



A REPORT
TO THE
ARIZONA LEGISLATURE

Special Investigative Unit

Special Investigation

Santa Cruz Valley Union High School District No. 840

Theft and Misuse of Public Monies

SEPTEMBER • 2007



Debra K. Davenport
Auditor General

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September 14, 2007

Members of the Arizona Legislature

Governing Board
Santa Cruz Valley Union High School District No. 840

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 Santa Cruz Valley Union High School District No. 840 for the period February 2005 through February 2006. The investigation determined 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 Santa Cruz Valley Union High School District No. 840. 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.

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.

Debbie Davenport
Auditor General

Enclosure

SUMMARY

In September 2006, the Pinal County Attorney's Office requested that the Office of the Auditor General investigate allegations of financial misconduct by Ms. April Smith, former student activities secretary for the Santa Cruz Valley Union High School District No. 840. As a result, our Office conducted an investigation of those financial improprieties and submitted our report to the Pinal County Attorney's Office. During our investigation, we determined that Ms. Smith embezzled and misused public money as well as falsified public records in order to conceal her crimes. The Pinal County Attorney has taken criminal action against Ms. Smith, which resulted in her indictment on felony charges. See the Conclusion on page 11 of this report.

Our investigation revealed that from February 2005 to February 2006, Ms. Smith embezzled at least \$11,000 and misused an additional \$7,899. This former employee used money raised by students for their activities such as prom and class trips and for uniforms to pay \$11,000 worth of her personal expenses including childcare, automobile insurance, and a trip to Disneyland. Ms. Smith also misused an additional \$7,899 of public money by failing to deposit student activities cash and checks into the District's bank account. Instead, she improperly kept those receipts in her desk drawer, including some checks that were kept there for almost a year, which allowed Ms. Smith to perpetuate her theft scheme. Further, she attempted to conceal her criminal actions by producing false financial reports regarding the student activities finances.

Despite repeated recommendations from the District's external auditors, management failed to establish appropriate safeguards over these student activities monies. The District's lack of internal controls allowed Ms. Smith to embezzle money for a year without being detected. Ms. Smith controlled student activities cash receipts from the point of collection to deposit without any oversight. In addition, no other employee consistently reviewed the bank statements or otherwise verified reported transactions.

Investigation Highlights:

- ◆ Ms. Smith embezzled at least \$11,000.
- ◆ Ms. Smith misused public money by withholding \$7,899 from the District for almost a year.
- ◆ Ms. Smith falsified public records to conceal her fraudulent scheme.

♦

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INTRODUCTION & BACKGROUND

The Santa Cruz Valley Union High School District No. 840 is located in Eloy, Arizona, within the Pinal County boundaries. Santa Cruz Valley Union High School is the sole school in the District, with approximately 500 students in grades 9 through 12. The District is accountable to its students, their parents, and the local community for the quality of education provided. The District is also financially accountable to taxpayers for the more than \$6 million it received in fiscal year 2006 to provide this education to its enrolled students.

As the District's student activities secretary since August 2004, Ms. April Smith was responsible for the proper accounting of monies raised by student organizations within the District. Ms. Smith worked under the supervision of the District's business manager. Prior to holding this position, Ms. Smith assisted the business manager with accounts payable and invoice processing for 2 years.

On March 3, 2006, Ms. Smith personally repaid the District \$11,000 by depositing cash directly into the District's student activities bank account. She admitted to the business manager that she had stolen district monies and she resigned from her position.

