

INVESTIGATIVE REPORT

RATTAN PUBLIC SCHOOL DISTRICT

July 1, 2008 through June 30, 2011



*Independently serving the citizens of
Oklahoma by promoting the
accountability and fiscal integrity of
governmental funds.*



Oklahoma State
Auditor & Inspector
Gary A. Jones, CPA, CFE

Rattan Public School District
Pushmataha and Choctaw Counties, Oklahoma
Petition Audit Report
July 1, 2008 – June 30, 2011



Oklahoma State Auditor & Inspector

2300 N. Lincoln Blvd. • State Capitol, Room 100 • Oklahoma City, OK 73105 • Phone: 405.521.3495 • Fax: 405.521.3426

July 5, 2012

Citizens and Petitioners
Rattan Public School District
Rattan, Oklahoma 74562

Transmitted herewith is the Petition Audit Report of the Rattan Public School District, Rattan, Oklahoma.

Pursuant to your request, and in accordance with the requirements of **74 O.S. § 212(L)**, we performed a petition audit for the period July 1, 2008 through June 30, 2011.

The objectives of our petition audit primarily included, but were not limited to, the areas noted in your petition. Our findings and recommendations related to these objectives are presented in the accompanying report.

Because a petition audit is not an audit conducted in accordance with generally accepted auditing standards, we do not express an opinion on the account balances or financial statements of the Rattan Public School District for the audit period.

The goal of the State Auditor and Inspector is to promote accountability and fiscal integrity in state and local government. Maintaining our independence as we provide this service to the taxpayers of Oklahoma is of utmost importance.

We wish to take this opportunity to express our appreciation for the assistance and cooperation extended to our office during the course of our petition audit.

This report has been prepared for the citizens and registered voters of the Rattan Public School District, and for school and state officials with oversight responsibilities, as provided by statute. Pursuant to **74 O.S. § 212(L)**, 10% of the registered voters of a political subdivision of the State may request the State Auditor and Inspector to audit the books and records of the political subdivision. This document is a public document pursuant to the Oklahoma Open Records Act, **51 O.S. § 24A.1, et seq.**

Sincerely,

A handwritten signature in blue ink, appearing to read "Gary Jones".

GARY JONES, CPA, CFE
OKLAHOMA STATE AUDITOR & INSPECTOR

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Board of Education
(As of March 1, 2012)

Johnny Corgill.....President
Terry Holland.....Clerk
Terry Gregg.....Member
Rick Self.....Member
Loyd Deaton.....Member

Superintendent
Bruce Lawless
July 1, 2003 to December 31, 2011

Superintendent
Shari Pillow
January 1, 2012 to Present

Introduction

The Rattan Public School District is part of the Oklahoma State System of Public Education, as described in **70 O.S. § 1-101 et seq.**, of the **Oklahoma School Code**.

The Board of Education (“Board”) of the Rattan Public School District (“District”) is responsible for the supervision, management, and control of the District, as provided for in **70 O.S. § 5-117**.

Both the Board and the District are subject to the provisions of the **Oklahoma School Code**, as well as other statutes found in various titles including, but not limited to, Title 25 (Definitions and General Provisions), Title 51 (Officers), Title 61 (Public Buildings and Public Works), Title 62 (Public Finance), and Title 68 (Revenue and Taxation).

The District is audited annually by a private independent auditing firm and such reports were available for our review.

All dollar amounts included in the report are rounded to the nearest dollar, unless otherwise specified.

The District’s fiscal year starts July 1 and ends June 30. In this report, fiscal years are abbreviated by using the ending calendar year. For example, the fiscal year of July 1, 2010 to June 30, 2011, will be identified as “FY11.”

The Office of State Auditor and Inspector conducted a petition audit of the District, primarily relating to the objectives listed in the *Table of Contents*. The results of our petition audit are included in the following report.

Objective I. Review possible non-certified teacher hired with Special Education Funds.

Background

Federal and state laws require school districts to have special education teachers for students with disabilities. Teachers who are employed for this purpose must be certified by the state department of education in the field of “special education.”

Due to the difficulty in filling special education teacher positions, previous state law allowed for “substitute teachers” that were not “certified” to function as special education teachers. Senate Bill 1493 was approved in the 2006 Legislative Session. SB 1493 amended **70 O.S. 2001, § 6-105 (C)** to require additional training for “long-term” substitute teachers, as follows:

Beginning with the 2007-08 school year, *any substitute teacher* employed to teach special education for the same assignment for more than fifteen (15) consecutive or thirty (30) total school days during a school year *who does not hold a valid certificate to teach special education shall be required to complete in-service training as prescribed by the State Board of Education.* The training shall be provided at no cost to the substitute teacher. [emphasis added]

The Oklahoma State Department of Education (OSDE) has a web page that includes a memorandum dated August 8, 2008, from Misty Kimbrough, then Assistant State Superintendent of Public Instruction. The memo advises superintendents, special education directors and human resources personnel of the requirements for the training under the new statutory language.

Superintendents, Special Education Directors/Contacts, and Human Resources Personnel
Page Two
August 8, 2008

When a district employs a long-term substitute in a special education position, the principal of the individual site must contact our office and provide the substitute’s full name, mailing address, and e-mail address to Ms. Tina Spence, Coordinator, or Ms. Kim Osmani, Associate State Director. Once that information is received in our office, Ms. Spence or Ms. Osmani will assign the individual to the modules.

