussion of action items that resulted in decisions.

Bank Account Management: The secretary and treasurer of the board have signature stamps on file in the business office. The financial administrator, also the founder's spouse, is authorized by the board to stamp signatures for all check payments within the approved budget. In interviews, the secretary and treasurer made no comment when asked if they reviewed and approved check payments; therefore, it is not possible to determine if commercial warrants issued were within budget limits.

Board minutes examined by the FCMAT study team do not record the opening or closing of bank accounts; however, the AIPCS schools statements and general ledgers show that three bank accounts were closed, and one new bank account opened between 2009-10 and 2010-11. Two additional bank accounts opened between 2010-11 and 2011-12 without board authorization.

The governing board should ensure that all commercial warrants are reviewed during each board meeting and that bank accounts can be opened or closed only by board authorization.

Purchasing: The current administration was unable to provide FCMAT with supporting documentation for purchases of more than \$10,000 in accordance with the purchasing policy. In addition, purchases of more than \$20,000 were not bid by a board approval process.

When supporting documents were requested, FCMAT was informed that supporting documentation for construction contracts and most expenditures requested by the team were missing from the business office along with board minutes, agendas and the server was stolen. FCMAT identified specific expenditures and requested that support documents be requested from the vendor or other third party sources. At the time of this report, FCMAT had not received several of these documents.

The governing board should ensure that board minutes, board agendas, contracts and other business records are secured in a place that is safe from theft or fire.

Purchasing: FCMAT found no evidence that informal quotations, requests for proposals or bids were employed in the procurement process. Instead, several contracts were issued to either the founder or his spouse without properly bidding. As mentioned earlier in the report, contracts of more than \$100,000 require formal bids in accordance with federal procurement regulations. The AIMS charter schools should implement a defined purchasing and procurement policy and hold staff accountable for following it.

Credit Card Purchases: The past practice has allowed site administrators to use credit cards in the name of the founder to purchase a variety of materials and supplies as well as confirm travel arrangements. More than one third of the purchases lacked supporting documentation, log sheets, or approval from site administrators.

Writing Checks: The board minutes include only one notation of individual commercial warrants or a list of commercial warrants. Several checks issued from September 2007 to March 2008 for more than the \$5,000 threshold were signed by the founder with no evidence that the board approved these expenditures. Three checks totaling \$157,000 were written to Lumbee Holdings, and two checks totaling \$76,000 were written to ADS for renovation and modernization without any support documentation other than a single page invoice with a brief comment regarding the renovation project.

#### Related party transactions

The founder and person credited with many of the successes of the AIPCS schools also is involved with companies that provide for facilities and services to the AIPCS schools. While integrally involved and influential in the administration of the charter and the recruitment of the board, the founder also has personal financial interests in companies that provide services to the charter.

Transactions from which the founder has financially benefited are numerous. FCMAT identified several lease agreements where the founder was either a signer and/or had interest in the transaction:

#### **Lease agreements:**

1. AIPCS (lessee) and American Delivery Systems (lessor)  
Address: 3637 Magee Oakland CA  
Term: Five years July 1, 2008 through June 30, 2013  
Amount: \$20,684.32 per month  
Founder interest: AIPCS and ADS  
Signed by: **Founder** as lessor  
Note: The exact contract was provided with signatures on July 8, 2008 with both lessor and lessee signatures unidentifiable.
2. Evangelical Lutheran Church of Our Redeemer (lessee) and American Delivery Systems (lessor)  
Address: 6038 Brann St Oakland CA  
Term: Five years January 1, 2007 through December 31, 2012  
Amount: \$6,000 per month with an increase the larger of 3% or COLA  
Founder interest: ADS  
Signed by: **Founder** as lessee

Amendment to lease agreement: June 2008

Extended the agreement four years from July 1, 2008 to June 30, 2012 and a new rent payment schedule was identified.

Founder interest: ADS

Signed by: **Founder** as lessee

3. Our Redeemer Lutheran Church (owner) and American Delivery Systems (lessor) and Unity Schools (lessee)

Address: 6038 Brann St Oakland CA

Term: Four years July 1, 2008 through June 31, 2012

Amount: \$12,500 per month

Founder interest: ADS and Unity

Signed by: **Founder** as lessor

Amendment to sublease: Increases the rent starting July 1, 2009 through June 30, 2012 and calls for improvements to be completed by tenant.

