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## CHIRON CHARTER SCHOOL

### Public Report August 25, 2006

The Minneapolis Police Department received allegations from a Chiron Charter School (Chiron) Board member of a misappropriation of funds at Chiron. The State Auditor's Office was asked to review Chiron's financial records.<sup>1</sup>

The State Auditor's Office obtained and reviewed financial documents from Chiron and from entities Chiron had hired to assist Chiron with its financial management.<sup>2</sup> We obtained additional Chiron financial information from the Center for Training and Careers (CTC), an alternative school that attempted to take over management of Chiron in February 2005. We also reviewed information from financial institutions provided to us by law enforcement. Finally, we conducted interviews regarding some of the documentation we received.

Based upon our review, it appears that:

- Chiron's Managing Director falsely reported the number of students attending Chiron to the Minnesota Department of Education, resulting in over-payments to Chiron by the Minnesota Department of Education.
- The Managing Director falsely reported to the Minnesota Department of Education how federal grant funds were expended.
- The Managing Director paid herself \$7,150.00 more in Chiron funds than alleged "loans" she made to Chiron.
- The Managing Director paid herself \$4,352.88 in Chiron funds for unauthorized "payroll" checks.
- The Managing Director paid herself an additional \$7,312.05 in Chiron funds for questionable "payroll" checks.
- The Managing Director paid herself \$7,568.03 in Chiron funds as reimbursements for expenses for which we were unable to locate supporting documentation.
- The Managing Director paid Chiron's District Secretary, at least \$6,970.00 in Chiron funds for unauthorized "payroll" checks.
- The Managing Director paid the District Secretary an additional \$1,200.00 in Chiron funds for questionable "payroll" checks.

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<sup>1</sup> The State Auditor's Office has authority to review charter schools. *See* Minn. Stat. § 124D.10, subd. 8 (i)(2004).

<sup>2</sup> According to Chiron Board member Chiron employee 4, we were provided with all financial-type documents that were located at Chiron when it closed. We also obtained Chiron-related financial documents from Stenmark, Inc., Designs for Learning, and a consultant working with Designs for Learning.

- The Managing Director paid the District Secretary \$1,055.11 in Chiron funds as reimbursements for expenses for which we were unable to locate supporting documentation.
- The Managing Director paid other employees “stipends,” “payroll advances” and other checks for which we were unable to locate supporting documentation.
- The Managing Director did not provide the Chiron Board with accurate financial information.

We found that adequate accounting and internal control procedures were lacking at Chiron.

## **I. Chiron Charter School - Background**

Chiron was once a middle school in the Minneapolis Public School District. It was closed as a traditional public school after the 2002 school year, and re-opened in the fall of 2002 as a charter school serving grades 6 - 8, sponsored by the Minneapolis Public School.<sup>3</sup> The Minneapolis School Board decided not to renew its sponsorship of Chiron as of June 2004.<sup>4</sup> Pillsbury United Communities, a nonprofit organization, then became Chiron’s sponsor.<sup>5</sup>

On February 15, 2005, Center for Training and Careers (CTC), an alternative school, agreed to take over Chiron’s management and financial responsibilities. CTC deposited \$80,000 into Chiron’s account. Chiron’s bank took \$51,666.49 of the CTC funds to pay off Chiron’s loans from the bank; and on February 18, 2005, CTC withdrew \$28,000 from Chiron’s account. At a February 18, 2005 Chiron Board emergency meeting, the Board voted to close Chiron, effective February 25, 2005, because it was unable to meet its payroll obligations.<sup>6</sup>

Chiron had accounts at Wells Fargo Bank (WFB) and Community National Bank (CNB).<sup>7</sup> The Managing Director was added to the bank’s records as an authorized signer on Chiron’s checks in August 2002.<sup>8</sup> Only one signature was required on Chiron’s checks, and the Managing Director maintained Chiron’s checkbooks.

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<sup>3</sup> Chiron’s Articles of Incorporation are dated April 8, 2002.

<sup>4</sup> According to a letter to Chiron from the Minneapolis Public Schools dated April 7, 2004, the Minneapolis School Board voted not to renew Chiron’s sponsorship because it was no longer a “conversion” charter school, where experienced teachers continued at the school. According to the letter, “[c]ontinuity was prevented because the experienced teachers separated from the school.”

<sup>5</sup> See August 30, 2004 Letter from the Minnesota Department of Education (approving Pillsbury United Communities as Chiron’s sponsor).

<sup>6</sup> See February 18, 2005 Chiron Board meeting minutes.

<sup>7</sup> Chiron’s WFB account was opened in 2002. Chiron’s CNB account was opened on February 23, 2004.

<sup>8</sup> The Managing Director became the sole signatory on Chiron’s WFB bank account as of February 2004. The Managing Director was also the signatory on Chiron’s CNB account when it was opened in February 2004. The Managing Director began working at Chiron in 2002. In a staffing proposal adopted at the September 26, 2002 Chiron Board meeting, She is identified as Systems Director and Instructor. In Chiron’s Financial Report for the year ended June 30, 2003, she is identified as the Director of District Services. She became the Interim Managing Director at the November 4, 2003 Board meeting. At the December 16, 2003 Board meeting, the title was changed from Interim Managing Director to Managing Director.

Chiron had contracts with Stenmark, Inc., and Designs for Learning for various accounting services. In addition, Chiron was required to have an annual financial audit.<sup>9</sup> Malloy, Montague, Karnowski, Radosevich & Co. (MMKR) completed Financial Reports of Chiron for April 9, 2002 (date of inception) through June 30, 2002, and July 1, 2002 through June 30, 2003.<sup>10</sup> However, the Financial Reports for July 1, 2003 through June 30, 2004 were never completed because Chiron's financial records were not in order.

## II. Minnesota Department of Education Payments to Chiron

The Minnesota Department of Education paid Chiron over \$4 million between 2002 and 2005.<sup>11</sup> We compared payments made by the Minnesota Department of Education with deposits in Chiron's bank accounts. We found that all Minnesota Department of Education payments to Chiron were deposited in Chiron's bank accounts.<sup>12</sup>

Many of the Minnesota Department of Education payments are based upon the number of students attending Chiron (the Average Daily Membership or "ADM"). Each school reports the number of students attending the school to the Minnesota Department of Education. Falsely inflating the number of students attending a school inflates the amount of money paid to the school by the Minnesota Department of Education.

We obtained from the Minnesota Department of Education a copy of a report dated January 3, 2005 submitted by Chiron to the Minnesota Department of Education that claims Chiron had a total ADM of 132.<sup>13</sup> The report was completed and verified by The Managing Director.

It is our understanding that, after Chiron closed, the Minnesota Department of Education conducted a review of the ADM reported by Chiron. As a result, we did not separately review this issue. However, during our review of documents, we found the following:

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<sup>9</sup> Charter schools are required to submit an audit report to the Commissioner of Education by December 31 each year. See Minn. Stat. § 124D.10, subs. 6a and 8 (i).

<sup>10</sup> For the fiscal year ended June 30, 2002, the audit was not timely filed with the Minnesota Department of Education. See Chiron Financial Report from April 9, 2002 (date of inception) to June 30, 2002 (Finding 2002-3).

<sup>11</sup> State payments to Chiron were as follows:

2002	\$ 914,451.91
2003	\$1,751,630.21
2004	\$1,216,540.10
2005	<u>\$ 160,293.78</u> (through February 24, 2005)
Total:	\$4,042,916.00

<sup>12</sup> To conduct our review, we compared a list of Minnesota Department of Education payments to Chiron with deposits in Chiron's accounts.

<sup>13</sup> Notations on the report show that it was updated on January 5, 2005 to reflect a total ADM of 129. The report is a "second update" for payments to be made January 30 through April 15, 2005. In the initial estimate report dated June 15, 2004, the Managing Director estimated that the school would have an ADM of 115; in the first update dated September 30, 2004, the Managing Director reported an ADM of 117.

- According to the October 4, 2004 Managing Director's Report to the Chiron Board, Chiron's enrollment on the first day of school in fall 2004 was not the 120 students Chiron had anticipated.
- According to the December 8, 2004 Board meeting minutes, the Director reported to the Board that enrollment was holding steady at 80.
- Caravan Kids Catering confirmed in a fax dated December 3, 2004 that the new count of students at Chiron was 76.
- A former employee informed us that she was responsible for maintaining spreadsheets listing students attending Chiron. She provided us with a copy of the spreadsheets. They show approximately 75 students at Chiron as of December 2004. The former employee informed us that she would provide the spreadsheet to The Managing Director, upon request, once or twice a year.
- A consultant for Designs for Learning, informed us that she learned in February 2005 from the Minnesota Department of Education that Chiron had reported 129 students for the 2004-2005 school year, but she learned from Chiron Board members that the actual number of students at Chiron for the 2004-2005 school year was between 60 and 83 students.
- According to the February 18, 2005 Chiron Board emergency meeting minutes, Chiron's report to the State of 129 students included 75 students that either never came to Chiron or came only briefly to Chiron.
- CTC representatives stated that, in February 2005, Chiron told them that Chiron had about 125 students as of February 2005; but a visit to Chiron indicated to CTC that Chiron only had approximately 80 students.

Based upon the documents available to us, it appears that the Managing Director falsely reported to the Minnesota Department of Education the number of students attending Chiron, resulting in inflated payments to Chiron.<sup>14</sup>

### **III. Chiron's Use of Federal Funds**

As a new charter school, Chiron was eligible for, and received, grant funds under the federal Public Charter Schools Program. Prior to opening, and in the fall of 2002, Chiron received \$140,000 as a planning or start-up grant.<sup>15</sup> Chiron then received two implementation grants, the first for \$150,000 (known as Subgrant 2), and the second for \$150,000 (known as Subgrant 3).<sup>16</sup>

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<sup>14</sup> According to a Chiron School Review dated December 7, 2003 by a consultant to the Minneapolis Public Schools, the Minnesota Department of Education had been paying Chiron at a higher level than justified by the student estimates due to "an ADM reporting error", and would be lowering its payment amounts, but no penalty or revenue recapture would occur at that time.

<sup>15</sup> Payments to Chiron were approved by the Minnesota Department of Education on May 2, 2002 (\$80,000), October 7, 2002 (\$10,000), October 28, 2002 (\$10,000), and December 9, 2002 (\$40,000).

<sup>16</sup> Payments to Chiron for Subgrant 2 were approved on January 24, 2003 (\$60,000), March 27, 2003 (\$60,000), and June 30, 2003 (\$30,000). Payments to Chiron for Subgrant 3 were approved on October 22, 2003 (\$50,000), January 28, 2004 (\$50,000), July 13, 2004 (\$10,000), September 9, 2004 (\$10,000), and September 27, 2004 (\$30,000).

The Managing Director was Chiron's contact person on these grants. The Managing Director submitted reports to the Minnesota Department of Education explaining how the grant funds were used. We found that the Managing Director submitted false reports to the Minnesota Department of Education regarding the use of these federal grant funds.

Specifically, we reviewed Chiron's final report for Subgrant 3, dated August 17, 2004, submitted by the Managing Director to the Minnesota Department of Education.<sup>17</sup> Subgrant 3 was effective October 29, 2003, and ended October 28, 2004. All funds received under Subgrant 3 had to be expended or encumbered between those dates.<sup>18</sup> Based upon this final report, the final \$30,000 of Subgrant 3 funds were released to Chiron.

Chiron's final Subgrant 3 report contained a narrative description and a four-page spreadsheet allegedly describing, in detail, how Chiron used the \$150,000 in Subgrant 3 funds. The spreadsheet listed individual check numbers allegedly reflecting expenditures of the grant funds. The detail contained in the report prompted the Minnesota Department of Education to thank the Managing Director for her "thorough, comprehensive and honest summary" of Chiron's third and final grant under this program.<sup>19</sup> In a clarification email dated September 1, 2004, the Managing Director reassured the Minnesota Department of Education that "[e]veryone has been paid under this grant agreement."

We found that Chiron misrepresented to the Minnesota Department of Education how Subgrant 3 funds were used.<sup>20</sup> In addition, we found that federal funds were used for unallowable costs under the federal grant, such as day-to-day operations, ongoing expenditures not directly related to initial start-up costs, student instruction, student field trips, and gift certificates.<sup>21</sup>

Specifically, \$91,100 in Subgrant 3 funds were allegedly expended for materials, supplies and equipment.<sup>22</sup> In the narrative description of the report, the main category of these purchases (\$48,850) was described as the purchase of "curriculum and instructional materials" "in all the core academic areas as well as art." Funds were also allegedly spent on the acquisition of computers and the purchase of a new computer server and related software (\$40,000). Finally, the purchase of "non-instructional supplies" allegedly included the purchase of paper, report cards, school forms, and other general office supplies (\$2,250).

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<sup>17</sup> See Public Charter Schools Program Progress Report (final): Subgrant 3.

<sup>18</sup> Expenditures could not be charged to the grant before the grant's official start date. All grant funds had to be fully expended no later than 90 days after the end date on the grant agreement, or the date of close-out, whichever occurs first.

<sup>19</sup> See August 19, 2004 email from the Minnesota Department of Education.

<sup>20</sup> Although not discussed in detail in this report, we found that reports submitted for the planning grant and Subgrant 2 also appear to contain misrepresentations.

<sup>21</sup> See, e.g., Minnesota Department of Education's Federal Public Charter Schools Program (PCSP) General Overview (August 7, 2003) and Federal Charter Schools Program (CSP) General Overview FY 2004 (updated December 2003) (allowable activities; allowable costs determined by approved budget; listing examples of unallowable costs). Further guidance on unallowable costs for federal grant awards are found in the Office of Management and Budget Circulars A-87 (Cost Principles for State, Local and Indian Tribal Governments), and A-122 (Cost Principles for Non-Profit Organizations). See also No Child Left Behind Act of 2001 (PL 107-110), Title V, Part B; available on the U.S. Department of Education's website, [www.ed.gov](http://www.ed.gov).

<sup>22</sup> These expenditures comprised "Project 5" of the grant.

