A REPORT
TO THE
ARIZONA LEGISLATURE

Special Investigative Unit

Investigative Report

Mohave Educational Services Cooperative

Financial Improprieties

MARCH • 2004

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

Debra K. Davenport
Auditor General

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STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

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AUDITOR GENERAL

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March 15, 2004

Members of the Arizona Legislature

Mohave County Board of Supervisors

The Honorable Mike File
Mohave County School Superintendent

The Honorable Terry Goddard
Attorney General

The Office of the Auditor General has conducted a special investigation of the Mohave Educational Services Cooperative for the period July 1997 through June 2001. The investigation was performed to determine the amount of public money misused, if any, and whether there were procurement violations during that period.

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

The accompanying Investigative Report describes the Office's findings as a result of this special investigation.

After this report is distributed to the members of the Arizona State Legislature, the Mohave County School Superintendent, and the Attorney General, it becomes public record.

Debbie Davenport
Auditor General

Attachment

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SUMMARY

In July 1999, the Office of the Attorney General requested the Office of the Auditor General to review allegations of financial improprieties involving the operation of the Mohave Educational Services Cooperative (MESC). Particularly, the allegations indicated that Mohave Educational Services Cooperative officials may have improperly conducted procurement, accepted gratuities, and unfairly charged certain fees to its members. As a result of that request, and in conjunction with the Attorney General's Office, we conducted an investigation of those allegations and submitted the following findings to the Attorney General in January 2003.

The findings are grouped into the following five sections:

- **MESC has not followed procurement statutes and rules**—Although MESC issues numerous contracts proclaimed to be based on procurement practices that adhere to the Arizona Procurement Code and the Arizona State Board of Education Procurement Rules, we found that MESC consistently failed to follow many of these rules. Specifically, MESC inappropriately used the more subjective request for proposal procurement process; did not properly evaluate vendor responses to those proposals; failed to make determinations of whether prices were fair and reasonable; and improperly awarded contracts to multiple vendors for the same products.

  During the course of our review, MESC hired its first procurement director and began revising their procurement practices to comply with the Arizona Procurement Code and the Arizona State Board of Education Procurement Rules.

- **MESC does not provide an economic value for its members**—MESC's procurement procedures and contract oversight practices did not consistently generate value for Arizona's public entities. In fact, despite MESC's purchasing power, several products on MESC contracts were priced higher than other purchasing cooperatives' and school districts' contracts. Also, MESC's negligent oversight of purchases made from its own contracts allowed at least one vendor to overcharge members.

- **MESC charges its members inequitably**—As a service program established pursuant to A.R.S. §15-365, MESC is required to share its administrative and general service costs on a user basis; however, MESC charges its members inequitably. Some members pay for services they don't use, some pay more than others, and others do not pay at all.

- **MESC's financial practices violate rules and regulations**—Although MESC is subject to Mohave County oversight, rules, and regulations, MESC spent its money without regard to county rules and regulations. Specifically, MESC's merit and personnel practices exceeded parameters within the Mohave County Merit System Rules and Regulations; MESC's travel-related purchases violated Mohave County's travel policy; and MESC officials improperly distributed certain benefits and gifts to themselves, other governmental officials, and vendors.

- **Other MESC operations are improper**—MESC officials engage in several other business practices that are improper or outside of their lawful authority. MESC unlawfully holds title to real property, and fails to comply with certain parts of the *Uniform Accounting Manual for Arizona Counties*.

INTRODUCTION & BACKGROUND

In July 1999, the Office of the Attorney General requested the Office of the Auditor General to review allegations of financial improprieties involving the operation of the Mohave Educational Services Cooperative (MESC). Particularly, the allegations indicated that MESC officials may have improperly conducted procurement, accepted gratuities, and unfairly charged certain fees to its members. As a result of that request, and in conjunction with the Attorney General's Office, we conducted an investigation of those allegations and submitted the following findings to the Attorney General in January 2003. The Attorney General's corrective legal action against MESC is pending.

