



**C**SIS California School Information Services

# **San Bernardino County Superintendent of Schools**

## **Extraordinary Audit**

of the

## **Hope Academy Charter School**

May 2, 2016

**Joel D. Montero**  
Chief Executive Officer







May 2, 2016

Ted Alejandre, Superintendent  
San Bernardino County Superintendent of Schools  
601 North E Street  
San Bernardino, CA 92415

Dear Superintendent Alejandre:

A study agreement between the Fiscal Crisis and Management Assistance Team (FCMAT) and the San Bernardino County Superintendent of Schools to provide an Assembly Bill 139 extraordinary audit of the Hope Academy Charter School was signed on January 7, 2016. Specifically, the agreement states that FCMAT will perform the following:

Assign professionals to conduct an extraordinary audit on behalf of the Morongo Unified School District/Hope Academy Charter School (Palm Desert).

1. Evaluate policies, procedures, internal controls for procurement practices performed by the charter school.

Evaluation of Policies and Procedures:

- a. Determine whether the charter's petition, memorandum of understanding, charter school bylaws or other policies and administrative regulations exist that include language pertaining to conflicts of interest pursuant to Government Code Section 1090.
- b. Identify documented positions with responsibility for initiating, reviewing, approving, and reconciling procurement activities.
- c. Review financial processes related to key purchasing activities including procurement authorization and vendor payments.

Evaluation of Internal Controls:

- a. Evaluate processes for adequate separation of duties and proper authorizations and approvals.
- b. Evaluate monitoring procedures and verify that controls are operating properly.
- c. Evaluate controls that prevent management from overriding internal controls to prevent misappropriation of funds.

**FCMAT**

Joel D. Montero, Chief Executive Officer

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Administrative Agent: Christine L. Frazier - Office of Kern County Superintendent of Schools

- d. Determine if clearly established lines of authority and responsibility exist and are documented in organizational charts.
2. Review the charter's policy on conflict of interest and the requirements under the Fair Political Practices Commission related to the disclosure of certain financial interests and sources of income to the public. Identify whether any actions by the superintendent/ executive director resulted in a personal or financial benefit to the director.
3. Conduct sample tests of transactions specific to the allegations for the 2015-16 fiscal year and one prior fiscal year. Testing of sampled transactions for this review will be based on the team's judgment and experience and may not include the testing of all transactions and records for this period.

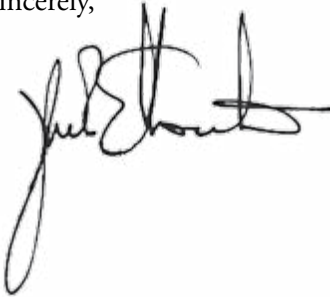
Transaction Testing Objectives:

- a. Determine whether transactions were conducted in accordance with established policy and procedures.
- b. Determine if expenditures made by the charter school are for legitimate educational purposes and in accordance with approved contracts.
- c. Determine whether the charter school engaged in related-party transactions and if those transactions were conducted in accordance with established policy and procedures and were transparent in nature.

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 San Bernardino County Superintendent of Schools 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

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# About FCMAT

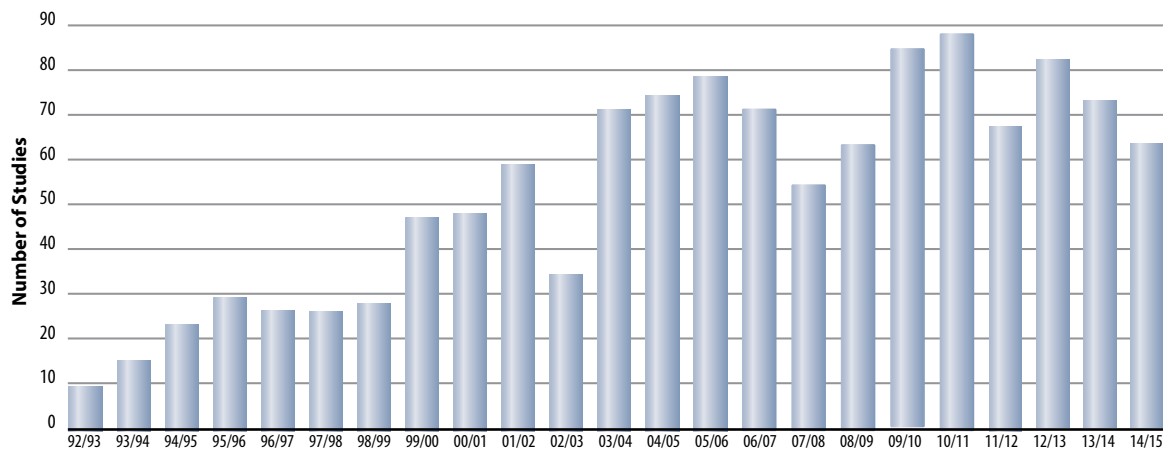
FCMAT’s primary mission is to assist California’s local K-14 educational agencies to identify, prevent, and resolve financial, human resources and data management challenges. FCMAT provides fiscal and data management assistance, professional development training, product development and other related 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, support the training and development of chief business officials and help to create efficient organizational operations. FCMAT’s data management services are used to help local educational agencies (LEAs) meet state reporting responsibilities, improve data quality, and inform instructional program decisions.

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 LEA 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.

FCMAT has continued to make adjustments in the types of support provided based on the changing dynamics of K-14 LEAs and the implementation of major educational reforms.

**Studies by Fiscal Year**



FCMAT also develops and provides numerous publications, software tools, workshops and professional development opportunities to help LEAs operate more effectively and fulfill their fiscal oversight and data management responsibilities. The California School Information Services (CSIS) division 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 (AB) 1200 in 1992 to assist LEAs to meet and sustain their financial obligations. AB 107 in 1997 charged FCMAT with responsibility for CSIS and its statewide data management work. AB 1115 in 1999 codified CSIS’ mission.

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

In January 2006, Senate Bill 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 more than 1,000 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 2015, the Fiscal Crisis and Management Assistance Team (FCMAT) received a request from the San Bernardino County Superintendent of Schools for an Assembly Bill (AB) 139 extraordinary audit of the Hope Academy Charter School. The county office had received allegations of multiple fiscal irregularities, questionable expenditures and inappropriate related-party transactions at the charter school. 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 1241.5, FCMAT entered into a contract with the county office to conduct an AB 139 extraordinary audit.

## Study Guidelines

FCMAT provides a variety of services to school districts and county offices of education upon request. Education Code Section 1241.5(b) (c) permits a county superintendent of schools to review or audit the expenditures and internal controls of any school district or charter school 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, questionable contracts with third-party vendors and conflict of interest to determine whether Hope Academy Charter School and/or its personnel may have been 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 conducted initial county office interviews in February 2016 and then visited the Victorville charter school main office in March 2016 to conduct interviews, collect data and review documents. Additional interviews were conducted in Los Angeles and by telephone with individuals that had significant knowledge of financial transactions and/or audited records of the school.

Specifically, FCMAT reviewed, analyzed and tested records that included audited financial statements, financial records, support documentation, lease documents, board meeting minutes, the charter petitions and other documentation from independent third party sources. The review also included interviews with the current and former superintendent/executive director, key management personnel, business office staff, current and former charter school employees,

the back-office provider, representatives from the California Department of Education-Charter Schools Division, representatives from the El Dorado County Special Education Local Plan Area (SELPA), and the 2014-15 independent auditor to evaluate information concerning any alleged mismanagement, fraud, or abuse.

The fieldwork focused on determining whether there is sufficient information to ascertain fraud, the misappropriation of funds and/or conflict of interest. Because of the allegations, the FCMAT team focused on related-party transactions, self-dealing through privately owned company transactions of management and key employees particularly the former superintendent/director of the charter school, his immediate relatives and breach of fiduciary duty.

Although there are many different types of fraud, a conflict of interest and breach of fiduciary duty 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:

- *Knowingly* making an *untrue representation* or a false claim of a *material fact*
- *Intent* to deceive, or *concealment* of the act
- *Reliance* on untrue information
- *Damages* or a *loss* of money or property

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
- Internal Control Elements
- Conflict of Interest
- Political Reform Act – Disclosure, Conflicts of Interest and Enforcement
- Government Code 1090 – Financial Interest of Public Officials, Officers and Employees
- California Corporations Code Section 5233
- Related-Party Transactions, Significant Influence, and Self-Dealing
- Irregular Purchase and Sale of Motor Home
- Misleading Reporting of Expenses– SB 740
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- Bonuses and Stipends Paid to Administrator, Spouse and Other Employees
- Questionable Legal Professional Services
- Audit Findings
- Hope Academy Charter School Summary of Related and Irregular Transactions

- Subsequent Events
  - Prevention and Detection
  - Recommendation
- V. Appendices

## Study Team

The FCMAT study team was composed of the following members:

Deborah Deal, CICA, CFE, CBO*	Colleen Patterson
Azusa Unified School District	FCMAT Consultant
Los Angeles, California	San Clemente, CA

Leonel Martínez  
FCMAT Technical Writer  
Bakersfield, CA

\*As a member of this study team, this consultant was not representing her respective employer but was working solely as an independent contractor for FCMAT. Each team member reviewed the draft report to confirm accuracy and achieve consensus on the final recommendations.

In writing its reports, FCMAT uses the Associated Press Stylebook, a comprehensive guide to usage and accepted style that emphasizes conciseness and clarity. In addition, this guide emphasizes plain language, discourages the use of jargon and capitalizes relatively few terms.



# Background

Hope Academy, Inc. was incorporated on April 6, 2011 and granted status as a nonprofit public benefit corporation, a 501 (c)(3) in the state of California, on December 3, 2014. The Morongo Unified School District approved the charter's petition for five years starting July 1, 2011 through June 30, 2016 to operate as a nonclassroom-based charter school. Three district teachers who wanted to start a program for underserved at-risk students in the Yucca Valley region originated the petition. Two of the original founders resigned from the charter school before 2014.

The academy was approved to serve students in the Morongo Basin according to its petition, which states the following:

Before going forward with any proposed expansion for a new independent study resource center outside the District's boundaries, there will be open communication between the District, Hope Academy, and the district in question.

Over time, Hope Academy expanded operations in several adjacent counties and districts located in San Bernardino, Kern and Riverside counties without the district's express permission or knowledge.

Hope Academy commenced operations during the 2011-12 fiscal year. The first resource center was opened in Yucca Valley in August 2011. The academy has several resource centers, supporting the Structured Time Enrichment Program (STEP) for students in transitional kindergarten through eighth grade, operating from 9 a.m. to 2:30 p.m. daily and independent study programs for students in grades kindergarten through 12 in several counties. Resource centers are located in Beaumont, Bloomington, Indio, Palm Desert and Victorville (opened in fiscal year 2013-14), Apple Valley, Big Bear, Bakersfield and Tehachapi (opened in fiscal year 2014-15.) The Apple Valley resource center closed during the current fiscal year.

On November 23, 2015, the Morongo Unified School District superintendent wrote a letter to the superintendent of the San Bernardino County Superintendent of Schools expressing concerns regarding conflict of interest. The concern focused on the involvement of the former superintendent/executive director of Hope Academy serving as a majority owner in SavantCo Education, the charter school's back-office service provider. A review of the master services agreement with the academy indicates that SavantCo Education was to perform finance and accounting; payroll; business consulting; board meeting support; attendance and student information systems; charter development; grant administration; and financing support.

Based on these concerns, the county office evaluated the preliminary investigation conducted by the district. Upon review of the allegations, the county office requested the Fiscal Crisis and Management Assistance Team (FCMAT) in December 2015 to provide for the assignment of professionals to study specific aspects of alleged fraud, misappropriation of funds and possible criminal activity in the Hope Academy Charter School organization.

## Scope and Procedures

The fraud investigation consisted of gathering adequate information on specific allegations, establishing an audit plan, and performing various audit test procedures to determine whether fraud may have occurred, and if so, evaluate the loss, determine who was involved, and determine how it occurred. During interviews, FCMAT study team members asked questions pertaining to levels of authority to enter into contracts, governing board oversight, financial management internal

controls, job duties and responsibilities, and questions related specifically to the related-party transactions between the former founder superintendent/executive director and companies he initiated, managed and/or controlled, amounts paid to the founder's companies for back-office financial work, technology, and the questionable purchase of a motor home from relatives. The FCMAT study team also asked questions about bonuses paid between January 2014 and June 2015 were distributed to the founder, his spouse and his mother.