Upon successful completion of all four modules a certificate of completion will be issued from OSDE-SES to the substitute and mailed directly to the substitute. Space is limited; therefore, no assignments will be made until the individual is hired for the position of long-term substitute (i.e., districts may not sign individuals up weeks before they will begin their position).

The District hired a new teacher for a special education position beginning in FY09. Approximately three years after the district hired this teacher, there were questions raised concerning her qualifications and an alleged lack of certification for “special education.”

Finding **Although the teacher in question did not hold “a valid certificate to teach special education,” she completed the necessary requirements to be hired as “a long-term substitute in a special education position,” in accordance with 70 O.S. 2001, § 6-105 (C).**

We obtained records related to the teacher in question from the Oklahoma State Department of Education. The teacher was not certified in special education *until* January 2011. *In the interim period*, OSDE records indicated this teacher had completed the annual required in-service training to qualify as a long-term substitute in special education.

Conclusion The District did not violate any statutes in hiring a not yet certified teacher for a special education position and employing her as a “long-term substitute” until she passed her certification test in 2011.

Recommendation No recommendation is provided for this objective.

Objective II. Review possible irregularities, a conflict of interest and questions concerning the ownership of property across from Rattan Public School.

Background

A special board meeting was held January 29, 2004, during which the school board approved the purchase of 311 acres of land. At the February 23, 2004 board meeting, the board approved the employment of financial advisor Stephen H. McDonald & Associates of Norman, Oklahoma, to assist the district in obtaining lease-purchase financing of the real estate. The board also voted to authorize former superintendent Lawless to represent the school in the transaction.

Seven years after the purchase of the 311 acres, allegations were raised that the former superintendent received a large commission in the purchase of the property or in the subsequent sale of a 40 acre parcel of the earlier real estate purchase. There was also a question about the sale of some timber on the property, as to whether or not the school received the funds.

Finding # 1

The District followed proper procedures in the purchase and sale of the real estate; we found supporting documentation for all transactions; all funds were accounted for. The documentation indicated no real estate commissions were paid on the purchase of the property or on the sale of a 40 acre parcel. We confirmed with the Pushmataha County Clerk that the property is recorded and titled to Rattan Public Schools.

At one time, the former superintendent held a realtor's license and worked for a local real estate broker in Antlers. According to Randy Weeks, the current managing broker of John Cocke Real Estate, LLC, at the time of the 2004 lease-purchase transaction, John Cocke (owner) had retired and the former superintendent's license had lapsed. Weeks also stated that he had listed the Messer property in 2003, but *that* contract had expired, and the Messer family chose not to relist the property.

We obtained the closing documents from Stephen H. McDonald & Associates (SHM), the financial advisor, showing the purchase price and additional costs associated with the sale. The purchase price was \$180,000, the District made a \$20,000 down payment from its general fund, and other fees paid by the school were \$1,319.

SHM had solicited bids on the interest rate for the lease-purchase from three different banks, and the district financed through the bank with the lowest interest rate, i.e. FirstBank of Antlers, OK. The lease was for an eight year period, renewable each year, in accordance with state law that prohibits lease-purchase contracts extending beyond one fiscal year. The cover letter for the lease agreement stated:

“The proposal also provides for a **0%** prepayment premium should there be an early payoff of the lease.” [emphasis added]

The District took advantage of that provision and paid the lease off in just three years, as noted below. Proceeds from the annual levy for the District’s “building fund” were used to make payments on the lease-purchase agreement. No additional levy for a “sinking” or debt service fund was necessary.

PYMT NUMR	PERIODIC PAYMENT DATE	PRINCIPAL AMOUNT OF PAYMENT DUE	NET INTEREST AMT OF PAYMENT DUE	NET PERIODIC PMT AMOUNT DUE	PURCHASE OPTION PRICE (*)
0	07-Apr-05	0.00 DP	0.00	0.00	161,347.98
1	07-Apr-06	17,961.70	5,300.85	23,262.55	143,386.28
2	07-Apr-07	18,551.81	4,710.74	23,262.55	124,834.47
3	07-Apr-08	19,161.30	4,101.25	23,262.55	105,673.17

Ron Fisher, President of Stephen H. McDonald & Associates, Inc., was contacted to request the closing documents and was asked about a commission. He indicated there were no commissions paid to Stephen H. McDonald and Associates, Inc., Government Leasing Company, Inc., or any other party, and there was no realtor involved in the sale. The Real Estate Purchase and Sale Contract, Page 5, Article 8 Real Estate Commission, states in part that there were “...no commissions, finder’s fees, or other monies due any other person or entity...”

8. REAL ESTATE COMMISSION. Each party warrants and represents to the other that it has incurred no commissions, finder’s fees or other monies due any other person or entity by virtue of this transaction. Each party shall indemnify and hold the other harmless from and against any and all loss, cost or expense (including attorneys’ fees and court costs) resulting from any claim for any fee, commission or other similar payment by any broker, agent, finder or salesman in connection with this transaction, claiming by, through or under the indemnifying party.

The agreement between SHM and the District did provide for “...no greater than one percent and one-quarter percent (1¼ %) of the amount of the lease-purchase” for a financial advisor fee. However, that fee was to be paid by the “financier on the lease.” In other words, that fee would be

calculated as a factor *in the bidding process* for the lease-purchase financing and paid to SHM by the winning bidder, not *directly* by the District, but indirectly through the percentage rate that was bid.

Following the early payoff of the lease-purchase in February 2008, paperwork was filed with the Pushmataha County Clerk to transfer title to the District. This paperwork may have caused some confusion that led citizens to question the land purchase transaction.