History of financial mismanagement

Over the past 18 years, the District has had a history of problems relating to its internal control deficiencies and failure to comply with the *Uniform System of Financial Records* (USFR). The USFR prescribes the minimum internal control policies and procedures to be used by Arizona school districts for accounting, financial reporting, budgeting, attendance reporting, and various other compliance requirements. Since 1989, the District's external auditors have made various recommendations to establish and strengthen key internal controls, including, but not limited to, student activities cash receipts; segregating the cash-handling and recordkeeping functions among employees for the District's bank accounts; and following School District Procurement Rules. For the year ended June 30, 2004, the District was found to be in noncompliance with the USFR. A subsequent status review on the District relating to those deficiencies and deficiencies cited in the District's audit reports for the year

ended June 30, 2005, found the District in continued noncompliance. As a result, in September 2006 the Arizona State Board of Education directed the Superintendent of Public Instruction to withhold state monies from the District until the deficiencies were corrected. Since October 2006, \$95,879 has been withheld. The District's poor financial management also directly impacts its mission to educate its students. For fiscal year 2006, this district ranked among the lowest in the State in terms of how much money it spent on classroom activities (188 of 229 districts).

FINDING 1

Employee embezzled public monies

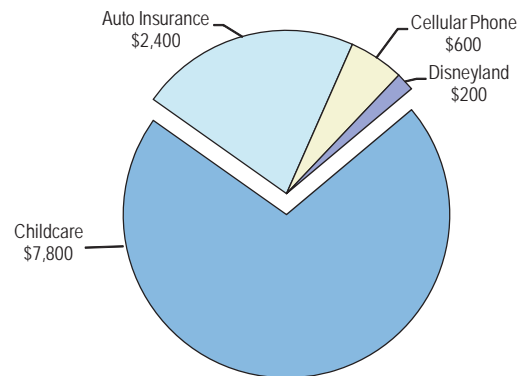
From February 2005 to February 2006, Ms. April Smith, in her capacity as student activities secretary, embezzled at least \$11,000 of Santa Cruz Valley Union High School District monies to pay her personal debts. Ms. Smith used the stolen monies primarily to pay her childcare expenses, but she also used the money to pay her monthly cell phone bill and automobile insurance, and for a winter trip to Disneyland for her family. Over this 1-year period, Ms. Smith repeatedly violated state laws related to theft, misuse, and fraudulent schemes to pay for these personal expenses. In addition, Ms. Smith misused at least \$7,899 by withholding cash and checks from the District and storing them in her office desk drawer for periods ranging from 19 to 340 days after their collection.

Ms. Smith was solely responsible for collecting, recording, depositing, and reconciling all receipts raised by student organizations. In fact, she exercised complete control over the District's student activities account with little to no supervision. As such, management may have detected or deterred Ms. Smith's thefts had proper monitoring and oversight identified her failure to properly account for and safeguard student activity receipts and consistently prepare bank reconciliations.

Skimming cash before deposit

From February 2005 through February 2006, Ms. Smith embezzled at least \$11,000 and she used the monies to pay her personal expenses. Based on Ms. Smith's explanation of those expenses, at a minimum she used the embezzled monies to pay her personal debts, as illustrated in Figure 1.

Figure 1: Use of Embezzled Monies February 2005 through February 2006



Source: Auditor General staff interview of April Smith.

Ms. Smith collected student activities receipts from teachers and students within the District on a regular basis. However, Ms. Smith did not deposit or record on any district record the total amount of money she received on behalf of the student activities fund. Instead, she kept some of the cash, placed some cash and checks in her desk drawer, and deposited any remaining cash and checks. Ms. Smith continued this scheme for approximately 1 year, taking district money as it was available and using it for her personal expenses. Her scheme was discovered during the last week of February 2006, when the financial auditors were scheduled to arrive. Ms. Smith indicated to Auditor General staff that she did not come to work because she was afraid the auditors would detect her thefts. During her absence, district employees discovered \$7,899 in her desk drawer.

In March 2006, Ms. Smith personally repaid the District \$11,000. She admitted to stealing from the District, and she submitted her resignation.

District bank statements, deposit records, and monthly financial reports revealed that Ms. Smith recorded approximately \$7,600 of her thefts. Ms. Smith deliberately failed to record the remaining amounts of cash she took from student activities receipts. Ms. Smith could not remember the exact amount she had stolen from the District and stated that she could repay only \$11,000. On March 3, 2006, Ms. Smith repaid the District \$11,000 by depositing that amount into the student activities bank account. She obtained that amount in cash by selling her automobile and receiving a gift from a relative. On March 4, 2006, Ms. Smith tendered her resignation.