Other questionable expenditures were revealed during fieldwork and included the amounts paid for back-office services and other services to the founder's company before board approval and at the same time that another back-office provider was under contract.

The primary focus of this review is to determine and report to the county office of education and the charter school whether there are reasonable assurances, based on testing, that adequate management controls are in place for the charter's reporting and monitoring of financial transactions, and whether fraud, misappropriation of funds or other illegal activities may have occurred. Management controls include the processes for planning, organizing, directing, and controlling program operations, including systems for measuring, reporting, and monitoring performance.

The FCMAT study team utilized fraud risk assessment checklists for conflict of interest and management/key employees in addition to conducting sample tests of financial transactions, other data and contracts to determine if fraud, misappropriation of funds or other illegal activities may have occurred. Testing for this review is based on 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 charter school's transactions and financial activity.

To accomplish this audit's objectives, 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, including supporting documentation provided by school personnel and the back-office provider. Supporting documentation for many transactions was reportedly missing, including the documents for credit card transactions, construction contracts, and several expenditure transactions. FCMAT specifically performed audit tests related general ledger transactions, payroll records, credit card transactions, check disbursements, construction expenditures, rent/facility lease agreements and federal forms W2, 990 and 1099 including the following:

- Review the charter school's petition documents and assurances.
- Review the governing board meeting minutes from July 2014 through February 2016.
- Review charter board policies for purchasing, contracting and conflict of interest.
- Analyze the charter school's compliance with laws and regulations relating to conflict of interest and the Political Reform Act and review of Forms 700.
- Review the charter school's internal control processes and procedures to determine possible weaknesses in prevention and detection of fraud, misappropriation and/or criminal activity.
- Review the general ledger records from July 2014-December 2015 for the charter school.
- Review payroll records from July 2014 through December 2015, including calendar year-to-date information.

- Review of proper authorization and available supporting documentation for lease agreements, contracts and inter-company transactions.
- Review credit card transactions and payments.
- Analysis of supporting documentation for credit card transactions.
- Review Federal Forms: W2, 990, and 1099 over the audit period.
- Review 2012-15 independent financial audit.
- Review Senate Bill (SB 740) nonclassroom-based funding certifications.
- Review School Accountability Report Card data from 2013-14 and 2014-15.
- Review SELPA maintenance-of-effort calculation.
- Review the charter school's fiscal policies and procedures.

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





# Findings and Recommendations

## Occupational Fraud

An organization's owners, executives, managers or employees 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 by telephone, email or online forms accounting for three times the number of any other fraud prevention method for this type of scheme, and for 39.1% of detection methods overall. According to the 2016 *Report to the Nations on Occupational Fraud and Abuse* the Association of Certified Fraud Examiners, Inc., corruption schemes accounted for 35.4% of all occupational fraud cases reported with a median loss of \$200,000.

Based on this study, the perpetrator's position and authority in the organization have a direct correlation with the losses incurred. Approximately 40.9% of fraudsters were employees; 36.8% were managers; 3.4% other categories, and 18.9% were owner/executives. Although the second lowest percentage is from owner/executives, this group generated the largest median loss of \$703,000 of the 2,410 cases reported worldwide between January 2014 and October 2015.

At Hope Academy, the lack of internal controls and integral relationship between the founder superintendent/executive director and related family members particularly between the founder, his spouse and extended family and his private businesses, created an environment that allowed the essential elements of fraud to occur, including motivation and opportunity.

## 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.

Internal Control Element	
<b>Control Environment</b>	<i>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.</i>
<b>Fraud Risk Assessment</b>	<i>Identification and assessment of organization’s objectives to establish and develop a strategy to react timely.</i>
<b>Control Activities</b>	<i>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 charter school’s assets, including the prevention of override of controls in the system by any employee.</i>
<b>Information and Communication</b>	<i>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.</i>
<b>Monitoring</b>	<i>Ongoing monitoring that includes periodic performance assessments for fraud deterrence by managers and employees.</i>

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 oversight or 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 sufficient due diligence by the organization to perform background and cross checks of employee Social Security numbers, bank account numbers and addresses to companies that do business with the organization to prevent conflict of interest. Hard controls also include segregation of duties, limiting access to cash, board/management review and approval, and reconciliations. Other types of internal controls include *soft* controls such as asking employees to disclose any potential conflicts of interest without verification, management tone, performance evaluations, training programs, and maintaining established policies, procedures, ethics training and expected 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.” This tone is an intangible internal control element that consists of the organization employees’ perception of the ethical conduct of 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 superintendent/executive director’s ability to access assets combined 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 does either of the following*:

1. Participates in the decision-making process
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.

Contracts between board members or administrators (their dependents, including spouses) who make or influence contractual decisions and the charter school are prohibited by law and cannot be cured by abstention. As to all other actions, board members must abstain from decisions that materially affect their personal financial interests.

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.

This report will demonstrate that conflict of interest exists at the academy, with charter officials participating in the decision-making process and exercising considerable influence that had major financial implications without full disclosure to the charter's governing board. Additionally, multiple transactions involved self-dealing with the founder's private businesses that allowed the founder and his spouse (the associate director and later acting superintendent) to gain financially from these decisions and contracts. Both individuals participated in subsequent actions to contracts, including signatory authority and approval of payments on behalf of both the charter school and their private back-office provider company.

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

In June 1974, Proposition 9 enacted the Political Reform Act, Government Code Sections 81000 - 91014. 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 Fair Political Practices Commission (FPPC) enforces the act's provisions, which 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 within 30 days of taking and exiting their official 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.

The Political Reform Act 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 five 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?

The Morongo Unified School District granted approval for the Hope Academy Charter School subject to the conditions contained in the school charter petition executed on March 15, 2011. Article IV "Governance Structure" contained in the Hope petition states the following:

Hope Academy shall be subject to Government Code Section 1090 *et seq.*, the Political Reform Act of 1974 (Gov Code Section 87100 *et seq.*, the "PRA") and any attendant regulations as they may be amended from time to time, and all conflict of interest laws and prohibitions applicable to California non-profit corporations and/or California charter schools. All officers, employees, and members of the governing board of Hope Academy shall comply with the requirement of each and all of those conflict of interest laws and regulations. Prior to the commencement of the 2011-2012 school year, Hope Academy shall adopt for Hope Academy the Fair Political Practices Commission's Model Conflict of Interest Code...

Hope Academy Board Policy 7002.1 dedicated eight pages to the Political Reform Act and conflict-of-interest regulations including exhibits of reporting categories. (The complete board policy is attached as Appendix A to this report.) Because board-meeting minutes have little or no detail and in some cases are missing, it is unclear when this board policy was officially approved; however, PRA regulations do not require board approval to be binding on the charter school. The petition between Hope Academy and Morongo Unified dated March 15, 2011 provides the contractual status and therefore, Hope Academy is subject to the conflict-of-interest statutes.

Until most recently, the academy's current governing board members, charter school officials, designated employees and qualifying consultants had not filed Form 700. Former governing board members, charter school officials, designated employees as well as qualifying consultants that met the conditions previously identified in this report have not filed them to date.

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

Simply stated, the intent of Government Code 1090 (Section 1090) is to prohibit public officials, 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, as is the case with Hope Academy, 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 anybody 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.

FCMAT found that charter conditions designed to disclose potential conflict of interest, including proof of compliance with the Political Reform Act of 1974, Government Code Section 87100, and Government Code Section 1090, were not in compliance as of the date of FCMAT’s fieldwork.

On March 15, 2011, the Morongo Unified School District and Hope Academy Charter School approved and executed the charter petition for five years. Section IV “Governance Structure,” as described in the previous section, provided that Hope would adhere to Government Code 1090 provisions.

Hope Academy’s conflict-of-interest policy includes the specific terminology and definitions contained in the Political Reform Act of 1974, the regulations of the Fair Political Practices Commission, California Code of Regulations Title 2, Division 6, Section 18730.

## California Corporations Code Section 5233

The purpose of California Corporations Code Section 5233 is to define self-dealing transactions where the corporation is a party “to which one or more of its directors has a material financial interest...” An extension of this code is included in new requirements in Part VI of the Federal Form 990 entitled, “Governance, Management, and Disclosure,” which can lead to questions regarding the continuance of tax-exempt status. According to California Attorney General Kamala D. Harris, “the IRS considers such policies and procedures generally to improve tax compliance. The absence of appropriate policies and procedures may lead to opportunities for excess benefit transactions, inurement, operation for non-exempt purposes, or other activities inconsistent with exempt status.” Unjust enrichment from earnings (gross or net) may be considered inurement.

This report will establish that a business relationship exists between one of the original founders of Hope Academy and his private companies that provided back-office service and technology services as evidenced by contracts, master agreements and consulting arrangements. Conclusive documentation supports that the founder, his spouse and several relatives exercised significant personal involvement and financial interest, violating the conflict-of-interest statutes as well as policies adopted by the academy’s governing board.

## Related-Party Transactions, Significant Influence and Self-Dealing

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 850-10-50 contains the disclosure requirements for related party relationships and transactions as follows:

- “Affiliates” of the entity.
- Entities for which investments in their equity securities would be required, absent the election of the fair value option under the Fair Value Option Subsection of Section 825–10–15, to be accounted for by the equity method by the investing entity.
- Trusts for the benefit of employees, such as pension and profit sharing trusts that are managed by or under the trusteeship of management.
- Principal owners of the entity and members of their immediate families.
- Management of the entity and members of their immediate families.
- Other parties with which the entity may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests.
- Other parties that can significantly influence the management or operating policies of the transacting parties or that have an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests.

The FASB ASC glossary, which is attached as Appendix B to this report, also defines the terms: affiliate, control, immediate family, management, and principal owners.

The executive management of nonprofit organizations such as Hope Academy have the responsibility to document in detail and fully disclose to the auditors, governing board, county oversight agencies, and the state for purposes of conflict of interest and full disclosure reporting requirements any and all potential related party transactions to comply with Generally Accepted Accounting Principles (GAAP). Failure to disclose related party transactions might be considered a departure from GAAP that could result in a qualified or adverse audit opinion and the potential for civil and criminal prosecution.

The facts below demonstrate that several related party transactions exist between the founder/former superintendent/executive director, back-office provider services and other companies.

Interviews indicate that in 2013, one of the academy’s founders married a fellow employee, and these two individuals served as the founder/superintendent/executive director and associate director, respectively. These positions were the highest-salaried administrative positions in the organization until the founder resigned in April 2015 and his spouse in December 2015. This husband and wife team had significant influence over several related party transactions from which they secured considerable financial benefit and excessive compensation based on comparable wages throughout San Bernardino County during the time period of this review.

The academy’s Board Policy 4002.1 on certificated salary indicates the following:

All employees will be compensated based on Board approved pay scales. Pay scales will be kept in line with those of districts throughout San Bernardino County. Raises in

pay and/or benefits from year to year will be determined by evaluating the financial situation of the school along with a review of neighboring district's raises in salary or other compensation.

A review of comparable salaries in the San Bernardino County area found that several other administrators employed by Hope Academy were paid wages that greatly exceed other school districts in the area. Excessive salaries and service fees for back-office services paid to the founder's company forced the charter school to factor (assign) accounts receivable to maintain sufficient cash flow for operations.

The table below shows a sample of compensation from surrounding districts. Information for these local districts is based on the most recent compensation data available from Transparent California ([www.transparentcalifornia.com](http://www.transparentcalifornia.com)) and the California Department of Education (CDE) enrollment data for the corresponding fiscal year. Hope Academy information is based on actual year-end payroll data and CDE enrollment certifications:

District/Charter	Enrollment	Superintendent/ Executive Director	Senior Certificated Administrator
<i>Morongo Unified</i>	<i>8,905</i>	<i>\$157,278 (2012)</i>	<i>\$73,067 (2012)</i>
<i>Hesperia Unified</i>	<i>23,735</i>	<i>\$156,260 (2014)</i>	<i>\$155,904 (2014)</i>
<i>Oro Grande Elementary</i>	<i>3,789</i>	<i>\$159,497 (2013)</i>	<i>\$140,000 (2013)</i>
<i>Hope Academy</i>	<i>1,744</i>	<i>\$220,275 (2014)</i>	<i>\$164,500 (2014)</i>

The academy has the lowest enrollment, but the highest compensation. A review of the information above shows that Hope Academy's compensation compared with other local school districts was excessive and did not meet the intent of the charter's board policy.