Purpose and structure

Mohave Educational Services Cooperative (MESC) was established in 1981 by the Mohave County Schools Superintendent under the authority of A.R.S. §15-365, which allows service programs to be created for functions that can be "… accomplished more efficiently and economically as multicounty or multidistrict operations."

Although MESC provides other services, such as a media library, its primary function is to competitively procure materials, services, and construction. MESC asserts that its main objective is "to serve our members by providing contracts for quality products and services at the best possible prices." Entities wishing to make purchases from an MESC contract must become MESC members by agreeing to terms outlined in written agreements. These agreements call for MESC to provide members with contracts procured in compliance with the Arizona Procurement Code and the Arizona State Board of Education School District Procurement Rules. Members are predominantly required to pay MESC an administration fee of 1 percent (minimum $10) of the purchase-ordered materials or services.

MESC currently has over 700 members, primarily from the public sector. School districts are the largest group with 225 members. Other members include charter schools, private schools, community colleges, and cities and towns. Members'

Yearly purchases from MESC contracts average over $100 million with about 91 percent coming from school districts.

purchases from MESC contracts average over $100 million a year. Approximately 91 percent of these purchases are made by school districts.

Established by the Mohave County School Superintendent as a service program, MESC is subject to county oversight, laws governing county operations, county rules and regulations, and the *Uniform Accounting Manual for Arizona Counties*. MESC is included as a component unit within the Mohave County audited Comprehensive Annual Financial Reports, and the Mohave County Board of Supervisors approves its budgets.

Budget

MESC is not directly supported with Mohave County tax money; rather, MESC is primarily funded by the administrative fees charged to most members. Most of these administrative fees are paid by public entities with public money. MESC's fiscal year 2003 operating revenue was $2,064,356; and operating expenses were $2,195,487, including salaries for approximately 25 employees.

FINDING 1

MESC has not followed procurement statutes and rules

Although MESC issues numerous contracts proclaimed to be based on procurement practices that adhere to the Arizona Procurement Code and the Arizona State Board of Education Procurement Rules, we found that MESC consistently failed to follow many of these rules. Specifically, MESC inappropriately used the more subjective request for proposal procurement process; did not properly evaluate vendor responses to those proposals; failed to make determinations of whether prices were fair and reasonable; and improperly awarded contracts to multiple vendors for the same products.

During the course of our review, MESC hired its first procurement director and began revising their procurement practices to comply with the Arizona Procurement Code and the Arizona State Board of Education Procurement Rules.

Procurement laws provide safeguards

Procurement statutes and rules provide safeguards to uphold the quality and integrity of procurement processes, thus helping to ensure the best value is obtained for goods and services purchased. Arizona school districts are required to follow procurement rules established by the Arizona State Board of Education. Since nearly all Arizona school districts use MESC's services, it is important that MESC follow the State Board of Education's Procurement Rules, as well as the Arizona Procurement Code, when awarding contracts to vendors. In fact, MESC states in its member agreements that its vendor contracts are awarded in accordance with both sets of rules. However, MESC did not always follow these procurement statutes and rules.

Although MESC's Cooperative Purchase Agreements state,

> "MESC shall conduct the procurement in compliance with the Arizona Procurement Code and the Arizona State Board of Education School District Procurement Rules (A.R.S. Title 41, Chapter 23 and State Board Rules, R7-2-1001 et seq),"

MESC did not always follow these procurement statutes and rules.