However, for the \$48,850 allegedly spent on instructional materials and curriculum, we found expenditures for such items as health insurance, food, and carpet cleaning services. For example, we found:

- Payment of \$7,000 to “Delta Science” was reportedly made for “instructional materials/curriculum.” However, the Chiron WFB check for \$7,000, was actually made payable to “CKC.” CKC stands for “Caravan Kids Catering” and was one of Chiron’s food service vendors.
- Payment of \$6,003.04 to “Scholastic” was reportedly made for “instructional materials/curriculum.” However, the Chiron CNB check for \$6,083.84 was actually made payable to Health Partners for group health insurance.<sup>23</sup>
- Payment of \$4,992.25 to “CMP Math” was reportedly made for “instructional materials/curriculum.” However, the Chiron WFB check for \$4,992.25 was made payable to Health Partners for group health insurance.<sup>24</sup>
- Payment of \$4,200 to “Accelerated Reader” was reportedly made for “instructional materials/curriculum.” However, the Chiron CNB check for \$4,200, was actually made payable to Chiron Charter School, and appears to have been deposited in Chiron’s WFB account.<sup>25</sup>
- Payment of \$2,536 to “Read Naturally” was reportedly made for “instructional materials/curriculum.” However, the Chiron CNB check was never issued; it was originally written to Chiron employee 1 for \$1,200, but the check was crossed out and remains in Chiron’s checkbook.<sup>26</sup>
- Payment of \$2,277.17 to “CPS” with a Chiron check was reportedly made for “instructional materials/curriculum.” However, the Chiron WFB check for \$2,277.17, was actually made payable to “Just Call Mike.” From invoices that we found in Chiron’s documents, it appears that Chiron has purchased a variety of supplies from Just Call Mike.
- Payment of \$1,831 to “CPS” was reportedly made for “instructional materials/curriculum.” However, the Chiron a WFB check for \$1,831.93, was actually made payable to “Just Call Mike.”
- Payment of \$1,868.08 to “Math Press” was reportedly made for “instructional materials/curriculum.” However, the Chiron CNB check for \$218 was actually made payable to Chiron employee 1.<sup>27</sup>
- Payment of \$946.12 to “Target” with a Chiron was reportedly made for “instructional materials/curriculum.” However, the Chiron CNB check was actually for \$1,200, made

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<sup>23</sup> We found only one Chiron check to Scholastic during Subgrant 3’s time frame: Chiron WFB check for \$218.23.

<sup>24</sup> We did not find any Chiron checks to CMP Math during Subgrant 3’s time frame.

<sup>25</sup> It appears that the deposit in Chiron’s WFB account was needed to cover Stenmark and Minnesota Child Support payments, and a \$70 check to the Managing Director. In addition, two Chiron WFB checks to the City of Minneapolis were returned as “nsf” after the \$4,200 deposit was made in Chiron’s WFB account. We did not find any Chiron checks to Accelerated Reader during Subgrant 3’s time frame.

<sup>26</sup> We did not find any Chiron checks to Read Naturally during Subgrant 3’s time frame.

<sup>27</sup> We found only one Chiron check to “Math Teacher’s Press” during Subgrant 3’s time frame: A Chiron WFB check for \$35.75. We did not find any Chiron checks to “Math Press” during Subgrant 3’s time frame.

payable to Chiron employee 1, with a notation of “recruitment” in the memo section of the check.

- Payment of \$170 to “Lancaster” with a Chiron check was reportedly made for “instructional materials/curriculum.” The same Chiron check was also reported later in the report as a \$170 payment to “Office Depot” for non-instructional supplies. However, the Chiron WFB check was actually for \$170 made payable to “Lancaster Dry Carpet Cleaning” for carpet cleaning services.
- Payment of \$175 to Chiron employee 2 with a Chiron check was reportedly made for “L.A. & Math (Reimburs)” as part of the “instructional materials/curriculum” expenditures.<sup>28</sup> However, the Chiron WFB check was made payable to a Chiron employee, and the memo section of the check contains the notation: “2 period teaching 2 10 days.”
- Payment of \$258.30 to Chiron employee 3 with a Chiron check was reportedly made for “Science (Reimburse)” as part of the “instructional materials/curriculum” expenditures. However, we found an undated Request for Check from Chiron employee 3, for a total of \$258.30. The expenditures included \$82.77 for bookcases and crates, \$34.61 for 65 notebooks, and \$48.36 for files from Office Max.
- Payment of \$258.65 to the Managing Director with a Chiron check was reportedly made for “instructional materials/curriculum.” However, we found receipts that appear to support the reimbursement paid with the Chiron WFB check and they included such items as gift cards, ice, drinks, tablecloths, and candy.<sup>29</sup> A notation on the check register stub states that the check was for Chiron’s “Spring Fling.”
- Payment of \$132.86 to Chiron employee 4 with a Chiron check was reportedly made for “Lab (Reimbursement)” as part of the “instructional materials/curriculum” expenditures. We found a Request for a Check from Chiron employee 4, for a total of \$132.86. The expenditures were described as “decorations for talent show” and “gift certificates,” and the attached receipts included \$99.96 for six Target gift cards.
- Payment of \$22.40 to Chiron employee 5 with a Chiron check was reportedly made for “instructional materials/curriculum.” However, we found two handwritten requests for reimbursement from Chiron employee 5 totaling \$22.40. The attached receipts reflect reimbursement for parking and postage expenses related to special education work performed by Chiron employee 5.
- Payment of \$106.60 to the Managing Director with a Chiron check was reportedly made for “instructional materials/curriculum.” However, the Chiron WFB check for \$106.60 was issued to the Managing Director with a notation on the memo section of the check: “Sam’s Club.”<sup>30</sup>
- Payment of \$659.79 to the Managing Director with a Chiron check was reportedly made for “instructional materials/curriculum.” However, it appears that the Chiron WFB check was voided, and another Chiron WFB check was issued to the Managing Director

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<sup>28</sup> “L.A.” appears to be an abbreviation for language arts.

<sup>29</sup> The specific purchases are listed on Attachment E.

<sup>30</sup> We found no supporting documentation for the reimbursement.

instead. According to a notation on the memo section of the check, the reimbursement was for “food and field trips.”<sup>31</sup>

- Payment of \$49.97 to Chiron Employee 4 with a Chiron check reportedly made for “Lab (Reimbursement)” as part of the “instructional materials/curriculum” expenditures. However, we found two Requests for Check forms from Chiron employee 4 totaling \$49.97, that included reimbursement for \$28 paid for lost books from the Minneapolis Public Library.
- Payment of \$31.50 to Chiron employee 2 with a Chiron check was reportedly made for “L.A. & Math (Reimburs)” as part of the “instructional materials/curriculum” expenditures. However, we found a Request for Check from Chiron employee 2 for \$31.50. The attached receipts were for five \$5 gift cards at Target, and 13 notebooks.
- Payment of \$784.33 to “CPS” with a Chiron check was reportedly made for “instructional material/curriculum” expenditures. According to the invoices from CPS Co-op supporting this expenditure, the items purchased were office supplies such as paper, a 3-hole punch, trash bags, highlighters, tissue, and towels.<sup>32</sup>
- Payment of \$29.99 to the District Secretary with a Chiron check was reportedly made for “L.A. (Reimbursement)” as part of the “instructional materials/curriculum” expenditures. However, we found a Request for Check from the District Secretary for \$29.99, describing the item purchased as “phone”.
- Payment of \$57.65 to Chiron employee 4 with a Chiron check was reportedly made for “Lab (Reimbursement)” as part of the “instructional materials/curriculum” expenditures. However, we found a Request for Check from Chiron employee 4 for \$57.65, seeking payment for three hours worked at the School Fair (\$45), and reimbursement for balloons purchased for the School Fair (\$12.65).

Subgrant 3’s detailed spreadsheet submitted by the Managing Director reported how \$2,250 was allegedly spent for “non-instructional supplies.” According to the narrative, “non-instructional supplies” included the purchase of paper, report cards, school forms, and other general office supplies. However, we found:

- Payment of \$450.10 to “Office Depot” with a Chiron check was reportedly made for “non-instructional supplies.” However, the Chiron WFB check was actually for \$450.10, made payable to “All Metro Glass” for replacing a broken door light.
- Payment of \$170 to “Office Depot” with a Chiron check was reportedly made for “non-instructional supplies.” However, as discussed previously in this report, the Chiron WFB check was actually for \$170 made payable to “Lancaster Dry Carpet Cleaning” for carpet cleaning services.
- Payment of \$500 to “Just Call Mike” with a Chiron check was reportedly made for “non-instructional supplies.” However, a Chiron WFB check does not appear to have cleared Chiron’s WFB account. The duplicate copy of the check found in the check book register shows that the Chiron WFB check was made payable to a painting supplies and service

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<sup>31</sup> We found no supporting documentation for the reimbursement.

<sup>32</sup> As discussed next in this report, Chiron reported \$2,250 in Subgrant 3 expenditures on “non-instructional supplies.”



provider for \$500. The check register stub for a Chiron WFB check has a notation of “painting supplies.”<sup>33</sup>

- Payment of \$180 to “Office Max” with a Chiron check was reportedly made for “non-instructional supplies.” However, the Chiron WFB was actually for \$180, made payable to “Qwest.”
- Payment of \$70 to “Armor” with a Chiron check, dated May 6, 2004, was reportedly made for “non-instructional supplies.” However, the Chiron WFB check was actually for \$70, made payable to a person we understand is the spouse of a Chiron employee. Notations in the memo section of the check and on the check register stub state “Locks.”<sup>34</sup>
- Payment of \$708.87 to “Brite Lite” with a Chiron check was reportedly made for “non-instructional supplies.” However, the Chiron WFB check was actually for \$732.40, made payable to Brite Lite, an electrical contractor, for electrical work completed in Chiron’s cafeteria.<sup>35</sup>

Subgrant 3’s final report states that \$9,000 of Subgrant 3 funds were spent on the evaluation and modification of Chiron’s curriculum. According to the narrative report, the main use of these funds was the modification of the curriculum “to make it suitable for low-level readers and non-readers.” Four core-curriculum teachers allegedly met weekly during the summer of 2004 with the Managing Director and a representative of the Minnesota Association of Charter Schools (MACS) to evaluate and modify Chiron’s curriculum for reading and math.<sup>36</sup> According to the narrative report, the four teachers and the Managing Director also conducted planning regarding discipline problems and staff development. However, we found that:

- Payments to five staff members for “Evaluation/Modification of Curriculum” were reportedly made with Chiron checks for a total of \$5,100. However, the Chiron WFB checks were never issued.
- Payment to Chiron employee 6 for “Evaluation/Modification of Curriculum” was reportedly made with a Chiron check for \$1,700. However, the Chiron WFB check does not appear to have cleared Chiron’s account. Furthermore, “Crowne Theater” was written in pen on the duplicate check contained in Chiron’s WFB checkbook was written on the check register stub.<sup>37</sup>

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<sup>33</sup> We found that this person was paid a total of \$3,021.88 for painting supplies and services in three checks.

<sup>34</sup> We located an undated invoice in the Chiron documents that reflected a charge of \$70 from this person for one lock and for lock installation. In the Chiron documents, we also found 2003 invoices from Armor Security, Inc., for work related to keys and doors.

<sup>35</sup> The Brite Lite invoice is dated February 12, 2004.

<sup>36</sup> We located a summary of a Chiron Student Discipline Workshop printed on MACS stationary with the MACS representative’s name on it, dated March 25, 2004. We understand that the MACS representative left MACS in approximately July 2004. We found two Chiron payments to him for work that appears to have been performed after Subgrant 3 funding had ended: Chiron CNB checks for work performed in November and December 2004 (and for one day, date unknown), as itemized in a December 9, 2004 invoice; and another Chiron CNB check for \$1,000 for work performed in January 2005, as itemized in a January 25, 2005 invoice. We found no other Chiron payments to the MACS representative.

<sup>37</sup> Chiron’s WFB checking account was closed on October 26, 2004. Although Chiron’s checkbook provides “duplicate originals,” any original writing on a Chiron WFB check duplicate is not legible.

- Payment of \$1,100 to Chiron employee 3 with a Chiron check was reportedly made for “Evaluation/Modification of Curriculum.” However, the Chiron CNB check was actually for \$1,182.20, and appears to reflect Chiron employee 3’s regular paycheck.
- Payment of \$1,100 to Chiron employee 7 with a Chiron check was reportedly made for “Evaluation/Modification of Curriculum.” The Chiron CNB check was actually payment to Chiron employee 7 of \$1,000 for “40 Hrs @ \$25 – Summer Stipen” (*sic*).

While reviewing Chiron’s documents, we found that some Chiron employees were paid for curriculum development that may have qualified as Subgrant 3 expenditures for the evaluation and modification of curriculum. However, these payments were not reported on Subgrant 3’s final report. For example, Chiron employee 3, Chiron employee 6, and Chiron employee 8 received payments that were identified with a notation “fed grant school/program planning.” Those checks, dated September 30, 2004, totaled \$2,500. The checks were dated after the August 17, 2004 final report was submitted to the Minnesota Department of Education, and after the final Subgrant 3 funds were approved for payment on September 27, 2004.<sup>38</sup> In addition, we found that Chiron employee 6 received a check dated August 27, 2004 for \$3,975 with a notation of “159 hours” in the memo section of the check. We found handwritten notes regarding the 159 hours, and some of the work appears to have been related to curriculum.<sup>39</sup> Similarly, Chiron employee 2 was paid \$1,312.50 for 52.5 hours of unspecified work in a check dated July 30, 2004.<sup>40</sup> Those payments were not included on the Subgrant 3 final report.<sup>41</sup>

Subgrant 3’s final report states that \$10,000 was used for printing costs, mailings, and advertising in various media, as part of Chiron’s efforts at marketing and recruiting. We found:

- Payment of \$2,646.42 to the Star Tribune was reportedly made with a Chiron check. We found the invoice that appears to be related to that payment. The billing date of the invoice is September 30, 2003, for ads that appear to have run in September 2003, prior to the October 29, 2003 start date of Subgrant 3. The invoice also included a balance forward amount of \$150.10.<sup>42</sup>
- Payment of \$682 to “Dunwoody” was reportedly made with a Chiron check. We found the invoice related to that payment. The billing was for behavior notice forms and behavior reporting forms.

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<sup>38</sup> See Minnesota Department of Education Grant Agreement Payment Request dated September 27, 2004 (final \$30,000 approved).

<sup>39</sup> The handwritten notes regarding Chiron employee 6’s hours for June through August 13, 2004 do not specify how many hours were spent on each type of work performed by Chiron employee 6 over the summer.

