

Arizona Auditor General

Investigative Report: Misuse of Public Monies by School District Officials



**June
1997**



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STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

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June 4, 1997

Members of the Arizona Legislature

The Honorable Grant Woods
Attorney General

The Honorable Richard M. Romley
Maricopa County Attorney

The Honorable Lisa Graham Keegan
State Superintendent of Public Instruction

In conjunction with the Maricopa County Attorney's Office, we have conducted a special investigation of the Cartwright Elementary School District No. 83 for the period January 1991 through December 1996. Our investigation was performed to determine if the District's internal control structure design and operation were adequate to prevent the misuse of public monies; and if not, the extent to which these monies had been misused.

Our investigation consisted primarily of inquiries and the examination of selected financial records and other documentation. Therefore, our investigation was substantially less in scope than an audit conducted in accordance with generally accepted auditing standards. Accordingly, we do not express an opinion on the financial records or internal control structure of the District, nor do we ensure that all matters involving the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants or other conditions that require correction or improvement were disclosed.

The accompanying Investigative Report describes our findings and conclusion as a result of this special investigation.

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

A handwritten signature in cursive script, appearing to read "Debbie Davenport".

Debbie Davenport
Deputy Auditor General

Attachment

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Summary

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Investigation Highlights:

- ☑ *District employees falsified procurement documents to unlawfully direct at least \$540,676 to preferred vendors.*
 - ☑ *Home remodeling costs for one of Mr. Freeman's friends were charged to District accounts.*
- ◆

In May 1996, the Arizona Legislature, the Superintendent of Public Instruction, and the Maricopa County Attorney requested that the Office of the Auditor General investigate allegations of financial improprieties on the part of former officials of Cartwright Elementary School District No. 83. As a result of that request and in conjunction with the Maricopa County Attorney's Office and the Office of the Attorney General, we conducted an investigation of those allegations and submitted the following findings to those offices.

Our investigation determined that from January 1991 through December 1996 the Superintendent, Dr. William R. Dabb, and Director of Maintenance, Mr. Gary Freeman, and other individuals, caused or allowed the misuse of public monies and District resources by violating Arizona Revised Statutes, school district procurement rules, and District policies. See Appendix on page 10 for a listing of the statutes violated. In particular:

- Dr. Dabb and Mr. Freeman caused or allowed purchases totaling at least \$540,676 to be directed to preferred contractors by evading competitive bid requirements, bid rigging, and falsifying bid documents.
- Jerry Everett Construction, a preferred contractor, charged the District for costs associated with remodeling a home belonging to one of Mr. Freeman's friends.
- Mr. Freeman directed or authorized District employees to use District materials and equipment for improvements to his and his relative's private real property.

In addition, Dr. Dabb and Mr. Freeman unlawfully obtained personal benefit by requesting or accepting gratuities from District contractors for themselves and other District employees. Finally, Mr. Freeman earned interest on a private loan he made to the owner of Phoenix Fence, a preferred contractor.

These financial improprieties occurred primarily because top management had personal interests and relationships with vendors. They engaged in self-dealing, had no regard for responsibilities associated with administering public monies, circumvented internal control structure policies and procedures, and coerced District employees into participating in the fraud.

Finding I

District Administrators Misused Public Monies

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Dr. Dabb directed subordinates to pay for unlawful purchases made in violation of the procurement rules.

By intentionally avoiding competitive procurement requirements and restricting free trade, the District may have paid more than the fair market value for certain construction projects.

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School district procurement rules and other applicable Arizona Revised Statutes exist to help ensure that districts receive the best possible value for the public money they spend, to prohibit restraint of free trade, and to prohibit unreasonable reduction of competition among vendors. However, during the period of July 1991 through June 1996, the Superintendent, Dr. William R. Dabb, and Director of Maintenance, Mr. Gary Freeman, of Cartwright Elementary School District No. 83, and other individuals, knowingly and unlawfully violated those rules and statutes. Moreover, they induced other District employees to violate those rules. As a result, the District lost the benefit of full and open competition and may have paid more than the fair market value for certain construction projects.