Founder interest: Unity and ADS

Signed by: **Founder** as proprietor and the executive director of Unity schools.

4. American Delivery Systems (lessor) and American Indian Public High School (lessee)

Address: 3626-28 35<sup>th</sup> Ave Oakland CA

Term: Five years from July 1, 2008 through June 30, 2013

Amount: \$20,280 month + \$5,000 deposit

Founder interest: ADS and AIPCHS

Signed by: Illegible

5. Lumbee Holdings (lessor) and American Indian Public Charter II (lessee)

Address: 171 12<sup>th</sup> St Oakland CA

Term: Five years from April 1, 2007 through March 31, 2012

Amount: \$21,600 month + \$21,600 deposit (1/3 of utilities and 1/4 of property tax)

\*rent to increase 4% per year effective 3/2009

Founder interest: Lumbee and AIPCS II

Signed by: illegible and president AIPCS II

Board approved at March 2007 meeting.

6. Amendment to #5

Storage Agreement

July 1, 2007 for \$1,900 month

“will pay utilities and taxes when Oakland Charter Academy vacates premises.”

Founder interest: Lumbee and AIPCS

Signed by: **Founder** (lessor) and president AIPCS II (lessee)

The above transactions create the perception of fraud, misappropriation of assets and possible criminal activity because of the following factors:

- The founder’s influence and ability to simultaneously control and benefit from these transactions.
- The lack of documentation to support transactions and safeguard board minutes and accounting records.

There is little evidence of responsible governance by the board and a clear lack of fiscal accountability by the administration. The governing board has failed to maintain and exercise its responsibilities, authority, and control.

## Prevention and Detection

As previously mentioned, the internal control environment includes ethical values and integrity displayed by the governing board and management, as well as the underlying tone established by the organization's site administrators. The tone of the organization, set by management through its words and actions, demonstrates to others that dishonest or unethical behavior will not be tolerated. An atmosphere in which employees feel safe to communicate concerns is a fundamental component of a strong and effective internal control environment.

The control environment is an essential element and provides the foundation for other internal controls to be effective in achieving the goals and objectives to prevent and/or deter fraud or illegal acts.

Regular external audits are a strong deterrent to mismanagement and fraud, but they cannot serve as the only method of ensuring accountability. It is imperative for the charter school, the director, and governing board to review this audit's findings and recommendations to implement the appropriate internal controls and hold the responsible parties accountable for their actions.

Internal controls clearly are among the most important aspects of any fraud prevention program. Managers are in a position of authority and therefore have a higher standard of care to establish the ethical tone and serve as examples to other employees. Employees with administrative responsibility have a fiduciary duty to the organization in the course of their employment to ensure that those activities are conducted in compliance with all applicable board policies, laws, regulations, and standards of conduct. Management personnel are entrusted to safeguard the charter school's assets and ensure that internal controls function as intended.

While the governing board and all employees in the organization have some responsibility for internal controls, the founder and his spouse had a fiduciary duty and responsibility to ensure that the assurances in the charter petition and the governing board fiscal policies and procedures were conducted responsibly and ethically.

Based on the documentation reviewed by FCMAT, there is sufficient evidence to demonstrate that fraud, mismanagement and misappropriation of the charter school funds and assets may have occurred. A significant material weakness exists in the charter school's internal control environment, which increases the probability of fraud and/or abuse. These findings should be of great concern to the AIMS governing board, Oakland Unified School District and the Alameda County Office of Education and require immediate intervention to limit the risk of fraud and/or misappropriation of assets in the future.

According to Education Code section 42638(b), action by the county superintendent shall include the following:

If the county superintendent determines that there is evidence that fraud or misappropriation of funds has occurred, the county superintendent shall notify the governing board of the school district, the state controller, the superintendent of public instruction and the local district attorney.

The county superintendent shall report the findings and recommendations to the governing board of the district within 45 days of completing the audit. The governing board of the school district shall notify the county superintendent within 15 days after receipt of the report of its proposed actions regarding the county superintendent's recommendations.

## Recommendation

*The county superintendent should:*

1. Notify the governing board of AIMS charter schools, the Oakland Unified School District governing board, the state controller, the superintendent of public instruction, and the local district attorney that there is sufficient evidence that fraud or misappropriation of assets and other illegal activities of charter funds may have occurred.