Withholding deposits

From March 2005 through February 2006, Ms. Smith misused at least \$7,899 of public money. Ms. Smith intentionally withheld from the District \$5,265 in cash and 39 checks totaling \$2,634, with check dates ranging from 19 to 340 days after the receipts were collected. Accordingly, a district employee who misuses public monies violates state law, and such conduct constitutes a felony as prescribed under A.R.S. §38-301.

Because Ms. Smith withheld almost \$8,000 from the District for just under a year, the District lost \$1,343 in revenues.

Because of Ms. Smith's failure to negotiate the checks in a timely manner, the District also suffered a financial loss of at least \$1,343. Nine checks dated as far back as March 2005 could not be cashed or deposited when they were recovered almost a year later because the accounts upon which they were written were either closed or had insufficient funds.

FINDING 2

Employee tampered with public documents

From June 2005 to February 2006, Ms. Smith intentionally filed at least seven public documents with the District that contained false financial information. Consequently, a district employee who knowingly tampers with a public record violates state law, and such conduct constitutes a felony as prescribed under A.R.S. §13-2407. As the student activities secretary, Ms. Smith was responsible for preparing a monthly financial report regarding the student activities account for the District's Governing Board's review and approval. Because Ms. Smith was pilfering money from the student activities revenues, she chose to hide her criminal behavior by submitting false financial information to the Governing Board in which she reported cash balances that were much higher than the actual bank account balances. As illustrated in Exhibit 1 below, Ms. Smith reported balances that were ultimately more than \$15,000 greater than the amount actually in the District's bank account.

Ms. Smith created false financial reports to conceal her embezzlement of district money.

Ms. Smith presented these reports during public meetings, falsely purporting the amounts as true and accurate account balances. Consequently, the Governing Board approved inaccurate student activities financial reports, filed according to laws governing open meeting and public document procedures.

Exhibit 1: Falsified Student Activities Account Financial Reports June 2005 through February 2006¹

<u>Report Date</u>	<u>Report Date</u>	<u>Bank Balance</u>	<u>Overstated Cash</u>
June 2005	\$25,743	\$23,739	\$ 2,004
August 2005	\$27,867	\$24,728	\$ 3,139
October 2005	\$33,042	\$20,505	\$12,537
November 2005	\$37,971	\$24,152	\$13,819
December 2005	\$37,092	\$24,851	\$12,241
January 2006	\$39,172	\$25,114	\$14,058
February 2006	\$37,291	\$21,761	\$15,530

¹Monthly reports were not available for July and September 2005.

Source: Auditor General staff analysis of district Governing Board reports and district bank records.

FINDING 3

District management failed to establish and maintain adequate controls

The District's management failed to implement an adequate system of internal controls over its student activities cash receipt process. In fact, the District's insufficient segregation of duties and ambiguous or absent policies weakened its control environment and allowed Ms. Smith to embezzle and misuse public monies without being detected for approximately 1 year.

Specifically, management allowed Ms. Smith to collect, record, deposit, and reconcile all student activities cash and cash receipts without any oversight. An appropriate level of internal control could have been accomplished by assigning responsibility for a portion of the cash and cash receipt process to other employees. At a minimum, cash-handling functions should be separate from recordkeeping activities. Employees who received cash should not record cash collections into the District's accounting ledger or make deposits. Additionally, employees who received cash should not reconcile this information to receipt and deposit documentation. For example, the District could have assigned the business manager to reconcile the bank account, while other administrators, such as the accounts payable clerk and the receptionist, could divide the responsibilities of preparing the bank deposit and recording the receipts. Further, maintaining a secondary review process, such as requiring the superintendent's approval of monthly bank reconciliations, could have contributed to an appropriate level of internal control. However, because Ms. Smith was responsible for all of the cash-handling, recordkeeping, and reconciliation functions, she was able to embezzle student activities cash without detection.

