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**STATE OF ARIZONA**  
OFFICE OF THE  
**AUDITOR GENERAL**

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August 1, 2017

Members of the Arizona Legislature

Governing Board  
Phoenix Union High School District

The Honorable Mark Brnovich, Arizona Attorney General

The Honorable Diane Douglas, Arizona State Superintendent of Public Instruction

The Office of the Auditor General (Office) has conducted a financial investigation of Phoenix Union High School District (District) for the period December 2012 through January 2016. The Office performed the investigation to determine the amount of public monies misused, if any, during that period and the extent to which those monies were misused.

The investigation consisted primarily of inquiries and examination of selected financial records and other documentation. Therefore, the investigation was substantially less in scope than an audit conducted in accordance with generally accepted auditing standards. Accordingly, the Office does not express an opinion on the adequacy of the District's financial records or internal controls. The Office also does not ensure that all matters involving the District's internal controls, which might be material weaknesses under standards established by the American Institute of Certified Public Accountants or other conditions that may require correction or improvement, have been disclosed.

The Financial Investigative Report describes the Office's findings and recommendations as a result of this investigation.

Sincerely,

Debbie Davenport  
Auditor General

Attachment

## Phoenix Union High School District Fraudulent Schemes and Theft

**Synopsis:** As part of its responsibility to prevent and detect fraud, Phoenix Union High School District (District) management took appropriate action by reporting a fraud allegation to the Office of the Auditor General (Office). We conducted an investigation revealing that from December 2012 through January 2016, Julie Kendall, former controller, orchestrated a fraud scheme to falsely reduce her and her sister's (also a district employee) income taxes. During her fraud scheme, she caused district software to generate electronic deposits of \$4,400 and \$4,000 to her and her sister's respective bank accounts. On July 24, 2017, Ms. Kendall was indicted on 13 felony counts.

### Overview

The District received \$326 million in fiscal year 2016 to educate about 27,000 students in 9th through 12th grade at 16 schools. For nearly 20 years Julie Kendall had payroll-related duties at the District, initially for processing payroll and later for supervising others who processed payroll. She consistently had payroll software access that allowed her to change employee wages, benefits, employer-related deductions, and tax-sheltered annuity plan contributions. Ms. Kendall's sister was a district employee for 28 years, during which the last half was spent working with federal programs. She never had any payroll-related duties or access to payroll software. After Ms. Kendall caused the District's payroll software to generate two deposits to her and her sister's respective bank accounts, the District placed both employees on administrative leave and conducted an internal investigation. In February and March 2016, Ms. Kendall and her sister each entered into resignation agreements and reimbursed the District for these deposits, paying \$4,400 and \$4,000, respectively.

### Ms. Kendall orchestrated a fraud scheme to falsely reduce her and her sister's income taxes

#### Ms. Kendall altered the District's payroll software information to report false amounts on her and her sister's W-2 forms—

For four years, Ms. Kendall fraudulently attempted to lower income taxes for herself and her sister. Specifically, on December 19, 2012, January 10, 2014, November 24, 2014, and November 30, 2015, Ms. Kendall made unauthorized entries in the District's payroll software that reduced wages and increased tax-sheltered annuity contributions reported on Wage and Tax statement (W-2) forms for herself and her sister. Actual wages paid to Ms. Kendall and her sister and actual tax-sheltered annuity contributions paid to third-party servicers were not changed; only the W-2 forms were affected. Specifically, as shown in the table, for tax years' 2012 through 2015 W-2 forms, Ms. Kendall falsely reduced her and her sister's reported wages and falsely increased amounts reported for their tax-sheltered annuity contributions for a total of

#### Effect of Ms. Kendall's unauthorized payroll software adjustments on W-2 forms and income taxes Tax years 2012 through 2015

Tax year	False reduction of W-2 form wages		Estimated federal and Arizona income taxes not paid	
	Ms. Kendall	Sister	Ms. Kendall	Sister
2012	\$12,000	\$12,000	\$ 2,985	\$1,760
2013	15,000	15,000	4,027	2,889
2014	18,000	18,000	4,453	3,602
2015	25,800	35,200	n/a <sup>1</sup>	n/a <sup>1</sup>
<b>Total</b>	<b>\$70,800</b>	<b>\$80,200</b>	<b>\$11,465</b>	<b>\$8,251</b>

<sup>1</sup> The District discovered Ms. Kendall's scheme and took corrective action prior to issuing 2015 W-2 forms. Accordingly, Ms. Kendall's and her sister's 2015 W-2 forms were accurate.