Inappropriate use of request for proposal process

When issuing sealed solicitations, MESC inappropriately used the "request for proposal" (proposal) process rather than the more objective "invitation for bid" (bid) process. School district procurement rules allow for the proposal process only under specific situations, when the governing authority determines that competitive sealed bidding may not be practicable or advantageous. MESC's governing authority has not made that determination for any of the proposals MESC has issued. Contracts resulting from the proposal process do not have to be awarded to the vendor with the lowest prices. Nearly 90 percent of the sealed solicitations MESC issued for purchases made by members during fiscal years 1997 through 2000 were requests for proposals. MESC could have followed the more competitive bid process for these solicitations and likely resulted in lower-priced contracts. In fact, the State Procurement Office (SPO) policy is to use the bid process whenever it is possible to quantify factors and clearly define specifications. The effect of MESC's proposal practice is further discussed in Finding 2 on page 9.

	Bid	**Proposal**
Must contract be awarded to responsive and responsible vendor with the lowest cost?	Yes	No
Allow discussions with vendors after opening vendors' response?	No	Yes
Allow changes in vendor responses after opening?	No	Yes

Vendor responses were not properly evaluated

Although school district procurement rules require that a contract be awarded to the offeror whose proposal is determined in writing to be the most advantageous to the school district based on the evaluation factors set forth in the request for proposals, MESC failed to do this. In fact, MESC awarded contracts without documenting an assessment of any evaluation factors. Evaluation factors are the standards by which a vendor may ensure its responding proposal meets the performance requirements.

MESC's proposals did not state the relative importance of price and other evaluation factors such as quality, timeliness, warranties, or service. Consequently, vendors responding to an MESC proposal would not know the value or weight of any evaluation factors and may not submit a competitive proposal that accurately reflects the performance requirements.

Omission of evaluation criteria and documentation also leads to a subjective evaluation process that may not be in MESC's members', and therefore, the public's, best interests. In fact, although the "Evaluation Checklist" forms were reportedly used to support the basis of contract awards, they do not allow a proposal evaluator to follow the course of the decision or establish that the awards were the most advantageous to a school district or other MESC member, based on the factors in the proposal. Rather, the "Evaluation Checklist" forms allow for the evaluator to have "no opinion" on both price and proposal evaluation and primarily serve to ensure the proposal is complete. MESC staff decides who shall be awarded a contract; however, there is no documentation to support that process. Contract awards were often unsubstantiated by or in conflict with the "Evaluation Checklist" forms. For example:

- MESC awarded a contract to a school consulting services vendor even though a school district superintendent serving as an evaluator described the vendor's pricing as "exorbitant."

- MESC failed to further evaluate a vendor's proposal for school buses despite the evaluators' opinions of "very competitive pricing," "service hours are better than others," or "recommend for further evaluation."

- MESC awarded a contract to a fence vendor who had been a contractor for only 3 months, yet denied a contract to a school equipment vendor because it had been in business less than 1 year.

- MESC failed to award a contract to a school equipment vendor because the vendor did not bid on 46 items in the proposal, even though this criterion was not an evaluation factor. Moreover, another vendor was awarded a contract despite not bidding on 165 items in the same proposal.

- MESC denied a contract to a flooring vendor because its "installed price was high in every case"; however, this statement was not supported by any evaluations or other analysis. In fact, the vendors' prices were equal to or lower than the other vendors.

MESC's "Evaluation Checklist" forms were often in conflict with its contract awards.

No determination of price being fair and reasonable

Although required by State Board of Education Procurement Rules, when only one bidder submitted a proposal, MESC officials failed to determine that the bidder's price was fair and reasonable and that other prospective bidders had reasonable opportunity to respond, or there was inadequate time to resolicit the proposal. Consequently, MESC may have limited competition and may not have received the best possible results in terms of both quality and cost. In fact, several vendors reported that they were unable to respond to an MESC solicitation for roofing services because of its restrictive language. Some of the vendors' observations include:

- “It is our opinion that the specification as prepared by Mohave was carefully structured to reduce competition rather than foster it”;
- “Bid seemed to be proprietary”; and
- “The tight specs prevent others from competing.”