Under their leadership, the District officials failed to obtain required sealed bids and written and oral price quotations, they split construction projects into two or more phases to avoid bidding requirements, and they falsified written and oral price quotation sheets. Dr. Dabb, Mr. Freeman, and their employees intentionally avoided required competitive procurement procedures in an effort to restrict free trade and direct construction projects to specific preferred vendors. In addition, they may have committed other illegal acts designed to direct District contracts to their preferred vendors.

School district officials deliberately violated school district procurement rules and intentionally restrained free trade in connection with the expenditure of at least \$540,676 of public monies. Consequently, for construction and construction-related projects costing less than \$15,000, Jerry Everett Construction received 88 percent of the building projects and Phoenix Fence received 100 percent of the fencing projects for three fiscal years. See Exhibit 1 on page 3 for details.

Exhibit 1

Summary of Misuses of Public Monies

| <u>Description</u> | <u>Amount</u> |
|---|------------------|
| Falsified written and oral price quotations | \$302,155 |
| Split purchases | 296,061 |
| Failed to obtain sealed bids, written price quotations, and oral price quotations | <u>114,748</u> |
| Total | <u>712,964</u> |
| Less items duplicated within the above three categories | <u>172,288</u> |
| Total misused public monies | <u>\$540,676</u> |

Source: Vendor invoices, written price quotations, oral price quotation memoranda, vendor confirmations, and investigation reports.

Falsified Written and Oral Price Quotations

Under Gary Freeman's direction, District employees falsified at least 88 price quotations. The District paid \$302,155 to the preferred vendors in those instances for which falsified quotations were retained as supporting documentation. Typical falsifications are described below.

- Written price quotations were altered by "whiting out" the project's name and location from original quotation sheets and using them as support for other projects. Employees attempted to hide the alterations by redrawing the lines appearing on the written price quotations.
- Phoenix Fence (a preferred fencing contractor whose owner is a personal friend of Mr. Freeman's) requested and obtained signed but otherwise blank bid proposal sheets from a competitor fencing contractor. Amounts higher than those proposed by Phoenix Fence were placed on the blank sheets. The purpose of this subterfuge was to demonstrate that required procedures were followed and that Phoenix Fence submitted the low bid.

- District employees completed at least 39 oral price quotation sheets after the work had been completed. They would use the names of legitimate contractors; however, those contractors never actually submitted oral price quotations. At times they would use the Yellow Pages as an inspiration to create names of fictitious contractors.

Split Purchases

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By directing construction jobs to be split, Mr. Freeman was able to ensure that the preferred vendors received most of the District's business.

To avoid compliance with the procurement rules detailed on page 10, Mr. Freeman instructed his staff to keep work orders under \$2,500 or \$5,000. As a result, they split 28 projects costing \$296,061 into 120 phases to avoid obtaining sealed bids, written price quotations, and oral price quotations. Without the illegal splitting, however, bids or price quotations on the 28 projects should have been obtained as follows:

- Sealed bids—8 projects costing \$159,873
- Written price quotations—15 projects costing \$118,076
- Oral price quotations—5 projects costing \$18,112

Frequently both Jerry Everett Construction and Phoenix Fence completed similar construction and fencing work at various schools within the same relatively short period. Mr. Freeman and other District officials allowed the two companies to bill these jobs on several separate invoices so that the individual component amounts would not exceed competitive procurement threshold amounts.

Failure to Obtain Sealed Bids, Written Price Quotations, and Oral Price Quotations

Dr. Dabb unlawfully circumvented required competitive procurement rules by directly and unilaterally authorizing a number of purchases, as described below.

- Authorized surveillance equipment installed at the District office and Estrella Junior High School for \$23,057. The Governing Board, Director of Business Services, and the Assistant Superintendent for Financial Services were not informed of the purchase until the equipment had been installed.

