



A REPORT  
TO THE  
ARIZONA LEGISLATURE

Special Investigative Unit

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Investigative Report

# Ganado Unified School District No. 20

Misfeasance by District Officials

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June • 2003



STATE OF ARIZONA

OFFICE OF THE  
**AUDITOR  
GENERAL**

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**Debra K. Davenport**  
Auditor General

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DEBRA K. DAVENPORT, CPA  
AUDITOR GENERAL

STATE OF ARIZONA  
OFFICE OF THE  
**AUDITOR GENERAL**

WILLIAM THOMSON  
DEPUTY AUDITOR GENERAL

June 23, 2003

Members of the Arizona Legislature

Governing Board  
Ganado Unified School District No. 20

The Honorable Terry Goddard  
Attorney General

The Honorable Tom Horne  
State Superintendent of Public Instruction

The Office of the Auditor General has conducted a special investigation of the Ganado Unified School District No. 20 for the period April 2000 through September 2000. The investigation determined the amount of public money misused, if any, and whether there were procurement violations during that period.

The investigation consisted primarily of inquiries and examination of selected financial records and other documentation. Therefore, the investigation was substantially less in scope than an audit conducted in accordance with generally accepted auditing standards. Accordingly, the Office does not express an opinion on the adequacy of the financial records or the internal controls of the Ganado Unified School District No. 20. The Office also does not ensure that all matters involving the District's internal controls that might be material weaknesses under standards established by the American Institute of Certified Public Accountants or other conditions that may require correction or improvement have been disclosed.

The accompanying Investigative Report describes the Office's findings and recommendations as a result of this special investigation.

After this report is distributed to the members of the Arizona State Legislature, the Attorney General, and the State Superintendent of Public Instruction, it becomes public record.

Sincerely,

Debbie Davenport  
Auditor General

Attachment

# SUMMARY

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In January 2001, the Office of the Attorney General requested that the Office of the Auditor General investigate certain allegations of financial improprieties involving officials of Ganado Unified School District No. 20. As a result of that request, we conducted an investigation of those allegations and have forwarded a copy of this report to the Attorney General for their review.

Our investigation revealed that from April 2000 to July 2000, Ganado Unified School District officials violated laws, rules, and regulations for construction projects totaling over \$2.8 million. Specifically, district officials awarded three construction projects totaling \$2,139,659 to a single vendor without following the proper procurement requirements. Further, the Superintendent and the Assistant to the Superintendent authorized \$546,750 of improper change orders for those projects. Finally, district officials overpaid the vendor \$191,661, unlawfully advanced \$125,852 to the vendor, and failed to maintain adequate procurement records.

In addition, during the time the vendor provided construction services to the District, the Superintendent personally contracted with the vendor to receive construction services on his home. The Superintendent personally benefited by receiving home improvements at cost and not making any payments for 4 months.

## Investigation Highlights:

- District officials violated various laws, rules, and regulations related to three construction projects totaling over \$2.8 million awarded to a single vendor.
- The Superintendent personally contracted with the same vendor and received personal benefits.



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# INTRODUCTION & BACKGROUND

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In January 2001, the Office of the Attorney General requested that the Office of the Auditor General investigate certain allegations of financial improprieties involving officials of Ganado Unified School District No. 20. As a result of that request, we conducted an investigation of those allegations and have forwarded a copy of this report to the Attorney General for their review.

The Arizona public school system has 239 districts that serve the entire State of Arizona. Each school district has a separate governing board that is elected by the district's voters and is held accountable to the local community for the quality of education provided. The Superintendent is responsible for ensuring that the governing board receives adequate information in order to make informed decisions when voting on the issues that face the district.

Districts are fiscally accountable to Arizona taxpayers for appropriately spending the state funding they receive. Ganado Unified School District No. 20 received state revenues of approximately \$9,600,000 for fiscal year 2002 based on a student count of 2,453. The City of Ganado has a population of 23,428 and is located in Apache County.

School district procurement rules, applicable Arizona Revised Statutes, and the *Uniform System of Financial Records* exist to help ensure that districts receive the best possible value for the public money they spend and school property they manage by prohibiting the restraint of free trade and unreasonable reduction of competition among vendors.





# FINDING 1

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## District officials violated procurement rules

School district procurement rules exist to assist public officials in obtaining the best possible value for public money by promoting competition among qualified vendors. Additionally, as public officials, district employees have a responsibility to prudently manage district assets on behalf of the community they serve. However, Ganado Unified School District officials failed to follow school district procurement requirements and promoted improper business practices.