Improper multiple awards

MESC’s practice of awarding contracts to multiple vendors for the same goods or services may be inhibiting the economic value of competition. State procurement rules allow multiple awards to be made only if a single award is not advantageous to the State, and further requires multiple awards to be limited to the fewest number of suppliers necessary. However, on at least 24 occasions during fiscal years 1997 through 2000, MESC awarded contracts to two or more vendors responding to the same solicitation without documenting any advantage to its members. In fact, as a result of one solicitation for school furniture, ten different vendors were awarded contracts. As described in Finding 2 on page 9, the prices on some of these contracts were higher than the State Procurement Office contracts for the exact same furniture.

FINDING 2

MESC does not always provide an economic value for its members

MESC's procurement procedures and contract oversight practices did not consistently generate value for Arizona's public entities. In fact, despite MESC's purchasing power, several products on MESC contracts were priced higher than other purchasing cooperatives' and school districts' contracts. Also, MESC's negligent oversight of purchases made from its own contracts allowed at least one vendor to overcharge members.

MESC contracts may cost more

Certain MESC contracts' prices were as much as 33 percent higher than other entities' contracts for the exact same products. We examined contracts for five types of commodities in which MESC and SPO used the same vendors for the same items. All of these items were identical in quality with matching distributors, manufacturers, and model numbers. Administrative fees were not included in the price comparison due to their disparate nature. For example, MESC charges $10 or 1 percent of the total purchase, whichever is higher, and SPO charges a $160 annual fee, regardless of purchase amount. As illustrated in Exhibit 1, MESC had higher contract prices for four of the five school district commodities we selected when compared to contracts issued by SPO.

Exhibit 1 Percentage by Which MESC Prices Exceeded SPO Prices for Selected School District Commodities Fiscal Year 2001

Commodity	Percentage MESC Prices Exceeded SPO Prices
Various basketball equipment	33.36%
School furniture: desks	14.83%
School furniture: computer tables, chairs	4.53%
Computers	1.62%
Printers	(7.22%)

Source: Auditor General staff analysis of MESC and SPO procurement records for the year ended June 30, 2001.

In addition, dairy products in MESC's contract were higher priced than dairy products in other entities' contracts. As illustrated in Exhibit 2, a different purchasing cooperative and several school districts, including large, urban, and even small and rural districts, had more competitive prices than MESC.

Exhibit 2 Percentage by Which MESC Prices Exceeded SPO Prices for Half-pint Milk Fiscal Year 2001

Entity	Percentage MESC Prices Exceeded Other Entities' Prices
Douglas USD	18.08%
Chloride USD	15.30%
Deer Valley USD	5.87%
Glendale ESD	5.28%
Greater Phoenix Purchasing Consortium of Schools	4.24%

Source: Auditor General staff analysis of MESC, Greater Phoenix Consortium, and Douglas, Chloride, Deer Valley, and Glendale district records for the year ended June 30, 2001.

Each comparison was for the same size and type of milk, with all but one district purchasing from the same vendor. Again, MESC administrative fees are not included in these prices. For food-related contracts, MESC charges an administrative fee ranging from 0.5 percent to 5.5 percent of the purchase, depending on the members' purchasing volume. The Greater Phoenix Purchasing Consortium of Schools and school districts noted in our comparison do not have any administrative fees or surcharges.

In contrast, a Phoenix accounting firm MESC hired to perform at least two savings studies found that members were saving 7 to 15 percent on their purchases. The first study covered the fiscal year July 1996 to June 1997, and the second study covered a 6-month period from January 1999 to June 1999. However, as explained below, the firm's methodology provided a limited analysis.

- The firm did not contact any equivalent vendors or otherwise account for competition. To make the comparison, the firm provided MESC vendors duplicate copies of their prior MESC purchase orders, which included the item number, description, quantity, and price. It then only asked vendors what price each would have charged to a non-MESC member for the same product or service.

- The firm did not review existing vendors' contracts with other government entities. For example, SPO had contracts with at least two of the vendors the firm contacted. As described on page 9, SPO had lower prices than MESC, even from the same vendor.