The December 2014 year-to-date employee compensation records show that several administrators and employees at the academy received high salaries and benefits compared to those in similar positions in the local geographical area, and many are relatives of the founder and his spouse. Comparisons of employee contracts with the April 2015 payroll found increases that are unsubstantiated by board action. Interviews with the founder, his spouse and others indicate that bonuses and stipends were paid for a variety of reasons including "low wages" due from previous years and stipends to ensure maintenance-of-effort (MOE) requirements for special education funding. Although interviews suggest that the governing board was fully apprised of these payments, no documented evidence supports these claims. (More information on bonuses, stipends and MOE is provided later in this report.)

## **SavantCo Education Inc.**

### **Factoring**

Factoring accounts receivable provides charter schools with short-term financing for periods of negative cash flows. Factoring agreements for charter schools generally have higher-than-average interest rates because banks are reluctant to loan money to charter schools without sufficient collateral.

The founder and his spouse signed a factoring agreement between Charter Asset Management Fund, LP (CAM) and Hope Academy, Inc. on September 2, 2014. The spouse signed as "Vice President, Board of Directors," misrepresenting her official title, for a \$7,874.87 administrative and discount fees on face value receivables of \$107,874.87.

The table below shows Schedule 2 – Prior Receivables Purchased By CAM attached to the September 2, 2014 factoring agreement, which dates back to December 27, 2013, totaled \$233,802.79 in administrative and discount fees while the charter school was maintaining excessively high compensation levels that included large bonuses.

### *Prior Receivables Purchased by CAM*

Funding Date	Face Value	Admin Fee	Discount
8/27/14	\$25,000.00	\$462.50	\$737.50
8/27/14	330,000.00	6,105.00	15,675.00
8/27/14	25,000.00	462.50	1,187.50
8/27/14	319,555.31	5,911.77	19,013.54
8/13/14	30,000.00	555.00	150.00
8/13/14	126,157.07	2,333.91	2,460.06
8/13/14	140,000.00	2,590.00	2,730.00
8/13/14	226,795.46	4,195.72	7,937.84
6/20/14	180,000.00	3,330.00	9,450.00
6/20/14	25,000.00	462.50	1,312.50
6/20/14	70,000.00	1,295.00	3,675.00
6/20/14	102,856.37	1,902.84	6,428.52
01/22/14	37,000.00	684.50	2,941.50
03/26/14	95,000.00	1,757.50	5,652.50
02/21/14	101,000.00	1,868.50	7,423.50
03/26/14	104,587.85	1,934.88	6,222.98
03/01/14	83,172.61	1,538.69	5,780.50
04/16/14	31,472.03	518.12	1,446.62
04/16/14	24,000.00	395.11	438.88
04/16/14	24,000.00	395.11	900.00
01/22/14	55,000.00	1,017.50	3,987.50
04/16/14	59,027.19	782.34	2,213.50
01/22/14	28,000.00	518.00	2,226.00
02/21/14	119,133.11	2,203.96	8,637.15
04/16/14	208,160.63	3,426.92	9,568.14
05/07/14	143,552.87	2,204.17	6,570.00
05/07/14	144,860.11	2,186.97	7,451.84
01/22/14	58,977.93	1,091.09	2,506.56
03/26/14	120,000.00	2,220.00	1,800.00
04/16/14	24,000.00	395.11	180.00
12/27/13	15,000.00	277.50	772.50
12/27/13	10,000.00	165.00	515.00
01/22/14	100,000.00	1,850.00	2,950.00
02/25/14	146,932.23	2,718.25	2,203.98
01/22/14	10,000.00	185.00	295.00
01/22/14	45,000.00	832.50	1,350.00
02/25/14	60,000.00	1,110.00	900.00
01/22/14	91,523.25	1,693.18	1,372.85
12/27/13	33,000.00	610.50	1,138.50
12/27/13	25,000.00	462.50	862.50
12/27/13	131,636.71	2,435.28	3,290.92
12/27/13	100,275.47	1,855.10	2,506.89
<b>Totals</b>	<b>\$3,829,676.20</b>	<b>\$68,940.02</b>	<b>\$164,862.77</b>

### **SavantCo Education, Inc. - Master Services Agreement**

On April 14, 2015, the governing board approved a new service agreement dated June 8, 2015 effective July 1, 2015. Following the founder's resignation on April 14, 2015, an additional amount of \$20,000 per month was added to the SavantCo Education contract for "Executive Administrative Services" bringing the total monthly charges to \$78,000 per month from April 2015 through June 2015.



The FCMAT study team requested board meeting minutes to support this increase to the contract, but could not determine if the governing board approved the additional amount for executive administrative services. SavantCo Education has agreed to return these funds, indicating that no board approval was ever received to support the increase.

Following the resignation of the founder in April 2015, his spouse continued employment with Hope Academy and exercised signatory authorization until July 2015 when the governing board appointed a new superintendent/executive director. The founder's spouse signed several contracts, lease agreements and checks as the "superintendent" during this time, including at least one check to her husband's back-office company, SavantCo Education, for executive administrative oversight totaling \$20,000 per month as previously reported.

During the interview with FCMAT, the spouse claimed she never had board authorization to sign as superintendent, but had general signatory authority and could not recall approving the invoices for the additional executive administrative services or signing several checks for additional services (such as lease agreements and other expenditures) although there is written evidence to support her approval by email and express approval on the checks and invoices. A review of board minutes presented to FCMAT concludes that there was no authority for her signature as superintendent.

The California Department of Corporations lists several entities that included the founder of Hope Academy as an officer and had related party transactions with Hope Academy as follows:

1. SavantCo Financial, Inc. for automobile lease agreements
2. SavantCo Education, Inc. as the back-office service provider
3. Savantech, Inc. for technology services

Until July 2014, the academy contracted with EdTec Inc., a back-office service provider, for accounting, finance, payroll, and attendance, grant administration, human resources, governance support, board presentation, compliance and accountability and facilities services. The monthly fee was \$9,771.25.

On March 11, 2014 the Hope Academy governing board approved a master services agreement with SavantCo Education effective July 1, 2014 through June 30, 2015 for a monthly fee of \$58,000, almost six times the amount previously paid to EdTec for similar services.

FCMAT found invoices from SavantCo Education to Hope Academy from as early as January 2014, before the board authorized a master services agreement, totaling \$130,890.40 in addition to the EdTec monthly charges of approximately \$10,000. These invoices include several charges that should not have been charged to Hope Academy. The following table delineates these charges.

Invoice Date	Monthly Retained Fee	Set-Up Fee	Air Quality-Beaumont	DropBox and Smarte Tools	Hiring Services/ Other Fees	Furniture Charge Back	Tech Buyback	Discount
January 2014	\$4,500		\$1,550					(\$605)
February 5, 2014	\$10,800		\$700		\$2,400			(\$394.60)
February 21, 2014	\$12,140		\$2,200		\$800			(\$757)
March 2014	\$19,000	\$450	\$750	\$3,000				(\$1,160)
April 2014	\$19,000	\$1,500	\$750	\$250				(\$1,025)
May 2014	\$19,000	\$4,000	\$750	\$250	\$1,200	\$1,040		(\$1,208)
June 2014	\$19,000		\$750	\$8,650	\$1,750		\$1,439	(\$1,579)
<b>Total</b>	<b>\$103,440</b>	<b>\$5,950</b>	<b>\$7,450</b>	<b>\$12,150</b>	<b>\$6,150</b>	<b>\$1,040</b>	<b>\$1,439</b>	<b>(\$6,728.60)</b>

On June 25, 2014, the founder signed the master services contract in his capacity as superintendent/executive director of Hope Academy while he was also a principal officer in SavantCo Education, Inc. His partner, another officer of SavantCo Education, countersigned this agreement.

FCMAT could not locate disclosure documentation or a reference in board minutes that publicly discloses the relationship of the founder as a principal officer in SavantCo before board approval of the master services agreement. The contract was terminated December 2015, and a new back-office vendor was approved as of January 2016 to provide equivalent services for \$22,000 per month with a \$20,000 initial set up fee.

### **SavantCo Financial Inc.**

SavantCo Financial Inc. provided vehicle-leasing services for the academy. According to the founder and confirmed by his SavantCo Education partner, the charter school was unable to secure vehicle financing. The founder along with his partner from SavantCo Education and the founder's spouse purchased and leased back several vehicles for administrators and employees who had long commutes between resource centers.

Interviews with the founder's partner from SavantCo Education confirms this arrangement, but added that the charge-back only includes a \$100 addition to the actual payment plus an administrative fee for handling the monthly lease billing of \$450. General ledger transactions and check copies from SavantCo Education confirm that Hope Academy made down payments for vehicles as well as monthly lease and administrative fee payments to SavantCo Education. FCMAT was unable to verify board approval for vehicle leases or verify the base monthly payments made to SavantCo Education, but verified the monthly administrative fees. On November 19, 2015, the governing board terminated all SavantCo Financial vehicle lease agreements.

### **Savantech**

Savantech provided technology related services to Hope Academy from January 2014 through September 2015. This was another related company owned and operated by the founder doing business with the academy. Savantech employees were authorized credit card holders on Hope Academy's credit card account charging supplies, equipment and gasoline.

FCMAT found that Hope Academy paid twice for some supplies and equipment when Savantech employees used the Hope Academy credit card for these items. Several of these expenditures were billed back to Hope Academy on the Savantech invoice. Purchases made on Hope Academy credit cards by Savantech totaling \$1,868.06 and subsequently billed to Hope Academy include the following:

- A replacement screen and glass for an LCD was charged on a card March 17, 2015 for \$52.97 and March 24, 2015 for \$147.88, and subsequently billed on a Savantech invoice dated March 25, 2015.
- Gray ink was purchased April 21, 2015 for \$190.37; a keyboard and mice purchased April 15, 2015 for \$157.60; and a color inkjet printer was purchased for \$368.60 on April 14, 2015, and subsequently billed on a Savantech invoice dated April 21, 2015.
- Paper totaling \$104.50 and switches for the computer network costing \$846.14 on April 23, 2015, and subsequently billed on a Savantech invoice dated on April 24, 2015.

## Irregular Purchase and Sale of Motor Home

The founder recommended to the governing board the purchase of a 2004 Bounder 27' Class A motor home as a mobile Web lab to fulfill the Western Association of Schools and Colleges (WASC) requirements for science. According to the founder, the intent was to remodel the motor home into a mobile lab that would provide hands on science to students at the various resource centers for academy students in order to be compliant with WASC.

The governing board approved the purchase for \$60,855.34 at the June 9, 2015 board meeting. According to the new superintendent/executive director, the founder did not disclose that the motor home was registered to his parents-in-law in Montana and that the amount of the purchase was the exact amount of the payoff from Commerce Bank. The founder's spouse signed the check dated June 15, 2015 for the payoff to her parents from academy's general bank account.

Renovation costs to convert the motor home into a mobile wet lab were prohibitive, causing the board to declare the motor home surplus property at the October 13, 2015 board meeting in conformance with Board Policy 3011.1. The motor home was sold for \$9,000 at public auction, a loss of \$51,855 four months after the original purchase.

## Misleading Reporting of Expenses – SB 740

Education Code Section 47612.5 (d) (1) as created by SB 740 (Chapter 892, Statutes of 2001) establishes that charter schools may receive funding for nonclassroom-based instruction only if a determination for funding is made, pursuant to Section 47634.2, by the State Board of Education (SBE).

The determination for funding is applied to all nonclassroom-based instruction and is subject to several conditions as prescribed by the SBE. Elements reported in the "Nonclassroom-Based Funding Determination Form" (SB 740) include the following:

1. Financial information: Revenues, expenditures; revenues over expenditures; fund balance; and reserves. The structure applied to financial reporting is defined by California School Accounting Manual (CSAM), and coded in a chart of accounts as designated in Standard Accounting Code Structure (SACS). This financial information is organized primarily by resource code, and secondarily by object code. Examples of function code are: Instruction, operations, facilities and administration.
2. Pupil-to-teacher ratio and the number of full-time equivalent employees who possess a valid teaching permit.
3. Entities receiving \$50,000 or more of the charter school expenditures.
4. Governing board information and affiliations with any entities listed in item three, above.

