



A REPORT
TO THE
ARIZONA LEGISLATURE

Special Investigative Unit

Special Investigation

Paradise Valley Unified School District No. 69

Theft and Misuse of Public Monies

August • 2013



Debra K. Davenport
Auditor General

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DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

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August 19, 2013

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Governing Board
Paradise Valley Unified School District No. 69

The Honorable Tom Horne
Office of the Attorney General

The Honorable John Huppenthal
State Superintendent of Public Instruction

The Office of the Auditor General has conducted a special investigation of the North Canyon High School Bookstore for the period July 2007 through November 2009. The North Canyon High School is one of six high schools within the Paradise Valley Unified School District No. 69. The investigation was performed to determine the amount of public monies misused, if any, during that period and the extent to which those monies were misused.

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 Paradise Valley Unified School District No. 69 or the North Canyon High School Bookstore. The Office also does not ensure that all matters involving the District's internal controls, which 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.

Debbie Davenport
Auditor General

Enclosure

SUMMARY

In April 2010, the Paradise Valley Unified School District No. 69 (District) requested that the Office of the Auditor General investigate allegations of financial misconduct by Beverly Hodges, former North Canyon High School (NCHS) bookstore manager.¹ As a result of our investigation, we determined that Ms. Hodges used a fraud scheme to embezzle and misuse public monies, creating false documents to conceal her misconduct. As a result, we submitted our report to the Arizona Attorney General's Office, and they have taken criminal action against Ms. Hodges resulting in her plea agreement to felony theft (see Conclusion on page 15 of this report).

Our investigation revealed that from July 2007 to November 2009, Ms. Hodges violated state laws related to theft, misuse of public monies, fraudulent schemes, and false filing by misusing at least \$72,511 of public monies, embezzling \$67,162 of this amount for her own purposes and misusing the remaining \$5,349 for the bookstore staff's personal food and beverage purchases. These monies were received at the NCHS bookstore for payment of extracurricular tax credit donations and for various fees such as those related to parking permits, athletic programs, certain classes, student identification card replacements, and tests. During the same time Ms. Hodges embezzled monies from the District, she deposited more than \$77,500 cash into her personal bank account, commingling this cash with other personal monies. These monies were then used to pay for her personal car and home equity loans, and for purchases at various retail outlets, grocery stores, and restaurants. Finally, to conceal her misconduct, Ms. Hodges falsified over 300 public documents that were related to her fraud scheme.

Specifically, Ms. Hodges embezzled district money by taking cash from the NCHS bookstore cash register throughout the school year. In addition, Ms. Hodges improperly instructed bookstore staff to withhold certain cash receipts from the deposit, which were later misused to purchase food and beverage items for herself and the bookstore staff. Ms. Hodges concealed her actions by rekeying transactions into the cash register, omitting amounts for which she had taken cash, then generating a new, false cash register summary tape she used to prepare daily deposit records. Ms. Hodges submitted these fraudulent deposit records to the NCHS principal and district officials.

Ms. Hodges embezzled and misused public monies by both abusing her authority as the NCHS bookstore manager and by taking advantage of NCHS' inadequate controls over the collection and deposit of district monies. Additionally, the NCHS principal at the time and certain district officials failed to exercise an appropriate level of oversight over Ms. Hodges' activities.

Investigation highlights

Former North Canyon High School Bookstore Manager Beverly Hodges:

- Misused \$72,511 of district money, embezzling \$67,162 of this amount for her own purposes
- Falsified 323 public documents in order to conceal her misdeeds

¹ This investigation of Beverly Hodges was separate from our investigation of former NCHS athletic director Brian Dyer (*Special Investigative Report Paradise Valley Unified School District No. 69 Theft and Misuse of Public Monies March 2013*).