In addition, management failed to adequately safeguard cash by ensuring that it was deposited in a timely manner, accurately, and intact. Management was aware of the constant stream of cash and checks received by Ms. Smith on behalf of student organizations. In order to safeguard cash receipts, management should deposit district monies into the bank account at least weekly, or daily when significant. At the time the theft was discovered, Ms. Smith had failed to deposit \$7,899 and had stored

the cash and checks in her desk drawer unnoticed by management. Some checks had been stored there from 19 to 340 days after the receipts were collected. In addition, management did not ensure that monies were deposited intact, meaning that all cash receipts were deposited and recorded in their entirety and true form. The appropriate policies and procedures could have prevented or at least detected Ms. Smith's misuse by establishing guidelines and independent review procedures.

Finally, district management failed to properly supervise Ms. Smith. Ms. Smith's failure to make timely, accurate deposits, consistently prepare monthly bank reconciliations, and complete correct financial reports went undetected. Not only did management fail to ensure monies were deposited intact, but management did not require and review any bank reconciliations. Further, management failed to properly review monthly financial reports Ms. Smith prepared for approval from the District's Governing Board. Management should establish appropriate policies and procedures to provide for an independent reconciliation between revenues received and deposited as well as an independent review of any financial reports.

RECOMMENDATIONS

Over the years, the District has repeatedly failed to implement the necessary internal controls. That failure has now resulted in the theft of district monies. To help protect and ensure the proper use of public monies, the District should establish effective internal controls over cash receipts including policies, procedures, and monitoring activities. Specifically, the District's Governing Board should ensure that the following actions are taken:

1. The Governing Board should establish and provide formal, written policies governing student activities procedures. The policies should provide clear guidelines for the segregation of cash-handling and recording duties, as well as proper supervision of all student activities functions.
2. The District should ensure that no employee has the ability to carry out all steps in the cash receipting process. Accordingly, the District should properly separate among employees the following cash-handling functions:
 - Receiving cash
 - Preparing bank deposits
 - Making deposits at the bank
 - Recording receipts into the accounting system

These functions can be effectively separated among the business manager and other administrative staff.

3. The District should document sales at student activities events by issuing prenumbered cash receipt forms or tickets, by using a cash register, or by performing counts of items on hand before and after each activity.
4. The District should prepare cash collection or activity reports for student activities events to document and reconcile cash collections and tickets or items sold. If it is not practical to sell tickets or count items before and after the sale, such as for bake sales, clubs should prepare cash collection reports to document cash collected.

5. The District should deposit all student activities cash receipts daily, if significant, or at least weekly into the student activities bank account, and retain bank deposit slips and reconcile them to validated deposit slips.
6. The District should prepare complete and accurate monthly written bank reconciliations for the student activities bank account to reconcile bank and checkbook balances. After the reconciliations have been prepared, investigate and resolve all differences, and make appropriate corrections. Also, ensure that the checkbook balance used to reconcile the student activities bank statements agrees to the student activities check register and accounting records. Bank reconciliations should be prepared by an employee not responsible for handling cash or issuing checks.
7. The District should ensure that a report of cash receipts, disbursements, transfers, and cash balances is prepared monthly by the student activities treasurer and submitted to the Governing Board in a timely manner.
8. The District should ensure proper monitoring procedures are performed to govern student activities duties. Controls can be further strengthened by employing an appropriate secondary review and approval process. Accordingly, the District should include the following monitoring procedures that review:
 - Bank account reconciliations
 - Financial reports submitted to the Governing Board

CONCLUSION

On September 13, 2007, the Pinal County Attorney's Office took criminal action against Ms. Smith through the Pinal County Grand Jury. This action resulted in the indictment of Ms. Smith on a total of 11 counts related to theft, fraudulent schemes, misuse of public money, and tampering with a public record.