Government Leasing Company, Inc. (GLC), a company associated with the financial advisor, Stephen H. McDonald & Associates, Inc., executed a warranty deed to transfer title from the Messer family to GLC on March 30, 2005, which was filed April 11, 2005. After finalizing the lease-purchase agreement between the District and FirstBank, GLC assigned title for the property to FirstBank with a “special warranty deed” filed April 27, 2005.

At the early conclusion of the lease-purchase, a special warranty deed was executed February 25, 2008, and filed March 11, 2008, transferring title from “Government Leasing Company” to “Rattan Public Schools.” This appeared to be a clerical error, since GLC had already transferred title to FirstBank in 2005, at the start of the lease-purchase. The error apparently was corrected January 23, 2009, when *FirstBank* filed a special warranty deed transferring title from FirstBank to “Rattan Public Schools” as of that date.

Whichever filing was the more correct filing, GLC’s or FirstBank’s, it would seem evident that the District received ownership of the property following the completion of the lease-purchase agreement.

Finding # 2

The district followed proper procedures in the sale of the 40 acres of land, referred to as Parcel B, with one exception.

At the time the district purchased the 311 acres of land across the street, it had no specific plans to use the *entire* acreage. A plan discussed by the school board was to sell a portion of the property and possibly develop a portion. Agenda items at the August 21, 2008, board meeting were to declare Parcel “B” as surplus, to hire Robert Lewis, Lewis Appraisal Service, to appraise the parcel, and proceed with selling the property by sealed bid.

On November 20, 2008, the board voted again to declare parcel B, which consisted of 40 acres, to be “surplus” and to be sold by sealed bid. The

Finding # 3

We reviewed the documentation on the sale of the timber from the property and found no irregularities in the procedures, but there was a second minor exception on the allocation of proceeds.

Also at its August 21, 2008 meeting, the board declared some timber on the “Messer property” as “surplus” and approved soliciting bids for the contract to harvest the surplus timber.

- | |
|---|
| <p>15. Rattan Board to act on declaring excess timber on Messer property as surplus and taking bids on the sale of selected timber.
Motion made by: Johnny Corgill to sell timber off former Messer property by sealed bid.
2nd by: Terry Gregg
All members present voted yes</p> |
|---|

We reviewed the documents on the bid and sale of the timber on the property. The minutes for September 18, 2008, report there were four bids for the timber. The contract was granted to the high bidder. We obtained source documents from the bank on the deposit of the funds. There was one deposit dated January 9, 2009, in the amount of \$1,974 and one deposit dated February 5, 2009, in the amount of \$2,267.

We contacted the logging company, and the owner confirmed there were only two cuttings and only those two payments were issued.

Again, accounting records indicated these payments were credited entirely to the building fund. Since the timber, as well as the land it grew on, was acquired with payments from both the general and building funds, the revenue from selling the timber should more appropriately have been proportionally allocated to the two funds.

Conclusion

Based on our review of the records and interviews done, there were no real estate commissions paid on either the 2005 purchase or the 2009 sale of the 40 acre parcel B. There was some confusion with the deeds for the original purchase, but that was corrected in 2009. All required procedures were followed and properly documented, with the exception of the allocation of proceeds from the sale of parcel B and the timber.

Recommendation

We recommend the District review the allocation of proceeds from the FY09 sale of parcel B and the timber sales with its legal advisor and/or its regular financial audit firm and make corrections, as necessary.

Objective III. Review possible irregularities with school property being furnished to a private citizen without fair market compensation to the District.

Background

One of the petition concerns was an allegation that the original 311 acres, and after the sale of parcel B, the remaining 271 acres of property had been utilized by a private citizen (the spouse of the former elementary school principal) without a contract and without compensation to the District for “pasturing” his cattle for six years. The former superintendent was alleged to have knowledge of this situation and to have allowed it.

Finding

The school board and administration allowed a private citizen to use 1.7 acres of school land without a formal contract or compensation, from the time the district purchased the property in April 2005 until mid-March 2011. The informal agreement was a continuation of an earlier agreement already in place with the prior owners when the school purchased the property.

We interviewed Bill Hedge, the citizen who was using the property. Hedge is also the husband of Cheryl Hedge, the former elementary school principal, now retired. Prior to the school purchasing the property in April 2005, Hedge had an agreement with the Messer family to use the approximate 1.7 acres which includes a small stock pen, a lot, and some outbuildings at no charge; in exchange, he would mow and maintain the area that fronted the highway. After the school purchased the property, the school continued to honor the previous agreement, but there was no formal written contract.

Interviews with both Hedge and the former superintendent indicated that Hedge was using the 1.7 acres under an informal (i.e. unwritten) agreement with the school that continued the previous arrangement that Hedge had with the Messer family. According to Hedge, he stored some hay for the ten bulls that were kept in the pen on the property. There was one occasion when he stored some hay for the FFA on the property. He also stored a hay baler there.

Hedge explained his use of the 1.7 acres was separate from his other cattle operations. He would purchase one-year-old bulls, keep them on the property for one year, then sell them, doing this each year that he used the land, and selling the last three bulls in March of 2011. He just used the

school property to keep the few young bulls separate from the rest of the herd. He had never kept more than ten head on the property at any one time.



We spoke with an official at the USDA office in Hugo and asked for a fair market rental on pasture land in the area. He told us “about \$40” per acre per year. Forty dollars per acre calculates to \$68 per year as the fair market value. Over the six years, the pasture rental value for the 1.7 acres (more or less) would be \$408, but this value did *not* include the improvements on the property, i.e. the storage building, carport and dilapidated small barn. It also does *not* include the exchange value of mowing/maintaining the frontage area which was part of the informal agreement.