<sup>40</sup> The check includes payment for 52.5 hours at \$25 per hour, plus reimbursement of \$55.66 for supplies, according to a notation in the memo section of the check. (52.5 hours X \$25/hr = \$1,312.50; \$1,312.50 + \$55.66 = \$1,368.16) We located a listing of 47.5 hours of work that Chiron employee 2 performed in July 2004, but the listing does not identify how Chiron employee 2 spent her time.

<sup>41</sup> We found that other employees were paid for time allegedly spent “recruiting” during the summer of 2004. The Subgrant 3 report has a separate section for the reporting of recruitment hours. Those payments are discussed later in this report.

<sup>42</sup> We also located an invoice for \$150.10. The balance on that invoice was included on the September 30, 2003 invoice, for a total of \$2,496.32. The amount paid in Chiron WFB check (\$2,646.42) appears to have paid the \$150.10 billing twice. (\$2,496.32 + \$150.10 = \$2,646.42)

The final report for Subgrant 3 states that payment of \$2,500 was made to the Minnesota Association of Charter Schools (MACS), for MACS membership, with a Chiron check. However, we found that the Chiron WFB check was actually for \$900, made payable to a person who did cleaning for Chiron. We found only one Chiron check payable to MACS during Subgrant 3's effective dates, a check for \$25, which MACS informed us was payment for Board training.<sup>43</sup> MACS confirmed that Chiron did not pay the MACS membership fee for either 2003-2004 or 2004-2005.

We also reviewed how much the Managing Director claimed that MACS was paid under all three of Chiron's federal grants (the planning grant, Subgrant 2, and Subgrant 3). Under the planning grant, the Managing Director claimed that MACS was paid \$4,000; under Subgrant 2, the Managing Director claimed that MACS was paid \$5,000.<sup>44</sup> Therefore, under the planning grant, Subgrant 2 and Subgrant 3, the Managing Director claimed that MACS was paid a total of \$11,500. MACS informed us that Chiron paid MACS only a total of \$5,125.<sup>45</sup> Therefore, under the three federal grants, it appears that the Managing Director over-reported payments to MACS by \$6,375.

The final report for Subgrant 3 states that Designs for Learning was paid a total of \$15,000: \$10,000 for work on an accountability system to produce an annual report for 2003 – 2004 that addressed Chiron's improvement plan goals; and \$5,000 for grant administration related to Subgrant 3. The payments were reportedly made in a Chiron check. A Chiron WFB check was made out for \$17,750 to Designs for Learning, but that check does not appear to have cleared Chiron's accounts. Instead, Designs for Learning was paid \$750 in a WFB check and \$17,000 in a Chiron CNB check. From Designs for Learning, we obtained copies of invoices for Chiron and Chiron's payment history. They show that the two checks Chiron wrote to Designs for Learning during the Subgrant 3 time period were payments for work performed in August 2003 (\$750), and for work performed under Subgrant 2 (\$17,000).<sup>46</sup> Designs for Learning invoices under Subgrant 3 remained unpaid.<sup>47</sup>

We also reviewed how much the Managing Director claimed Designs for Learning was paid under all three of Chiron's federal grants. Under the planning grant, the Managing Director claimed that Designs for Learning was paid \$15,000; under Subgrant 2, the Managing Director

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<sup>43</sup> See Chiron WFB check # 1553. MACS confirmed that the \$25 payment was the only payment MACS received during Subgrant 3's effective dates.

<sup>44</sup> The report for the planning grant did not reference specific checks. However, the Managing Director reported in the final expenditure report for Subgrant 2 that MACS was paid \$5,000 for MACS membership in a Chiron check. However, the Chiron WFB check was actually for \$750, made payable to the District Secretary.

<sup>45</sup> MACS also provided us with copies of unpaid Chiron invoices totaling \$10,756.72.

<sup>46</sup> See Designs for Learning invoices dated June 30, 2003 and December 15, 2003, each for \$8,875 (each for 50% progress billing on Subgrant 2 work). The documents also show that Designs for Learning wrote off \$750 from the invoices as a bad debt. ( $\$8,875 + \$8,875 = \$17,750$ ; Chiron paid \$17,000, a difference of \$750)

<sup>47</sup> A Designs for Learning invoice dated May 10, 2004 covered 50% progress billing for Chiron's annual reports for 2003 and 2004, and for financial administration of Subgrant 3. That invoice remained unpaid.

claimed that Designs for Learning was paid \$15,000.<sup>48</sup> Therefore, under the planning grant, Subgrant 2 and Subgrant 3, the Managing Director claimed that Designs for Learning was paid a total of \$45,000. Designs for Learning's records show that, in total, Chiron only paid \$32,750 to Designs for Learning.<sup>49</sup> Therefore, under the three federal grants, it appears that the Managing Director over-reported payments to Designs for Learning by \$12,250.

Subgrant 3's final report states that \$6,000 was spent on "Equipment (Technology)." Specifically, CDWG was reportedly paid \$6,000 for technology equipment in Chiron check # 4045 dated June 4, 2004. The Chiron CNB check was actually payable to the District Secretary for \$1,008.05. However, Chiron did pay \$5,480.11 to CDWG in a different Chiron CNB check after the August 17, 2004 final report was submitted for approval to the Minnesota Department of Education.<sup>50</sup>

It also appears that an amendment to Subgrant 3 was not properly signed. Subgrant 3 was originally for \$125,000, but was later increased to \$150,000. As a result, an amendment to the original grant agreement was required. The amendment appears to have been signed on June 23, 2004, by Chiron employee 3, who was also a Chiron Board member and the District Secretary. Both Chiron employee 3 and the District Secretary's title on the amendment agreement is stated as "Board." According to the meeting minutes, the District Secretary was never a Board member, and we know of no authority for the District Secretary to sign the amendment to the grant agreement on behalf of the Board.<sup>51</sup>

#### **IV. Chiron Payments to The Managing Director**

We reviewed original cancelled checks, or copies of cancelled checks, written on Chiron's WFB and CNB checking accounts.<sup>52</sup> The checks were signed by The Managing Director. We found the Managing Director was paid a total of \$177,195.52 during the time period January 1, 2003 through February 25, 2005. These checks were allegedly for one of three purposes: loan repayments, payroll, or the reimbursement of expenses.

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<sup>48</sup> The report for the planning grant did not reference specific checks. However, the Managing Director reported in the final expenditure report for Subgrant 2 that Designs for Learning was paid \$5,000 for grant administration in a Chiron check. We found that the Chiron WFB check was actually for \$200, and made payable to Chiron employee 4. The Managing Director reported in the final expenditure report for Subgrant 2 that Designs for Learning was also paid \$10,000 for an accountability system in a Chiron check. However, the Chiron WFB check cleared Chiron's account two times – according to Stenmark's records, the check cleared once as a \$254.50 payment to the City of Minneapolis, and once as a \$489.24 payment to Citicapital Commercial. We did not locate the duplicate original of the check(s), and the check register stub for the Chiron WFB check is blank.

<sup>49</sup> Designs for Learning also informed us that unpaid Chiron invoices total \$40,330.

<sup>50</sup> We found no supporting invoice for the expenditure, although we located a charge of \$13.65 for next day delivery service on August 27, 2004 for a mailing to CDW Government.

<sup>51</sup> The Minnesota Department of Education sent an email to the Managing Director confirming that two signatures were needed on the amendment, and explaining that "usually it's the board chair and treasurer or another board officer."

<sup>52</sup> The documents were obtained from Stenmark, Designs for Learning, CTC and Chiron.

Based upon our review, it appears that 1) the Managing Director paid herself \$7,150 more in Chiron funds than any “loans” she may have made to Chiron; 2) the Managing Director paid herself \$4,352.88 in Chiron funds for unauthorized “payroll” checks; 3) the Managing Director paid herself an additional \$7,312.05 in questionable “payroll” checks; and 4) the Managing Director paid herself \$7,568.03 in reimbursements for which no supporting documentation was found.

#### **A. The Managing Director’s Alleged “Loan” to Chiron**

During the time period January 1, 2003 through February 25, 2005, the Managing Director received checks from Chiron allegedly for payroll and for the reimbursement of expenses. In addition to these checks, the Managing Director received an additional \$48,450 from Chiron. Several of these additional checks contained a notation from the Managing Director indicating that the checks were repaying the Managing Director for a loan that the Managing Director allegedly made to Chiron.<sup>53</sup> Based upon our review, it appears that some of The Managing Director’s representations about loan repayments were false, and resulted in payments to which the Managing Director was not entitled.

According to Stenmark, Designs for Learning and Center for Training Careers (CTC) representatives, the Managing Director informed them that she wrote herself checks from the Chiron accounts to repay loans that she had made to the school. A Designs for Learning representative said that the Managing Director told her that the Managing Director had loaned Chiron \$23,000.00 during the 2003-04 school year. The CTC representative said that the Managing Director told him the Managing Director had loaned Chiron \$22,000, and she made a check out to herself when she needed it.

We reviewed deposits into Chiron’s accounts from the time period January 1, 2003 through February 28, 2005.<sup>54</sup> Based upon the information available to us, it appears that the Managing Director deposited \$41,300.00 from her personal accounts into Chiron’s accounts. The results of our review are reflected in Attachments A and B.

We then compared the \$41,300.00 in deposits that the Managing Director appears to have made into Chiron’s accounts with payments Chiron made to Ms. Laxton. It appears that the Managing Director repaid herself at least \$48,450.00 from the Chiron accounts. Based upon our review, it appears that some of The Managing Director’s “loan repayment” claims were false, and resulted

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<sup>53</sup> For example, a notation on one of the Chiron checks the Managing Director wrote to herself states: “loan repayment \$12,000 of \$23,000”. Another check had a notation of “500.00 repayment of 5000.00, 4500 remain” on the stub in the check register; however, Stenmark was later informed that the check was for “reimbursement for non-classroom supplies”.

<sup>54</sup> We reviewed deposit information for Chiron’s CNB account from the date the account was opened (February 23, 2004) through February 28, 2005. We reviewed WFB statements from January 1, 2003 through October 26, 2004, the date the account was closed. We received some, but not all, deposit detail from Chiron’s WFB account. Complete deposit detail for Chiron’s WFB account should allow us to verify whether the deposits into the account were actually from the Managing Director or from another source.

in payments to the Managing Director of at least \$7,150.00 to which she was not entitled. The results of our review are reflected in Attachment C.

One of the “loan repayment” checks to the Managing Director was written on a Chiron check taken out of sequence, from the end of the checkbook. The check was a CNB check for \$1,000.00. The CTC representative said that he questioned the Managing Director about why the check was written out of sequence, and from the back of the checkbook; the Managing Director told him that she was repaying herself a loan. However, it appears that this claim was false because any “loans” the Managing Director may have made to Chiron had already been fully repaid.

Designs for Learning, Stenmark, and the CTC representatives told us that they requested, but never received, written documentation regarding the alleged “loans” by the Managing Director. The CTC representative told us that the Managing Director told him that the record of her “loan” to Chiron was in the Chiron Board meeting minutes. We reviewed the Board meeting minutes that Chiron provided to us.<sup>55</sup> They do not show Board discussion or approval of the alleged “loans” by the Managing Director.<sup>56</sup> In addition, according to two Board Members, the Chiron Board did not know about the Managing Director’s alleged loans to the school until February 2005. We found no other documentation supporting the alleged “loans.”

## **B. “Payroll” Checks to The Managing Director**

Chiron hired Stenmark to prepare Chiron’s payroll checks, and to provide other financial services to Chiron. However, on several occasions, the Managing Director did not use the checks prepared by Stenmark. Instead, she wrote manual checks to pay herself and other Chiron employees.

We reviewed Chiron “payroll” checks to the Managing Director for the time period January 1, 2003 through February 25, 2005, including both payroll checks created by Stenmark, and manual checks that the Managing Director wrote to herself and identified as a form of compensation. Based upon our review, it appears that the Managing Director received \$4,352.88 more in “payroll” checks than she was authorized to receive.<sup>57</sup> We found an additional \$7,312.05 in “payroll” payments that are questionable. The results of our review are contained in Attachment D.

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<sup>55</sup> Minnesota law requires charter schools to maintain meeting minutes. *See* Minn. Stat. § 124D.10, subd. 6a (2004).

<sup>56</sup> The Board meeting minutes reflect Board authorization for other loans received by Chiron. Specifically, the Board approved Chiron obtaining a line of credit. *See* December 16, 2003 Chiron Board meeting minutes. On February 23 2004, Chiron obtained Loan No. 30975 for \$25,178.09 and a \$100,000 line of credit (Loan No. 30976) from CNB. According to a CNB commercial lending officer, Loan No. 30975 was used to pay off a Community Loan Technologies loan to Chiron. According to the November 10, 2004 Chiron Board meeting minutes, the Managing Director reported that the \$100,000 line of credit was paid off, and she sought and obtained approval to seek a \$50,000 line of credit at CNB.

<sup>57</sup> Chiron employees were to be paid every two weeks. We compared checks the Managing Director received as a form of compensation with Chiron payroll dates from January 1, 2003 through February 11, 2005.

Specifically, we found \$4,352.88 in “payroll” checks to the Managing Director that appear to be unauthorized:

- In a handwritten check dated February 3, 2005, the Managing Director advanced herself \$600.00 for her February 11, 2005 paycheck, but then paid herself her full salary on February 11, 2005.<sup>58</sup>
- The Managing Director received two checks dated November 30, 2004, for the December 3, 2004 payroll date, resulting in \$1,876.00 in unauthorized payments.<sup>59</sup>
- The Managing Director received a handwritten payroll check dated April 16, 2004, resulting in \$1,876.88 in unauthorized payments. The April 16, 2004 check contained a notation in the memo section of the check stating: “replace lost check.” The Managing Director’s Stenmark-prepared payroll check dated April 9, 2004 did not clear Chiron’s bank until June 1, 2004. Therefore, the April 9, 2004 check may have been “lost” temporarily, but was apparently “found” and negotiated, resulting in double payment for the April 9, 2004 pay period.<sup>60</sup>

In addition to the \$4,352.88 in unauthorized “payroll” payments, we question whether the Managing Director was authorized to receive an additional \$7,312.05 in “payroll” payments. Specifically, we found:

- The Managing Director paid herself an additional \$100 in the January 28, 2005 payroll check. According to a note to Stenmark, who was preparing Chiron’s payroll checks, the additional \$100 was for “overtime pay 1-21-05.” We question whether, as a salaried employee, the Managing Director was entitled to receive this “overtime pay.”
- The Managing Director paid herself \$2,561.94 in a check dated December 17, 2004. The Managing Director received the payment after she notified Stenmark, that she was to receive payment for 15 vacation days that she had not taken. In the documents we received from Stenmark, we found a letter on Chiron letterhead dated December 15, 2004, that is signed with a Chiron’s Board Chair’s name, stating that the Managing Director was to receive payment for 15 days of unused vacation from the 2003-2004 school year.<sup>61</sup>

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<sup>58</sup> The Managing Director’s February 11, 2005 payroll check was prepared by Stenmark, based upon The Managing Director’s authorization faxed to Stenmark on February 9, 2005.