A certification as to the accuracy of the information listed above provided by the charter school's director, principal or governing board chairperson, along with several statements, which include that the charter's board has adopted and implemented conflict-of-interest policies and that all of the charter school's transactions, contracts, and agreements are in the best interest of the school and reflect a reasonable market rate for all goods, services and considerations rendered for or supplied to the school.

Three quantitative elements reported on the SB 740 determination form are used to calculate the annual funding percentages for charter school funding. The determination percentages are one of the following: 100%, 85%, 70% or zero. The final determination has the following three separate components:

1. Direct certificated salaries and benefits charged to function 1000 equal to 40% of federal and state revenues, and
2. Direct certificated salaries and benefits plus support services charged to function 1000 - 3999 for a cumulative total of 80% (including item #1 and any expenditures in this item) of federal and state revenues for books, supplies, other support and instructional services, and
3. Class size pupil to teacher ratios no greater than 25:1.

A review of the detailed general ledger expenditures to support the reports filed with CDE for 2014-15 resulted in concerns regarding Hope Academy's compliance with the SB 740 determination request, and possible manipulation of expenditures to increase the determination to 100%.

Determination for 2012-13: CDE – The Charter School Division confirmed that Hope Academy was granted an exception to its 2012-13 SB 740 filing based on fiscal year 2011-12 reported data. A finding of mitigating circumstances was granted by the CDE and a payment of \$350,000 in bonuses was subsequently paid to all 2012-13 employees. During this reporting period, Hope Academy reported \$98,050 in total "operations and facilities" for the Yucca Valley site. A February 15, 2013 letter documented the mitigating circumstances, and the attached SB 740 certified declaration signed by the founder as "superintendent/chief executive" that the board had adopted, and implemented, a conflict-of-interest policy and that all of the charter school's transactions, contracts and agreements were in the best interest of the school and reflect a reasonable market rate for all goods, services and considerations rendered for or supplied the school.

Determination for 2013-14: Hope Academy filed the 2014-15 SB 740 determination request for fiscal year 2013-14. Despite having the Yucca Valley campus, opening five resource centers that year, and having previously claimed facility expenditures, the SB 740 determination request did not include any facilities and operations costs. The declaration listed \$128,502 in management service fees paid to SavantCo Education that had been coded as direct instructional services by SavantCo Education.

These expenditures were not direct instructional services, but effectively increased the direct services category to meet the 100% determination. Not claiming the facility expenditures and miscoding the management service fees (legal fees, audit fees and other fees) as direct educational services created an inaccurate calculation that CDE relied on to make a 100% determination for the academy.

Once again, the SB 740 declaration filed January 15, 2015 certified that the board had adopted and implemented conflict-of-interest policies and indicated that all of the charter school's transactions, contracts and agreements were in the best interest of the school and reflect a reasonable market rate for all goods, services and considerations rendered for or supplied the school. The deputy superintendent of Hope Academy signed this declaration on January 22, 2015.

Audit reports are used to verify and match SB 740 expenditures reported in various categories including direct instructional and support services. A review of June 30, 2012 and June 30, 2013 independent audit reports prepared by Hosaka, Rotherham & Company Certified Public

Accountants supported the inaccurate SB 740 filings prepared by the academy and failed to properly reclassify expenditures in the correct categories necessary to support the 2012-13 and 2014-15 SB 740 filings. The audit reports also failed to disclose in a footnote the related-party transactions between the academy and SavantCo Education, a requirement of SB 740 disclosure. Interviews with SavantCo administration indicated that two Hosaka employees assigned to academy audits went on to become co-owners in SavantCo Education in March or April 2014.

A comparison of SB 740 filings to the 2013 audit found several variances and misapplication of SACS. Hope Academy grew rapidly between 2012 and 2013, adding several resource centers, but a sampling of the general ledger maintained by SavantCo Education showed an excessive amount of expenses coded to direct instruction and instruction related services; no expenditures in operations and facilities; and comparatively few coded to administration. The overreporting of expenses related to instruction and instructional services had a significant effect on the SB 740 determination calculations applied to fiscal years 2012-13 and 2013-14, increasing the percentage of annual funding.

## Federal Form 990

Hosaka prepared the 2012-13 and 2013-14 Internal Revenue Service Form 990 Return of Organization Exempt from Income Tax for Hope Academy. Both tax returns checked “No” to the following question:

1. Was the organization a party to a business transaction with one of the following parties:
  - A current or former officer, director, trustee, or key employee?
  - A family member of a current or former officer, director, trustee, or key employee?
  - An entity of which a current or former officer, director, trustee or key employee was an officer, director, trustee, or direct or indirect owner?

The 2012-13 and 2013-14 IRS tax forms both checked “Yes” to the following question:

2. Did the organization have a written conflict of interest policy?
  - Were officers, directors or trustees and key employees required to disclose annually interests that could give rise to conflicts?

Schedule O, states that board members and key employees must file Form 700 annually and that the signing officer reviews Form 990 before filing. Hope Academy’s founder signed both tax returns under penalties of perjury.

## Bonuses and Stipends Paid to Administrator, Spouse and Other Employees

The FCMAT study team could not locate board approval for stipends and/or bonuses remitted to the senior administrators and other staff members. Interviews with several administrators state that stipends and special education bonuses were paid to some employees.

### **Bonus Payment 2013-14**

A single payment of \$45,000 was listed in the 2013-14 payroll records labeled as “Bonus.” This payment was paid to the founder. FCMAT was unable to verify authorization for this bonus through board minutes or other supporting documentation.

### **Special Education Bonuses 2013-14**

Although interviews with the founder indicated that all employees who served special education students benefited from a special education bonus, payroll records show two entries coded as Special Education Bonus that totaled \$8,000. A \$6,000 amount was paid to the founder’s spouse and \$2,000 to one teacher.

### **Stipends 2014-15**

FCMAT reviewed monthly stipend payments in the November 2014 payroll register totaling \$13,200 to nine employees including the founder’s wife for \$6,000; the deputy superintendent for \$1,000; the founder’s mother for \$1,000; and six other employees shared the balance of \$5,200.

### **Special Education Bonuses 2014-15**

In June 2015, only two special education bonuses were paid: \$35,000 to the founder’s spouse and \$15,000 to one teacher. Evidence of board action was not provided to support payments of stipends or bonuses.

Interviews with the founder and several academy administrators indicated that bonuses had to be paid to meet the special education maintenance-of-effort (MOE) calculation requirements; however, a review of the expenditures indicated that Hope Academy had met the MOE requirements in 2013-14 and 2014-15 without consideration of the bonuses.

MOE requires local agencies (school districts and charter schools) that receive a federal grant award under the Individuals with Disabilities Education Act, Part B (IDEA – B) to maintain at least the same level of state and local expenditures on a per-pupil basis to support federal programs from one fiscal year to the next to ensure that local agencies provide services to disabled students. Districts and charter schools must comply with the MOE requirement to receive IDEA-B funding each fiscal year (34 CFR §300.203.) The 20 United States Code [USC] Section 1413 and 34 Code of Federal Regulation [CFR] Section 300.231 prohibits the amounts received under IDEA - B from being used to reduce the level of expenditures for the education of disabled children with limited exceptions on an aggregate or per-capita basis from the preceding fiscal year.

Interviews with SELPA administration indicated that 2013-14 was the first year that Hope Academy was a SELPA participant. As a result, there was no maintenance-of-effort requirement because this was the base year for per-pupil expenditures, yet the founder indicated that bonuses had to be paid to meet this requirement.

In the 2014-15 fiscal year, the academy per-pupil expenses totaled \$11,690. Compared to 2013-14 base year expenditures of \$7,814 per pupil, this represented an increase of 50%. Sufficient expenditures were charged to special education to meet the MOE. A statement from SELPA staff to FCMAT indicated Hope Academy never consulted SELPA staff about MOE concerns or issues related to meeting the MOE.

FCMAT conducted an extensive review of the general ledger maintained by SavantCo Education for the academy. These records show that 62 entries totaling \$602,492.16 were made during year-end closing for the 2014-15 fiscal year that reclassified expenditures from the unrestricted general fund to special education. Repeated requests to SavantCo Education for supporting documentation to the journal entry were ignored.

### Accounting Reclassifications – Salaries and Benefits

CSAM Procedure 910-10 provides that salaries and wages charged to a specific goal such as special education require supporting documentation indicating how the costs relate to that goal for those specific activities. For federal or state restricted funds, personnel activity reports, activity worksheets, or equivalent documentation are generally necessary.

Because IDEA – B funding is funded from federal sources, the charter school is required to follow federal regulations. Employees that are split funded with any portion from federal sources must complete a Personnel Activity Report (PAR) in accordance with Federal Office of Management and Budget Circular 87 which states:

Each employee paid in part from a single cost objective and in part from other revenue, or an employee paid from multiple cost objectives, completes a Personnel Activity Report (PAR) each pay period, or an approved sampling method is used.

No time study, or other documentation, to support salaries charged to IDEA-special education were provided to support the year-end journal entry reclassifying certificated or classified salaries. Journal entries are correcting entries that should be supported by documentation that identifies the purpose for the correction.

### Administrative Services and Wages

FCMAT requested administrative employment contracts to support actual payroll records. On the documents provided to FCMAT, only the contract for the deputy superintendent had a signature. A table comparing employment contract base pay shows differences between board authorization and actual payments:

Position	Contractual Base Salary	Difference	Comments
<i>Deputy Superintendent – Contract as of 7/1/2014</i>	\$135,000	\$10,000	<i>7/1/14 contract allows for modification “Before first payroll of each year.” First contract year did not end until June 30, 2015.</i>
<i>Senior Director of Programs (spouse of Founder) – Contract as of 7/1/2013</i>	\$110,000	\$33,500	<i>8/1/13 contract allows for renegotiation, with “increases...discussed in June.” First contract year ended June 30, 2014.</i>
<i>Assistant Superintendent of Elementary Programs</i>	\$85,000	0	<i>7/1/14 contract allows for renegotiation June 2015.</i>
<i>Assistant Superintendent of Secondary Programs</i>	\$125,000	0	<i>7/1/14 contract allows for renegotiation June 2015.</i>
<i>Founder/ Superintendent</i>	\$0	N/A	<i>No contract provided.</i>

Deputy Superintendent: The founder executed the deputy superintendent’s employment contract with an effective date of July 1, 2014. The first payroll following the effective date of the contract was \$10,000 more than the board-authorized contract amount. During interviews, the deputy superintendent indicated that he was properly approved for this increase although FCMAT could find no evidence of this.

Senior Director of Programs: The founder/superintendent was the Hope Academy administrator listed as the signatory for the August 1, 2013 contract for the senior director of programs, his spouse. This is the only employment contract provided by the academy that includes an employer paid tax-sheltered annuity (TSA) of \$500 per month. In addition to the stipends and bonuses, the TSA contributions are not included in the employment contract approved by the governing board. FCMAT was not provided documentation demonstrating subsequent board approval.

Additional payments recorded in the payroll records show \$33,500 in payments prior to board approval of her next contract July 1, 2014. The governing board should approve any increases in compensation before actual payments to the employee.

Founder/Superintendent: Upon his resignation from Hope Academy, a \$20,000 per month administrative fee was added to the SavantCo Education invoice for April, May and June 2015. During interviews, the founder stated that this fee was paid for SavantCo Education (his company) to “back-fill” the administrative services even though the academy had on staff a deputy superintendent and four other administrators with compensation levels in excess of \$120,000 per year including his spouse. The spouse was signing as the superintendent on contracts, warrants and other documents approving expenditures following the founder’s resignation. Board minutes do not reflect governing board approval to increase the SavantCo Education contract by \$20,000 per month following the resignation of the founder/superintendent. During interviews with FCMAT, a partner and chief financial officer of SavantCo Education said these funds would be returned to Hope Academy.