In particular, the principal continually failed to examine documents or otherwise verify that bookstore deposit documentation was appropriate. In addition, the principal and certain district officials failed to take corrective action in response to several district internal audit reports of improper bookstore deposits. Moreover, district administrators allowed the NCHS bookstore to use an outmoded cash register system without ensuring that cash-handling, recordkeeping, and depositing duties were appropriately separated and adequate controls were in place. Lastly, district officials failed to properly review and reconcile revenue reports, thereby overlooking red flags of potential misuse of public monies.

Although no internal control system can completely prevent dishonest behavior such as Ms. Hodges', there are ways to improve control over public monies to help deter and detect fraud (see Recommendations on page 13 of this report). In the time since the Office of the Auditor General's investigation began, district administration identified and implemented some improvements to its controls over payments received at its bookstores, including providing additional annual training to district and school office staff on cash-handling procedures, adding cash-handling criteria to principal performance evaluations, eliminating obsolete cash registers at the NCHS bookstore, and purchasing and implementing a new student payment system to monitor bookstore collections.

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◆ concluded

INTRODUCTION & BACKGROUND

Paradise Valley Unified School District No. 69 (District) is located in the metropolitan area of Phoenix, encompassing portions of northeast Phoenix and north Scottsdale. The District is composed of 32 elementary schools, 8 middle schools, 6 high schools, and 1 online school. The District is accountable to taxpayers for the nearly \$290 million it received in fiscal year 2012 to educate approximately 33,000 students. The District has five publicly elected Governing Board members who are responsible for establishing all district policies and are the final authority over all school district business.

The District's North Canyon High School (NCHS), with approximately 2,456 students, employs one manager and one clerk to handle bookstore operations.

Beverly Hodges' district employment included bookstore duties

Ms. Hodges began her employment with the District in October 1985 as a noon duty aide at one of the District's elementary schools. Over time, Ms. Hodges held several other positions within the District, including special education aide, receptionist, and records clerk. In July 2003, NCHS hired Ms. Hodges as the bookstore clerk and promoted her to bookstore manager in July 2005.

Accordingly, Ms. Hodges was responsible for managing bookstore operations, including helping to collect, process, and record student and school-related fees (e.g., parking permits, lost textbooks, testing, and class fees) and extracurricular tax credit donations. She was also responsible for depositing those payments related to the Auxiliary Operations Fund and other miscellaneous receipts. In addition, Ms. Hodges managed bookstore supplies, school textbooks, and student identification cards, along with supervising the bookstore clerk. The clerk's responsibilities included helping to collect, process, and record student and school-related fees, issuing textbooks to students, and depositing the payments related to the Student Activities Fund.

Ms. Hodges officially retired from the District in January 2009; however, she continued to work as the bookstore manager in a contracted position until her final departure on November 20, 2009.²

Ms. Hodges' bookstore manager responsibilities included:

- Collecting, processing, and recording student and school-related fees
- Depositing Auxiliary Operations Fund and other miscellaneous receipts
- Processing bookstore expenditures for supplies
- Ordering, maintaining, and issuing school textbooks
- Issuing student identification cards
- Supervising bookstore clerk

² Ms. Hodges was contracted to work at the District through an Arizona corporation. Individuals in these contracted positions have generally retired from public school systems and receive Arizona State Retirement System benefits, but they are contracted and paid to work in their original position through the Arizona corporation.

New NCHS bookstore manager determined monies were missing from prior deposits

The bookstore manager who replaced Ms. Hodges soon discovered discrepancies between the amounts previously recorded in NCHS's student payment system and the amounts deposited into the District's bank account. Specifically, the new bookstore manager determined that for at least the last few months that Ms. Hodges had been managing the bookstore, some deposits were consistently less than the amount collected. She informed the District's internal auditor about these discrepancies during the annual bookstore audit in March 2010. As a result, the District requested the Office of the Auditor General to perform a review to determine the amount of public monies misused, if any, and the extent to which those monies were misused.