Source: Auditor General staff analysis of district and personal income tax records.

\$70,800 and \$80,200, respectively. Correspondingly, Ms. Kendall prepared and filed income tax returns for herself and her sister for three of these years with this false wage information, resulting in Ms. Kendall failing to pay \$11,465 and her sister failing to pay \$8,251 of estimated federal and state income taxes (see table on the previous page). Before Ms. Kendall could file 2015 income tax returns, the District discovered her scheme and issued accurate 2015 W-2 forms.

**Ms. Kendall caused the District’s payroll software to generate payments totaling \$8,400 to herself and her sister**—Because Ms. Kendall made unauthorized adjustments to the District’s payroll software in November 2015 that were substantially larger than her previous adjustments, she caused the software for the first time to activate automatic refund payments to herself and her sister. Specifically, Ms. Kendall and her sister received \$4,400 and \$4,000, respectively, on their December 18, 2015, electronic paycheck deposits because Ms. Kendall’s 2015 unauthorized adjustments exceeded allowable contribution limits for tax-sheltered annuity plans by these amounts. Consequently, the payroll software automatically corrected for these apparent overpayments by refunding the excess through their electronic payroll deposits. These payments were included in a system report and on December 22, 2015, a district employee noticed them and forwarded the information to her supervisor. Consequently, the supervisor discovered additional payroll-related anomalies, prompting the internal investigation mentioned earlier.

**Ms. Kendall altered the District’s payroll software information to conceal her scheme**—On Saturday, January 2, 2016, Ms. Kendall used her remote access login credentials and made unauthorized entries to the District’s payroll software, reversing the amounts she had previously falsified for tax years 2012 through 2014. District officials were already reviewing her unauthorized adjustments to tax year 2015, hence, Ms. Kendall did not make any reversing adjustments for that year.

## District officials initially failed to provide adequate oversight but took prompt and appropriate actions after detecting Ms. Kendall’s scheme

Although district officials took prompt and appropriate actions after detecting Ms. Kendall’s fraud scheme, prior to this discovery, officials had not provided adequate oversight or maintained effective internal controls to ensure W-2 form amounts were appropriately recorded and processed. Accordingly, Ms. Kendall was able to make unauthorized entries in the District’s payroll software without being detected because she was solely responsible for processing the District’s W-2 forms and no one reconciled any payroll reports to the W-2 forms. However, since becoming aware of Ms. Kendall’s fraud scheme, district officials took timely action to deter her scheme and help prevent future fraudulent actions. Specifically, district officials promptly reported the fraud allegation to this Office; conducted an internal investigation; placed relevant employees on administrative leave; mailed relevant Form W-2c, Corrected Wage and Tax Statements, for tax years 2012 through 2014 to the Internal Revenue Service, Social Security Administration, and the Arizona Department of Revenue; and ensured all stolen monies were repaid to the District. Additionally, district officials reported implementing improvements to controls over payroll and W-2 form processes, including preparing reconciliations of employee withholdings to amounts reported to the Internal Revenue Service, Arizona Department of Revenue, and tax-sheltered annuity plan servicers. Moreover, the District reported that its technology department conducts daily reviews and the District’s internal audit department conducts yearly reviews of employee access to financial software programs to ensure employees’ access is limited to that necessary for performing their job duties.

## Conclusion

Our investigation revealed that from December 2012 through January 2016, Julie Kendall, former controller, illicitly altered district payroll software information, falsely reducing income amounts reported to federal and state taxing authorities for herself and her sister (also a district employee). Ms. Kendall prepared and filed her and her sister’s income tax returns with this false information, resulting in Ms. Kendall’s failure to pay \$11,465 and her sister’s failure to pay \$8,251 in estimated federal and state income taxes. Additionally, Ms. Kendall’s actions caused the software to generate electronic deposits of \$4,400 and \$4,000 to her and her sister’s respective bank accounts. Lastly, Ms. Kendall attempted to conceal her scheme by again altering district payroll software, but this time reversing her earlier unlawful adjustments. We have submitted our report to the Arizona Attorney General’s Office, which, on July 24, 2017, presented evidence to the Arizona State Grand Jury. The action resulted in the indictment of Ms. Kendall on 13 felony counts related to fraudulent schemes, theft, misuse of public monies, preparing a false tax document, and computer tampering.