# Appendices

**A: Referenced Documents**

**B: Study Agreement**



## Appendix A - Referenced Documents

### LUMBEE Properties, LLC

171 12th Street, #4  
Oakland, CA 94607  
Phone (520) 743-0771

#### PROPOSAL

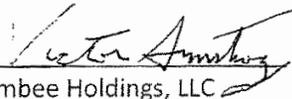
Project: American Indian Public Charter School II

171 12th Street  
Oakland, CA 94607

This is an outline of proposed work for AIPCS II. We will demolish existing walls for classrooms and offices. Remove all demolition material. Repaint walls with white semi-gloss paint. Locate rebar and tension cables embedded in the concrete slab of floor.

- I. Complete new or alternate existing walls with metal studs, sheet rock and smooth texture. Six classrooms will be designed and created to accommodate 20-35 students. The school will be charged for two classes.  
1)-----\$75,000.00
- II. Remove all carpet and padding. Replace with 16x16 tile in six classrooms, two offices and center mixed used space. American Indian symbols will be designed in the floor in each room.  
2)-----\$35,000.00
- III. Girls bathroom will be remodeled to reflect modern design, energy efficient, replace tile on walls, floor, and paint walls.  
3)-----\$38,000.00
- IV. Create at least two rooms that will be used as administrative offices or multi-purpose room.  
4)-----\$47,500.00

Proposed by:

  
Lumbee Holdings, LLC

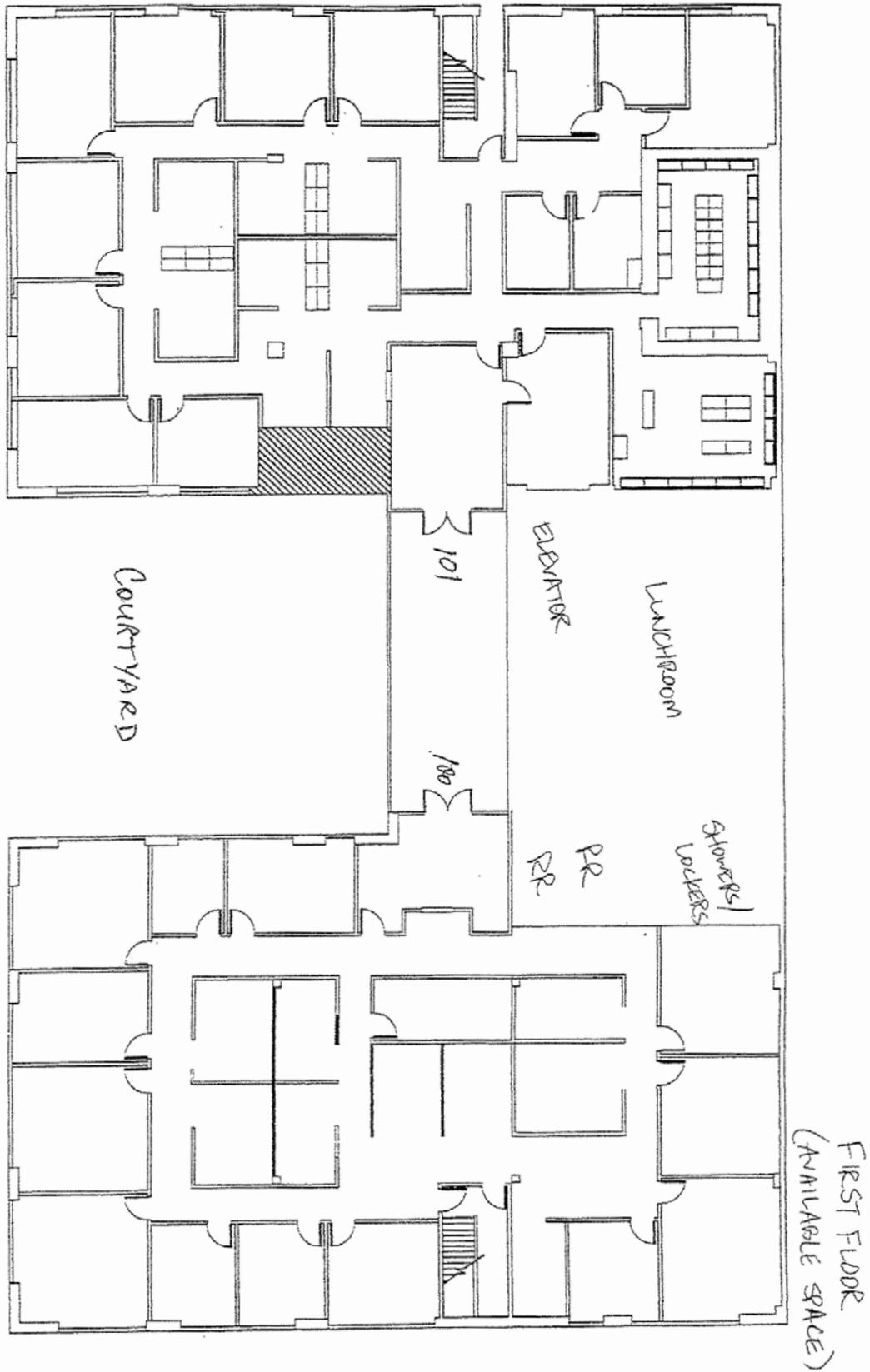
4/2/07  
Date

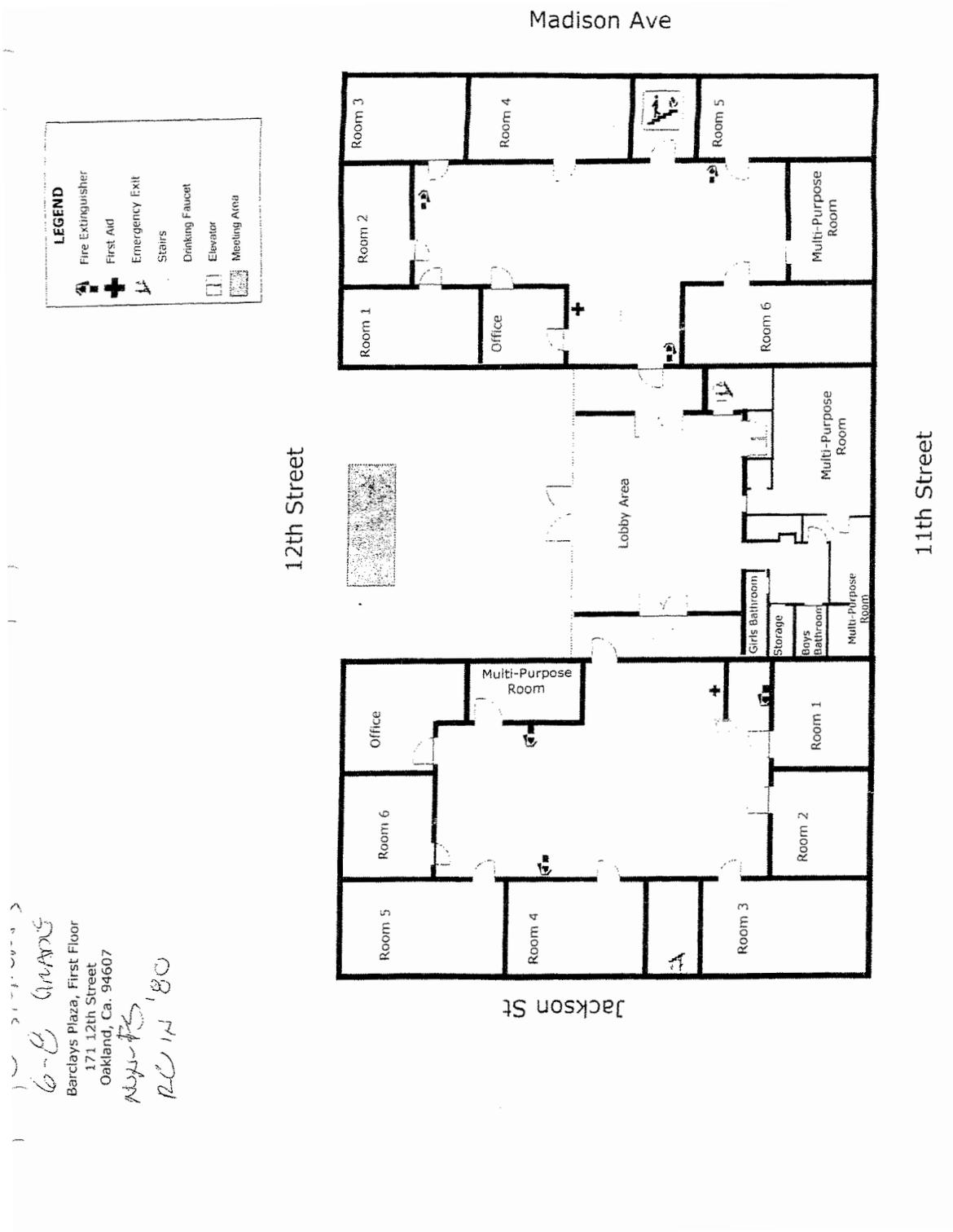
Approved by:

 4-22-07  
AIPCS Board member Date

  
AIPCS Board member

4-2-07  
Date







# PERMIT APPLICATION WORKSHEET

CEDA - Permit Center  
 250 Frank H. Ogden Pl.  
 2nd Floor, Suite 211  
 Oakland, Ca 94612  
 (510)238-3891  
 Hours:  
 8 am-4pm: M-F, Th  
 9:30 am-4 pm: Wed  
 10 am-4 pm: Sat/Sun

PLEASE COMPLETE ALL INFORMATION. APPLICANTS WITH INCOMPLETE WORKSHEETS MAY BE ASKED TO GET A NEW NUMBER. INACCURATE INFORMATION MAY LEAD TO SUSPENSION OF THE PERMIT. ADDITIONAL PERMITS MAY BE REQUIRED, i.e., Electrical, Plumbing, Mechanical, Sewer, Obstruction.

TYPE OF PERMIT: (circle one) RIGHT OF WAY		<b>BUILDING</b>		SIGN	SCHOOL FEE (SE) Commercial \$0.36 Residential \$2.24	ADDRESS FEE \$63.00 \$43.00
TYPE OF WORK (circle one)		(1) NEW CONSTRUCTION    (2) REPAIR    (3) ADDITION (4) CELL SITE    (5) ALTERATION / I.I.		Site Plan Review    3-20 cars \$1528.00    21-40 cars \$1646.00 41-120 cars \$1759.00    121-300 cars \$1877.00    >300 cars \$1995.00		
(6) DEMOLITION    (7) SOLAR PANELS (SE)		(8) RETROFIT    (9) C.O./S.A.		<b>(10) CHANGE IN USE</b>		
IS THIS APPLICATION RELATED TO ANY OTHER PERMIT? TO ANY OTHER COMPLAINT?				IF YES, INDICATE PERMIT #, PLANNING CASE FILE # OR COMPLAINT #:		
<input type="radio"/> YES <input checked="" type="radio"/> NO						
SITE ADDRESS/JOB LOCATION <b>171 12th ST</b>				ASSESSOR'S PARCEL NO.		
DESCRIPTION OF PROPOSED WORK <b>CONVERT 1ST FLOOR OFFICES INTO A 6-8 GRADE SCHOOL FROM OUSD</b>						
WORK IS VISIBLE FROM FREEWAY/BART <input type="radio"/> NO <input type="radio"/> YES						
EXTERIOR WORK ON BUILDING <input type="radio"/> NO <input type="radio"/> YES (PHOTOS REQUIRED. PLEASE ATTACH)						
VALUATION OF PROPOSED WORK <b>S</b>	EXISTING # OF RESIDENTIAL UNITS	# OF STORIES: <b>3</b>		<input type="radio"/> SFD/DUPLEX <input type="radio"/> APARTMENTS <input checked="" type="radio"/> COMMERCIAL <input type="radio"/> INDUSTRIAL		
	PROPOSED # OF UNITS	FIRE SPRINKLER <input type="radio"/> YES <input checked="" type="radio"/> NO				
PROPERTY OWNER'S NAME <b>Lumbee Holding, LLC</b>				PROPERTY OWNER'S PHONE NUMBER <b>510-499-4163</b>		
PROPERTY OWNER'S ADDRESS (street, city and zip code) <b>663 Haddon Rd, Oakland, CA 94610</b>						
PERSON SUBMITTING PLANS / CONTACT/PERSON <b>Jorge Lopez</b>				PHONE NUMBER <b>(510) 333-7816</b>	FAX NUMBER <b>(510) 332-6753</b>	
ARCHITECT'S/DESIGNER'S NAME				PHONE NUMBER	FAX NUMBER	
CONTRACTOR'S LICENSE NUMBER				SIGNATURE OF APPLICANT 		DATE <b>3/5/08</b>