<sup>59</sup> One of the checks was prepared by Stenmark, based upon The Managing Director’s authorization faxed to Stenmark on November 29, 2004; the other was handwritten by Ms. Laxton. The reverse side of the handwritten check contained the following notice: “The undersigned Payee, in endorsing this check declares that the same is received in payment of a just and correct claim against CHIRON Charter School, and that no part of it has heretofore been paid.” *See* Minn. Stat. §§ 124D.01, subd. 8 (i), 471.38 and 471.391. The handwritten check was endorsed by the Managing Director. Any person who willfully and falsely makes the declaration provided for in Minn. Stat. §§ 471.38 and 471.391 is guilty of a felony. Minn. Stat. § 471.392 (made applicable to charter schools in Minn. Stat. § 124D.01, subd. 8 (i)).

<sup>60</sup> The Managing Director also received a Stenmark-prepared paycheck for the following pay period ending April 23, 2004.

<sup>61</sup> During our review of documents, we also found an unsigned Settlement Agreement and Release of Claims. In addition to having Chiron’s insurer pay the Managing Director \$75,000.00, it appears that Chiron agreed to provide the Managing Director with “ten additional personal days to be taken at her discretion by December 31, 2004.”

- The Managing Director received \$1,875.11 in a check dated September 5, 2003. We found a note that appears to be written by Stenmark indicating that the check was for two weeks of vacation.<sup>62</sup>
- The Managing Director received \$1,500 in a check dated February 11, 2003. In the memo section of the check is a notation: “30 hrs @ 50” and “School Stipen” (*sic*). However, the Managing Director received paychecks for the pay periods surrounding February 11, 2003, causing us to question the additional 30 hours of pay.<sup>63</sup>
- The Managing Director received \$1,275 in a check dated January 3, 2003. In the memo section of the check is a notation: “Stipen – Scheduling.” However, the Managing Director received paychecks for the pay periods surrounding January 3, 2003, causing us to question the additional pay.<sup>64</sup>

We did not find the Managing Director’s contract with Chiron in the documents we received. However, we found “Projected Expenditures” documents included with Chiron’s Board of Directors meeting minutes, and Chiron’s 2003-2004 projected budget submitted to the Minnesota Department of Education as part of Chiron’s 2002-2003 Annual Report.<sup>65</sup> The documents provide gross salaries for various Chiron employees. The Managing Director’s gross salary for fiscal years 2003-2004 and 2004-2005 is consistently reported as \$52,500.<sup>66</sup>

However, we found that Chiron paid the Managing Director more in compensation than the \$52,500 per year that she reported in Chiron’s financial documents. Specifically, we found that Stenmark first began to prepare payroll checks for the Managing Director for the two-week pay period ending September 13, 2002. Based upon a fax authorized by the Managing Director, Stenmark calculated the Managing Director’s pay to be \$46,000, spread over 20 pay periods (through June 20, 2003).<sup>67</sup> Stenmark was then informed of a salary change for the Managing Director, retroactively effective to August 19, 2002. Stenmark was instructed to pay the Managing Director \$52,000. Stenmark first calculated the \$52,000 spread over 26 pay periods (a

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<sup>62</sup> We did not find an employment contract for the Managing Director in the documents we received. Therefore, we were unable to determine if the additional vacation pay was authorized.

<sup>63</sup> The Managing Director received a payroll check for \$1,600.92 dated February 14, 2003, and a payroll check for \$1,484.03 dated January 31, 2003.

<sup>64</sup> The Managing Director received a payroll check for \$1,717.21 dated January 17, 2003, and a payroll check for \$1,596.69 that was also dated January 3, 2003. We noticed that on January 3, 2003, other Chiron employees also received checks for “stipens” (*sic*). The January 2003 stipends ranged from \$75 to \$530.

<sup>65</sup> From the meeting minutes, it appears that the Managing Director prepared the documents and presented them to the Chiron Board. The 2003-2004 budget adopted by the Board at its November 4, 2003 meeting differed from the 2003-2004 budget sent to the Minnesota Department of Education; the difference was based on the number of students attending Chiron (85 or 75 students).

<sup>66</sup> See, e.g., FY 2003-2004 Projected Expenditures Revised 11/04/03 accepted at the November 4, 2003 Board Meeting (see meeting minutes item 5; budget revised to reflect 75 students); and FY 2004-2005 Projected Expenditures August 14, 2004, adopted as Chiron’s budget at the August 17, 2004 Board Meeting (see meeting minutes item 6). The FY 2003-2004 document expressly states that the \$52,500 salary is for a 52 week work schedule. See also Chiron Projected Budget, 2003-2004 attached to Chiron’s 2002-2003 Annual Report (director paid \$52,500 for 52 week work schedule). Fiscal year 2004 - 2005 is July 1, 2004 through June 30, 2005; fiscal year 2003 - 2004 is July 1, 2003 through June 30, 2004.

<sup>67</sup> The fax was sent on September 11, 2002.  $\$46,000 / 20 = \$2,300$ . At \$2,300 per two-week pay period, The Managing Director’s annual salary for 52 weeks would have been \$59,800 ( $\$2,300 \times 26$  pay periods = \$59,800).



full calendar year;  $\$52,000 / 26$  pay periods =  $\$2,000$  per pay period). However, Stenmark was then instructed to distribute the Managing Director's  $\$52,000$  salary over 22 pay periods (10 months, the school year).<sup>68</sup> Thus, Stenmark calculated the Managing Director's gross pay for each two-week pay period to be  $\$2,363.64$ .<sup>69</sup> During the rest of her employment with Chiron, the Managing Director continued to be paid at the rate of  $\$2,363.64$  per pay period. The Managing Director was paid during the entire calendar year. As a result, the Managing Director's actual yearly gross contract salary amount was  $\$61,454.64$ , not  $\$52,500$  as the Managing Director reported to the Board, and as approved by the Board in Chiron's budgets.<sup>70</sup>

However, in addition to receiving pay under her contract, the Managing Director received various other forms of compensation from Chiron. As a result, Stenmark reported The Managing Director's gross pay for tax purposes as  $\$67,363.74$  for 2004, and  $\$63,818.28$  for 2003.<sup>71</sup> Based upon Stenmark's calculation, it appears that the Managing Director understated her compensation on the financial documents presented to the Board, by  $\$14,863.74$  in 2004 and by  $\$11,318.28$  in 2003.

### C. Questionable "Reimbursements"

In addition to checks for "payroll" and "loan repayments," the Managing Director wrote herself Chiron checks that allegedly were for the reimbursement of expenses. These "reimbursement" checks total  $\$16,854.71$  for the time period January 1, 2003 through February 25, 2005. The results of our review are contained in Attachment E.

We reviewed the documentation supporting these reimbursements, including miscellaneous loose receipts, provided to us by Chiron, CTC, Designs for Learning and Stenmark. We were unable to find supporting documentation for  $\$7,568.03$  of the reimbursements.

When requesting reimbursement for expenses, Chiron employees were to complete a "Request for Check" form describing the item purchased, and attaching receipts to the form. The form contained a space for the requester to sign, certifying that the claim against Chiron for reimbursement was true and correct. The form also contained a space where the request could then be approved for payment.

We found that the Managing Director issued reimbursement checks to herself and to others without consistently requiring completion of the "Request for Check" form or submission of

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<sup>68</sup> In a fax to Stenmark dated October 9, 2002, the Managing Director authorized a change in her pay to "The new rate which you are aware of." Using the 22 pay periods for the school year appears to be consistent with the Leadership Staffing Proposal adopted at the September 26, 2002 Chiron Board meeting which states that the proposal was based on the school year "August 19, 2002 to June 18, 2002" (*sic*).

<sup>69</sup>  $\$52,000 / 22$  pay periods =  $\$2,363.64$ .

<sup>70</sup>  $\$2,363.64 \times 26$  pay periods =  $\$61,454.64$ .

<sup>71</sup> W-2 forms are used to report wages. For calendar year 2003, Stenmark also prepared a Form 1099 for individuals paid miscellaneous, non-employee compensation by Chiron. Stenmark prepared W-2 forms for calendar year 2004, but not Form 1099s because, as of July 1, 2004, Stenmark was only hired to prepare Chiron's payroll, not to perform general accounting services. No Form 1099 was found for the Managing Director for 2003.

supporting receipts. At times, the Managing Director issued checks to herself without a second person approving the payments.

Several of the Managing Director's "reimbursement" checks raise specific concerns beyond the lack of supporting documentation for the alleged expenses and the lack of internal controls reflected in the reimbursement procedures. For example, we found the following reimbursements:

- The Managing Director was reimbursed \$281.62 for "staff gifts."<sup>72</sup> The purchases included gift cards. Generally, public funds may not be used for employee gifts.<sup>73</sup> We found a reference to a December 15 Winter Frolic in the Managing Director's Report to the Chiron Board dated January 19, 2005. Specifically, the Report stated that the Winter Frolic had an excellent turnout, and many families went home with gift certificates (one per family). Therefore, we are unable to determine whether the gift cards were for staff members or for students' families. In any event, we question the use of public funds for gift certificates, even if the gift certificates were given to students' families.<sup>74</sup>
- The Managing Director was reimbursed \$96.70 with no supporting documentation. The memo section of the check indicated an asset & gift certificates were purchased. The current location of the asset is unknown.
- The Managing Director was reimbursed \$179.99 for an asset. The current location of the asset is unknown.
- The Managing Director was reimbursed \$950.00 for "Deposit for Dinner; Winter Frolic 12-15-04" with no supporting documentation. From the documents available to us, we were unable to determine what deposit was required for this event.
- The Managing Director was reimbursed \$563.09. We did not locate a Chiron "Request for Check" form for this reimbursement. However, a Designs for Learning representative informed us that she found loose receipts when she went to Chiron in early 2005 and attempted to organize Chiron's records. For this reimbursement check, she found a receipt totaling \$565.19.<sup>75</sup> The receipt included the purchase of an asset.<sup>76</sup> We are unable to verify at this time that the November 15, 2004 purchase was made by the

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<sup>72</sup> See Chiron CNB check # 4533 to Kristin Laxton dated December 17, 2004.

<sup>73</sup> See, e.g., Ops. Att'y Gen 107-a-3 (January 22, 1980), 270-D (August 12, 1977)(prohibiting retroactive pay increases or bonuses to public employees), 59-A-3 (May 21, 1948) and 59a-22 (December 4, 1934). See also School District Expenditures, by Mark F. Kerr, Assistant Legal Counsel, State Auditor's Office at page 6 (available at: [http://www.osa.state.mn.us/other/educationalmaterials/public\\_purpose\\_school\\_districts.pdf](http://www.osa.state.mn.us/other/educationalmaterials/public_purpose_school_districts.pdf)).

<sup>74</sup> In contrast, the Interim Managing Director's Report for December 2003 solicits the donation of prizes for Chiron's Winter Family Fun Night to be held December 17, 2003. The donation of prizes is permitted.

<sup>75</sup> The Designs for Learning representative found no other receipts that appeared to support the reimbursement reflected by Chiron check. There were also numerous loose receipts in the documents we received from Chiron. We found no other receipts that appeared to support this reimbursement.

<sup>76</sup> The total consists of merchandise of \$536.80 and tax of \$28.39 for a total of \$565.19. The items purchased included an asset for \$399.99, an asset for \$99.99, an asset for \$15.83, and an asset for \$20.99. According to the receipt, \$600 in cash was used to pay for the purchase. If this reimbursement is for the purchase, the amount of the reimbursement is short by \$2.10. [\$565.19 – \$563.09 (Chiron CNB check) = \$2.10.]

Managing Director for Chiron, or was reimbursed in the November 24 check. However, the current location of the asset reflected in the receipt is unknown.<sup>77</sup>

- The Managing Director was reimbursed \$500.00 for “open house & painting,” according to the notation on the memo section of the check. We question the even dollar amount of this reimbursement with no supporting documentation. In addition, we found other Chiron checks that appear to have paid expenses related to the “open house” and painting supplies.
- The Managing Director was reimbursed \$200.00 for “supplies reimbursement,” according to the notation on the memo section of the check. We question the even dollar amount of this reimbursement with no supporting documentation.<sup>78</sup>
- The Managing Director was reimbursed \$746.38 for an asset and supplies.<sup>79</sup> The current location of the asset is unknown.<sup>80</sup>

We suggested Interviews with former Chiron staff may provide further insight regarding these and other “reimbursement” checks received by the Managing Director.

## V. Debits from Chiron’s Accounts

In addition to reviewing check activity in the Chiron accounts, we reviewed other debits from the Chiron accounts. The results of our review are contained in Attachments F and G.

It appears that most of the debits are related to Chiron, or a known Chiron vendor. However, we could not identify the following debits, and therefore we could not determine whether they were personal expenditures, or Chiron expenditures:

- \$330.18 debit from Chiron’s CNB account. The only explanation for the debit on the bank statement was: “Purpwer Speedpay Speedpay Purchase Power.” CNB was unable to provide us with additional information about the debit.
- \$1,477.35 debit from Chiron’s WFB account on October 24, 2003 for “T-Mobile Pcs Svc.” In a check dated October 15, 2003, Chiron reimbursed the Managing Director \$1,412.31 for portions from five months of The Managing Director’s personal AT&T cellular telephone bills.<sup>81</sup> Prior to August 2003, “Verizon Wireless Epayments” were deducted from Chiron’s WFB account. Additional “T-Mobile Pcs Svc” debits from

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<sup>77</sup> The Minnesota Department of Education informed us that they did not recall seeing the asset at Chiron when Chiron closed. The Academy of Bioscience informed us that they did not receive any like assets.