Negligent oversight of members' purchases

Because MESC regularly promotes that it makes sure its members' purchase order prices match its contracts, MESC has a fiduciary duty to ensure that all purchases are in compliance with contract terms. However, MESC rarely performed this service. MESC verified only 8.5 percent of 550 purchase orders that we randomly selected for review. Because MESC does not reliably ensure that purchase order prices meet the contract terms, members cannot be assured that the product ordered is actually on the contract or is listed at the correct price.

For example, MESC's failure to review purchase orders allowed one vendor to substitute unauthorized products and overcharge nine school districts by approximately $175,306.

This vendor has several contracts with MESC for products such as modular buildings, bleachers, gymnasium apparatus, and flooring. Because MESC did not make sure that items and prices ordered by members were in compliance with its contracts, the vendor was allowed to overcharge several districts by using outdated prices, charging extra for items included in contract prices, and making mathematical mistakes.

We examined 15 purchase orders to this vendor totaling over $2.3 million and for which MESC had not verified prices. As illustrated in Exhibit 3, our analysis found that for 10 of the 15 purchase orders, MESC allowed 9 districts to be overcharged a total of $175,306. In addition, the vendor substituted allegedly lesser-quality products for those specified in their contract.

Described below are the various ways in which MESC's inaction resulted in members paying too much for those purchases. Because the associated administrative fees MESC charges are a percentage of the purchases, these charges to the districts were also inflated.

- MESC allowed the vendor to overcharge one school district $66,081 for a modular building by not using the final contract price, not correcting the vendor's mathematical mistakes, and failing to correct the vendor's charging of extra costs for items already included in the contract price. For example, restrooms were included in

"Every Mohave contract has been awarded following the Arizona procurement code. When an agency uses a Mohave contract, it sends its purchase order to Mohave's office in Kingman. A procurement specialist checks the purchase order for three things: is the product being ordered actually on bid; is the price on the purchase order correct; are the correct products being ordered."
-MESC advertisement

"Mohave reviews the purchase order and confirms the purchase is allowable under the Mohave contract."
-MESC vendor information guide

"When we receive your p.o., we will verify the prices and order the products to be shipped directly to your school."
-MESC Contract Summary

Exhibit 3 Price and Product Discrepancies for Selected Vendor Orders

Invoice Total	Amount Member Was Overcharged	Value of Products Substituted
$ 309,899	$ 0	$ 0
315,228	0	0
148,665	7,277	0
55,521	9,545	0
386,378	39,745	0
150,109	10,650	0
53,567	13,691	0
11,923	2,100	6,840
307,347	66,081	0
10,223	800	6,400
99,914	15,540	0
134,022	9,877	5,200
200,007	0	7,200
75,019	0	0
85,464	0	0
$2,343,286	$175,306	$25,640

Source: Auditor General staff analysis of MESC Records.

the scope of the contract, but the vendor charged the district extra for restrooms. In addition, MESC permitted the vendor to charge the district more for "upgrades" like HVAC units and doors without crediting the district for the costs associated with the contract "standard" items.

- MESC allowed the vendor to overcharge six school districts a total of $44,063 for bleachers by not ensuring the most updated prices were used and by permitting the vendor to add freight and labor charges, despite the contract price's inclusion of delivery and installation.

- MESC let the vendor overcharge one of the six school districts (mentioned above) $39,745 for a modular building by not using the final contract price and by not correcting the vendor's mathematical mistakes.

- MESC allowed the vendor to overcharge two districts a total of $25,417 for bleachers, basketball equipment, and lockers by not using the proper contract and not affording the districts the lower "special pricing" that the vendor was offering to MESC members at the time. Even though MESC contracts require that any price reductions be available to all members equally, MESC did not ensure that these discounts were appropriately applied.

FINDING 3

MESC charges its members inequitably

As a service program established pursuant to A.R.S. §15-365, MESC is required to share its administrative and general service costs on a user basis; however, MESC charges its members inequitably. Some members pay for services they don't use, some pay more than others, and others don't pay at all.