FINDING 1

Beverly Hodges embezzled and misused public monies

From July 2007 through November 2009, Ms. Hodges, former North Canyon High School (NCHS) bookstore manager, misused \$72,511 of public monies, embezzling approximately \$67,162 of that amount for her own personal purposes (see Table 1). Ms. Hodges misspent the remaining \$5,349 on food and beverage items for bookstore staff. The embezzled monies included payments made by parents and other individuals for extracurricular tax credit donations, parking permits, athletic programs, certain classes, student identification card replacements, lost textbooks, and testing fees. These monies belonged to the Paradise Valley Unified School District No. 69 (District) for the benefit of NCHS students and should have been deposited into the appropriate district accounts. In addition, Ms. Hodges deposited over \$77,575 cash into her personal bank account during the same time frame she embezzled monies from the bookstore. This cash was commingled with her salary and other personal monies; she then used these monies to pay for her personal expenses.

Table 1: Public monies embezzled and misused by Ms. Hodges July 2007 to November 2009

Description	Amount
Embezzled and misused	\$67,162
Misused for staff food and beverages	<u>5,349</u>
Total embezzled and misused	<u>\$72,511</u>

Source: Auditor General staff analysis of district records and interviews with district staff.

Ms. Hodges misappropriated district monies by taking cash and preparing false records to conceal her actions

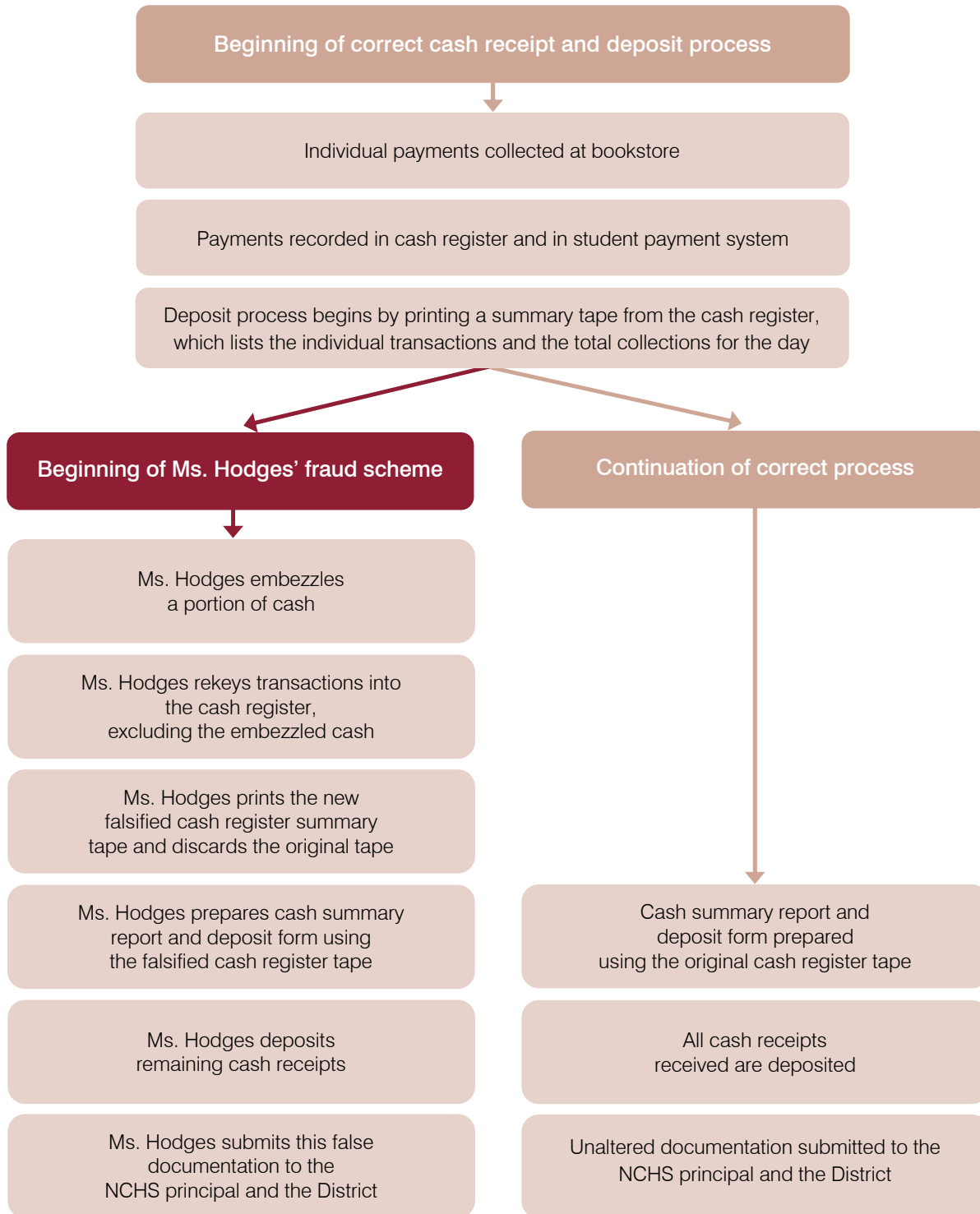
Ms. Hodges embezzled public monies for over 2 years by taking cash from the bookstore cash register. She attempted to disguise her theft by creating false receipt records. Nevertheless, her scheme, illustrated in Figure 1 on page 5, was revealed by Auditor General staff analysis of district records, including cash register tapes Ms. Hodges had falsified and student payment system accounts that had not been altered.³