From January 2015 through June 2015, the salary for the founder’s spouse was increased by \$2,083.33 per month (\$12,500), yet board minutes do not reflect action to approve a new contract or any temporary increase in compensation. The table below is a summary of administration services and wages reported through the general ledger accounts and federal forms for July 1, 2014 through December 2015:

### ***Services and Wages Paid to Founder, His Companies and Spouse, over 18-Month Period***

<b>Payee</b>	<b>Service</b>	<b>Fiscal Year 2014-2015</b>	<b>July-Dec 2015</b>	<b>TOTAL</b>
<b>SavantCo Education</b>	<b>Business Services</b>	<b>\$439,205</b>	<b>\$353,107</b>	<b>\$792,312</b>
<b>SavantCo Finance</b>	<b>Financing Services</b>	<b>\$15,321</b>	<b>\$24,966</b>	<b>\$40,287</b>
<b>Savantech</b>	<b>Technology Support</b>	<b>\$37,225</b>	<b>\$45,101</b>	<b>\$82,326</b>
<b>Spouse</b>	<b>Wages</b>	<b>\$159,583</b>	<b>\$97,833</b>	<b>\$257,416</b>
<b>Founder</b>	<b>Wages</b>	<b>\$158,166</b>	<b>\$0</b>	<b>\$158,166</b>
<b>Total</b>		<b>\$809,500</b>	<b>\$521,007</b>	<b>\$1,330,507</b>

In addition to the wages and service income listed above, one Savantech employee had a credit card issued in his name that was used to purchase materials and supplies; the founder/superintendent and spouse had numerous credit card charges for personal expenditures including computers and software that are not accounted for, meals and travel charged to Hope Academy. Several credit card charges have no supporting documentation or lack a detailed description of goods/services and several others include the description “Admin lunch.”



## Questionable Legal Professional Services

In addition to several of the founder's relatives that worked for the academy, professional services for legal issues were provided by the founder's uncle and his firm located in Royal Oak, Minnesota. Although some bills were addressed to SavantCo Education and others to Hope Academy, the charter paid all the bills through invoices submitted to Hope.

A review of Federal Forms 1099 for the 2015 calendar year show that Hope Academy paid \$108,577.27 for legal services from May through December 2015, and three more invoices were paid in 2016, when the academy severed its relationship with the firm.

A review of the individual invoices shows brief descriptions for professional legal services that relate to SavantCo Education and the founder (denoted as "JM") following his resignation. Some examples of billings charged to the academy from SavantCo Education from July 2015 include the following:

- Follow up conference with JM;
- Review new California cases on point and 1090 issues;
- Analysis and research of Charter School's compliance with three California statutes regarding conflict of interest;
- Research on primary source material for Political Reform Act and Section 1090 conflict-of-interest provisions; and
- Emails to and from JM; develop facts and drafting.

The following is a list of all payments made from Hope Academy to the law firm in 2015 totaling \$108,577.27, of which \$23,316.44 for checks 3999, 4017 and 4227 listed below were signed by the founder's spouse following his resignation in April 2015 and contain questionable charges.

### *Payments Made to Hope Academy*

Date	Check No	Amount
5/4/2015	3999	\$1,107.00
5/7/2015	4017	\$7,969.00
7/8/2015	4227	\$14,240.44
9/14/2015	4516	\$3,977.00
9/21/2015	4535	\$8,284.00
10/6/2015	4606	\$27,549.98
10/30/2015	4723	\$18,289.02
11/12/2015	4766	\$14,974.35
12/14/2015	4871	\$2,186.48
<b>Total Payments</b>		<b>\$108,577.27</b>

## Audit Findings

FCMAT interviewed the audit partner engaged by the newly appointed Hope Academy administration to perform the 2014-15 annual audit. The following comments were discussed with the FCMAT study team.

The auditor noted in the annual 2014-15 audit the following:

Substantial audit findings,

- Questionable costs,
- Lack of internal controls,
- Related-party transactions,
- Questionable accounting practices provided by the back-office provider,
- Unreasonable and inequitable charge backs from the back-office provider, and
- Substantial doubt of going concern due to a decrease in net assets coupled with current liabilities that exceed its total assets by \$721,155.

**Financial Statement Findings:** There are five audit findings, four involving internal controls. The following is a summary of the findings, conditions and effects as a result of poor oversight and/or full disclosure to the governing board, lack of internal controls, and inadequate accounting practices for which the school paid monthly fees that exceeded industry standards:

Finding	Condition	Effect
2015-01 – State Compliance	Student eligibility records were not consistent with the data reported in CalPADS causing an over reporting of unduplicated pupil counts.	A reduction in funding of \$140,354.
2015-02 – Internal Control	Numerous instances where the back-office provider has no documentation, record or substantiation to verify charge backs to the charter school based on the Master Services Agreement. Expenses could be deemed out of the scope of “applicable industry standards.”	School has incurred unallowable or unauthorized expenses.
2015-03 – Internal Control	Motorhome was purchased from a relative of the “Executive Director/employee” of the school and CEO of the back-office provider. Board approval lacked full disclosure of related-party. No sales agreement.	School may have incurred unallowable or unauthorized expenses.
2015-04 – Internal Control	No written policies or procedures for processing, approval and recording of payroll, stipends and/or bonuses to employees causing some employees being improperly paid.	School could potentially incur unallowable or unauthorized payroll, stipends and bonuses.
2015-05 – Internal Control	Weakness in internal control over financial reporting. Adjustments approved by management to increase other revenue and decrease prepaid expenses caused beginning net assets to be misstated and out of balance. Back-office provider failed to balance the books at year-end closing.	Misstatements can be misleading and under- or over-estimate the financial condition.

Charges of \$58,000 per month by SavantCo Education exceed industry standards according to the audit report and two separate back-office services providers. Levels of back-office service range greatly, however, based on the number of students in the charter school and the master agreement provided by SavantCo Education, comparative services should range from \$20,000 to \$30,000 per month. EdTec had previously charged \$9,771 per month, and the current back-office provider charges \$22,000 per month.

As previously stated in this report as well as the audit report, SavantCo Education charged a premium price for the monthly back-office services in addition to other expenses that should not have been charged to Hope Academy. Prior to FCMAT’s investigation, the new academy superintendent billed SavantCo Education for unauthorized charges totaling \$130,016.02.

Included in these bill-backs are invoices for SavantCo Education to attend and host a vendor booth at the annual charter school convention; Verizon cell phone bills for SavantCo Education employees and their spouses, and other individuals along with the SavantCo Education main line; several expenses directly for SavantCo Education business including business cards, travel, Xerox machine, grant writing conference expenses, a truck liner for a vehicle Hope Academy has never operated; insurance on vehicles that were leased to Hope Academy with an administrative fee of \$450 per month designed to cover insurance, maintenance and repairs; business software SavantCo Education uses for all its back-office clients; services not identified in the master services agreement for hiring employees and credentialing; and executive administrative services.

During FCMAT interviews, the SavantCo Education chief financial officer and CPA acknowledged receipt of the Hope Academy bill-back and agreed that at least \$113,000 will be reimbursed to the academy. The partners of SavantCo Education terminated their relationship with the academy founder and former partner of SavantCo Education effective March 1, 2016 citing concerns that the FCMAT AB 139 audit will affect their business with other charter school clients.

## **Hope Academy Charter School Summary of Related and Irregular Transactions**

The table below is a compilation of payments and questionable costs made through the academy to the founder/former superintendent, family members of the founder and close associates. The founder authorized many of these payments in his capacity as both owner/partner of SavantCo Education and superintendent of the charter school.

### *Hope Charter School Summary of Related and Irregular Transactions*

	Time Period	Type	Accounting Records
SavantCo Education – unapproved service charges	January 2014 through June 2014	No board approval.	\$130,890.40
Motor home purchase.	June 2015	Lacked full disclosure to the governing board.	\$60,855.34
Bonuses paid – Special Education MOE	2012-13	Payments after the fact questionable approval and understanding of MOE requirements.	\$350,000
Special Education Bonuses	2013-14	Lacked board approval. Not required for MOE.	\$6,000 to spouse and \$2,000 to teacher.
Stipends	2014-15	Involving nine employees including spouse for \$6,000, mother \$1,000, deputy superintendent \$1,000. No board authorization available.	\$13,200
Special Education Bonuses	June 2015	Payment to spouse \$35,000 and \$15,000 to teacher. Unauthorized.	\$50,000
Payments beyond employment contract.	2014-15	Deputy superintendent was paid in excess of the board approved contract.	\$10,000
Payments beyond employment contract.	2014-15	Spouse was paid in excess of board-approved contract.	\$44,000
SavantCo Education	April, May and June 2015	Payments made for “Executive Administrative Services” following resignation of founder.	\$60,000
Payments beyond employment contract.	January 2015 through June 2015	Spouse monthly contract was increased by \$2,083.33 per month without board approval.	\$12,500
Professional legal services.	Calendar year 2015	Questionable costs with legal firm located in Minnesota and relative of founder.	\$108,577.27
Bill backs.	2013-2014 through December 2015	Bill backs from Hope Academy to SavantCo Ed including the administrative services list above.	\$130,016.02
Misuse of credit card.	January 2014 through December 2015	Credit card charges made by Savantech on Hope’s credit card and charged back by invoice to Hope Academy.	\$1,868.06

The above transactions represent significant influence that the Hope Academy founder/former superintendent, spouse of the founder and close associates had over financial decisions that personally benefited them. The founder’s spouse authorized several of these transactions for payment and gave these individuals the ability to simultaneously control and benefit from these transactions. The lack of documentation to support transactions through board approval, policy, procedures and records creates the perception of fraud, misappropriation of assets and possible criminal activity.

There is little evidence of responsible governance by the board and clearly a lack of fiscal accountability by the former charter administration.

## Subsequent Events

As of July 1, 2015, the governing board appointed a new superintendent whose spouse is the business technician. In addition, a new back-office service provider contract was awarded on January 1, 2016. The legal firm with a relative of the founder/former superintendent no longer provides professional legal services.

Special attention to internal controls and review processes are evident; however, the governing board should adopt policies and written procedures should be developed and implemented to prevent the breaches of internal control that have existed and delineate proper segregation of duties especially with related parties.

The governing board meeting minutes should provide clear documentation to support vendor and employment contracts and ensure that requirements contained in Government Code 1090, the Political Reform Act, Form 990 and disclosure requirements under FASB accounting coding standards 825-10-15 have a process that verifies compliance.

## Prevention and Detection

As previously mentioned, an effective internal control environment includes ethical values and integrity displayed by management combined with the effective oversight as well as the underlying tone set 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 where 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 county office and Hope Academy's governing board to review the findings and recommendations of this audit 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. Administrators and 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. The charter should not employ relatives of employees on a permanent or part-time basis so that the relative reports directly to the employee, or the employee exercises any direct influence on the relative's hiring, salary placement, promotions, evaluations, pay increases, payments for stipends or bonuses.

While the governing board and all employees in the organization have some responsibility for internal controls, the founder/former superintendent, his spouse and close associates holding key administrative positions had a fiduciary duty and responsibility to make certain that the assurances in the charter petition and the governing board fiscal policies and procedures were conducted responsibly and ethically.

Based on the evidence presented to FCMAT, there is sufficient documentation to demonstrate that fraud, mismanagement and misappropriation of the charter school funds and assets may have occurred. The charter school's internal control environment has significant weaknesses, which increases the probability of fraud and/or abuse. These findings should be of great concern to the governing boards of Hope Academy and the San Bernardino County Superintendent of Schools and require immediate intervention to limit the risk of fraud and/or misappropriation of assets in the future.

The existence of fraud is solely the purview of the courts and juries, and FCMAT will not make statements that could be construed as a conclusion that fraud has occurred.

In accordance with 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 local agency, the State Controller, the Superintendent of Public Instruction and the local district attorney.

## Recommendation

*The county superintendent should:*

1. Notify the governing board of Hope Academy Charter School, San Bernardino County Superintendent of Schools governing board, the State Controller, the Superintendent of Public Instruction, and the local district attorney that fraud, misappropriation of assets or other illegal activities may have occurred.

# Appendices

- A. Hope Academy Board Policy 7002.1**
- B. FASB-ASC Glossary**
- C. Study Agreement**





## Appendix A – Hope Academy Board Policy 7002.1

### Hope Academy

**Subject: Board-Staff Communications**

**Effective Date: September 6, 2011**

**Approved By: Board of Directors**

**Policy: 7002.1**

Role of the Board

### Board-Staff Communications

Hope Academy Charter School desires to maintain open channels of communication between the Board and the staff. However, the basic line of communication between the Board and staff will be through the Executive Director.