MESC subsidizes food operations

Users of MESC's food-related contracts belong to a group known as Arizona School Partners In Nutrition (ASPIN). These contracts are primarily used by school districts for their breakfast and lunch programs. Members sign an addendum to their agreement with MESC enabling them to purchase from these food-related vendors and pay MESC administrative fees ranging from 0.5 percent to 5.5 percent of purchases, depending on the members' purchasing volume. However, these fees are inadequate to cover the administration costs associated with managing food-related purchases, and ASPIN has consistently operated at a deficit. See Exhibit 4. MESC subsidizes ASPIN's operations with revenue from members not associated with ASPIN. As of June 2001, MESC had used at least $143,721 of monies paid by other members to support ASPIN operations.

Exhibit 4 ASPIN-Related Operating Losses and Equity Deficits Fiscal Years 1998 to 2001

Description	**1998**	**1999**	**2000**	**2001**
Operating losses	(3,606)	(47,129)	(76,966)	(6,317)
Total equity deficits	(93,188)	(115,177)	(130,093)	(44,248)

Source: Mohave Educational Services Cooperative audited financial statements for the years ended June 30, 1998 through 2001.

Some members not assessed fees

For non-ASPIN contracts, MESC charges most members 1 percent of their total purchase or $10 per purchase order, whichever is higher. However, although statute requires that costs be shared based on use, MESC improperly allows Mohave County members to purchase from MESC contracts without paying any associated fee. MESC also allows members of a New Mexico purchasing cooperative to purchase from the contracts without a fee. Consequently, Arizona members not located in Mohave County have subsidized MESC operations.

MESC improperly retains discounts

Some members paid MESC 5 percent of certain purchases.

MESC retains discounts that could be credited to members' accounts or purchase orders, thus increasing the ultimate costs of products to its members. Certain vendors offer a "quick pay" discount ranging from 0.5 percent to 4 percent of the invoice price if payment is received anywhere from 10 to 45 days after the invoice date. However, MESC does not notify all members that the discount is available or that MESC, not the member, will receive the benefit if the member pays within the discount period. MESC received about $60,000 per year in discounts. From a sample of 117 invoices we found that members paid non food-related invoices within the discount period about 26 percent of the time. Even when MESC contract terms required that discounts for payments received after 45 days be reflected in the contract price, MESC retained the discounts. Consequently, considering MESC's standard administrative fee of 1 percent and its retention of up to 4 percent in "quick pay" discount, some members effectively paid MESC up to 5 percent of their non food-related purchases.

FINDING 4

Many of MESC's financial practices violate rules and regulations

Although MESC is subject to Mohave County oversight, rules, and regulations, it has spent its money without regard to the county rules and regulations. Specifically, MESC's merit and personnel practices exceeded parameters within the Mohave County Merit System Rules and Regulations; MESC's travel-related purchases violated Mohave County's travel policy; and MESC officials improperly distributed certain benefits and gifts to themselves, other governmental officials, and vendors.

Excessive salaries and benefits

MESC's merit and personnel practices are not consistent with, and in some cases exceed, the Mohave County Merit System Rules and Regulations. For example, many MESC employees' salaries exceed those of equivalent Mohave County employees; in one case, by as much as 128 percent. In addition, fringe benefits for certain MESC employees exceed those of Mohave County employees. Finally, all MESC employees are given more paid holidays than county employees.

- **Salaries**—Despite less fiscal and administrative responsibility, MESC management salaries surpassed the highest salaries permitted for comparable Mohave County personnel. Exhibit 5 (see page 16) illustrates that MESC employees' salaries greatly exceed comparable Mohave County personnel salaries.