- Purchased carpeting from a preferred vendor for \$8,024 after instructing the District's buyer to cancel carpeting ordered through the state contract. Written price quotations were obtained subsequent to the purchase, and the dates were changed to make it appear that they were received prior to the purchase.
- For three fiscal years, directed work on preparing the District's annual report and parents' handbook to Information Services, a business owned by a social acquaintance, for a total of \$12,919. No attempt was made to obtain written or oral price quotations.
- Bought telephone indexes for \$2,617 without obtaining the required oral price quotations. The supporting documentation improperly indicated the need for "sole-source" procurement; however, even that determination was made after receiving the invoice for the order.

Also, Mr. Freeman did not always ensure that required written and oral price quotations were obtained. We noted 13 instances totaling \$68,131 in which the District failed to obtain quotations for construction projects.

Finding II

Employees Unlawfully Received Economic Benefits

A public official is in a fiduciary position to do business on behalf of the citizens. That business should be conducted at “arm’s length,” in an open, aboveboard manner. For public officials to profit personally from their official business dealings is to violate the public trust.

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Personal relationships between administrators and certain vendors caused conflicts of interest.

Dr. William Dabb and Mr. Gary Freeman profited personally from their relationships with their preferred contractors and the District’s contracted architect. The terms of the architect’s contract made his performance of service for the District dependent on Dr. Dabb and Mr. Freeman’s requests. The District paid its contracted architect \$609,887, \$543,999, and \$445,171 in fiscal years 1993-94, 1994-95, and 1995-96, respectively. District jobs comprised 29 of 36 new projects initiated by the architect in those same years.

- Phoenix Fence gave Mr. Freeman iron fence panels. The panels were installed at the Freeman residence in Cholla Bay, Mexico, next door to the Phoenix Fence owner’s residence.
- Mr. Freeman earned over \$2,000 interest on a private loan he made to the owner of Phoenix Fence.
- The contracted architect hosted an excursion to the San Diego area from August 18 to August 20, 1995. He provided airfare, lodging at the Hotel del Coronado, a charter fishing expedition, and a number of meals. The recipients were Dr. Dabb and his guest, the owner of Information Services; Mr. Freeman and his guest, a recipient of remodeling work done on her home by Jerry Everett Construction; and Mr. Ed Kunkel, Director of Business Services, and his wife. This excursion’s value totaled \$2,996.
- Upon request, the contracted architect provided golf outings for certain District employees.

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Administrators and their guests attended a weekend excursion paid for by the contracted architect.

- The contracted architect also provided other gifts to District employees. These included televisions for District Christmas party raffles, and hams and candy. The value of these gifts totaled \$8,888 for fiscal years 1992-93 through 1995-96.
- Also, numerous meals and alcoholic beverages were provided to District officials and staff as they met with potential and existing District vendors.

Finding III

District Administrators Misused District Resources

An important school district management responsibility is maintaining district facilities for the safety and comfort of its students. However, between January 1991 and December 1996, the Director of Maintenance, Mr. Gary Freeman, and his nephew, Mr. Roger Freeman, a District Principal, used the labor of District employees, District materials, and District equipment to improve real property they owned.

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Mr. Freeman directed employees to work on his private properties.
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As Director of Maintenance, Mr. Freeman was responsible for supervising maintenance personnel. He was also responsible for safekeeping and using District materials and equipment for and on the District property. However, several District employees stated they were asked to work on improvements to Mr. Freeman's private properties and, at times, with District materials. The employees complied, considering such work a condition of their continued employment. Typical examples of such work are described below.

- A District painter used District paint to coat the exterior of Mr. Freeman's Munds Park property. During the same weekend, a District carpet layer installed 80-90 yards of District carpet in the same property. Each employee observed the other using District materials to improve Mr. Freeman's private property.
- A District air conditioning maintenance man examined and repaired units at private rental properties owned by Mr. Freeman. Numerous instances of this work were performed on District time.
- For six months, Roger Freeman had possession of a District tractor for use at his private residence. While in his custody, the tractor, along with Gary Freeman's trailer, was damaged. The District paid for repairs to both the tractor and trailer.

In addition, Jerry Everett Construction worked on remodeling the private residence owned by one of Mr. Freeman's friends, then transferred certain costs of this remodeling to projects that were paid for by the District.

Conclusion

Arizona taxpayers in general and Cartwright Elementary School District No. 83 in particular were denied the benefits of full and open competition and may not have received fair value for certain expenditures for the following reasons.