³ NCHS bookstore cash registers automatically assigned a unique, sequential number to each summary tape generated, called the Z number. Auditor General staff noted large and improper gaps in the Z number sequences, indicating a potential irregularity.

Cash register tapes falsified—Typically, at the end of the school day, Ms. Hodges generated a false cash register tape by rekeying most transactions into the cash register, but omitting amounts for which she had taken cash. She then discarded the original cash register tape and used the false one to report bookstore sales to the NCHS principal and the district office. In an interview with Auditor General staff, Ms. Hodges acknowledged that she had rekeyed transactions and created false cash register tapes to conceal the money she had taken from the District for her own personal benefit.

Student payment system accounts unaltered—Although Ms. Hodges was able to exclude payments from the bookstore's cash register tapes, she was not able to alter the District's student payment system. As a result, Ms. Hodges' theft amounts were detectable because nearly all payments received at the bookstore were related to individual students and were therefore specifically recorded in the District's student payment system. Hence, these student accounts inclusively identified amounts that Ms. Hodges had embezzled and deceptively omitted from the cash register tapes.

Figure 1: Comparison of Ms. Hodges' fraud scheme and the correct cash receipt and deposit process



Source: Auditor General staff interview of district personnel and analysis of district records.

Because of Ms. Hodges' misappropriations, several school account balances were understated

Because Ms. Hodges falsified documents by omitting the amounts she embezzled, her actions resulted in several NCHS account balances being understated by the amount she embezzled. As illustrated in Table 2 below, Ms. Hodges underreported monies collected for various purposes totaling \$67,162, the majority of which were intended for tax credit donations, class fees, and parking permits. Although many of these payments were made by check, Ms. Hodges did not embezzle actual check payments. Rather, she substituted checks for the cash she had embezzled. For example, on August 20, 2009, the bookstore collected and recorded a \$180 check payment for student parking fees. Ms. Hodges omitted this transaction from the deposit documents, making it appear as though this \$180 parking fee was never received nor deposited. However, Ms. Hodges submitted this check for deposit with the District on August 27, 2009, but withheld \$180 cash from another payment made in cash. Because this check was not recorded as a parking fee or documented as deposited, the District did not know it existed, which resulted in the parking account being understated by \$180.