<sup>78</sup> Other checks to the Managing Director with even dollar amounts and no supporting documentation included reimbursements of \$70 and \$45.

<sup>79</sup> See Chiron WFB check to the Managing Director for \$3,505.12. The Request for Check form signed by the Managing Director supporting this reimbursement included several supporting receipts, including a November 28, 2003 receipt for the assets.

<sup>80</sup> The Minnesota Department of Education informed us that they did not recall seeing an asset at Chiron when Chiron closed. The Academy of Bioscience informed us that they did not receive any assets.

<sup>81</sup> See Chiron WFB check for \$2,336.32. Documentation supporting the reimbursement was comprised of several items, including the summary portion of The Managing Director’s AT&T cellular telephone bills for March, April, June, August and September 2003 totaling \$1,412.31. No detailed statements itemizing the calls were provided.

Chiron's WFB account occurred in January and April 2003. It is unclear which telephone service(s) Chiron was actually using.

We also found that Chiron paid \$2,366 in overdraft charges on its CNB account during the time period February 23, 2004 through February 28, 2005. We found that Chiron paid \$2,460 in "nsf" (not sufficient funds) and overdraft fees on its WFB account during the time period January 2003 through October 2004. With proper fiscal oversight, Chiron would have avoided these charges.

## **VI. Chiron Payments to Other Chiron Employees**

During our review of Chiron's checking account activity, we found that several Chiron employees received unauthorized "payroll" checks. Specifically, we found payments of \$6,970 to the District Secretary that appear to be unauthorized, and additional payments of \$1,200 that appear questionable. We found that other employees received "stipends," "payroll advances" and other payments for which we found no supporting documentation. Finally, we found documentation that another employee appears to have made a "loan" to Chiron.

### **A. Payments to the District Secretary**

We reviewed checks made payable to Chiron's District Secretary, from Chiron's WFB and CNB accounts for the time period January 1, 2003 through February 25, 2005 (when Chiron closed). The District Secretary received checks from Chiron for payroll and for the reimbursement of expenses. The Managing Director signed all of the checks to the District Secretary.

#### **1. "Payroll" Checks to the District Secretary**

During our review, we found that the District Secretary appears to have received at least \$6,970 in unauthorized "payroll" checks. Our review is reflected in Attachment J.

The District Secretary was paid \$15 per hour while employed at Chiron.<sup>82</sup> As noted earlier in this report, Chiron employees were paid every two weeks. The District Secretary's gross pay, therefore, for a two-week pay period was \$1,200 (80 hours X \$15/hour = \$1,200).

It appears that the District Secretary may have received at least \$6,970.00 in unauthorized "payroll" payments. Specifically, we found:

- The District Secretary was paid \$300.00 as an "advance" for her February 11, 2005 paycheck; however, the Managing Director then reported to Stenmark that only \$200 had been advanced to the District Secretary, resulting in an unauthorized payment of \$100 in the District Secretary's February 11, 2005 paycheck.
- The District Secretary was paid an "emergency advance" of \$1,700.00 in a check dated January 28, 2005; that amount was not deducted in future paychecks.

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<sup>82</sup> We did not locate a contract between Chiron and the District Secretary in the documents that we reviewed. Most full-time Chiron employees were salaried, rather than hourly, employees.

- The District Secretary was paid \$600.00, allegedly for forty hours, in a check dated January 4, 2005; however, the District Secretary was paid for 80 hours in the pay period's prior and subsequent to January 4, 2005.
- The District Secretary was paid \$600.00, allegedly for forty hours, in a check dated September 16, 2004; however, the District Secretary was paid for 80 hours in the pay periods prior and subsequent to September 16 2004.
- The District Secretary was paid \$120 for "8 hours recruiting" in a check dated August 10, 2004, and \$600 for "40 hours recruitment" in a check dated July 30, 2004; however, the District Secretary was paid for 80 hours in the August 13, 2004 and July 30, 2004 paychecks. Furthermore, at the Managing Director's and the finance committee's request, the District Secretary's position appears to have been reduced from full-time to ¾-time, according to the June 22, 2004 Chiron Board meeting minutes. The minutes reflect that the District Secretary's position was returned to full-time status at the August 17, 2004 Chiron Board meeting. However, the payroll checks to the District Secretary do not reflect these changes. Instead, the District Secretary was paid for full-time work, plus 48 additional hours allegedly spent recruiting.
- The District Secretary was paid \$300.00, allegedly as a payroll advance, in a check dated June 7, 2004; however, the District Secretary was paid for 80 hours in the pay periods prior and subsequent to June 7, 2004.
- The District Secretary was paid \$600.00, allegedly as a payroll advance, in a check dated May 28, 2004; however, the District Secretary was paid for 80 hours in the pay periods prior and subsequent to May 28, 2004.
- The District Secretary was paid \$375.00 in a check dated May 14, 2004 that appears to have been coded as a payroll check by Stenmark; however, the District Secretary was paid for 80 hours in the pay periods prior and subsequent to May 14, 2004.
- The District Secretary was paid \$300.00, allegedly for twenty hours of work, in a check dated April 27, 2004; however, the District Secretary was paid for 80 hours in the pay periods prior and subsequent to April 27, 2004.
- The District Secretary was paid \$300.00 in a check dated April 15, 2004; however, the District Secretary was paid for 80 hours in the pay periods prior and subsequent to April 15, 2004.
- The District Secretary was paid \$300.00 in a check dated February 24, 2003 (although it appears that check date was actually February 24, 2004) that was coded by Stenmark as a check for "general supplies"; however, we found no supporting documentation for any general supplies reimbursed by this payment. Based upon the dollar amount, this check appears to be another unauthorized payroll check. The District Secretary was paid for 80 hours in the pay periods prior and subsequent to February 24, 2004.
- The District Secretary was paid \$375.00 in a check dated January 9, 2004; however, the District Secretary was paid for 80 hours in the pay periods prior and subsequent to January 9, 2004.
- During the two-week pay period ending November 7, 2003, the District Secretary appears to have been paid for 60 hours of work in checks dated October 30, 2003 (handwritten check for \$600) and November 7, 2003 (payroll check for \$261.75, based upon The Managing Director's note to Stenmark that the District Secretary should be paid for 20

hours of work). However, the District Secretary was paid an additional \$700 during that pay period in a handwritten check dated October 31, 2004.

In addition to the \$6,970 that appears to be unauthorized “payroll” payments, we question the following additional “payroll” payments totaling \$1,200:

- The District Secretary was paid \$225 for “sub pay” in a check dated January 20, 2005; however, the District Secretary was paid for 80 hours in the paychecks prior and subsequent to January 20, 2005. We question whether \$225 in “sub pay” should have been paid where the District Secretary was also paid for her regular full-time work.
- The District Secretary was paid \$975 in a check dated September 5, 2003 containing a notation in the memo section of the check stating “65 Hours.” However, the District Secretary was then paid for 40 hours of work in a September 12, 2003 payroll check prepared by Stenmark based upon The Managing Director’s authorization that the District Secretary be paid for 40 hours of work. We are unable to determine the number of hours that the District Secretary actually worked during the two-week pay period ending September 12, 2003.

For the two-week pay periods ending July 18, July 4, June 20, June 6 and May 9, 2003, the Managing Director informed Stenmark that the District Secretary should be paid for zero hours, but the District Secretary was paid by checks handwritten by the Managing Director. We are unable to determine the number of hours the District Secretary actually worked during those pay periods.

We recommended that the District Secretary be interviewed about these payments.

## **2. Expense Reimbursement Checks to the District Secretary**

In addition to checks allegedly for payroll during the time period January 1, 2003 through February 25, 2005, the District Secretary received \$3,726.81 in checks allegedly reimbursing the District Secretary for expenses. We reviewed the documentation supporting these reimbursements, including Request for Check forms and miscellaneous loose receipts provided to us by Chiron, Designs for Learning and Stenmark. We found no supporting documentation for reimbursements totaling \$1,055.11. Our review is reflected in Attachment K.

### **B. Checks to the Spouse of a Chiron Employee**

During our review of Chiron’s expenditures, we found that the Managing Director wrote ten checks from Chiron’s bank accounts, totaling \$3,334.08 to a person we understand to be the spouse of a Chiron employee between April 8, 2004 and February 3, 2005. We found no supporting documentation for \$1,362.08 of the payments. The checks are reflected in Attachment L. From notations on the checks, and from the supporting documentation we did find, the payments appear to be for repair work allegedly performed at Chiron.

### **C. Other Questionable Employee Payments**

Stenmark created payroll checks for Chiron. Every two weeks, Stenmark received a document from Chiron for the two-week pay period, indicating whether each employee should receive “normal” pay, or some other amount of pay. For hourly employees, the document identified the number of hours that the employee worked during the pay period, and the employee’s hourly pay rate. The Managing Director signed the document as the authorized signature. Stenmark would then calculate appropriate deductions, prepare the checks, and send the unsigned checks to the Managing Director for her signature and distribution. However, rather than using the payroll checks that Stenmark prepared, we found that the Managing Director often prepared handwritten checks for Chiron employees.

Previously in this report, we discussed questionable Chiron payments to the Managing Director and the District Secretary. However, we found that several other employees were also given handwritten checks described by the Managing Director as “stipends” or “payroll advances.” We found that some employees were paid more than their contract salary amount. We found additional handwritten checks to employees for which we found no supporting documentation.

#### **1. “Stipends” and Other Special Compensation**

We found several instances where Chiron employees and Board members received handwritten checks that were identified by the Managing Director as “stipends” or other forms of special compensation. We were unable to locate Board authorization for these payments, or written contracts supporting these payments.

##### **a. Coaching Stipends**

Some of the stipends may have been for coaching responsibilities. According to the July 24, 2003 Chiron Board meeting minutes, the Board decided to pay coaches \$1,500, consistent with the practice of the Minneapolis Public Schools.<sup>83</sup>

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<sup>83</sup> According to the June 2, 2003 Chiron Board meeting minutes, a boys’ baseball team and a girls’ softball team were being organized, and stipends for coaches would be requested at the next Board meeting. According to an e-mail from Designs for Learning dated July 22, 2003, the subject of coach compensation was not addressed at the Board’s June 23, 2003 meeting (for which we do not have minutes), but the e-mail expressed his view that approving \$1,500 for coaches would not require Board action unless it required amending the previously approved budget. We disagree, and believe that coach appointments should have been approved by the Board and documented in contracts. *See* Minn. Stat. § 124D.10, subd. 11(charter schools’ authority to hire employees; board of directors to decide matters relating to the operation of the school, including budgeting, curriculum and operating procedures); Chiron Bylaws at Article II, Section 1 (Board has general management and control of all Chiron business and affairs) and Article IV, Section 1 (Board may authorize, either generally or in specific instances, any officer or agent to enter into any contract). We found no evidence that the Chiron Board generally delegated employment contracts to the Managing Director; to the contrary, for some employment contracts in 2004, the Managing Director sought Board approval. *See, e.g.*, August 17, 2004 Board Meeting Minutes (Item 4). In a June 2003 report, a Minneapolis School District consultant similarly concluded that the Board had not approved contracts for Chiron’s staff or administrators.

For example, Chiron employee 9 was issued a check dated April 15, 2004 for \$700 that contained the notation “advance” on the memo line of the check. However, a copy of the check submitted to Stenmark had the word “advance” crossed out and replaced with the notation “softball coach pay.” If the April 15, 2004 check was an “advance,” it should have been repaid.<sup>84</sup> If the check was for coaching pay, it is unclear why the check amount was less than \$1,500.

Chiron employee 9 was also issued a check dated March 5, 2004 for \$750 that contained the notation “Basketball Stipen” (*sic*) on the memo line of the check. Chiron employee 9 had previously been issued a check for \$500 dated January 13, 2004 that was described to Stenmark as “extra pay Basketball Coach.”<sup>85</sup> We also found that Chiron employee 9 was issued a check dated July 15, 2003 for \$650 that contained the notation “Stipen” (*sic*) in the memo section of the check. We found no contracts documenting Chiron employee 9’s coaching responsibilities, and we found no references in the Chiron’s Board meeting minutes indicating that the Chiron Board approved Chiron employee 9’s coaching assignment(s).

We found that Chiron employee 10 was paid two \$1,500 stipends:

- In a check dated February 6, 2004, Chiron paid Chiron employee 10 \$1,500. In the memo section of the check is the notation: “stipen” (*sic*).
- In a check dated July 30, 2003, Chiron paid Chiron employee 10 \$1,500. Stenmark was told that this payment was a “stipen” (*sic*).

If the payments were for coaching, we found no contracts documenting Chiron employee 10’s coaching responsibilities, or Chiron Board approval of his coaching assignment(s). We found no other documentation regarding these “stipends.”

#### b. Additional Compensation to Chiron Employees

We found other checks written to Chiron employees for work allegedly performed in addition to their contracted services.

For example, in addition to their regular paychecks, Chiron employee 6 and Chiron employee 8 were each paid \$1,200, and Chiron employee 3 was paid \$100, in checks dated September 30, 2004. In a note to Stenmark, the three payments were described as “fed grant school/program planning.” However, Chiron hired Chiron employee 8 in August 2004, and she then received salary payments according to her Letter of Understanding. In addition, we found notes from Chiron employee 6 and Chiron employee 8 documenting hours worked between August 13 and August 20, 2004. Those hours do not appear to equal \$1,200 of pay.<sup>86</sup> Furthermore, in addition

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<sup>84</sup> We found no evidence that the funds were repaid or deducted from a subsequent paycheck.

<sup>85</sup> It appears that Chiron employee 9’s total compensation for basketball coaching was \$1,250 (\$750 + \$500 = \$1,250). Once again, it is unclear why the alleged coaching pay was less than \$1,500.