From April 2000 to July 2000, Ganado Unified School District officials violated various laws, rules, and regulations when procuring construction projects totaling over \$2.8 million. District officials contracted with a Mesa construction company (the vendor) to complete three major construction projects and requested that the company's owner employ many of their relatives as crewmembers. Consequently, the Assistant to the Superintendent's brother and nephew, the Superintendent's secretary's husband, and a governing board member's son were all hired as part of the vendor's construction crew.

District officials contracted with a Mesa construction company and requested that the owner employ many of their relatives.

Violations of laws, rules, and regulations include:

- District officials improperly procured three construction projects totaling \$2,139,659 from the same vendor. In addition, district officials failed to maintain adequate procurement records and many critical procurement records were incomplete or unavailable for review.
- The Superintendent and the Assistant to the Superintendent initiated three improper change orders totaling \$546,750 that did not relate to the original contract work and should have been separately procured.
- The District overpaid the vendor a total of \$191,661 by failing to monitor progress billings and changes to the original contracts.
- District officials unlawfully advanced \$125,852 to the vendor for one of these construction projects before services were performed.

**Exhibit 1:** Summary of Ganado Unified School District  
Construction Project Violations  
April 2000 to July 2000

<u>Description</u>	<u>Amount</u>
Improperly procured construction services <sup>1</sup>	\$2,139,659
Improper change orders	546,750
Vendor overpayment	<u>191,661</u>
<b>Total</b>	<b><u>\$2,878,070</u></b>

<sup>1</sup> Included in this amount is \$125,852 paid to the vendor before services were received.

Source: Auditor General staff analysis of Ganado Unified School District No. 20 records and vendor records.

## District officials improperly procured construction services

Within a 4-month period, district officials used incorrect procurement methods for three major construction projects totaling over \$2.1 million.

From April 2000 to July 2000, Ganado Unified School District officials improperly procured three construction projects totaling \$2,139,659. One vendor was awarded all three contracts. District officials failed to use competitive sealed bidding required by school district procurement rules for construction contracts. Instead, district officials incorrectly used competitive sealed proposals for two construction projects and a design-build procurement methodology for one construction project.

School district procurement rules prohibit the use of competitive sealed proposals for construction. That process allows vendor responses to be evaluated on factors other than cost and permits discussions with vendors who may then change their response. Furthermore, school district procurement rules did not allow for the design-build procurement method until August 2000, 4 months after district officials used it. Almost 2 months after the contract was awarded, the construction consulting firm completing the master planning of the project notified the District, in writing, that the District had violated school district procurement rules when procuring this project. They recommended that the District contact their legal counsel. Consequently, district officials cancelled the \$1,258,521 design-build project. However, the District's vendor had already incurred over \$22,000 in preliminary project expenses. Because the District did not obtain an initial legal review of the bid proposal and failed to follow proper procurement procedures, the District paid over \$22,000 for a project that was never completed by the vendor.

Not only did the District use incorrect procurement methods when contracting these construction services with the same vendor, district officials failed to advertise the solicitations at least 2 weeks before the response deadlines. School district procurement rules require districts to provide potential vendors with at least 14 days' notice so vendors can have adequate time to prepare and respond to a district's solicitations. As a result, district officials restricted competition among qualified vendors by failing to provide potential vendors with enough time to respond to the District's solicitations. Only two vendors responded to each of the first two bid solicitations and only one vendor responded to the last.

In addition, the District's procurement records for these construction projects were incomplete or could not be located by district officials. The District's failure to retain significant documents supporting several construction contracts restricted our review of the District's administrative activities. The following are examples of deficiencies within the District's procurement files:

The District's procurement records for these construction projects were incomplete or could not be located.

- A vendor's response to a solicitation of a \$518,875 construction project could not be located.
- Documentation regarding the advertisement of that construction project was incomplete.
- That project also did not have required documentation as to whether the price was fair and reasonable.
- Information related to the solicitations for all three construction projects was missing. Specifically, the District failed to record the names, time and date received, and amounts related to vendor responses that the District received.
- Mailing lists of potential bidders were not maintained for two of the construction projects.
- Purchase order, invoice, and payment documentation related to the construction vendor was incomplete.

## The Superintendent and the Assistant to the Superintendent wrongfully authorized improper change orders

The Superintendent and the Assistant to the Superintendent authorized \$546,750 in improper change orders that were outside the scope of the contract.

The Superintendent and Assistant to the Superintendent authorized improper contract changes totaling \$546,750. The change orders were outside the scope of the contract and included constructing a new agricultural barn, installing new offices, and painting various buildings not included in the original contract.