Table 2: NCHS account balances understated as a result of Ms. Hodges' misappropriations July 2007 to November 2009

NCHS account description	Amount understated
Tax credit donations	\$24,370
Class fees	19,030
Parking permits	12,977
Athletic-related accounts ¹	5,108
Testing fees	2,659
Lost textbooks	2,431
School store proceeds	304
Lock deposits	283
Total theft	<u>\$67,162</u>

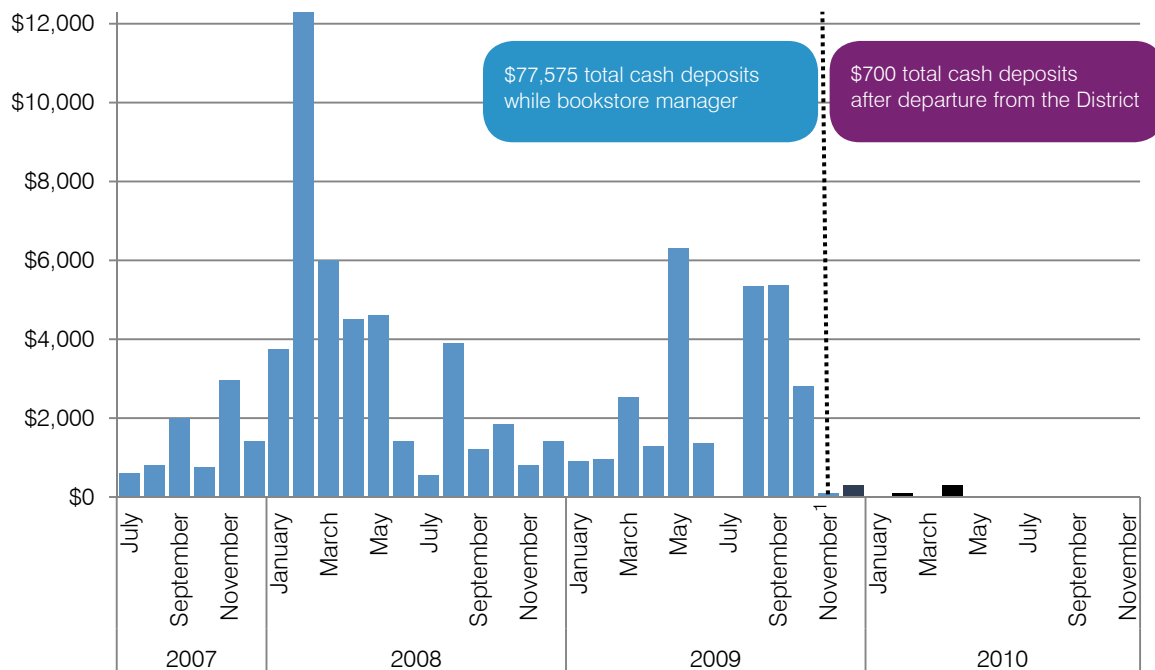
¹ NCHS athletic-related accounts include Arizona Interscholastic Association and athletic-related fees.

Source: Auditor General staff analysis of district records and interviews with district staff.

Ms. Hodges deposited a large amount of cash into her personal bank account

From July 2007 up until her departure from the District in November 2009, Ms. Hodges deposited \$77,575 cash into her personal bank account. As illustrated in Figure 2, these deposits occurred during the same time Ms. Hodges embezzled monies while she was the bookstore manager. In the 12 months following her departure from NCHS, Ms. Hodges' cash deposits greatly decreased to a total of \$700 for that year.

Figure 2: Monthly cash deposits into Ms. Hodges' personal bank account while bookstore manager and after her November 2009 departure July 2007 to November 2010



¹ Ms. Hodges departed from the District in November 2009.

Source: Auditor General staff analysis of Ms. Hodges' personal bank account records.