We spoke with two of the current board members and asked if they had knowledge of the use without payment. Both agreed they were aware, but thought that because it was such a small amount, they didn’t think much of it. We interviewed two other board members who also were aware of the arrangement and expressed concerns about the situation. The fifth board member works out of town and was not interviewed. We reviewed two years of board meeting minutes (July 2009 through June 2011) and found no discussion of the informal agreement. The matter apparently was not brought up in an open meeting in recent years, although known to board members.

One of the board members indicated he had ridden over the entire 311 acres on horseback, prior to the school purchasing the property, with the idea of buying it himself. One of the reasons he decided against the purchase was that a portion of the property did not have a fence and the fence on the rest of the property was in poor condition.

One of our investigators was given a tour of the property by a school employee. Based on her observation, the property adjoins a county road on

the west boundary and a state highway on the south boundary and that approximately 25% or so is not fenced, making it unsuitable and unsafe for pasturing cattle. The photograph shown below was taken on the western boundary of the property, just north of a utility sub-station.



In addition to the four board members, we interviewed various persons, including a number of citizens, concerning the issue of cattle being pastured on the major area of the property. Of the non-board member interviews, two said they *had* seen cattle on the unfenced portion of the school's property. Seven other citizens interviewed, who were not connected with the District, and including one who lived across the road, reported they had *not* seen cattle on the unfenced portion of the property.

One interviewee reported an occasion of having seen Hedge's bulls when they had gotten "out of the pen," but then also reported seeing "horses and a brown cow" on other occasions. However, those animals were strays on the property from a different owner and were not Hedge's livestock. The "horses and a brown cow" observation was confirmed in an interview with another citizen. The stray animals on the property would also appear to confirm the inadequate fencing.

We interviewed Sheriff Duncan, who drives the local roads and highways and lives in the area. He indicated that Hedge kept a few young bulls in a small area, but other than that, there had not been any cattle on the property, and that the fencing was poor. He added that if there had been cattle on the entire property, his office (the Pushmataha Sheriff's Office) would have been getting calls by the "dozens," due to the poor condition of the fence.

However, *according to the sheriff*, the former superintendent is married to a relative of his, and the sheriff also had family members working for the school district. When asked, the sheriff could not provide any names for individuals that may be able to provide an objective opinion of the situation. He observed that it was a small town/rural school district, where everybody knows everybody, and that the community was divided, making it less likely that a local person could provide an objective opinion, without tilting towards either of the two sides.

It was also alleged that Hedge had not mowed as required by the informal agreement, but that one of the neighbors mowed it, which we confirmed. We interviewed that neighbor, and he and his wife both stated that they had made a deal with Hedge to mow the property for him in exchange for hay for their horse.

Conclusion

The District did allow the use of an approximately 1.7 acre area of school land without a written contract or agreement and without compensation, other than the value of keeping some frontage property (also owned by the District) mowed. We concluded that “fair market” compensation, less the value of the mowing service provided, was undetermined but likely negligible, even over a six-year period.

We also concluded that the larger allegation involving the entire property (311 acres and/or 271 acres) being used for pasture to the benefit of Hedge was improbable and unsubstantiated, due to the conflicting accounts of the various District employees and various non-school related local citizens that were interviewed.

We did note a separate occasion in the April 22, 2010, board minutes, of school property described only as “a lot on Hooker Road” being rented to an individual for \$100 per month for a “double-wide” mobile home. We observed that this agreement was brought to the Board for approval.

We also observed that the fact that there was a relationship between Hedge (whose wife is the former elementary school principal) and the District made it *all the more important to formalize the agreement* for the use of the school property and to obtain Board approval for such an agreement. Failure to do so was virtually certain, at some point, to present the “appearance of impropriety” and the potential for a charge of “favoritism” with regard to the personal use of the District’s property.

Recommendation If the District allows the use of any school property for non-District purposes, it should be in the form of a written contract, include reasonable provisions and/or restrictions on the use of the property, include provisions to protect the District from liability for any potential damages resulting from the lessee's use(s) or misuse(s) of the property and be approved by the Board in an open meeting.

Objective IV. Review possible irregularities with regard to the use of school employees and school equipment in the February 2011 school board election.

Background

There was an allegation that elementary school administrators and/or teachers were printing and distributing campaign material during the February 2011, school board election. The alleged campaign material was a copy of the special audit report prepared by the State Auditor and Inspector and issued in the year 2000 and a spreadsheet showing historical financial information of the District prepared by the former superintendent.

Finding

This allegation could not be substantiated due to the lack of corroboration.

We interviewed Dana House, the current elementary school principal, who was the second grade teacher at the time of the election. She had not seen any teachers or other staff members printing, making copies, or distributing campaign material.

We also spoke with Cheryl Hedge, the prior elementary school principal, who was alleged to have made copies and distributed them to teachers and staff members. She admitted to putting out copies of the prior audit report in the teachers' lounges, but stated that she had paid to have the copies made elsewhere; she did not use school equipment or supplies.

We spoke to Sherri Grimmett, the elementary school secretary, who has held this position for the past sixteen years. She indicated she had not made copies of the audit report or other election material during school hours or using any school equipment and had not seen anyone else on staff doing so.

We interviewed former Superintendent Lawless about the campaign material. He stated that he had prepared and printed a fifteen year historical financial summary (cash balances at June 30, total revenues, and total expenditures for each fiscal year) at his home, in his home office. We conducted the interview in his home and observed his home office that included a computer, printer, and copy machine.