I ACKNOWLEDGE THAT REFUNDS ARE LIMITED PER Section 107.6 of O.B.C. INITIAL \_\_\_\_\_ DATE \_\_\_\_\_

A:\vt\Windows\Form\Permit Application Worksheet

## Appendix B - Study Agreement



CSIS California School Information Services

**FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM  
AB139 STUDY AGREEMENT  
January 13, 2012**

The FISCAL CRISIS AND MANAGEMENT ASSISTANCE TEAM (FCMAT), hereinafter referred to as the Team, and the Alameda County Office of Education hereinafter referred to as the COE, mutually agree as follows:

**1. BASIS OF AGREEMENT**

The Team provides a variety of services to school districts and county offices of education upon request. Based on the passage of Senate Bill 430 and the provisions of Education Code Section 1241.5 (c), a County Superintendent of Schools may review or audit the expenditures and internal controls of any charter school in his or her county if he or she has reason to believe that fraud, misappropriation of funds, or other illegal fiscal practices have occurred that merit examination. The extraordinary audits conducted by the county superintendent shall be focused on the alleged fraud, misappropriation of funds, or other illegal fiscal practices and shall be conducted in a timely and efficient manner.

The Alameda County Office of Education has requested that the Team provide for the assignment of professionals to study specific aspects of the American Indian Model Schools (AIMS) charter schools which shall include the American Indian Public Charter School grades 6-8, the American Indian Public High School grades 9-12 and the American Indian Public Charter School II grades 5-8. These professionals may include staff of the Team, County Offices of Education, the California State Department of Education, school districts, or private contractors. All work shall be performed in accordance with the terms and conditions of this Agreement.

**2. SCOPE OF THE WORK**

A. Scope and Objectives of the Study

The scope and objectives of this study pursuant to the provisions of Education Code Section 1241.5:

The Alameda County Office of Education has requested the FCMAT Team to provide for the assignment of professionals to conduct an AB 139 Extraordinary Audit. Pursuant to Education Code section 1241.5 (c), the Superintendent of Alameda County has reason to believe that fraud, misappropriation of funds or other illegal practices may have occurred and shall conduct a review of the American Indian Model Schools (AIMS) charter schools as referenced above on behalf of the Oakland Unified School District. In addition to the authority granted under 1241.5 (c) and 47604.3, the county superintendent may conduct an

investigation of the AIMS charter schools based upon written complaints by parents or other information that justifies the review under Education Code 47604.4.

The scope of work shall consist of the following:

1. Review the revenues and expenditures for the AIMS charter schools related to the After School Education and Safety (ASES) Federal Program Grant for the current and two prior fiscal years and determine if fraud, misappropriation of funds or other illegal activities have occurred. The ASES Program funds the establishment of local after school education and enrichment programs. These programs are created through partnerships between schools and local community resources to provide literacy, academic enrichment and safe constructive alternatives for students in kindergarten through ninth grade (K-9). Funding is designed to: (1) maintain existing before and after school program funding; and (2) provide eligibility to all elementary and middle schools that submit quality applications throughout the State of California.
2. Review the AIMS charter schools application for funds received from SB 740 Charter School Facility Grant Program and determine if fraud, misappropriation of funds or other illegal activities have occurred during the current and two prior fiscal years. The Grant is a noncompetitive program that provides assistance with facilities rent and lease expenditures for charter schools that meet specific eligibility criteria. The grant program was enacted to reimburse charter schools for rental and lease costs in low-income areas. This program is targeted toward schools and communities with high proportions of economically disadvantaged students. Eligible applicants must have at least 70 percent of students enrolled at the charter school who are eligible for free or reduced-price meals or the charter school must be physically located in an elementary school attendance area where at least 70 percent of students enrolled are eligible for free or reduced-price meals. The charter schools must also give a preference in admissions to students who reside in the elementary school attendance area. The charter schools are funded \$750 per unit of classroom-based average daily attendance or 75 percent of its annual facilities rent and lease costs for the school, whichever is less.
3. Determine if any of the AIMS charter schools violated any applicable conflict of interest disclosure requirements in accordance with the Political Reform Act of 1974 ("the Act") regarding California's conflict of interest laws for public officials. The Act requires certain "designated" public officials at all levels of government to publicly disclose their private economic interests and requires all public officials to disqualify themselves from participating in decisions in which they have a financial interest.