This cash was commingled with her salary and with other personal monies. Ms. Hodges then used these monies for her own personal benefit, including paying for personal purchases at various retailers, grocery stores, and restaurants, and for her personal credit card debt, as well as car and home equity loans. For example:

- **Personal purchases**—From July 2007 to November 2009, Ms. Hodges spent nearly \$200,000 from her personal bank account on her credit card payments and on purchases at various retail outlets, grocery stores, and restaurants.
- **Prepayments on car loan**—During the 9 months leading up to her departure from the District, Ms. Hodges made ten prepayments totaling \$4,891 on her car loan. These prepayments were in addition to the \$329.79 that was normally due each month.
- **Prepayments on home loan**—From July 2007 to November 2009, Ms. Hodges remitted a total of \$40,920 to pay her home equity loan, which was \$37,398 more than the required interest-only monthly payments. These prepayments helped to reduce the principal amount owed on the home loan. The 5 months leading up to her departure from the District represented a significant portion of her prepayments, which totaled \$17,128. Afterward, Ms. Hodges' prepayments decreased greatly, totaling only \$2,105 in the 11 months following her departure from the District.⁴

Ms. Hodges unlawfully used district monies for bookstore staff food and beverages

From July 2007 to November 2009, Ms. Hodges misused public monies totaling at least \$5,349 by improperly directing bookstore staff to withhold certain cash receipts that were later used to purchase food and beverage items for herself and the other bookstore staff. This money belonged to the District and should have been deposited into the appropriate district account. According to Arizona Revised Statutes §35-301, "Duties and liabilities of custodian of public monies," it is a felony to appropriate public monies for personal use or for use by others.

Specifically, Ms. Hodges instructed her staff to not deposit monies received for replacement student identification cards, but to put the money in the bookstore's safe for use in purchasing food and beverage items for the bookstore staff. Ms. Hodges had no authority to withhold, or direct other employees to withhold, public monies from being deposited into the appropriate district account. Therefore, Ms. Hodges inappropriately misused these public monies for her and her staff's personal snacks.

⁴ Auditor General staff reviewed Ms. Hodges' personal bank records through October 2010.

FINDING 2

Beverly Hodges falsified documents to conceal her improper actions

From July 2007 to November 2009, Ms. Hodges concealed her thefts from the Paradise Valley Unified School District No. 69 (District) by creating at least 323 sets of false documents. These false records related to monies received at the North Canyon High School (NCHS) bookstore that should have been deposited in the District's accounts, but were instead embezzled by Ms. Hodges as described in Finding 1. Specifically, Ms. Hodges prepared 323 fraudulent daily deposit packages to conceal her theft of NCHS receipts. Deposit packages typically included a set of three documents: cash register tape, cash summary report, and deposit slip. She provided these documents to the NCHS principal for review and approval, later submitting the approved documents to the District, each time falsely purporting the information was true.

As described in Figure 1 on page 5, Ms. Hodges created false cash register summary tapes at the end of the day by rekeying transactions and omitting amounts for which she had embezzled cash. She used these false cash register tapes to prepare cash summary reports thereby listing false daily totals of various Auxiliary Operations Fund and miscellaneous receipts and causing NCHS account balances to be understated. Ms. Hodges then prepared the deposit slip to match the other records she fabricated and submitted this package of fraudulent documents to the NCHS principal. After the principal signed them, Ms. Hodges sent the package to the District, representing the deceptive documents to be genuine and true.

FINDING 3

Former NCHS principal and certain district officials failed to safeguard and control district monies

The North Canyon High School (NCHS) principal at the time of Ms. Hodges' misappropriations failed to properly protect and control Paradise Valley Unified School District No. 69 (District) monies she was responsible for, and district officials did not ensure adequate internal controls were in place or that reports of financial irregularities were properly addressed. Specifically, the principal continually failed to evaluate or otherwise determine that the bookstore's deposit documents were appropriate, and she did not respond to several district staff reports of improper bookstore deposits. Likewise, certain district officials let the NCHS bookstore use an outmoded cash register system without ensuring adequate internal controls were in place. Officials also failed to properly review and reconcile revenue reports, thereby overlooking red flags of potential misuse.

The principal signed each of the bookstore's deposit packages; however, she acknowledged to Auditor General staff that she did this without examining any of the documentation or otherwise ensuring the amounts were properly and accurately recorded. Moreover, when expressly informed of improper bookstore deposits, she still failed to act. Specifically, as early as 2003, the District's internal auditor reported to her and to district officials on a nearly annual basis that the bookstore deposits had incomplete or inaccurate source documentation. Certain district officials failed to require the principal to correct these deficiencies.