Under **51 O.S. § 307** of the *Political Subdivision Ethics Act*, any complaint regarding an election issue would be filed with the local District Attorney. We checked with the District #17 District Attorney's office and found no formal complaint was filed regarding the Rattan School District election of 2011.

Conclusion

While we recognize the *potential* for misuse and abuse by public sector employees of public sector supplies and equipment in *any* election cycle, such allegations are difficult to confirm, absent corroborating information. Paper supplies and toner are generic in nature and untraceable, except perhaps by forensic analysis.

The alleged campaign materials were not overtly political in their content. The previous SAI special audit report published in 2000 is a "public record" document, not campaign literature. The fifteen year financial summary, which the former superintendent asserted that he had prepared in his home office, also was not overtly political campaign material, except by inference, and in the context of certain issues raised during the campaign. The document in question did not encourage or direct District staff to vote for a specific school board candidate.

We were unable to substantiate this allegation.

Recommendation

No recommendation is provided for this objective.

Objective V. Review possible irregularities with restricted funds and commingling of restricted funds with the general fund.

**General
Background**

According to a common website, the definition of “Fund accounting” is an accounting system emphasizing *accountability* rather than *profitability*. *Fund accounting* is used by non-profit organizations and governments. In this system, a *fund* is a self-balancing set of accounts, segregated for specific purposes in accordance with laws and regulations or special restrictions and limitations.

For example, most public entities will have a “general fund” that will have revenue accounts, appropriation accounts, encumbrance accounts, expenditure accounts, as well as asset and liability accounts, such as cash, investments, accounts payable, warrants payable, etc.

In the governmental sector, *it is important to distinguish* between a “fund,” such as a general fund, a building fund, a debt service or “sinking” fund, a special revenue fund, a capital project fund, a state or federal grant fund, etc., versus the monetary term “funds” when used to describe *money* being collected, transferred, deposited, saved or spent.

The District operates with two bank checking or “demand deposit” accounts, one for the general operations of the school system and a separate bank account for the “activities” fund. The operational bank account is labeled “General Fund,” but technically, that is a misnomer.

It is not the *general fund’s* account, using the accounting term “fund” to describe the bank account. It would be more accurate to call it a “general operations” *bank account*, which includes a variety of *statutory and grant funds* in the one bank account. A different more applicable title or label using “operations” or “operational” bank account would more accurately describe the function of the bank account, rather than the source(s) of funding (accounting definition) being deposited and expended from the bank account.

The “commingling” of money of a school district’s various funds is not unusual for public school districts that often utilize multiple sources of local, state and federal grant funding for various personnel, operational, capital and debt service expenditures. For example, a teacher’s salary may be funded in part with both “general fund” appropriations (cash) and a “federal grant fund” (cash).

Another example was described earlier in this report. The \$20,000 down payment for the land purchase was charged to the District's "general fund," but the lease-purchase payments were charged to the District's "building fund," although all the check/warrants were written on the same operational bank account.

Using a "general" or "operational" bank account requires an accounting system that will separately account for and track the balances of the statutory funds (general fund, building fund and sinking fund) and the variety of state aid, state grant funds, and federal grant funds. A "commingling" of funds does not necessarily occur just because money from two or more funds is combined in one bank account, provided that adequate records are maintained.

Finding #1

The District is not "commingling" funds in the negative or "improper" sense of the term.

When the accounting system is designed to "account" for the separate "funds," a public entity may utilize a single bank account and not have a "commingling" issue. The District operates in the same manner as a large percentage of Oklahoma school districts with regard to the design of its fund accounting system and banking procedures.

The following three issues were reviewed under the general objective of misuse of "restricted" funds.

Allegation #1: Special education funding was diverted to purchase equipment used in regular classrooms.

Background

Both federal and state governments provide funding to school districts for instructing students with disabilities. These funds are restricted for use for students with disabilities and may be spent on instruction, *equipment* and/or additional training for faculty members teaching special education, and other needs for the disabled student's education.

Depending on the type of disability and the severity, the school may also be required to supply a "Para-professional" to assist the student with their daily activities and classroom work, which the school employs on an as-needed basis.

One allegation state that “restricted” special education funds had been used to benefit regular classroom instruction, rather than to benefit special education students.

Finding #2

We found no basis for the allegation that equipment was being purchased with special education funds and being used in regular classrooms for non-disabled students.

We obtained the payroll audit report reflecting the total amounts paid to District employees for both base and extra duty contracts. The records indicated the District had three full time and one part-time special education teachers, as well as a Para-professional for the 2010-2011 school year.

We obtained school expenditure reports for the three fiscal years of FY09 through FY11. FY11 was selected, as those transactions were the most current records. We prepared a spreadsheet summarizing the District’s special education expenses. We compared these to the expenditure information submitted to OSDE. The warrants issued, plus encumbrances, agreed to the amounts reported per OSDE records.

EncumbranceSummary								
Instruction 1000	Instructional Staff Training 2213	Psychological Educaional Service 2140	State & Federal Relations Services 2330	SOIC OT, PT, & Speech Therapy 2152, 2135, 2152	Oklahoma Health Care 8900	DaVinci Network Services 2511	Encumbered Balance	Warrants to Date
\$ 39,044.34	\$ 238.44	\$ 415.60	\$ 216.74	\$ 10,118.36	\$ 3,736.91	\$ 809.90	\$ 3,000.00	
16256.35	103.33	6147.39	8277.07	5217.61				
3219.73	498.22	2138.58	7142.89	9988.64				
5360.36		1,700.00		17205.65				
21441.44				837.56				
86038.83								
83.12								
5475.73								
309.73								
\$ 177,229.63	\$ 839.99	\$ 10,401.57	\$ 15,636.70	\$ 43,367.82	\$ 3,736.91	\$ 809.90	\$ 3,000.00	\$ 252,022.52

Summary of District expenditure reports for FY11.