<sup>86</sup> Chiron employee 6 reported 32 hours for the week of August 16, 2004; Chiron employee 8 reported 41.75 hours for August 13, 2004 through August 20, 2004. (32 hours X \$25/hr = \$800; 41.75 hours X \$25/hr = \$1,043.75)



to her regular pay, Chiron employee 6 received a check dated August 27, 2004 for \$3,975 containing a notation of “159 Hours” in the memo section of the check.<sup>87</sup> The handwritten documentation submitted for the 159 hours covers the time period June 23, 2004 through August 13, 2004, and the work described appears to include school/program planning. Therefore, it is unclear why Chiron employee 6 and Chiron employee 8 each received an additional \$1,200 for school/program planning. We found no other documentation supporting the three September 30, 2004 payments.<sup>88</sup>

We found that at least one Chiron employee was paid for work allegedly performed in the summer of 2004 prior to the time that the Chiron Board authorized his employment.<sup>89</sup> According to the Chiron Board meeting minutes, the Managing Director requested and received permission on August 17, 2004 to offer contracts to new staff, including Chiron employee 8.<sup>90</sup> However, prior to August 17, 2004, the Managing Director paid Chiron employee 8 \$1,000 in a check dated August 6, 2004. According to a note in the memo section of the check, the payment was for “40 hrs @ \$25 – summer stipen” (*sic*). We found a document itemizing 40 hours of work by Chiron employee 8 between July 15, 2004 and August 6, 2004. It therefore appears that the Managing Director paid Chiron employee 7 for work performed prior to the time that the Board approved Chiron employee 7’s hiring.

We found that other Chiron employees were paid for work allegedly performed during the summer of 2004.<sup>91</sup> For example, Chiron employee 2 received a check for \$1,368.16 dated July 30, 2004 that included payment for 52.5 hours of work performed in the summer. In addition, Chiron employee 1 and Chiron employee 2 each received several checks, totaling \$10,455.26, for hours allegedly spent recruiting in July, August and September 2004. It appears that Chiron employee 1 was even paid for vacation days during the summer. Although the Chiron Board meeting minutes reference summer recruitment efforts by the Managing Director, Chiron employee 1 and Chiron employee 4, we found no contracts describing this employment.

As discussed earlier in this report, the District Secretary also received “recruiting” pay during the summer of 2004. Unlike Chiron employee 1 and Chiron employee 4 who were salaried employees with contracts covering the school year and not the summer months, the District Secretary was an hourly worker. The District Secretary received pay for 40-hours of work each week during the summer of 2004, in addition to hourly wages for her alleged recruiting. While we found documentation from Chiron employee 1 and Chiron employee 4 regarding their summer hours, we found no similar documentation from the District Secretary.

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<sup>87</sup> \$3,975 / 159 hours = \$25/hour.

<sup>88</sup> The May 2004 Managing Director’s Report references planned curriculum review over the summer by the Managing Director, Chiron employees 3, 4, and 6.

<sup>89</sup> Similarly, Chiron employee 8 appears to have been offered employment in a letter dated August 13, 2004, although the Board did not approve that offer until the August 17, 2004 Board meeting. Chiron employee 8 submitted hours for work beginning August 13, 2004.

<sup>90</sup> We did not find a Letter of Understanding for Chiron employee 7 in the Chiron, Stenmark or CTC documents.

<sup>91</sup> Most full-time Chiron employees signed a letter of understanding with Chiron that covered the school year.

We found that some Chiron employees were paid for work during the school year that was allegedly performed outside the hours specified in their contracts. For example, Chiron checks dated January 4, 2005 were issued to Chiron employee 1 for \$50 and to Chiron employee 4 for \$100. A notation in the memo section of each check states: "Staff Workroom." A note in the Designs for Learning documents states that these checks were stipends for helping outside normal contract hours. However, both of these employees' letters of understanding for the 2004 – 2005 school year stated that all Chiron employees were expected to provide no less than 40 hours of service per week, plus any additional hours required to fulfill the terms of the letter and/or as directed by Chiron's administration. Both of the letters of understanding listed various responsibilities, including "[o]ther duties and/or responsibilities as assigned by the administration." We found no documentation supporting the additional hours reflected in these checks.

We found that several employees also received "stipends" in January and August 2003.<sup>92</sup> Again, we found no contracts defining the services performed for the additional compensation, and we found no Board authorization for the payments.

c. Payments to Board Members

We found that some Chiron Board members also received payments described as "stipends." For example, Board Member 1 was, at various times, the principal, superintendent, director, and special education director for Chiron. Board Member 2 was a guidance counselor with Chiron. With the support of both, their contracts with Chiron were not renewed at the end of 2003 due to fiscal concerns. They then joined the Chiron Board of Directors.

During the five months that Board Member 1 was on the Chiron Board, three checks totaling \$7,500 were issued to him, in addition to salary checks. During the approximately 15 months that Board Member 2 was on the Chiron Board, he was issued 17 checks totaling \$18,145, in addition to salary checks. It appears that the rest of the Chiron Board was aware that Board Members 1 & 2 would continue working for Chiron even though their contracts were not renewed.<sup>93</sup> Furthermore, the Board "re-instated" them as part-time employees at a January 2004 Board meeting.<sup>94</sup> However, we found no contracts setting forth the terms of their continued employment with Chiron, and no itemization of the services performed.

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<sup>92</sup> The stipend payments were issued as separate checks in January 2003, and were included with the payroll checks in August 2003.

<sup>93</sup> See Chiron Board meeting minutes for November 4, 2003 (Item 4: Board members 1 and 2 would be "semi-retired" but continue to offer their services through December 19, 2003).

<sup>94</sup> See Chiron Board meeting minutes for January 27, 2004 (Item 6: Board members 1 and 2 reinstated as part-time employees, agreeing to defer payment until Chiron financially stable).

## 2. “Advances”

We found that the Managing Director issued employees “advances” on their pay. In several cases, employees were paid an “advance” and then had the “advance” deducted from future paychecks. We know of no authority for the payment of payroll “advances” with public funds.<sup>95</sup>

However, we found seven instances where it appears that the “advance” was not deducted from a future paycheck, thus resulting in unauthorized additional compensation.<sup>96</sup>

- Chiron employee 4 appears to have received several “advances.” It appears that most of the advances were deducted from future paychecks. However, we found no evidence that two advances in November 2004, totaling \$1,500, were deducted from future paychecks: a check to Chiron employee 4 for \$300, dated November 19, 2004, with the notation “Advance” in the memo section of the check; and a check to Chiron employee 4 for \$1,200, dated November 30, 2004, with the notation “emergency advance” in the memo section of the check.
- A check to Chiron employee 1 for \$350 dated December 3, 2004 contained the notation “Advance” in the memo section of the check. Another check to Chiron employee 1 for \$235 dated June 18, 2004 contained no explanation for the check in the memo section of the check. However, in a note to Stenmark, the check was identified as a payroll advance. We found no evidence that these advances were deducted from future paychecks.
- A check to Chiron employee 2 for \$500 dated December 6, 2004 contained the notation “Advance” in the memo section of the check. We found no evidence that this advance was deducted from future paychecks.
- A check to Chiron employee 3 for \$500 dated October 1, 2004 contained the notation “Payroll Advance” in the memo section of the check. We found no evidence that this advance was deducted from future paychecks.
- A check to Chiron employee 11 for \$500 dated September 25, 2003 contained the notation “Advance” in the memo section of the check. We found no evidence that this advance was deducted from future paychecks.

We recommended that these former Chiron employees be interviewed about these payments.

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<sup>95</sup> Chiron’s 2003 – 2004 contract with Stenmark expressly provided that any payroll advances paid from a petty cash account had to be recorded as advances so payroll records could be adjusted in the next payroll. *See* Stenmark, Inc. Service Agreement with Chiron (July 2003) at II.B.5 (page 3). Based upon notations we found in Stenmark’s files, it appears that Stenmark was not promptly notified by Chiron about some of the “advances” and was therefore unable to deduct the advances from the next payroll check. Minnesota law permits nonprofit corporations to advance money to employees to cover reasonably anticipated expenses for which they would be entitled to reimbursement in the absence of an advance. *See* Minn. Stat. § 317A.505. The statute does not authorize payroll advances.

<sup>96</sup> As previously discussed in this report, we found “advances” to the Managing Director and the District Secretary that also were not deducted from future paychecks.

### 3. Payments In Excess of Contract Amounts

We found that two employees routinely received handwritten checks in addition to their regular paychecks. We found no Board authorization for these payments.

We found that, in addition to her regular, authorized paychecks, Chiron employee 1 received a handwritten check for about \$265 in at least 16 pay periods during the 2003 – 2004 school year.<sup>97</sup> The Managing Director described the payments to Stenmark as “extra pay.”<sup>98</sup> We found no contract describing the extra work reflected in the extra pay. To the contrary, the letters of understanding that we reviewed correspond to the salary reflected in the regular, Stenmark-prepared paychecks.

We found that during the 2003 – 2004 school year, Chiron employee 4 was operating under an interim letter of understanding with a baseline salary equivalent of \$32,000 for the school year. The interim letter of understanding was for only fourteen weeks, but Chiron employee 4’s employment with Chiron was then extended through the end of the school year. Her gross pay for each pay period during the original fourteen-week contract had been calculated using a ten-month (22 payments) schedule ( $\$32,000 / 22 \text{ payments} = \$1,454.55$  gross pay). However, Chiron employee 4 continued to be paid at that rate throughout the school year and during the following summer, as if on a twelve-month (26 payments) schedule. As a result, it appears that Chiron employee 4 received four extra, unauthorized summer payments for the 2003-2004 school year, for a total of \$4,254.40.<sup>99</sup>

For the 2004 – 2005 school year, the Chiron budget approved by the Board reflected that Chiron employee 4 was again to be paid a salary of \$32,000. Similarly, a facsimile sent to Stenmark dated August 24, 2004 had a notation indicating that Chiron employee 4 was to be paid \$32,000 per year. Chiron employee 4 selected to receive her salary on a twelve-month (26 payments) schedule during the 2004 – 2005 school year. As a result, Stenmark prepared Chiron employee 4s’ checks to spread her \$32,000 salary over 26 pay periods, which resulted in gross pay each pay period of \$1,230.77 ( $\$32,000 / 26 \text{ pay periods} = \$1,230.77$ ). However, in a letter of understanding dated August 23, 2004, and apparently signed by the Managing Director and Chiron employee 4 on September 3, 2004, Chiron employee 4 was offered a salary of \$37,800 for the 2004 – 2005 school year.<sup>100</sup> Beginning with the November 19, 2004 paycheck, the Managing Director wrote Chiron employee 4 an extra check each pay period for about \$147, making Chiron employee 4s’ pay period equal to that of the prior year’s payments that had been

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<sup>97</sup> Each year, Chiron employee 1 chose to be paid on a ten-month schedule (22 payments, instead of a twelve-month schedule with 26 payments). As previously discussed in this report, Chiron employee 1 then appears to have been paid during the summer of 2004 on an hourly basis for recruiting.

<sup>98</sup> One of the notations was “extra hours worked” instead of “extra pay.” See Chiron WFB check # 3255 dated February 26, 2004.

<sup>99</sup> In addition to these salary payments in the summer of 2004, Chiron employee 4 also received the payments discussed previously in this report for alleged summer recruiting hours.

<sup>100</sup> We did not find a copy of Chiron employee 4’s 2004 – 2005 letter of understanding in the Chiron or Stenmark files. However, we obtained a copy of the letter from CTC.

based on 22 (instead of 26) payments.<sup>101</sup> The extra payments raised Chiron employee 4s' pay to approximately the amount reflected in the August 23, 2004 letter of understanding.<sup>102</sup>

#### 4. Other Unexplained Employee Payments

We found the following employee payments, with even-dollar amounts, for which we found no supporting documentation or Board authorization:

<u>Employee</u>	<u>Check Date</u>	<u>Check Amount</u>
Chiron employee 4	July 8, 2004	\$ 700.00 <sup>103</sup>
Chiron employee 12	March 10, 2004	\$ 750.00
Chiron employee 13	September 15, 2004	\$ 100.00 <sup>104</sup>

In addition, we found no supporting documentation or Board authorization for the following Chiron checks:

- A handwritten check to Chiron employee 14 dated September 30, 2004 for \$997 had a notation of "payroll" on the copy of the check provided to Designs for Learning. However, Chiron employee 14 appears to have received her regular paychecks for the pay period's prior and subsequent to September 30, 2004.
- A handwritten check to Chiron employee 11 dated October 15, 2003 for \$1,500 had a notation of "retro pay increase" in the memo section of the check.<sup>105</sup> However, the Managing Director wrote a letter to Stenmark dated September 22, 2003 directing Stenmark to revert Chiron employee 11 to her 2002-2003 salary.
- A handwritten check to Chiron employee 15 for \$200 dated September 26, 2003 contained the notation "Fed Tax Refund" in the memo section of the check.

We found one other instance of an alleged "loan" to Chiron. In the documents that we received from Chiron, we found a copy of Chiron employee 10's personal check for \$2,000 made payable to Chiron dated July 22, 2003, with a handwritten note stating: "loan to school." We found a deposit into Chiron's WFB account for \$2,000 on July 22, 2003. In a check dated July 30, 2003, Chiron paid Chiron employee 10 \$2,000. Therefore, it appears that the July 30, 2003 payment of

<sup>101</sup> Because Chiron employee 4 selected a twelve-month payment schedule, she would have been paid through the August 12, 2005 pay period, if Chiron had remained open.

<sup>102</sup>  $\$37,800 / 26 \text{ weeks} = \$1,453.85 \text{ gross pay}$ ;  $\$32,000 / 22 \text{ weeks} = \$1,454.55 \text{ gross pay}$ .

<sup>103</sup> During this same period of time, as previously discussed in this report, Chiron employee 4 received several checks for alleged recruiting. While this payment may also have been for alleged recruitment efforts, it was not identified as such.

<sup>104</sup> The minutes for the August 17, 2004 Chiron Board meeting state that Chiron employee 13 and the other member of the janitorial staff were to receive \$5,000 each per year as pay increases. Each then had their two-week paychecks increased by \$50. This \$100 payment is in addition to those raises.

<sup>105</sup> We found no mention of a pay increase for Chiron employee 11 in the Chiron Board meeting minutes that we reviewed.

\$2,000 repaid Chiron employee 10 for his “loan” to the school. We found no other documentation for this “loan.”

We recommended that former Chiron employees be interviewed about these payments.

## VII. Lack of Accounting and Internal Control Procedures

A Designs for Learning representative informed us that when she went to Chiron in 2005, Chiron’s records were in disarray. Similarly, we were informed that CTC and a Chiron Board member also found Chiron’s records in disarray in February 2005. Designs for Learning and CTC representatives found that invoices, receipts and other documents were in boxes. They found that mail to Chiron had gone unopened, and bills had not been paid.<sup>106</sup> The Designs for Learning representative said that the boxes contained all of the mail that a school receives, as well as some of The Managing Director’s personal records, in no recognizable order.