Valid change orders are permissible when unforeseen services, labor, and/or materials that directly relate to the original contract are needed to complete the project. School district procurement rules require governing board approval for any changes that increase contract amounts in excess of \$15,000 or 5 percent of the original contract, whichever is greater. In addition, the Superintendent is responsible for ensuring that the governing board receives all necessary information in order to make informed decisions pertaining to any issues presented for approval.

The Superintendent allowed approximately \$200,000 in services related to the improper change orders to be completed before informing the governing board of these changes.

Although the Superintendent eventually obtained governing board approval for these change orders, he provided the governing board with limited and inadequate information regarding the contract changes and amounts. In fact, the work associated with nearly \$200,000 of these change orders was already completed before the Superintendent presented the information to the governing board. Because these contract changes did not directly relate to their original contract, the Superintendent should have ensured that they were separately bid. Further, written justification for change orders was insufficient and incomplete.

## District officials paid the vendor in excess of the contracted amount

District officials overpaid the vendor \$191,661 as a result of inadequately reconciling vendor billings with district records. In particular, district officials paid the vendor without performing a reconciliation of vendor progress billings and actual construction progress schedules. District officials were unaware of this overpayment until independent auditors and the Office of the Auditor General brought it to their attention. As of June 2003, district officials have failed to recover these monies.

## District officials unlawfully advanced monies before receiving services

District officials not only violated laws and regulations, they failed to prudently manage district assets and did not serve the best interests of their citizens. State law and the *Uniform System of Financial Records* do not permit advances for construction services and, therefore, no school district has authority to advance cash payments for construction or any other services. Nevertheless, district officials paid the vendor \$125,852 before any services were rendered.



# FINDING 2

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## Superintendent received personal benefits

Arizona law restricts public employees from using or attempting to use their official position to secure any valuable benefit that would not ordinarily accrue within their official duties. From May 2000 to September 2000, the Superintendent personally contracted with the District vendor, rather than an unrelated party, in order to receive construction services on his home and was able to obtain benefits through their agreement.

During the time the District improperly contracted with the construction vendor referred to in Finding 1, the Superintendent personally approached the vendor with a job offer to complete various home improvements on his personal residence. The Superintendent used his official position in order to obtain construction services on his home from the District vendor and personally benefited from the agreement.

Specifically, the Superintendent received home improvements at cost, including bathroom renovations, roof repair, deck replacement, interior painting, installation of wood blinds, and a complete kitchen remodel with new cabinets, countertops, and appliances.

In addition, the Superintendent did not make any payments for 4 months until the Attorney General's Office requested documentation regarding the home improvements, at which time he sent \$40,163 by express overnight delivery.

The Superintendent received personal benefits by personally contracting with a vendor he professionally employed.





# RECOMMENDATIONS

In order to ensure proper control over public monies, the District should implement the following policies and procedures.

1. All purchases should follow the competitive sealed bidding process outlined in Administrative Code R7-2-1021 through R7-2-1033. This procurement method allows the District to award a contract to the lowest bidder only. If the District determines in writing that the use of bidding is either not practicable or not advantageous to the school district, a contract may be entered into by competitive sealed proposals. However, the competitive sealed proposal method may not be used for construction services.
2. The District must determine in writing that the price of a sole bid response is fair and reasonable, and that either other prospective bidders had reasonable opportunity to respond, or there is not adequate time for resolicitation.
3. The District must maintain a prospective bidder's list and ensure all potential vendors have at least 2 weeks to respond to solicitations.
4. According to the *Records Retention and Disposition Manual for Arizona School Districts*, the District must adhere to the following procurement record retention rules:
  - Bid and contract files, including but not limited to, invitation for bids, requests for proposals, advertisement documentation, evaluations, and award determinations, must be retained for 6 years.
  - Purchase order, invoice, and payment records must be retained for 3 years.
  - Vendor lists and files must be retained for 1 year.

5. All district contract changes must relate to the original contract. If the changes increase the contract amount in excess of \$15,000 or 5 percent of the original contract amount, the District must have the changes approved by the governing board, in writing, finding that the change order is advantageous to the District. Further, the District should not begin any work related to the contract changes until such approval is obtained.
6. To help ensure the proper and lawful use of public money, the District should not pay for construction goods or services before they are received.
7. The District must implement proper internal controls related to expenditures such as reconciling vendor progress billings with contract changes and actual construction progress schedules before issuing any payments to ensure the District is not overpaying for services. In addition, the District must recover their \$191,661 overpayment for construction services.