District officials also did not ensure that NCHS bookstore duties were appropriately separated to compensate for the use of an outmoded and easily manipulated cash register. NCHS was the District's only high school bookstore still using a cash register to collect and record cash receipts. The other five high school bookstores used the student payment system to record these receipts. Nonetheless, the District was unable to refute Ms. Hodges' claims that she could not print receipts from the student payment system and thereby allowed her to continue using the cash register. Accordingly, Ms. Hodges was able to manipulate this outdated system and conceal her misdeeds because cash-handling, recordkeeping, and depositing duties were not appropriately separated. Specifically, Ms. Hodges was responsible for collecting and recording receipts, generating cash register summary tapes, and preparing the daily cash summary report and associated deposit.

Further, district officials did not recognize red flags of potential misuse. In particular, although all NCHS bookstore deposit packages were submitted to the District for review and reconciliation with other revenue reports, officials did not notice large and irregular gaps in the Z number sequence of the bookstore's cash register tapes (see page 3). If district officials had followed up, comparing transactions on the cash register tapes to those in the student payment system, they would have been able to discover the discrepancies and stop Ms. Hodges' fraud scheme.

RECOMMENDATIONS

In the time since the Office of the Auditor General's investigation began, district administrators identified and implemented improvements to controls over its bookstores' cash receipts process. Specifically, district administration reported that it conducted additional annual trainings for district and school office staff about cash-handling procedures. The District also updated principal performance evaluations to include criteria outlining the employee's responsibilities for following these cash-handling procedures. Further, it purchased and implemented a new bookstore student payment system, which now allows the District to monitor all of its school bookstores' financial activity online and in a timely manner. It also created two accounting positions at the District to perform reconciliations between the student payment system and the cash receipt documentation, accounting records, and bank statements. Finally, the District discontinued using cash registers in the NCHS bookstore, standardizing procedures with the other high school bookstores.

However, there are additional actions the District could have taken and should take now to improve control over public monies and help deter and detect fraud. Specifically, the District should:

1. Ensure that no single employee has responsibility for cash-handling and recordkeeping functions. Specifically, the bookstore employee who receives and documents the cash collections should not also reconcile sales to cash collections or prepare the deposit. In addition, the District should train an independent school employee how to review all supporting documentation, such as the student payment system report, deposit slip, and cash summary report, to ensure that all monies are appropriately and accurately documented.
2. Continue to perform reconciliations between the cash receipts documentation and the accounting records and bank statements on at least a monthly basis. In addition, any adjustments to the revenues recorded should be fully reviewed and contain the appropriate supporting documentation. This will help ensure accuracy and allow for the early detection of errors or irregularities.
3. Continue to provide training to those school office employees, including principals, assistant principals, and bookstore staff, responsible for collecting monies to educate them about district and *Uniform System of Financial Records for Arizona School District* policies and procedures concerning cash receipts. These policies and procedures should be periodically updated as necessary. For accountability purposes, the District should consider requiring employees to sign a training log or form acknowledging their understanding of these policies and procedures. This form can be maintained in a master file or within each employee's personnel file.

Additionally, the District should consider including criteria in bookstore employee performance evaluations outlining the employees' responsibilities for following cash-handling procedures.

4. Ensure that district and school administrators appropriately address deficiencies listed in external financial audit reports, as well as internal audit reports. Specifically, district administrators, including those who oversee school principals, should monitor these audit reports and ensure that, when applicable, school principals address and correct those deficiencies identified therein. Additionally, the District should consider including criteria in principal performance evaluations outlining the principals' responsibilities for correcting deficiencies.

CONCLUSION

On August 16, 2013, Ms. Hodges pled guilty to one felony count related to theft. As part of the accepted plea agreement with the Attorney General's Office, Ms. Hodges agreed to pay \$72,511 in restitution to the Paradise Valley Unified School District No. 69.