We were provided with the financial records that remained at Chiron when it was closed. We also found that the documents were not well organized. During our review, we also found that, in some instances:

- Bills were unpaid for more than 45 days;<sup>107</sup>
- Loose receipts were in the Chiron records;
- Documents were not filed, or were not filed in the proper files;
- Chiron checks were not recorded in Chiron’s checkbook registers;

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<sup>106</sup> We were informed that the Managing Director had a rule that she was the only person allowed to handle Chiron’s mail. We were also informed that the Managing Director kept the Chiron checkbook in her purse.

<sup>107</sup> Where a governing body meets at least once a month, vendors must be paid within 35 days of the receipt of the goods, services or invoice (whichever is later) unless the contract with the vendor specifies otherwise. *See* Minn. Stat. §§ 124D.10, subd. 8(i) (charter schools subject to section 471.425) and 471.425, subd. 2 (pay within 35 days if governing body meets at least once a month; otherwise within 45 days). It appears that Chiron’s Board was to meet monthly. *See, e.g.*, September 26, 2002 Board Meeting Minutes (Item 11: – Board to meet on 4<sup>th</sup> Thursdays of the month); August 17, 2004 Board Meeting Minutes (Item 9: Board to meet on first Wednesday of every month). Chiron’s Financial Report for year ended June 30, 2003, contained a finding that Chiron did not pay all vendor obligations within 45 days. *See* Finding 2003-4. Chiron responded to the finding by stating that Chiron was working towards meeting its financial obligations within the 45-day time period. *Id.* Examples of late payments include TRA and PERA payments. We also found a variety of unpaid invoices in the documents we received from Chiron. For example, we found: an invoice dated January 22, 2005 from Sepler and Associates, Inc., adding \$83.08 in finance charges to a bill of \$564.59 owed from July 1, 2004; a collection letter from the State Fire Marshal for \$100 owed from an October 7, 2004 invoice; a February 15, 2005 letter from Chiron’s food vendor Caravan Kids Catering (CKC) stating that \$3,296.10 was still past due, even after a deposit of \$4,200 from Chiron in CNB check # 4603 dated February 15, 2005, and notifying Chiron that CKC would now require COD payments from Chiron; a February 7, 2005 statement from McGraw-Hill for \$2,581.11 from invoices dated October 10, 15 and 28, 2003, and November 2, 2004; February 3, 2005 statements from PCI Educational Publishing for \$592.09 from invoices dated March 15 and 18, 2004, and for \$283.18 from an invoice dated November 22, 2004. *See also* April 8, 2004 letter to the Managing Director from the Minneapolis Public Schools, enclosing an invoice dated January 21, 2004 for sponsorship fees of \$3,600; Chiron paid the bill in May 2004. *See* Chiron WFB check # 3377 dated May 12, 2004.

- Chiron checks were written out of sequence;
- Chiron staff were given pre-signed blank checks;<sup>108</sup>
- Chiron checks were written for dates in the future;<sup>109</sup>
- Chiron checks were written and then held before being issued;
- Since at least July 1, 2004, Chiron did not maintain a formal reconciliation of the cash balance on its monthly bank statements;
- Chiron paid \$4,826 in bank nsf and overdraft charges because Chiron did not have sufficient funds in its accounts;<sup>110</sup>
- Electronic fund transfers were used by Chiron without statutorily required controls in place, such as the approval of all such transfers at the next regular board meeting;<sup>111</sup>
- Federal taxes were not paid, or were not paid in a timely manner, resulting in interest charges and penalties, and a total federal IRS liability of \$157,379.34 as of October 26, 2005;
- Retirement fund payments were not paid, or were not paid in a timely manner, resulting in delinquency charges;
- Child support payments were not forwarded, or were not forwarded in a timely manner, to the Minnesota Child Support Payment Center;
- Employees, at times, were paid their gross pay amount, instead of their net pay amount;
- W-2 Statements prepared by Stenmark, and based upon information provided by Chiron, may have inaccurately reported wages paid;
- Employees received payroll advances;
- Some employee advances were never recovered, becoming additional, unauthorized compensation;
- Terms and conditions of employment for several Chiron employees and consultants were not documented in writing, or authorized by the Chiron Board, according to the Chiron Board meeting minutes;<sup>112</sup>
- Hourly employees did not submit time sheets, and the brief handwritten listing of hours submitted by some hourly employees were not signed by the employee and approved by a supervisor;
- Reimbursements were paid without supporting documentation;

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<sup>108</sup> For example, it appears that on several occasions Chiron employee 10 was given a signed, blank check to purchase items at locations such as Office Depot.

<sup>109</sup> For example, we found seven checks written in sequence to “M.C.M.” It appears the checks were written to Chiron’s attorneys, MacKall, Crouse & Moore, to pay outstanding legal fees of \$41,243.56. Although the checks were written sequentially, they are dated one month apart, from October 30, 2004 through April 30, 2005, for a total of \$40,000.

<sup>110</sup> See Attachments F and G of this report.

<sup>111</sup> See Minn. Stat. § 471.38, subs. 3 and 3a (applicable to charter schools in Minn. Stat. § 124D.10, subd. 8 (i); permitted uses of electronic funds transfers, including vendor payments; only permitted if specific policy controls in place, including annual written delegation of authority, identification of initiator of electronic transfer, written confirmation, and list of all electronic fund transfers submitted to school board at next regular meeting).

<sup>112</sup> The Minneapolis School District Consultant concluded in his June 2003 report that the Chiron “Board did not act on the employment of teaching staff, on the custodial staff or on the contracts of administrators.”

- Request for Check forms, itemizing claims and containing the declaration that the claim was just and correct and no part of it had been paid, were not completed prior to all reimbursements;<sup>113</sup>
- Chiron's checks did not consistently have a declaration on the reverse side stating that the claim was just and correct and no part of it had been paid;<sup>114</sup>
- Only one signature was required on Chiron's checks;
- The Managing Director wrote checks to herself, without anyone else authorizing the payment;
- Chiron funds were used for gifts for staff members;
- Chiron took out one loan to pay off another loan.<sup>115</sup>

Chiron was not using basic internal control procedures. The procedures used by Chiron did not segregate duties.<sup>116</sup> Some controls appear to have been routinely subject to The Managing Director's management override.<sup>117</sup> The Chiron Board approved some Chiron contracts, but not others.<sup>118</sup> The Chiron Board approved some of Chiron's expenditures, but not others.<sup>119</sup>

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<sup>113</sup> See, e.g., Attachments E and K of this report. Claims must not be allowed until the person claiming payment itemizes the claim in writing and signs a declaration that the claim is just and correct and that no part of it has been paid. See Minn. Stat. §§ 124D.10, subd. 8 (i) (charter schools subject to section 471.38) and 471.38 (claims payment procedures). Chiron's failure to comply with Minn. Stat. § 471.38 was an audit finding in 2002 and 2003. Chiron Financial Report from April 9, 2002 (date of inception) to June 30, 2002 (Finding 2002-2); Chiron Financial Report for year ended June 30, 2003 (Finding 2003-2).

<sup>114</sup> See Minn. Stat. §§ 124D.10, subd. 8 (i) (charter schools subject to section 471.391) and 471.391 (form of declaration on reverse side of check). In response to audit findings that Chiron was not obtaining the required declaration, Chiron agreed to include the required declaration above the endorsement line on its manual checks. See Chiron Financial Report from April 9, 2002 (date of inception) to June 30, 2002 (Finding 2002-2); Chiron Financial Report for year ended June 30, 2003 (Finding 2003-2).

<sup>115</sup> For example, a loan for \$25,000 from the Minnesota Nonprofits Assistance Fund was obtained in January 2004, and paid off with a subsequently obtained line of credit.

<sup>116</sup> Chiron's audits noted Chiron's limited segregation of duties in a number of areas, due to the limited size of Chiron's office staff. See Chiron Financial Report from April 9, 2002 (date of inception) to June 30, 2002 (Finding 2002-1); Chiron Financial Report for year ended June 30, 2003 (Finding 2003-1). In response, Chiron stated that Chiron's management would attempt to maximize the segregation of duties in all areas within the limits of its available staffing.

<sup>117</sup> See, e.g., failure to use the Request for Check form for reimbursements; Attachment E.

<sup>118</sup> For example, according to the June 22, 2004 Board meeting minutes, expenditure of \$4,155 was approved to advertise Chiron on radio station B96. However, we found that three payments of \$4,155 were actually made to B96-Radio One. All three payments to B96-Radio One were in the form of cashier's checks. Two of the three cashier's checks were purchased with Chiron CNB checks, both for \$4,155, made payable to B96. The third cashier's check to Radio One for \$4,155 was dated September 23, 2004. The source of funds used to purchase the September 23, 2004 cashier's check was not from Chiron's WFB or CNB accounts. As previously discussed in this report, Chiron did not approve many employment contracts. See also the Minneapolis School District Consultant's June 2003 report at page 6.

<sup>119</sup> According to the June 2, 2003 Board meeting minutes, the Minneapolis School District Consultant informed the Chiron Board that it needed to approve all expenditures.



### **VIII. Lack of Effective Board Oversight**

Many of the issues identified in this report could have been avoided or mitigated if Chiron's Board of Directors had exercised due diligence in their oversight role.

Chiron was in precarious financial shape at least as early as July 2003.<sup>120</sup> At both the September 25, 2003 and the December 16, 2003 meetings, the Managing Director requested that Chiron seek a line of credit to meet cash flow needs. In November and December 2003, correspondence between Chiron's attorneys and the attorney for the Minneapolis Public Schools showed that a consultant to the Minneapolis Public Schools had concerns about his ability to obtain financial information from Chiron. In a December 7, 2003 Chiron School Review, the consultant warned Chiron that the Minnesota Department of Education would be lowering its payment amounts because it had been paying Chiron at a higher level than justified by the student estimates previously reported by Chiron. At least two employment contracts were not renewed at the end of 2003 due to fiscal concerns.<sup>121</sup> A representative of the Minnesota Association of Charter Schools (MACS) expressed concern to the Chiron Board in May 2004 that Chiron was fully extended through its line of credit, and cautioned Chiron about entering into any new service contracts.<sup>122</sup> Although the Minneapolis School District Consultant concluded that Chiron was financially solvent through June 30, 2004, he noted that Chiron may need to do some short-term borrowing for cash flow purposes.<sup>123</sup>

Despite these warnings, it appears that no one on Chiron's Board reviewed Chiron's actual expenditures or financial procedures after June 30, 2003. There appears to have been no effective oversight of The Managing Director's actions.

#### **A. Chiron's Board**

As a nonprofit corporation under Minnesota Statutes Chapter 317A, Chiron's Board was responsible for managing the business and affairs of the nonprofit corporation.<sup>124</sup> The Board had a fiduciary duty, including the duty of care to maintain an active role in Chiron's affairs, to ensure accurate record keeping, to be familiar with Chiron's books and records, and to review

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<sup>120</sup> Chiron's budget approved in July 2003 for the 2003-2004 school year was based on 160 students. *See* September 25, 2003 Chiron Board meeting minutes. According to the September 25, 2003 Chiron Board meeting minutes, Chiron's enrollment was at 70 students, and the Board would need to decide Chiron's future at the next Board meeting, including the possibility of closing Chiron.

<sup>121</sup> *See* Chiron Board meeting minutes for November 4, 2003 (Item 4).

<sup>122</sup> *See* Chiron Board meeting minutes for May 19, 2004 (Item 4).

<sup>123</sup> The Minneapolis School District Consultant's December 7, 2003 Review actually concludes that Chiron will be financially solvent through "June 30, 2003." However, based upon a letter dated December 16, 2003 to Chiron and Chiron's attorney, from the District General Counsel for the Minneapolis Public Schools, and based upon the date of the consultant's review, it appears that the consultant meant to conclude that Chiron's financial condition was adequate to support school operations through the end of the 2003-2004 school year, through June 30, 2004.

<sup>124</sup> *See* Minn. Stat. § 317A.201. *See also* Minn. Stat. § 124D.10, subd. 11(charter schools' authority to hire employees; board of directors to decide matters relating to the operation of the school, including budgeting, curriculum and operating procedures); Chiron Bylaws at Article II, Section 1 (Board has general management and control of all Chiron business and affairs).

the performance of Chiron's officers.<sup>125</sup> It appears that the Chiron Board did not perform these duties.

Chiron's Bylaws specified that the Board must have a treasurer who shall have custody of all funds, subject to regulations that may be imposed by the Board.<sup>126</sup> According to the Chiron Board meeting minutes, when Chiron was first formed, a 7<sup>th</sup> grade student was appointed Chiron's treasurer.<sup>127</sup> However, the student was removed from the Board in July 2003, after being absent from meetings.<sup>128</sup> Thereafter, the minutes do not clearly define who, if anyone, filled the role of treasurer.

Chiron's Bylaws provided that the Board could authorize, either generally or in specific instances, any officer or agent to enter into any contracts or execute any instrument on behalf of Chiron.<sup>129</sup> The Bylaws also provided that Chiron checks could be signed by the authorized officers or agents and in the manner as determined by resolution of the Board of Directors.<sup>130</sup> In the absence of further determination by the Board, checks could be signed by any one of the officers.<sup>131</sup> We found no evidence that the Managing Director was a Chiron officer. We found no Board resolution authorizing the Managing Director to enter contracts and to handle all financial matters on behalf of the Board.

We found that the financial reports the Managing Director provided to the Chiron Board did not accurately reflect Chiron's financial situation. For example, we found:

- The Managing Director under-reported her compensation by approximately \$9,000 each year.<sup>132</sup>
- For the 2004-2005 school year, Chiron employee 4's salary appears to have been under-reported.<sup>133</sup>

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<sup>125</sup> See Minn. Stat. §§ 317A.251 (standard of conduct for directors); 317A.257 (liability of directors and officers); and 317A.361 (standard of conduct for officers). See also Fiduciary Duties of Directors of Charitable Organizations, A Guide for Board Members From the Office of Minnesota Attorney General Mike Hatch, available at: <http://www.ag.state.mn.us/charities/charDuties.html>.