### Staff Communications to the Board

Communications from staff members to the Board or its committees shall be submitted through the Executive Director. The Executive Director shall forward such communications received from staff members to the Board. This procedure is not intended to deny any staff member his/her constitutional right of free speech or the right to appeal to or otherwise address the Board on important matters through established procedures.

If approached by a staff member with a complaint not using the appropriate process (*Board Policy 2001.1: Uniform Complaint Procedures*), members of the Board should report it as soon as possible to the Board President.

### Board Communications to Staff

All official communications, policies, and directives of the Board that would be of interest and concern to the staff will generally be communicated through the Executive Director. The Executive Director shall also keep staff members informed of the Board's concerns and actions.

If the Board is in need of clarification about agenda items, Board members may contact senior staff in order to obtain available information. This should be done, when possible, with the knowledge of the Executive Director as a courtesy and also in order not to undermine the Executive Director's authority. The intent of communication is to share current and available information and never to direct or manage the staff member's time or activities.

### Social Interaction

Both staff and Board members share an interest in the school and in education generally, and it is to be expected that when they interact at social affairs and other functions, they will informally discuss such matters as educational trends, issues, and innovations, and general activities of the School. However, since Board members are not authorized to act

on behalf of the Board unless by quorum, in open public session, or when specifically vested with such authority, Board members and members of the staff should not discuss any matter which may result in the individual Board member(s) making some decision and giving the staff member a directive as a result.

In no case should Board members pass information on to staff or students. The route from the Board to staff or students is via the Executive Director. Board members should never discuss divisions within the Board, emerging Board policy, hiring or layoff matters involving staff, or student due process. Board members should not discuss individual personalities, personnel grievances, or other complaints with staff members or others outside the appropriate setting. It is very damaging to discuss rumors which may prove to be unfounded and which may damage morale, or which may be used by one faction against another, or by one staff person against another. Board members may not always be aware of the factions which may exist among staff and students or of the ambitions of particular individuals, and it is harmful to pass on information which may inadvertently be used to further interpersonal intrigues or other problems at staff or student levels. It is also dangerous to discuss any actions, which could, theoretically, result in legal proceedings and interfere with the job of the Executive Director and Board.

Instead, all such matters should be addressed in accordance with the procedures established in Board policy.

### **Hope Academy Conflict-of-interest Code**

#### **Adoption**

In compliance with the Political Reform Act of 1974, California Government Code Section 87100, et seq., Hope Academy Charter School hereby adopts this Conflict of Interest Code (“Code”), which shall apply to all governing board members, candidates for member of the governing board, and all other designated employees of Hope Academy Charter School (“Charter School”), as specifically required by California Government Code Section 87300.

#### **Designated Employees**

Employees of this Charter School, including governing board members and candidates, who hold positions that involve the making or participation in the making, of decisions that may foreseeably have a material effect on any financial interest, shall be designated employees. The designated positions are listed in “Exhibit A” attached to this policy and incorporated by reference herein.

#### **Statement of Economic Interests: Time of Filing**

Each designated employee, including governing board members and candidates, shall file a Statement of Economic Interest (“Statement”) at the time and manner prescribed below, disclosing reportable investments, interests in real property, business positions, and income required to be reported under the category or categories to which the employee’s position is assigned in “Exhibit A.”

An investment, interest in real property or income shall be reportable, if the business entity in which the investment is held, the interest in real property, the business position, or

source of income may foreseeably be affected materially by a decision made or participate in by the designated employee by virtue of his or her position. The specific disclosure responsibilities assigned to each position are set forth in “Exhibit B.”

### **Initial Statements**

All designated employees employed by the Charter School on the effective date of this Code, as originally adopted, promulgated and approved by the Charter School, shall file statements within 30 days after the effective date of this Code. Thereafter, each person in a position that becomes by an amendment to this Code a “designated employee” shall file an Initial Statement within 30 days after the effective date of the amendment.

### **Governing Board Candidates**

Candidates for election to the governing board shall file statements within 5 days after the final date for filing nomination petitions.

### **Assuming Office Statements**

All persons assuming designated positions after the effective date of this Code shall file statements within 30 days after assuming designated positions.

### **Annual Statements**

All designated employees shall file statements no later than **April 1**.

### **Leaving Office Statements**

All persons who leave designated positions shall file statements within 30 days after leaving office.

### **Statements for Persons Who Resign 30 Days after Appointment**

Persons who resign within 30 days of initial appointment are not deemed to have assumed office or left office provided they did not make or participate in the making of, or use their position to influence any decision and did not receive or become entitled to receive any form of payment as a result of their appointment. Such persons shall not file either an assuming or Leaving Office Statement.

### **Statements Filed With the Charter School**

All Statements shall be supplied by the Charter School. All Statements shall be filed with the Charter School. The Charter School’s filing officer shall make and retain a copy and forward the original to the County Board of Supervisors.

### **Statements of Economic Interests: Contents of and Time Period Covered by the Statements**

#### **Contents of Initial Statements**

Initial Statements shall disclose any reportable investments, interests in real property and business positions held on the effective date of the Code and income received during the 12 months prior to the effective date of the Code.

**Contents of Assuming Office Statements**

Assuming Office Statements shall disclose any reportable investments, interests in real property and business positions held on the date of assuming office and income received during the 12 months prior to the date of assuming office.

**Contents of Annual Statements**

Annual Statements shall disclose any reportable investments, interest in real property, income and business positions held or received during the previous calendar year provided, however, that the period covered by an employee's first Annual Statement shall begin on the effective date of the Code or date of assuming office, whichever is later. The statement shall include any reportable investment or interest in real property, partially or wholly acquired or disposed of during the period covered by the statement, with the date of acquisition or disposal.

**Contents of Leaving Office Statements**

Leaving Office Statements shall disclose reportable investments, interest in real property, income and business positions held or received during the period between the closing date of the last statement filed and the date of leaving office. The statement shall include any reportable investment or interest in real property, partially or wholly acquired or disposed of during the period covered by the statement, with the date of acquisition or disposal.

**Statements of Economic Interests: Manner of Reporting****Investment and Real Property Disclosure**

When an investment or interest in real property is required to be disclosed, the statement shall contain the following:

1. A statement of the nature of the investment or interest;
2. The name of the business entity in which each investment is held, and a general description of the business activity in which the business entity is engaged;
3. The address or other precise location of the real property; and
4. A statement whether the fair market value of the investment or interest in real property exceeds one thousand dollars (\$1,000), exceeds ten thousand dollars (\$10,000), or exceeds one hundred thousand dollars (\$100,000). This information need not be provided with respect to an interest in real property which is used principally as the residence of the filer. Reportable investments or interest in real property do include those in excess of one thousand dollars (\$1,000) held by the filer's spouse and dependent children as well as a pro rata share of any investment or interest in real property of any business entity or trust in which the filer, spouse and dependent children together own a direct, indirect or beneficial interest of 10% or more.

**Personal Income Disclosure**

Personal income is required to be reported under this Code, the statement shall contain the following:

The name and address of each source of income aggregating \$250 or more in value or \$50 or more in value if the income was a gift, and a general description of the business activity, if any, of each source;

1. A statement whether the aggregate value of income from each source, or in the case of a loan, the highest amount owed to each source, was one thousand dollars (\$1,000) or less, greater than one thousand dollars (\$1,000), or greater than ten thousand dollars (\$10,000);
2. A description of the consideration, if any, for which the income was received;
3. In the case of a gift, the name, address and business activity of the donor and any intermediary through which the gift was made; a description of the gift; the amount or value of the gift and the date on which the gift was received; and
4. In the case of a loan, the annual interest rate and the security, if any, given for the loan.

### **Business Entity Income Disclosure**

When income of a business entity, including income of a sole proprietorship, is required to be reported, the statement shall contain:

1. The name, address, and a general description of the business activity; and
2. The name of every person from whom the business entity received payments if the filer's pro rata share of gross receipts from such a person was equal to or greater than ten thousand dollars (\$10,000).

### **Business Positions Disclosure**

When reporting business positions, a designated employee shall list the name of each business entity not specified above in which he/she is a director, officer, partner, trustee, employee, or in which he/she holds any position of management; a description of the business activity in which the entity is engaged; and designated employee's position with the business entity.

### **Disqualification**

No designated employee shall make, participate in making, or try to use his/her official position to influence any Charter School decision which he/she knows or has reason to know will have a reasonably foreseeable material financial effect, distinguishable from its effect on the public generally, on the official or a member of his or her immediate family or on:

1. Any business entity or real property in which the designated employee has a direct or indirect investment or interest worth one thousand dollars (\$1,000) or more.
2. Any source of income totaling two hundred fifty dollars (\$250) or more provided or promised to the designated employee within twelve months prior to the decision. (This category does not include gifts or loans made at regular rates by commercial lending institutions.)
3. Any business entity in which the designated employee is the director, officer, partner, trustee, employee, or any kind of director.
4. Any donor of gifts totaling \$250 or more in value provided or promised to the designated within twelve months prior to the decision; any intermediary or agency for such a donor.

No designated employee shall be prevented from making or participating in any decision to the extent that his/her participation is legally required for the decision to be made. (The need to break a tie vote does not make the designated employee's participation legally required.)

### **Manner of Disqualification**

#### **Non-Governing Board Member Designated Employees**

When a non-Governing Board member designated employee determines that he/she should not make a decision because of a disqualifying interest, he/she should submit a written disclosure of the disqualifying interest to his/her immediate supervisor. The supervisor shall immediately reassign the matter to another employee and shall forward the disclosure notice to the Charter School Director, who shall record the employee's disqualification. In the case of a designated employee who is head of an agency, this determination and disclosure shall be made in writing to his/her appointing authority.

#### **Governing Board Member Designated Employees**

Governing Board members shall disclose a disqualifying interest at the meeting during which consideration of the decision takes place. This disclosure shall be made part of the Board's official record. The Board member shall then refrain from participating in the decision in any way (i.e., the Board member with the disqualifying interest shall refrain from voting on the matter and shall leave the room during Board discussion and when the final vote is taken).

### **Definition of Terms**

As applicable to a charter school, the definitions contained in the Political Reform Act of 1974, the regulations of the Fair Political Practices Commission, specifically California Code of Regulations Section 18730, and any amendments or modifications to the Act and regulations are incorporated by reference to this Code.

**Hope Academy  
Conflict of Interest Code**

**EXHIBIT A**

Designated Positions

- I. Persons occupying the following positions are designated employees and must disclose financial interests in all categories defined in “Exhibit B” (i.e. categories 1, 2, and 3).
  - A. Members of the Governing Board
  - B. Candidates for Member of the Governing Board
  - C. Corporate Officers (e.g., Executive Director/President, CFO/Treasurer, Secretary)
  - D. Executive Director of Charter School
  - E. Chief Administrative Officer
  - F. Chief Educational Officer
  - G. Consultants<sup>1</sup>
  - H. Other Employees<sup>2</sup>
  
- II. Persons occupying the following positions are designated employees and must disclose financial interests defined in Category 1 of “Exhibit B.”
  - A. Controller
  - B. Assistant Controller
  - C. Other Employees<sup>3</sup>
  
- III. Persons occupying the following positions are designated employees and must disclose financial interests defined in Categories 2 and 3 of “Exhibit B.”
  - A. Director of Technology
  - B. Contractor
  - C. Other Employees<sup>4</sup>

<sup>1</sup> The Director may determine, in writing, that a particular consultant, although a “designated position,” is hired to perform a range of duties that is limited in scope and thus not required to fully comply with the disclosure requirements in this section. Such written determination shall include a description of the consultant’s duties and, based upon that description, a statement of the extent of disclosure requirements. The Director’s determination is a public record and shall be retained for public inspection in the same manner and location of interest code.

<sup>2</sup> “Other Employees” include any employee occupying a position that requires the employee to make a governmental decision that foreseeably and materially affects a personal financial interest, source of income, or a business position in a business entity.

<sup>3</sup> “Other Employees” include any employee with authority to make purchases that may foreseeably and materially affect an investment and/or business position in business entities or who are in a position to influence a governmental decision that may foreseeably and materially affect an investment and/or business position in a business entity.