Exhibit 5 Salary Comparison of Comparable Positions
Fiscal Year 2001

MESC		Mohave County		Amount by Which MESC Exceeds Mohave County	
Title	**Salary level**	**Title**	**Maximum salary**	**Amount**	**Percentage**
Executive Director	115,335	County Manager	97,739	17,596	18%
Asst. Executive Director	101,425	Asst. County Manager	44,429	56,996	128%
Chief Financial Officer	115,306	Chief Financial Officer	54,475	60,831	112%
Purchasing Director	80,000	Procurement Officer	48,485	31,515	65%
Associate Director	75,000	Administrative Supervisor	48,485	26,515	55%
Contract Manager	59,789	Buyer Senior	37,336	22,453	60%
Contract Specialist	55,218	Buyer Senior	37,336	17,882	48%
CIS Manager	55,633	Computer Services Coordinator Senior	31,408	24,225	77%
Accounting Manager	51,249	Office Assistant Senior	27,997	23,252	83%
Accounts & Collections	37,809	Office Assistant Clerk	25,688	12,121	47%

Source: Auditor General staff analysis of individual MESC employment contracts for fiscal year 2001 and Mohave County Classification Listing and Job Position Descriptions and Responsibilities.

- **Benefits**—Certain MESC employment contracts include fringe benefits that are not allowable under the Mohave County Merit System. In addition to their participation in the Arizona State Retirement System, three employees receive $5,200 in tax-sheltered annuities every year and have the opportunity to take ownership of an MESC personal computer if it is more than 2 years old. Numerous employees also have at least ten more paid personal days for vacation, sick, or bereavement leave per year than allowed under the Mohave County Merit System Rules.

  One employment contract allows the employee to select a leased vehicle of his choice. Consequently, MESC paid the associated expenses for a Lexus Gs300, and later for a BMW 323ci convertible. For calendar years 1998 through 2000, MESC paid at least $33,611 for these vehicle-related expenses.

- **Holidays**—MESC observes at least 15 holidays per year whereas Mohave County observes only 11.

Travel benefits beyond policy limits

MESC officials spent at least $41,834 from fiscal year 1997 through fiscal year 1999 on food, lodging, and other travel-related purchases that were in violation of Mohave County's travel policy. These purchases were not approved by MESC's governing authority, and MESC had no documentation to support why this travel was an allowable county expense. Examples of improper travel purchases include:

- Numerous purchases for food and lodging even though the employee was in his or her hometown and not traveling. None of these purchases were approved to be "special meals" as required by Mohave County's travel policy.
- Hotel stays that included unnecessary weekend stays.
- An employee reimbursed for playing golf at Tucson resort hotels.
- Meal reimbursements that exceeded Mohave County limits.
- Meals purchased for non-MESC and non-Mohave County employees.
- Receipts that were not retained for many purchases that total over $9,000.

Improper benefits and gifts

MESC officials improperly disbursed certain benefits and gifts to themselves, other government officials, and vendors. Any public purpose that may have been associated with these gifts was not documented or approved by MESC's governing authority.

The Arizona Constitution prohibits the use of public money for private benefit unless that benefit is incidental to a public purpose being served by the expenditure and the public value is not far exceeded by the amount being paid.

MESC spent at least $29,427 during the 5 years from 1997 through 2001 on Laughlin resort hotel dinners, catered suites at Diamondback baseball games, and chartered

The Arizona Constitution prohibits gifting of public funds, including using public money for entertainment and other personal benefits.

The Arizona Constitution, Article IX, Section 7, states: "Neither the State, nor any county, city, town, municipality, or other subdivision of the State shall ever give or loan its credit in the aid of, or make any donation or grant, by subsidy or otherwise, to any individual, association, or corporation, or become a joint owner with any person, company, or corporation, except as to such ownerships as may accrue to the State by operation or provision of law."