Line 1	Total Expenditures for Children with Disabilities.....	\$255,022.52
Line 2	Total State Aid for Current Operating Expenditures.....	\$3,167,278.30
Line 3	Total State Aid for Children with Disabilities.....	\$224,863.00
Line 4	Total Funds from Part B of the Individuals with Disabilities Education Improvement Act 2006.....	\$137,988.00
Line 5	Other sources of aid received for children with disabilities (Medicaid, etc.).....	\$28,031.85

Special education amounts reported for FY11, based on records from OSDE.

We reviewed purchasing procedures for requisitioning, approval of requisitions, ordering of supplies, receiving of supplies and purchases, payment of purchase orders, the allocation and posting of costs, and reporting to OSDE. We concluded there was an adequate segregation of duties in relation to the purchasing process for special education supplies.

We tested 100% of FY11 charges to special education expenditure accounts with no findings. Based on the above, it can be observed that the major portion of expenditures was for staffing and therapy services.

We interviewed the director of special education and one of the special education teachers, who indicated they had received all the necessary equipment they had requested/requisitioned, as well as some equipment they had not requested.

Based on our interviews, most of the District's special education students were "mainstreamed" into regular classrooms. Accordingly, some equipment items, such as iPads, were often taken from the special education classroom to the regular classroom *by the special education students themselves*. We visited the special education classroom and confirmed three laptop computers, two iPads, a smart board, and other items of equipment.

Conclusion We found no substantiation for the allegation of special education funds being misused or that special education funding had somehow been diverted to benefit regular classroom instruction.

Recommendation No recommendation is provided for this allegation.

Allegation #2: There were concerns and questions regarding payments to a bank variously referred to as "a bank in Utah" or "Zions Bank in Utah" or "Zions Bank in Dallas."

Background The District makes a payment annually to Zions First National Bank, Salt Lake City, Utah, in the amount of \$11,286. During fieldwork, this issue was brought up as a questionable transaction.

Finding #3

The questioned payment applies to a method of financing called a Qualified Zone Academy Bond or QZAB. The funds borrowed through this federally created program were used for roof repairs and other improvements for the District's Junior High Building, WPA Classroom Building and WPA P.E./Auditorium Building.

According to a commonly used website:

“Qualified Zone Academy Bonds (QZABs) are a U.S. debt instrument created by Section 226 of the Taxpayer Relief Act of 1997. QZABs allow certain qualified schools to borrow at nominal interest rates (as low as zero percent) for costs incurred in connection with the establishment of special programs in partnership with the private sector.”

The annual allotment each year has been \$400,000,000 allocated to the fifty states and U.S. territories. According to a “Frequently Asked Questions” website on QZABs, the federally subsidized funds can be used for “renovation and modernization” to an existing school structure, *but not for new construction.*

During the 2006-2007 school year, the District applied for participation in the state’s allocation of QZAB funding in order to make some repairs to the District’s buildings. The application for the QZAB program was processed through the Oklahoma State Department of Education. However, each school district must arrange for its own financing through the ordinary channels of financial advisors and bond attorneys usually involved in the issuance of “general obligation” school bond issues for new construction, renovation, or transportation equipment.

District staff maintain a separate binder clearly labeled “QZAB,” complete with the application which included the statement of assurances by the issuer of the bond, notification of allocation, legal documents, instructions for vendor payments, amortization schedule, account statement, fax on expenditure of funds, and invoices sent to the bank.

According to QZAB regulations, the District must use 95% of the bond funds for a “qualified” purpose, which is stated in the application, and the school must have a public-private partnership, which results in a minimum qualified contribution of 10% of the capital involved.

According to the District’s application, the “10% matching contribution” would be provided by First State Bank, Lazy J Welding, and Rattan Ag Boosters. The following is the qualified purpose as described in the District’s application:

The total costs of improvements to be made at the District's school sites are estimated to be \$100,000.00. The improvements include expenses associated with the renovation at the Junior High Building, WPA Classroom Building, and WPA P.E./Auditorium Building. Among the improvements anticipated to be undertaken at the various sites are: standing seam metal roofs, ceiling tiles, and miscellaneous equipment and personal property. QZAB obligations will be issued to pay the cost of those projects.

Since the QZAB program is nationwide, financial institutions (i.e. banks, insurance companies, and other financial corporations) can make offers or bids for QZAB funded projects, likely through some type of clearinghouse for the program.

Working through its financial advisor (Stephen H. McDonald & Associates) and an attorney firm (Burt, Brown, Kissinger, PLLC), the District obtained its QZAB project funding through Zions First National Bank, Salt Lake City, Utah. The QZAB funds were issued to the District in January 2008, but held in "escrow" by BancFirst, acting as the "trustee" bank. Invoices for school building repairs and renovations are sent to BancFirst for payment; much the same as would happen if the District had issued ordinary "general obligation bonds" to fund the repairs, etc.