<sup>4</sup> “Other Employees” include employees with authority to make purchases that may foreseeably and materially affect investments and business positions in business entities which provide services, supplies, materials, or equipment in which the employee has authority to purchase.

**Hope Academy  
Conflict of Interest Code**

**EXHIBIT B**

**Disclosure Categories**

**Category 1 Reporting**

- A. Interest in real property which is located in whole or in part either (1) within the boundaries of the District, or (2) within two miles of the boundaries of the District, including any leasehold, beneficial or ownership interests or option to acquire such interest in real property, if the fair market value of the interest is greater than \$1,000. (Interests in real property of an individual include a business entity's share of interest in real property of any business entity or trust in which the designated employee or his or her spouse owns, directly, indirectly, or beneficially, a ten percent interest or greater.)
- B. Investments in or income from persons or business entities which are contractors or sub-contractors which are or have been within the previous two-year period engaged in the performance of building construction or design within the District.
- C. Investments in or income from persons or business entities engaged in the acquisition or disposal of real property within the jurisdiction. Investment includes any financial interest in or security issued by a business entity, including but not limited to common stock, preferred stock, rights, warrants, options, debt instruments and any partnership interest or other ownership interests. Investments of any individual include a pro rata share of investments of any business entity or trust in which the designated employee or his or her spouse owns, directly, indirectly or beneficially, a ten percent interest or greater. Investment does not include a time or demand deposit in a financial institution, shares in a credit union, any insurance policy, or any bond or other debt instrument issued by any government or government agency. No investment or interest in real property is reportable unless its fair market value exceeds \$1,000. No source of income is reportable unless the income received by or promised to the public official aggregates \$250 or more in value or \$50 or more in value if the income was a gift during the preceding 12-month reporting period.

**Category 2 Reporting**

- A. Investments in or income from business entities which manufacture or sell supplies, books, machinery or equipment of the type utilized by the department for which the designated employee is Director or Director. Investments include interests described in Category 1.

**Category 3 Reporting**

- A. Investments in or income from business entities which are contractors or sub-contractors engaged in the performance of work or services of the type utilized by the department for which the designated employee is Director. Investments include the interests described in Category 1.



## Appendix B – FASB-ASC Glossary

Related Parties

1961

### AU Section 334

#### *Related Parties*

(Supersedes Statement on Auditing Standards No. 6, AU sec. 335.01–.19.)<sup>\*</sup>

Source: SAS No. 45.

See section 9334 for interpretations of this section.

Effective for periods ended after September 30, 1983, unless otherwise indicated.

.01 This section provides guidance on procedures that should be considered by the auditor when he is performing an audit of financial statements in accordance with generally accepted auditing standards to identify related party relationships and transactions and to satisfy himself concerning the required financial statement accounting and disclosure.<sup>1</sup> The procedures set forth in this section should not be considered all-inclusive. Also, not all of them may be required in every audit.

#### Accounting Considerations

.02 Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 850, *Related Party Disclosures*, gives the requirements for

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<sup>\*</sup> This section also withdraws the following auditing interpretations dated March 1976 (AU sec. 9335.01–.11):

- Evaluating the Adequacy of Disclosure of Related Party Transactions
- Disclosure of Commonly Controlled Parties
- Definition of "Immediate Family"

<sup>1</sup> Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 850-10-50 contains the disclosure requirements for related party relationships and transactions. The FASB ASC glossary defines *related parties* as

- a. Affiliates of the entity
- b. Entities for which investments in their equity securities would be required, absent the election of the fair value option under the Fair Value Option Subsection of Section 825–10–15, to be accounted for by the equity method by the investing entity
- c. Trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of management
- d. Principal owners of the entity and members of their immediate families
- e. Management of the entity and members of their immediate families
- f. Other parties with which the entity may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests
- g. Other parties that can significantly influence the management or operating policies of the transacting parties or that have an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests. The FASB ASC glossary also defines the terms *affiliate*, *control*, *immediate family*, *management*, and *principal owners*. FASB ASC 850-10-05-3 provides examples of related party transactions.

[Footnote revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

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related party disclosures. Certain accounting pronouncements prescribe the accounting treatment when related parties are involved; however, established accounting principles ordinarily do not require transactions with related parties to be accounted for on a basis different from that which would be appropriate if the parties were not related. The auditor should view related party transactions within the framework of existing pronouncements, placing primary emphasis on the adequacy of disclosure. In addition, the auditor should be aware that the substance of a particular transaction could be significantly different from its form and that financial statements should recognize the substance of particular transactions rather than merely their legal form.<sup>2</sup> [Revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

**.03** Transactions that because of their nature may be indicative of the existence of related parties include<sup>3</sup> —

- a. Borrowing or lending on an interest-free basis or at a rate of interest significantly above or below market rates prevailing at the time of the transaction.
- b. Selling real estate at a price that differs significantly from its appraised value.
- c. Exchanging property for similar property in a nonmonetary transaction.
- d. Making loans with no scheduled terms for when or how the funds will be repaid.

## Audit Procedures

**.04** An audit performed in accordance with generally accepted auditing standards cannot be expected to provide assurance that all related party transactions will be discovered. Nevertheless, during the course of his audit, the auditor should be aware of the possible existence of material related party transactions that could affect the financial statements and of common ownership or management control relationships for which FASB ASC 850-10-50 requires disclosure. Many of the procedures outlined in the following paragraphs are normally performed in an audit in accordance with generally accepted auditing standards, even if the auditor has no reason to suspect that related party transactions or control relationships exist. Other audit procedures set forth in this section are specifically directed to related party transactions. [Revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

**.05** In determining the scope of work to be performed with respect to possible transactions with related parties, the auditor should obtain an

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<sup>2</sup> Some pronouncements specify criteria for determining, presenting, and accounting for the substance of certain transactions and events. Examples include (1) presenting consolidated financial statements instead of separate statements of the component legal entities (FASB ASC 810, *Consolidation*); (2) capitalizing leases (FASB ASC 840, *Leases*); and (3) imputing an appropriate interest rate when the face amount of a note does not reasonably represent the present value of the consideration given or received in exchange for it (FASB ASC 835, *Interest*). [Footnote revised, June 1993, to reflect conforming changes necessary due to the issuance of Statement of Position 93-3. Footnote revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

<sup>3</sup> FASB ASC 850-10-05-4 gives other examples of common types of transactions with related parties. FASB ASC 850-10-05-5 states that "transactions between related parties are considered to be related party transactions even though they may not be given accounting recognition. For example, an entity may receive services from a related party without charge and not record receipt of the services. While not providing accounting or measurement guidance for such transactions, FASB ASC 850 requires their disclosure nonetheless." [Footnote revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

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understanding of management responsibilities and the relationship of each component to the total entity. He should consider controls over management activities, and he should consider the business purpose served by the various components of the entity. Normally, the business structure and style of operating are based on the abilities of management, tax and legal considerations, product diversification, and geographical location. Experience has shown, however, that business structure and operating style are occasionally deliberately designed to obscure related party transactions.

**.06** In the absence of evidence to the contrary, transactions with related parties should not be assumed to be outside the ordinary course of business. The auditor should, however, be aware of the possibility that transactions with related parties may have been motivated solely, or in large measure, by conditions similar to the following:

- a. Lack of sufficient working capital or credit to continue the business
- b. An urgent desire for a continued favorable earnings record in the hope of supporting the price of the company's stock
- c. An overly optimistic earnings forecast
- d. Dependence on a single or relatively few products, customers, or transactions for the continuing success of the venture
- e. A declining industry characterized by a large number of business failures
- f. Excess capacity
- g. Significant litigation, especially litigation between stockholders and management
- h. Significant obsolescence dangers because the company is in a high-technology industry

### Determining the Existence of Related Parties

**.07** The auditor should place emphasis on testing material transactions with parties he knows are related to the reporting entity. Certain relationships, such as parent-subsidary or investor-investee, may be clearly evident. Determining the existence of others requires the application of specific audit procedures, which may include the following:

- a. Evaluate the company's procedures for identifying and properly accounting for related party transactions.
- b. Request from appropriate management personnel the names of all related parties and inquire whether there were any transactions with these parties during the period.
- c. Review filings by the reporting entity with the Securities and Exchange Commission and other regulatory agencies for the names of related parties and for other businesses in which officers and directors occupy directorship or management positions.
- d. Determine the names of all pension and other trusts established for the benefit of employees and the names of their officers and trustees.<sup>4</sup>
- e. Review stockholder listings of closely held companies to identify principal stockholders.

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<sup>4</sup> FASB ASC glossary term *related parties* includes "trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of management." [Footnote revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

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- f.* Review prior years' working papers for the names of known related parties.
- g.* Inquire of predecessor, principal, or other auditors of related entities concerning their knowledge of existing relationships and the extent of management involvement in material transactions.
- h.* Review material investment transactions during the period under audit to determine whether the nature and extent of investments during the period create related parties.

**Identifying Transactions With Related Parties**

**.08** The following procedures are intended to provide guidance for identifying material transactions with parties known to be related and for identifying material transactions that may be indicative of the existence of previously undetermined relationships:

- a.* Provide audit personnel performing segments of the audit or auditing and reporting separately on the accounts of related components of the reporting entity with the names of known related parties so that they may become aware of transactions with such parties during their audits.
- b.* Review the minutes of meetings of the board of directors and executive or operating committees for information about material transactions authorized or discussed at their meetings.
- c.* Review proxy and other material filed with the Securities and Exchange Commission and comparable data filed with other regulatory agencies for information about material transactions with related parties.
- d.* Review conflict-of-interests statements obtained by the company from its management.<sup>5</sup>
- e.* Review the extent and nature of business transacted with major customers, suppliers, borrowers, and lenders for indications of previously undisclosed relationships.
- f.* Consider whether transactions are occurring, but are not being given accounting recognition, such as receiving or providing accounting, management or other services at no charge or a major stockholder absorbing corporate expenses.
- g.* Review accounting records for large, unusual, or nonrecurring transactions or balances, paying particular attention to transactions recognized at or near the end of the reporting period.
- h.* Review confirmations of compensating balance arrangements for indications that balances are or were maintained for or by related parties.
- i.* Review invoices from law firms that have performed regular or special services for the company for indications of the existence of related parties or related party transactions.
- j.* Review confirmations of loans receivable and payable for indications of guarantees. When guarantees are indicated, determine their nature and the relationships, if any, of the guarantors to the reporting entity.

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<sup>5</sup> Conflict-of-interests statements are intended to provide those charged with governance with information about the existence or nonexistence of relationships between the reporting persons and parties with whom the company transacts business. [Footnote revised, April 2007, to reflect conforming changes necessary due to the issuance of Statement on Auditing Standards No. 114.]

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**Examining Identified Related Party Transactions**

**.09** After identifying related party transactions, the auditor should apply the procedures he considers necessary to obtain satisfaction concerning the purpose, nature, and extent of these transactions and their effect on the financial statements. The procedures should be directed toward obtaining and evaluating sufficient appropriate audit evidence and should extend beyond inquiry of management. Procedures that should be considered include the following:

- a. Obtain an understanding of the business purpose of the transaction.<sup>6</sup>
- b. Examine invoices, executed copies of agreements, contracts, and other pertinent documents, such as receiving reports and shipping documents.
- c. Determine whether the transaction has been approved by those charged with governance.
- d. Test for reasonableness the compilation of amounts to be disclosed, or considered for disclosure, in the financial statements.
- e. Arrange for the audits of intercompany account balances to be performed as of concurrent dates, even if the fiscal years differ, and for the examination of specified, important, and representative related party transactions by the auditors for each of the parties, with appropriate exchange of relevant information.
- f. Inspect or confirm and obtain satisfaction concerning the transferability and value of collateral.

[Revised, March 2006, to reflect conforming changes necessary due to the issuance of Statement on Auditing Standards No. 105. Revised, April 2007, to reflect conforming changes necessary due to the issuance of Statement on Auditing Standards No. 114.]