<sup>126</sup> Chiron Bylaws at Article III, sections 1 and 7. See also Chiron Board meeting minutes for November 7, 2002 (Item 5: Board treasurer's role not reviewed).

<sup>127</sup> See Chiron Board meeting minutes for April 8, 2002; April 17, 2002;

<sup>128</sup> See Chiron Board meeting minutes for July 24, 2003.

<sup>129</sup> See Chiron Bylaws at Article IV, section 1.

<sup>130</sup> See Chiron Bylaws at Article IV, section 2.

<sup>131</sup> *Id.*

<sup>132</sup> See, e.g., December 16, 2003 Chiron Board meeting minutes, FY 2003-2004 Projected Expenditures Revised 12/12/03 (Director 52 week work schedule salary of \$52,500). See also Chiron's Projected Budget, 2003-2004 submitted to the Minnesota Department of Education as part of Chiron's 2002-2003 Annual Report (prepared by Designs for Learning) at pages 26-28; FY 2004-2005 Projected Expenditures October 4, 2004 (Laxton at \$52,500 for 52 week contract).

<sup>133</sup> See Budget approved at the August 17, 2004 Board meeting; FY 2004-2005 Projected Expenditures August 14, 2004 (Salary at \$32,000); letter of understanding dated August 23, 2004 (Salary of \$37,800). See also FY 2004-2005 Projected Expenditures October 4, 2004 (Salary at \$35,000). Chiron employee 4 was a Board member at the time.

- Additional compensation paid to Chiron employees was not included in the “Projected Expenditures” presented to the Chiron Board.
- Unpaid retirement fund, tax payments and penalties were not reported to the Chiron Board.
- Unpaid tax obligations were not reported to the Chiron Board.
- General expenses such as telephone bills, repairs, and legal expenses were not included on “Projected Expenditures” presented to the Chiron Board.
- “Nsf” and penalty charges were not reported to the Chiron Board.
- The Managing Director’s alleged loans were not reported to the Chiron Board.
- The Managing Director’s January 19, 2005 Managing Director’s Report failed to mention that Chiron’s required audit had not been completed.<sup>134</sup>

According to the Board meeting minutes, the Board was told that it needed to approve all expenditures and contracts, and the Board discussed the need for more active participation.<sup>135</sup> However, we found that the Board did not approve all expenditures and contracts. Instead, it appears the Board relied on The Managing Director’s handling of Chiron’s finances, without exercising effective oversight.

## **B. Financial Services Contracts**

Chiron had contracts for financial services, but we found that the contracts were never fully implemented.

Chiron had contracts with Stenmark for certain financial and business services.<sup>136</sup> Specifically, for fiscal years 2002 – 2003 and 2003 – 2004, Stenmark was hired to perform payroll functions for Chiron, to maintain account information based upon information provided by Chiron, to reconcile Chiron’s bank accounts (up to two accounts) on a monthly basis, to prepare 1099s and W-2s, to serve as the primary contact with Chiron’s audit firm at the end of the fiscal year, and to process invoices or requests for payments for the issuance of system checks (Stenmark-prepared checks, as opposed to manual checks).<sup>137</sup> During fiscal year 2002 – 2003, Stenmark issued system checks for payroll and for various vendors. However, during fiscal year 2003 – 2004, Stenmark found the recording of financial information into Chiron’s books to be difficult

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<sup>134</sup> The December 8, 2004 Chiron Board meeting minutes mention that Chiron’s audit is due December 31, 2004.

We had an agenda, but no minutes for the Board’s January 19, 2005 meeting. The Managing Director’s January 19, 2005 Managing Director’s Report stated that the Managing Director did not “foresee needing to make further reductions in our expenses at this time.”

<sup>135</sup> See February 26, 2003 Chiron Board meeting minutes (Board training and the need for more active participation discussed); June 2, 2003 Chiron Board meeting minutes (Minneapolis School District Consultant reports that Board need to approve all expenditures).

<sup>136</sup> During fiscal year 2002 – 2003, Stenmark also agreed to provide up to two days of consulting to set up and review procedures. We found a copy of Stenmark, Inc.’s Service Agreement with Chiron, July 1, 2002, signed by the Managing Director, in Chiron’s documents. We found unsigned copies of Stenmark’s July 2003 contract with Chiron. Except for Stenmark’s Fee Schedule contained in Appendix A, the language of the two agreements appears to be virtually identical.

<sup>137</sup> Fiscal year 2002 – 2003 was from July 1, 2002 through June 30, 2003. Fiscal year 2003 – 2004 was from July 1, 2003 through June 30, 2004.

because so many of Chiron's checks were manual checks, written by the Managing Director without being processed through Stenmark. Beginning July 1, 2004, Stenmark's relationship with Chiron was terminated by Chiron, but Stenmark was then asked to process certain payroll information.

It appears that Stenmark was unable to meet its contractual obligations because Chiron failed to perform its duties under the fiscal year 2003 – 2004 Stenmark contract. As a result, Chiron's required audit for fiscal year 2003 – 2004 could not be performed.

Under the Stenmark contract, Chiron was required to provide Stenmark with, among other items, information on the banks it used.<sup>138</sup> However, Chiron opened an account at CNB in February 2004, but Stenmark did not learn about the account until months later. Stenmark continued to prepare payroll checks on the WFB account, only to discover that the Managing Director was writing manual checks to employees from the CNB account. Stenmark continued to prepare checks for retirement accounts, but we found several unsigned retirement account checks in the documents we received from Chiron. Under the contract, Chiron was required to provide Stenmark with descriptions of the purpose for which payments were made.<sup>139</sup> However, Stenmark was still seeking information in January 2005 regarding some of Chiron's fiscal year 2003 – 2004 payments.<sup>140</sup> Under the contract, Chiron was required to identify the source of all funds received.<sup>141</sup> However, in January 2005, Stenmark was still seeking information regarding certain Chiron deposits.<sup>142</sup> Under the contract, Chiron was required to provide Stenmark with a copy of manual checks, and all supporting documents for the checks.<sup>143</sup> However, we found that Chiron did not provide Stenmark with copies of all of Chiron's checks, and supporting documents were lacking for many of the check copies that were provided to Stenmark.

We found no evidence that Stenmark informed the Chiron Board of the problems it was having in obtaining timely information from the Managing Director, or in preparing for Chiron's audit.

Chiron also had various contracts with Designs for Learning. In an August 17, 2004 Contract for Consulting Services, for \$25,000 (\$2,500 per month), Designs for Learning agreed to provide

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<sup>138</sup> See Stenmark contracts section II.B.1.

<sup>139</sup> See Stenmark contracts section II.B.1.

<sup>140</sup> See, e.g., Stenmark memorandum dated January 24, 2005. The Stenmark documents also contain a notation that the Managing Director was asked to identify the items on November 24, 2004. Stenmark ran unidentified checks through "clearing accounts" in order to produce bank reconciliations. As of December 30, 2004, debits in the clearing accounts totaled \$490,578 and credits in the clearing accounts totaled \$493,381. Stenmark could see transactions from Chiron's bank statements, but had no idea what the transactions were for. As of December 30, 2004, Stenmark had unsuccessfully sought information from the Managing Director on at least three different occasions regarding the transactions in the clearing accounts.

<sup>141</sup> See Stenmark contracts section II.B.1.

<sup>142</sup> See, e.g., Stenmark memorandum dated January 24, 2005. For example, in November 2004, Stenmark requested information from Chiron on the CNB and the Community Loan Technologies loans. Stenmark learned about the CNB and Community Loan Technologies loans from the CNB bank statements.

<sup>143</sup> See Stenmark contracts section II.B.3.

financial management, accounting and audit preparation services, among other services.<sup>144</sup> More specifically, under the contract, among other things, Designs for Learning agreed to:

- Assume responsibility for all financial management functions of the school;
- Pay bills regularly with school funds;
- Manage the expense reporting process and procedures;
- Reconcile bank statements on a timely basis;
- Prepare financial statements for internal and board review, at least three times per year;
- Advise on cash flow, cash management, and credit issues;
- Assist the director and board leadership with the preparation and maintenance of school budgets.

Beginning in September 2004, Designs for Learning invoiced Chiron \$3,325 per month for “Financial Management, accounting, and audit preparation,” and “Government Reporting.”<sup>145</sup> However, Designs for Learning did not perform the financial services itemized in the August 17, 2004 contract, and Chiron did not pay Designs for Learning for the services billed in these invoices.<sup>146</sup> Designs for Learning informed us that it was unsuccessful in obtaining financial documents from the Managing Director until December 2004. We found no evidence that prior to that date, Designs for Learning reported to the Board on its unsuccessful attempts to implement the new contract.<sup>147</sup> We found no evidence that the Board questioned whether the new Designs for Learning contract had been implemented, even though the terms of the contract had been reviewed with them in August. Rather than relying on the contracted financial services provided by Designs for Learning, it appears that the Board approved a \$50,000 line of credit at its November 10, 2004 meeting based upon a report that the Managing Director provided to the Board.<sup>148</sup>

### C. Chiron’s Sponsors

In a letter dated November 12, 2003, the Minneapolis School District (District) gave Chiron notice of termination of its sponsorship because there had been a 50% reduction in Chiron’s enrollment that could cause a sudden closure, and Chiron had not provided financial information requested by the sponsor. The notice of termination was withdrawn after Chiron apparently provided the information to the District. The Minneapolis School District’s consultant then provided the District with a report concluding that Chiron’s financial condition was adequate to support Chiron’s operations through the end of the 2003-2004 school year. The consultant’s

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<sup>144</sup> See Contract for Consulting Services between Chiron and Designs for Learning (August 17, 2004). The contract was approved at the August 17, 2004 Chiron Board meeting (Item 5).

<sup>145</sup> “Financial Management, accounting, and audit preparation” services were billed at \$2,550 per month. “Government Reporting” was billed at \$775 per month.

<sup>146</sup> Designs for Learning confirmed that the last payment it received from Chiron was on April 14, 2004.

<sup>147</sup> A Designs for Learning representative was present at the February 18, 2005 Chiron Board meeting when Chiron decided to close. As noted previously, we did not find January 19, 2005 Chiron Board meeting minutes. The December 8, 2004 and November 10, 2004 Board meeting minutes do not mention anyone from Designs for Learning or the Designs for Learning contract.

<sup>148</sup> See Chiron Board meeting minutes for November 10, 2004, item 4.

conclusion appears to have been based, in part, on information provided by the Managing Director . The Minneapolis School Board decided not to renew its sponsorship of Chiron as of June 2004 because it was no longer a “conversion” charter school since the experienced teachers were no longer with Chiron.<sup>149</sup>

Pillsbury United Communities (Pillsbury) entered an agreement to become Chiron’s sponsor in June 2004. Pillsbury provided Chiron with Pillsbury’s Charter School Policy and Sponsorship Guidelines.<sup>150</sup> The Guidelines states that “[o]ne of the primary responsibilities of the sponsor is to provide oversight to the school.”<sup>151</sup> The Guidelines also state that Pillsbury offers “a high quality package of administrative services,” including accounting and asset management, to charter schools it sponsors.<sup>152</sup> Pillsbury did not provide accounting and asset management services to Chiron. Instead, the contract Chiron signed with Pillsbury placed the operation of Chiron with Chiron’s Board of Directors, and provided that Pillsbury had no authority, control, power, or administrative or financial responsibility over Chiron.<sup>153</sup>

Unlike the reports the Minneapolis School Districts’ consultant prepared when the Minneapolis School District was Chiron’s sponsor, we found no reports from Pillsbury.<sup>154</sup> From the Chiron Board meeting minutes available to us, it appears that between June 2004 and February 2005, a Pillsbury representative attended only two meetings: the August 17, 2004 meeting where Chiron was welcomed to the Pillsbury family, and the February 18, 2005 meeting where the Pillsbury representative recommended that another school (Minnesota Transitions School) help transition Chiron students when Chiron closed.<sup>155</sup>

## **IX. Misrepresentations to CTC**

It appears that the Managing Director misrepresented Chiron’s financial situation to CTC in 2005, in order to secure CTC’s financial support. CTC informed us that they were approached by Chiron, and were told that Chiron needed only \$80,000 in order to meet its financial obligations for the remainder of the 2004 – 2005 school year. CTC informed us that they gave CTC \$80,000 based upon those claims. However, CTC quickly discovered that Chiron’s debts and payroll obligations exceeded \$80,000. We confirm that Chiron’s debts and payroll obligations exceeded \$80,000 at the time Chiron closed.

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<sup>149</sup> See Letter to Chiron from the Minneapolis Public Schools dated April 7, 2004.

<sup>150</sup> The Charter School Policy and Sponsorship Guidelines (Pillsbury Guidelines) are dated March 2004, and were approved at the Pillsbury Board’s March 18, 2004 meeting.

<sup>151</sup> See Pillsbury Guidelines at page 13.

<sup>152</sup> See Pillsbury Guidelines at page 8. The financial management role of the sponsor includes sharing financial information at each board meeting on current student enrollment (MARSS), other income, current expenses, an up-to-date balance sheet, and any other financial related issues. See Pillsbury Guidelines at page 13.

<sup>153</sup> See Charter School Contract between Pillsbury Untied Communities, Sponsor, and Chiron Charter School dated June 30, 2004 at sections 4 (management and administration) and 5.2.

<sup>154</sup> We found no evidence that Chiron paid Pillsbury any sponsorship fees. Compare Chiron WFB check paying Minneapolis Public Schools \$3,600 for January 21, 2004 invoice for sponsorship fees.

<sup>155</sup> It appears there was no July 2004 meeting (June 22 minutes were approved at the August 17 meeting), and we only found agendas for meetings set for September 6, 2004, January 19, 2005, and February 16, 2005. The agenda for the February 16, 2005 meeting contains “Approve minutes from February 14 meeting” as an agenda item.

## **X. Conclusion**

We found a lack of effective oversight and a lack of internal controls at Chiron. We found that the Managing Director misreported the number of students attending Chiron, resulting in Chiron receiving public funds to which it was not entitled. We found that the Managing Director misreported how federal funds were expended. We found that the Managing Director made unauthorized and questionable payments to herself, to Chiron employees, and to others.

This report is being referred to the Minneapolis Police Department, and has been filed with the Hennepin County Attorney to institute such proceedings as the law and public interest require.<sup>156</sup>

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<sup>156</sup> See Minn. Stat. §§ 6.51, 6.715, subd 3.