The funding agreement with Zions First National Bank is another lease-purchase agreement for a term of ten years, with an annual payment beginning February 14, 2009 of \$11,285.65. A copy of the amortization schedule shows the future payments under the agreement:

Pmt. #	Pmt. Date	Principal Amount	Interest Amount	Total Payment	Remaining Principal	Prepayment Amount
					\$103,092.78	\$104,123.71
1	14-Feb-09	\$9,553.69	\$1,731.96	\$11,285.65	\$93,539.09	\$94,474.48
2	14-Feb-10	\$9,714.19	\$1,571.46	\$11,285.65	\$83,824.90	\$84,663.15
3	14-Feb-11	\$9,877.39	\$1,408.26	\$11,285.65	\$73,947.51	\$74,686.99
4	14-Feb-12	\$10,043.33	\$1,242.32	\$11,285.65	\$63,904.18	\$64,543.22
5	14-Feb-13	\$10,212.06	\$1,073.59	\$11,285.65	\$53,692.12	\$54,229.04
6	14-Feb-14	\$10,383.62	\$902.03	\$11,285.65	\$43,308.50	\$43,741.59
7	14-Feb-15	\$10,558.07	\$727.58	\$11,285.65	\$32,750.43	\$33,077.93
8	14-Feb-16	\$10,735.44	\$550.21	\$11,285.65	\$22,014.99	\$22,235.14
9	14-Feb-17	\$10,915.80	\$369.85	\$11,285.65	\$11,099.19	\$11,210.18
10	14-Feb-18	\$11,099.19	\$186.46	\$11,285.65	\$0.00	\$0.00
TOTALS		\$103,092.78	\$9,763.72	\$112,856.50		

At the time of fieldwork, the District had expended approximately \$58,100 for repairs and renovations as of February 2012. Under the terms of the QZAB program, the District has up to five years to complete its projects, but there is a provision for an extension. The first five-year period is ending early next year.

Conclusion The QZAB funds expended at the date of fieldwork were used to make repairs and renovations as stated in the application. We found no irregularities in either obtaining or expending QZAB funds.

Recommendation If the District has *not* completed its QZAB funded projects, it should do so before the five-year term has expired in early 2013, or determine its eligibility to file for an extension to complete its repairs and renovations.

Allegation #3: “Johnson-O’Malley” federal funds, passed through the Choctaw Nation of Oklahoma, were misused, resulting in eligible Native American students not receiving school supplies.

Background A third allegation of misuse concerned “Johnson-O’Malley” (JOM) federal funds given to the District by the Choctaw Nation of Oklahoma (Tribe). JOM funds are to be expended for the benefit and support of Native American students enrolled in the District.

Also according to a commonly used website:

The **Johnson-O’Malley Act** was an Act of the United States Congress passed on April 16, 1934, to subsidize education, medical attention, and other services provided by States or Territories to Native Americans living within their borders. The act came about as a federal aid program during the Indian New Deal of the 1930s to help offset costs of tax-exempt Indians making use of State-owned and funded schools, hospitals, and other services.

In order to qualify for the program a student must show proof of Indian descent by means of a Certificate of Degree of Indian Blood (CDIB) card. The CDIB card is issued by the Federal Bureau of Indian Affairs. All qualified Native American students enrolled in the District are eligible for the JOM funding, not just members of the Choctaw Nation.

A committee of citizen parents oversees the program in each public school district and must approve all requests for reimbursement from the Tribe. The committee consists of parents, not District personnel or school board members. School district committee members must be approved by the Tribe.

Each year, as a reminder to submit an application, the District receives a letter in early March from the Choctaw Nation JOM program. The letter states the number of eligible students and the dollar amount per student that will be funded. The District must then submit a proposal to the Choctaw Nation JOM program with a proposed budget attached. Below is an excerpt from the letter stating the allocation for the 2010-2011 school year.

A child count and a total allocation (based on \$65.00 per child) for your school has been determined and is as follows:

Count: 181 Allocation: \$11,765.00

Finding #4

We found no irregularities in the use of JOM funds or the distribution of the supplies to eligible students. We reviewed the budget of \$11,765 and itemized receipts in the amount of \$10,842.

We spoke at length with the program coordinator. Felicia Morse is an employee of the Rattan Public Schools and serves in the position of librarian and JOM Coordinator. Her salary is partially funded with JOM funds. Her responsibilities include purchasing the necessary school supplies and maintaining sufficient supplies on hand throughout the school year to provide each eligible Native American student with any needed supplies and making distributions as necessary. During our interview, we were shown a large container of glue, pencils, crayons, and other miscellaneous supplies for the students.

On the day of pre-enrollment, she issues each student a packet with the required supplies applicable to their grade level. Parents or legal guardians of the younger students are required to sign the pick-up sheet; the older students sign for themselves. When additional supplies are needed, the student simply makes a request for the necessary item(s), which are disbursed immediately. The student must sign the additional supplies form.

Besides common classroom supplies, the program pays a portion of the cost of eligible senior students' cap/gown expenses for graduation ceremonies, and membership dues to school organizations such as FFA or VICA. The program also pays for one college entrance exam per year. It does not cover the cost of *personal* items such as back packs, or "show" animals, as was once requested.

Each quarter, the school submits an expenditure reimbursement request, signed by the chairperson and secretary of the Indian Education Committee to the Tribe. The request is reviewed for qualifying expenditures and the Tribe issues a reimbursement check to the school.