**.10** When necessary to fully understand a particular transaction, the following procedures, which might not otherwise be deemed necessary to comply with generally accepted auditing standards, should be considered.<sup>7</sup>

- a. Confirm transaction amount and terms, including guarantees and other significant data, with the other party or parties to the transaction.
- b. Inspect evidence in possession of the other party or parties to the transaction.
- c. Confirm or discuss significant information with intermediaries, such as banks, guarantors, agents, or attorneys, to obtain a better understanding of the transaction.
- d. Refer to financial publications, trade journals, credit agencies, and other information sources when there is reason to believe that unfamiliar customers, suppliers, or other business enterprises with which material amounts of business have been transacted may lack substance.
- e. With respect to material uncollected balances, guarantees, and other obligations, obtain information about the financial capability of the

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<sup>6</sup> Until the auditor understands the business sense of material transactions, he cannot complete his audit. If he lacks sufficient specialized knowledge to understand a particular transaction, he should consult with persons who do have the requisite knowledge.

<sup>7</sup> Arrangements for certain procedures should be made or approved in advance by appropriate client officials.

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other party or parties to the transaction. Such information may be obtained from audited financial statements, unaudited financial statements, income tax returns, and reports issued by regulatory agencies, taxing authorities, financial publications, or credit agencies. The auditor should decide on the degree of assurance required and the extent to which available information provides such assurance.

**Disclosure**

**.11** For each material related party transaction (or aggregation of similar transactions) or common ownership or management control relationship for which FASB ASC 850-10-50 requires disclosure, the auditor should consider whether he has obtained sufficient appropriate audit evidence to understand the relationship of the parties and, for related party transactions, the effects of the transaction on the financial statements. He should then evaluate all the information available to him concerning the related party transaction or control relationship and satisfy himself on the basis of his professional judgment that it is adequately disclosed in the financial statements. [Revised, March 2006, to reflect conforming changes necessary due to the issuance of Statement on Auditing Standards No. 105. Revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]<sup>8</sup>

**.12** Except for routine transactions, it will generally not be possible to determine whether a particular transaction would have taken place if the parties had not been related, or assuming it would have taken place, what the terms and manner of settlement would have been. Accordingly, it is difficult to substantiate representations that a transaction was consummated on terms equivalent to those that prevail in arm's-length transactions.<sup>9</sup> If such a representation is included in the financial statements and the auditor believes that the representation is unsubstantiated by management, he should express a qualified or adverse opinion because of a departure from generally accepted accounting principles, depending on materiality (see section 508.35 and .36).

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<sup>8</sup> Also, see section 431, *Adequacy of Disclosure in Financial Statements*. [Footnote revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

<sup>9</sup> FASB ASC 850-10-50-5 states that if representations are made about transactions with related parties, the representations "shall not imply that the related party transactions were consummated on terms equivalent to those that prevail in arm's-length transactions unless such representations can be substantiated." [Footnote revised, June 2009, to reflect conforming changes necessary due to the issuance of FASB ASC.]

**AU §334.11**

## Appendix C – Study Agreement

# FCMAT

FISCAL CRISIS & MANAGEMENT  
ASSISTANCE TEAM

CSIS California School Information Services

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### FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM AB139 STUDY AGREEMENT January 7, 2016

The Fiscal Crisis and Management Assistance Team (FCMAT), hereinafter referred to as the team, and the San Bernardino County Superintendent of Schools, 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. Pursuant to the provisions of Education Code (EC) Section 1241.5 (c), a county superintendent of schools may review or audit the expenditures and internal controls of any 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 and EC Section 47604.4(a); the county superintendent may conduct an investigation of the charter school based on written complaints by parents or other information that justifies the review.

Allegations have been received regarding potential for conflict of interest issues based on Government Code Section 1090. Primary assertions indicate that an administrator of the Hope Academy Charter School (Palm Desert) inappropriately executed and entered into contractual agreements with vendor companies and/or individuals for procurement of goods and services in which a direct financial interest exists. The primary focus of this review is to identify and advise the COE, based on the testing performed, whether sufficient evidence exists supporting an allegation that fraud, misappropriation of funds or other illegal fiscal practices may have occurred.

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. 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 San Bernardino County Superintendent of Schools has requested that the team assign professionals to conduct an extraordinary audit on behalf of the Morongo Unified School District/Hope Academy Charter School (Palm Desert). Per EC Section 1241.5(c), the superintendent has reason to believe that fraud, misappropriation of funds, or other illegal practices may have occurred.

The review will include but not be limited to the following:

1. Evaluate policies, procedures, internal controls for procurement practices performed by the charter school.

**Evaluation of Policies and Procedures:**

- a. Determine whether the charter's petition, memorandum of understanding, charter school bylaws or other policies and administrative regulations exist that include language pertaining to conflicts of interest pursuant to Government Code Section 1090.
- b. Identify documented positions with responsibility for initiating, reviewing, approving, and reconciling procurement activities.
- c. Review financial processes related to key purchasing activities including procurement authorization and vendor payments.

**Evaluation of Internal Controls:**

- a. Evaluate processes for adequate separation of duties and proper authorizations and approvals.
  - b. Evaluate monitoring procedures and verify that controls are operating properly.
  - c. Evaluate controls that prevent management from overriding internal controls to prevent misappropriation of funds.
  - d. Determine if clearly established lines of authority and responsibility exist and are documented in organizational charts.
2. Review the charter's policy on conflict of interest and the requirements under the Fair Political Practices Commission related to the disclosure of certain financial interests and sources of income to the public. Identify whether any actions by the superintendent/executive director resulted in a personal or financial benefit to the director.
  3. Conduct sample tests of transactions specific to the allegations for the 2015-16 fiscal year and one prior fiscal year. Testing of sampled transactions for this review will be based on the team's judgement and experience and may not include the testing of all transactions and records for this period.

**Transaction Testing Objectives:**

- a. Determine whether transactions were conducted in accordance with established policy and procedures.



- b. Determine if expenditures made by the charter school are for legitimate educational purposes and in accordance with approved contracts.
- c. Determine whether the charter school engaged in related-party transactions and if those transactions were conducted in accordance with established policy and procedures and were transparent in nature.

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

1. **Orientation Meeting** - The team will conduct an orientation session at the COE, authorizing district and/or charter school to brief management and supervisory personnel on the team's procedures and the purpose and schedule of the study.
2. **On-site Review** - The team will conduct an on-site review at the charter school 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. **Exit Meeting** – The team will hold an exit meeting at the conclusion of the on-site review to inform the COE of significant findings to that point.
5. **Draft Report** – When appropriate, electronic copies of a preliminary draft report will be delivered to the COE's administration for review and comment on a schedule determined by the team.
6. **Final Report** - Electronic copies of the final report will be delivered to the COE following completion of the review. Printed copies are available from the FCMAT office upon request.
7. **Follow-Up Support** – If requested, the team will meet with the COE, authorizing district and/or charter school to discuss the findings and recommendations of the report.

**3. PROJECT PERSONNEL**

The study team will be supervised by Michael H. Fine, Chief Administrative Officer, Fiscal Crisis and Management Assistance Team, Kern County Superintendent of Schools Office. The study team may also include:

- |           |                                |                                   |
|-----------|--------------------------------|-----------------------------------|
| <b>A.</b> | <b><i>To Be Determined</i></b> | <b><i>FCMAT Staff</i></b>         |
| <b>B.</b> | <b><i>To Be Determined</i></b> | <b><i>FCMAT Consultant(s)</i></b> |

#### 4. **PROJECT COSTS**

The cost for studies requested pursuant to EC Section 42127.8 (d) (1) shall be:

- A. \$800 per day for each staff team member while on site, conducting fieldwork at other locations, preparing and presenting reports, or participating in meetings. The cost of independent FCMAT consultants will be billed at their actual daily rate.
- B. All out-of-pocket expenses, including travel, meals and lodging.

**Based on the elements noted in Section 2A, the total estimated cost of the study will be \$25,000.**

- C. Any change to the scope will affect the estimate of total cost.

Payments for FCMAT services may be reimbursed from funds pursuant to EC Section 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, DISTRICT AND/OR CHARTER SCHOOL**

- A. The COE, district and/or charter school will provide office and conference room space during on-site reviews.
- B. The COE, district and/or charter school will provide the following if requested:
  - 1. Policies, regulations and prior reports addressing the study request
  - 2. Current or proposed organizational charts
  - 3. Current and two (2) prior years' audit reports
  - 4. Any documents requested on a supplemental list. Documents requested on the supplemental list should be provided to FCMAT only in electronic format; if only hard copies are available, they should be scanned by the COE, district and/or charter school and sent to FCMAT in an electronic format
  - 5. Documents should be provided in advance of field work; any delay in the receipt of the requested documents may affect the start date and/or completion date of the project. Upon approval of the signed study agreement, access will be provided to FCMAT's online SharePoint document repository where the COE, district and/or charter school shall upload all requested documents.
- C. The COE's 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 Section 45125.1(c), representatives of FCMAT will have limited contact with pupils. The county office, district and/or charter school shall take appropriate steps to comply with EC Section 45125.1(c).

## 6. PROJECT SCHEDULE

The following schedule outlines the planned completion dates for different phases of the study and will be established upon the receipt of a signed study agreement:

<i>Orientation:</i>	<i>To be determined</i>
<i>Staff Interviews:</i>	<i>To be determined</i>
<i>Exit Meeting:</i>	<i>To be determined</i>
<i>Preliminary Report Submitted:</i>	<i>To be determined</i>
<i>Final Report Submitted:</i>	<i>To be determined</i>

## 7. COMMENCEMENT, TERMINATION AND COMPLETION OF WORK

FCMAT will begin work as soon as it has assembled an available and appropriate study team consisting of FCMAT staff and independent consultants, taking into consideration other jobs FCMAT has previously undertaken and assignments from the state. The team will work expeditiously to complete its work and deliver its report, subject to the cooperation of the COE, district and/or charter school and any other parties from whom, in the team's judgment, it must obtain information. Once the team has completed its field work, it will proceed to prepare a preliminary draft report and a final report. Prior to completion of field work, the COE may terminate its request for service and will be responsible for all costs incurred by FCMAT to the date of termination under Section 4 (Project Costs). If the COE does not provide written notice of termination prior to completion of field work, the team will complete its work and deliver its report and the COE will be responsible for the full costs. The COE understands and agrees that FCMAT is a state agency and all FCMAT reports are published on the FCMAT website and made available to interested parties in state government. In the absence of extraordinary circumstances, FCMAT will not withhold preparation, publication and distribution of a report once field work has been completed, and the COE shall not request that it do so.

## 8. INDEPENDENT CONTRACTOR

FCMAT is an independent contractor and is not an employee or engaged in any manner with the COE. The manner in which FCMAT's services are rendered shall be within its sole control and discretion. FCMAT representatives are not authorized to speak for, represent, or obligate the COE in any manner without prior express written authorization from an officer of the COE.

## 9. INSURANCE

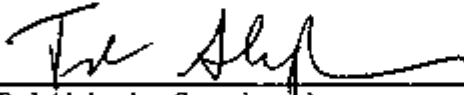
During the term of this agreement, FCMAT shall maintain liability insurance of not less than \$1 million unless otherwise agreed upon in writing by the COE, automobile liability insurance in the amount required under California state law, and workers compensation as required under California state law. FCMAT shall provide certificates of insurance, with additional insured endorsements, indicating applicable insurance coverages upon request.

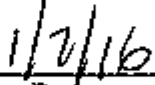
**10. HOLD HARMLESS**

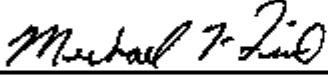
FCMAT shall hold the COE, its board, officers, agents and employees harmless from all suits, claims and liabilities resulting from negligent acts or omissions of its board, officers, agents and employees undertaken under this agreement. Conversely, the COE shall hold FCMAT, its board, officers, agents and employees harmless from all suits, claims and liabilities resulting from negligent acts or omissions of its board, officers, agents and employees undertaken under this agreement.

**11. CONTACT PERSON**

Contact: Richard De Nava, Assistant Superintendent, Business Services  
 Telephone: (909) 386-2459  
 E-mail Address: [richard\\_denava@sbcss.k12.ca.us](mailto:richard_denava@sbcss.k12.ca.us)

  
 Ted Alejandre, Superintendent  
 San Bernardino County Superintendent of Schools

  
 Date

  
 Michael H. Fine  
 Chief Administrative Officer  
 Fiscal Crisis & Management Assistance Team

January 7, 2016  
 Date