Attorney General Opinion I85-051 states in part: "While public funds may not be loaned or given to private individuals or entities, an incidental private benefit is not prohibited by Article IX as long as there is a public purpose served by the expenditure or loan of funds and the value to be received by the public is not far exceeded by the consideration being paid."

scenic tours for MESC employees and their families. Employees reimbursed MESC $1,931 for family members attending the events. The total of $29,427 includes costs associated with travel, meals, and admission fees for the featured event. No costs were identified by MESC for any type of training, such as educational speakers. The public purpose was not identified and the cost appears to greatly exceed any benefit to the public.

Other questionable purchases include gift certificates to Dillard's department store and restaurants at Bank One Ballpark, in addition to flowers and candy for a total of $1,683. These items were given to other county and school district employees.

FINDING 5

Some of MESC operations are improper

MESC officials engage in some business practices that are improper or outside of their lawful authority. MESC unlawfully holds title to real property and fails to comply with certain parts of the *Uniform Accounting Manual for Arizona Counties*.

- **Unlawful property ownership**—MESC has no authority to own property. However, as shown in Exhibit 6, it holds title to three real properties in Kingman valued at $274,886.

  Although MESC filed documents with the Mohave County Recorder's Office listing MESC as owner, no statutory authority exists that enables a department, subdivision, or service program of a county created by the county school superintendent to hold title to real property. Any property purchased by MESC should be titled in the name of Mohave County.

Exhibit 6 MESC-Owned Kingman Properties

Location	Purchase Price
625 E. Beale Street	$122,800
631 E. Beale Street	$64,313
211 N. 7th	87,773
Total	$274,886

Source: First American Title Insurance Agency of Mohave, Inc. escrow documents.

  Furthermore, MESC improperly insures property and other items described in Exhibit 7 (see page 20) through the Arizona School Risk Retention Trust in the name of Mohave County District No. 31. However, MESC is neither a school nor a school district, and A.R.S. §11-251(15) empowers only the County Board of Supervisors to insure this property in the name of and for the benefit of the county.

- **UAMAC noncompliance**—MESC does not follow provisions of the *Uniform Accounting Manual For Arizona Counties* (UAMAC) related to revolving funds and assets disposal. The UAMAC was developed in accordance with A.R.S. §41-1279.21 to develop a uniform system of accounting for counties. The

Exhibit 7 Property MESC Insured Through Arizona School Risk Retention Trust Fiscal Year 2001

Description	Value
Business office contents, 400 W. Camelback, Phoenix	$ 23,000
Business office contents, 4730 N. Oracle, Tucson	29,000
Conference center building, 631 E. Beale, Kingman	90,000
Conference center contents, 631 E. Beale, Kingman	50,000
Business office building, 625 E. Beale, Kingman	515,000
Business office contents, 625 E. Beale, Kingman	464,000
Ford Windstar, 1998	23,737
Lexus Gs300, 1998	39,575
BMW 323ci, 2000	41,910
Nissan Maxima SE, 2000	28,716
Nissan Maxima SE, 2000	28,716
Total	$1,333,654

Source: Arizona School Risk Retention Trust, Inc. "*Report of Values and Additional Information*."

County Board of Supervisors is primarily responsible for establishing internal control structure policies and procedures for all county departments; however, in at least two respects, MESC does not abide by procedures outlined in the UAMAC. Specifically, MESC improperly established a revolving fund and improperly disposed of assets.

- Revolving fund—MESC did not seek approval from the Mohave County Board of Supervisors when establishing its revolving fund, as required by UAMAC VI-C-10. MESC used the revolving fund for various expenditures including gifts, reimbursements, and restaurant meals.

  In addition, one employee signed revolving fund checks made payable to himself. Having both physical control and endorsement responsibility causes an inadequate segregation of duties. Proper separation of asset custody and authorization duties among employees is critical to deter fraud and concealment of errors and helps ensure the integrity and propriety of transactions.

- Asset disposal—MESC disposes of assets without approval from the Mohave County Board of Supervisors as required by UAMAC VI-E-3.7. MESC has autonomously traded, sold, donated, or otherwise disposed of numerous assets such as cars, computers, scanners, and other electronic equipment.