**B. Services and Products to be Provided**

- 1) Orientation Meeting - The Team will conduct an orientation session at the American Indian Model Schools to brief Charter management and supervisory personnel on the procedures of the Team and on the purpose and schedule of the study.
- 2) On-site Review - The Team will conduct an on-site review at the Charter office and at school sites if necessary; and will continue to review pertinent documents off-site.
- 3) Progress Reports - The Team will inform the COE of material issues as the review is performed.
- 4) Draft Reports – When appropriate, electronic copies of a preliminary draft report will be delivered to the COE administration for review and comment.
- 5) Final Report - electronic copies of the final study report will be delivered to the COE and District following completion of the review. The final report will be published on the FCMAT website.
- 6) Follow-Up Support - Subsequent to the completion of the study, the Team will meet with the COE and/or District at their request, to discuss the findings and recommendations of the report.

**3. PROJECT PERSONNEL**

The study team will be supervised by Anthony Bridges, CFE, Deputy Executive Officer, Fiscal Crisis and Management Assistance Team, Kern County Superintendent of Schools Office. The study team may also include:

- |    |                      |                                      |
|----|----------------------|--------------------------------------|
| A. | Deborah Deal, CFE    | FCMAT Fiscal Intervention Specialist |
| B. | Anthony Bridges, CFE | FCMAT Deputy Executive Officer       |

Other equally qualified consultants will be substituted in the event one of the above noted individuals is unable to participate in the study.

**4. PROJECT COSTS**

The cost for studies requested pursuant to E.C. 42127.8 (d) (1) shall be:

- A. \$800 per day for each FCMAT Team Member while on site, conducting fieldwork at other locations, presenting reports, or participating in meetings.
- B. All out-of-pocket expenses, including travel, meals, lodging, etc.
- C. Any change to the scope will affect the estimate of total cost.

**Based on the elements noted in section 2A, the total cost of the study is estimated at \$30,000.**

Payments for FCMAT services may be reimbursed from funds pursuant to EC 1241.5 set aside for this purpose. Other payments, when deemed necessary, are payable to Kern County Superintendent of Schools - Administrative Agent.

## **5. RESPONSIBILITIES OF THE COE AND DISTRICT**

- A. The District will provide office and conference room space while on-site reviews are in progress.
- B. The COE or District will provide the following (if requested):
  - 1) A map of the local area
  - 2) Existing policies, regulations and prior reports addressing the study request
  - 3) Current or proposed organizational charts
  - 4) Current and two (2) prior years' audit reports
  - 5) Any documents requested on a supplemental listing
  - 6) Any documents requested on the supplemental listing should be provided to FCMAT in electronic format when possible.
  - 7) Documents that are only available in hard copy should be scanned by the district and sent to FCMAT in an electronic format.
  - 8) All documents should be provided in advance of field work and any delay in the receipt of the requested documentation may affect the start date of the project.
- C. The COE administration will review a preliminary draft copy of the study. Any comments regarding the accuracy of the data presented in the report or the practicability of the recommendations will be reviewed with the Team prior to completion of the final report.

Pursuant to EC 45125.1(c), representatives of FCMAT will have limited contact with pupils. The Charter shall take appropriate steps to comply with EC 45125.1(c).

## 6. PROJECT SCHEDULE

The following tentative schedule outlines the planned completion dates for key study milestones:

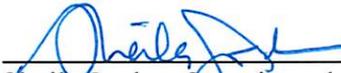
Orientation:	January, 2012
Staff Interviews:	To be determined
Exit Interviews:	To be determined
Preliminary Report Submitted	To be determined
Final Report Submitted	To be determined
Board Presentation	To be determined

## 7. CONTACT PERSON

Name of contact person: Sheila Jordan, Superintendent

Telephone (510) 887-0152 FAX \_\_\_\_\_

E-mail Address: [sjordan@acoe.org](mailto:sjordan@acoe.org)

  
 \_\_\_\_\_  
 Sheila Jordan, Superintendent  
 Alameda County Office of Education  
 Date 1/12/12

  
 \_\_\_\_\_  
 Anthony L. Bridges, CFE  
 Deputy Executive Officer  
 Fiscal Crisis and Management Assistance Team  
 Date January 13, 2012