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Investigative Results:

- Dr. Dabb and Mr. Freeman no longer work for the District.*
- The Attorney General's Office filed a civil racketeering, bid rigging, and antitrust complaint against 4 current or former District employees, 4 vendor businesses, and 4 vendor business owners or directors.*
- The Maricopa County Attorney's Office obtained criminal indictments against 9 persons, including 6 current or former District employees.*

- District administrators manipulated, ignored, or circumvented required school district procurement rules.
- District administrators fostered a climate of disregard for the proper use of public monies.
- District administrators maintained personal relationships with preferred contractors and accepted gratuities from them.

In addition, District administrators misappropriated District resources to their own use and that of their friends.

Subsequent to a hearing on these matters, the Governing Board terminated its contract with the Superintendent, Dr. William R. Dabb, for cause on November 23, 1996. In addition, it allowed its contract with Mr. Gary Freeman to expire on June 30, 1996.

On May 8, 1997, the Arizona Attorney General's Office filed a civil racketeering complaint against various individuals and businesses alleging violations of Arizona procurement, racketeering, antitrust, and malfeasance in office laws.

On June 3, 1997, the Maricopa County Attorney's Office took criminal action against 9 individuals through the Maricopa County Grand Jury. This action, consisting of more than 100 felony counts, includes theft, fraudulent schemes, bid rigging, conspiracy to restrain trade, and criminal damage.

Appendix

Applicable Arizona Revised Statutes

State and local government prosecuting agencies have taken legal action against Dr. Dabb, Mr. Freeman, other District officials, and their preferred vendors for violations of the following Arizona Revised Statutes.

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Exhibit 2

Arizona School District Procurement Requirements

- Purchases of \$2,500 or less were at the Superintendent's discretion.
- Transactions in excess of \$2,500 but less than \$5,000 required verbal price quotations from at least three vendors.
- Transactions costing at least \$5,000 but less than \$10,000 for nonconstruction or \$15,000 for construction required written price quotations from at least three vendors.
- Transactions costing \$10,000 or more for supplies, equipment, or outside professional services or \$15,000 or more for construction required sealed bids.

Source: *Uniform System of Financial Records for Arizona School Districts*

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- **Theft.** A.R.S. §13-1802(A), *Theft; classification*. "A person commits theft if, without lawful authority, such person knowingly. . . converts for an unauthorized term or use services or property of another entrusted to [such person] or placed in [such person's] possession for a limited, authorized term or use; or . . . diverts another's services to his own or another's benefit without authority to do so."
- **Racketeering Act.** A.R.S. §13-2312(B), *Illegally conducting an enterprise*. "A person commits illegally conducting an enterprise if such person is employed or associated with any enterprise and conducts or participates in the conduct of such enterprise's affairs through racketeering."
- **Arizona Procurement Code.** A.R.S. §41-2616(B), *Violations; classification; liability; enforcement authority*. "A person who intentionally or knowingly contracts for or purchases any material, services or construction pursuant to a scheme or artifice to avoid the . . . rules adopted by the state board of education [A.R.S. §15-213]. . . is guilty of a class 4 felony."
- **Arizona Antitrust Act.** A.R.S. §44-1402, *Contract, combination or conspiracy to restrain or monopolize trade*. "A contract, combination or conspiracy between two or more persons in restraint of, or to monopolize, trade or commerce, any part of which is within this state, is unlawful." A.R.S. §44-1416(C), *Government contract, combination or conspiracy to restrain trade or commerce; violation; classification*. "A person who enters into a contract, combination, conspiracy or other act in violation of this section is guilty of a class 4 felony. . . ."

- **Conflict of Interest.** A.R.S. §38-504(C), *Prohibited acts*. “No public officer or employee may use or attempt to use his official position to secure any valuable thing or valuable benefit for himself that would not ordinarily accrue to him in the performance of his official duties. . .” A.R.S. §38-505(A), *Additional income prohibited for services*. “No public officer or employee may receive or agree to receive directly or indirectly compensation other than as provided by law. . . .”