Johnson O'Malley Program Expenditures 2010 -2011									
Date	Program Coordinator Salary Expense	Other Payroll Expenses	Supplies	FCCLA FFA VICA	Skills USA	Book Fair	Total	Paid by JOM	Variance
10/12/2010	\$ 851.66	200.82	\$ 604.89	\$ 420.00			\$ 2,077.37	\$ 2,077.37	\$ -
2/15/2011	\$ 1,277.49	\$ 301.80	\$ 255.20	\$ 363.00	\$ 144.00	\$ 476.49	\$ 2,817.98	\$ 2,801.68	\$ 16.30
3/22/2011	\$ 1,277.49	\$ 301.71	\$ 698.00				\$ 2,277.20	\$ 2,257.20	\$ 20.00
5/25/2011	\$ 1,703.36	\$ 385.67	\$1,624.07				\$ 3,713.10	\$ 3,705.26	\$ 7.84
							\$ -		\$ -
	\$ 5,110.00	\$ 1,190.00	\$3,182.16	\$ 783.00	\$ 144.00	\$ 476.49	\$ 10,885.65	\$ 10,841.51	\$ 44.14

The variance noted above was an amount for some book fair expenses that was disallowed by the Tribe.

Conclusion We found no irregularities with regard to the handling of JOM funds.

Recommendation No recommendation is provided for this allegation.

Objective VI. Review questions concerning the amounts of the District's investments and the financial institutions holding the District's investment balances.

Background Concerns were raised as to the financial stability of the District, whether the District did in fact have funds in excess of \$1.2 million dollars, and if there were any significant encumbrances on the funds.

Finding #1 We reviewed annual audit reports for the petition audit period. Cash and investment balances, after deducting the outstanding warrants and encumbrances, routinely exceeded \$1.7 million.

The following cash plus investment balances, *less outstanding warrants and encumbrances*, were reported in the District's annual audit reports:

FiscYr/Funds	General	Special Revenue	Debt Service	Trust & Agency	Total
FY09	\$1,071,995	\$703,162	\$6,563	\$67,493	\$1,849,213
FY10	874,650	799,793	12,281	67,794	1,754,518
FY11	1,192,226	903,659	29,656	86,935	2,212,476
3-Yr Averages	\$1,046,290	\$802,205	\$16,167	\$74,074	\$1,938,736

According to the audit reports, the District has no general obligation bonds outstanding. The FY11 footnotes to the regulatory basis financial statements reported lease-purchase agreements for the QZAB project and a Ford F250 pickup with outstanding balances totaling \$121,095 and an operating lease agreement for five school buses with an annual payment of \$61,250, due in April of each year. The operating lease for the buses terminates in April 2013.

Finding #2

We obtained bank statements and account confirmations from the two banks in which the District has its primary banking activity. For the nineteen month period of July 2010 through January 2012, the District had an average balance of \$955,500 per month in its operational or “general fund” checking account. The District’s certificates of deposit totaled \$961,782 at the time of fieldwork.

The District has one operating account in which all funds except the QZAB escrow fund and the “activities” fund are deposited. Tracking of the different fund amounts (i.e., general fund, building fund, sinking fund) is done through the District’s accounting system. The District has a separate checking account for the “activities fund” and there is still a balance in the QZAB escrow account at BancFirst.

We performed an analysis of beginning and ending balances, and deposits and withdrawals for the operational or “general fund” bank account for the nineteen month period of July 2010 through January 2012. The monthly average ending balance was approximately \$955,500. The fluctuations in the ending balance appeared more or less typical with the higher monthly ending balances occurring in the first half of the calendar year, largely due to the District’s property tax revenue for its general, building and sinking funds being collected in the December through April time frame.

On March 5, 2012, we obtained the District’s bank records for accounts held at FirstBank in Antlers, Oklahoma. We obtained the bank statements and the statements on three certificates of deposit. We also obtained bank records from AmeriState Bank of Antlers.

As of February 29, 2012, the District had \$1,492,400 in its general and activities bank accounts at FirstBank and another \$1,500 in an inactive bank account at Ameristate Bank. There were five certificates of deposit at the two banks, as follows:

Certificates of Deposit	
<i>Bank</i>	<i>As of March 5, 2012</i>
FirstBank	\$150,000
FirstBank	\$208,656
FirstBank	\$200,064
AmeriState Bank	\$134,893
AmeriState Bank	\$268,168
<i>Total C.D. balances:</i>	\$961,781

According to the school treasurer, the original purpose of the inactive bank account was to gain some additional interest revenue. For a time, Ameristate Bank had a promotional campaign to encourage the opening of new accounts. Ameristate offered more interest on certificates of deposit if a private or public customer also had a regular bank account.

Under **62 O.S. § 517.1, et al**, the “*Security for Local Deposits Act*,” the treasurers of local governments and public entities, including school districts, are required to obtain additional “collateral” for bank deposits that exceed the deposit insurance coverage provided by FDIC. We obtained the *pledged collateral* reports from the banks. These reports indicated the District was adequately secured for its excess bank deposits.

Conclusion

Both the District’s annual audit reports and the account balance confirmations from the two depository banks indicated that the District’s cash and investment balances were in excess of the \$1.2 million figure alleged to be questionable or inflated. We verified the District’s pledged collateral for deposits in excess of FDIC insurance was adequate.

Recommendation

No recommendation is provided for this objective.

DISCLAIMER

In this report there may be references to state statutes and legal authorities which appear to be potentially relevant to the issues reviewed by this Office. The State Auditor and Inspector has no jurisdiction, authority, purpose, or intent by the issuance of this report to determine the guilt, innocence, culpability, or liability, if any, of any person or entity for any act, omission, or transaction reviewed. Such determinations are within the exclusive jurisdiction of regulatory, law enforcement, and judicial authorities designated by law.



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