January 26, 2021

This is a complaint regarding the financial and regulatory relationship between ASU Prep Charter Schools and Arizona State University:

1. The lack of oversight by ASU as the charter sponsor of ASU Preparatory Academies
2. The lack of operational and financial decision making provided the ASU Prep Board of Directors
3. The inappropriate financial and managerial role ASU maintains in the operations of ASU Prep

Arizona State University is the sponsor of twelve ASU Prep charter schools, the only charter schools in Arizona that are not authorized and regulated by the Arizona State Board for Charter Schools (ASBCS). ASBCS is guided by 19 pages of rules and regulations in Title 7 Chapter 5 of the Arizona Administrative Code in addition to Arizona Revised Statues pertaining to charter schools and multiple ASBCS polices. ASU has no such rules or policies governing their role as a charter school sponsor.

**The lack of oversight by ASU as the charter sponsor of ASU Preparatory Academies**

ARS 15-182(R) requires that sponsoring entities provide oversight and administrative responsibility for the charter schools that they sponsor. Based on publicly available information at the Board of Regents, ASU, and ASU Prep websites, there are no rules and regulations regarding ASU’s role in oversight and administrative responsibility for the operation of ASU Prep. The ASU Prep website (<https://asusponsor.asu.edu/>) simply states that *“... Arizona State University serves as an authorizing agency for charter schools in Arizona. ASU oversees the application and review process and monitors school performance once a charter is established.”* There is no information on the ASU Prep website about who at ASU reviews and monitors ASU Prep and what policies and procedures guide that process. The Arizona State Board of Regents and ASU policy manuals make no mention of policies governing ASU’s sponsorship of charter schools.

By tracing the ownership of ASU Preparatory Academy, we found that ASU employees Jose Cardenas and James Rund are listed by the Corporation Commission as principals in the non-profit company. Mr. Cardenas is ASU Senior VP General Counsel and Mr. Rund is the Senior VP for the Educational Outreach and Student Services division of ASU. The website for this division includes a link to ASU Prep, indicating that ASU Prep falls under the supervision of the ASU Educational Outreach Division. There is no mention of Educational Outreach’s relationship with ASU Prep on any ASU Prep website.

ASU policy for affiliated entities, such as ASU Prep, states that two ASU employees must be on the entity’s corporate board. It is questionable that a corporate board member of ASU Prep is the head of the ASU division that apparently sponsors and provides oversight for the charter schools.

There are many statutory requirements for charter sponsors that require rules and procedures to implement:

* Assuring schools notify parents when a school receives a “D” of “F” rating (ARS 15-241)
* Requiring failing schools to present an improvement plan to the charter sponsor in an open meeting (ARS 15-241.02(C)).
* Conducting a five-year review of each charter school (ARS 15-183(I)(3).
* Assuring that all school employees have current fingerprint clearance cards. (ARS 15-183, 15-512)
* Assuring that charter schools obey open meeting laws, are in good standing with regulatory bodies, and that special education screenings and IEPs are on file and all special education instruction is provided by certified teachers.
* The establishment of procedures to conduct administrative hearings on determination by the sponsor that grounds exist to revoke a charter (ARS 15-183(Q).
* An audit review of average daily membership as required by ARS 15-914(G) *“Every audit contract shall include a systematic review of average daily membership, as defined in section 15-901, using methodology that is consistent with guidelines established by the auditor general. “*

ASBCS requires every annual charter audit to include a Legal Compliance Questionnaire, completed by the auditor, to ensure that issues such as these, and other legal issues, have been properly addressed. ASU Prep audits have no such compliance assurance.

ASU utilizes a Performance Framework that does not address the above regulatory issues when evaluating the schools. The Performance Framework rating for each school is not available to the public. The 2020 ASU Annual Charter Sponsor Report submitted to the Auditor General (that is not available anywhere online) indicates that all ASU Prep schools met Financial and Operational Performance standards but that four schools did not meet Academic Performance Standards in 2020. The actual ratings for each school on the specific elements of the three performance indicators is not available to the public. ASU Prep annual audits, sponsor staff, and policies are not publicly available as well. Transparency is almost non-existent in the University’s supervision of ASU Prep.

The lack of University supervision at ASU Prep is evident by the errors and omissions that dominate their 2020 Annual Financial Reports, School Level Reports, and the Classroom Site Fund Narratives:

1. All ASU Prep schools submitted identical 2020 School Level Financial Reports for all schools, with the same revenue and expenditures that in no way reflect the actual revenue and expenditures of each school as disclosed on 2020 Annual Financial Reports.
2. ASU Prep South Mountain Middle did not disclose the number of teachers or teacher salaries on their 2020 Annual Financial Report (AFR).
3. The following ASU Prep schools did not disclose special education certified salaries in their 2020 AFRs. IDEA requires certified teachers to deliver all special education instruction.
   1. Phoenix Elementary
   2. South Mountain Elementary
   3. Poly Elementary
   4. Tempe High School
   5. Digital
4. Capital assets do not appear to be accurately disclosed at:
   1. Phoenix Middle $0
   2. Phoenix Elementary $10,456
   3. Phoenix High School $5,128
5. ASU Prep codes all Classroom Site Funds in the Instruction lines on pages 3 and 4 of each AFR. Based on the CSF Narratives submitted by each school, ASU Prep universally gives CSF bonuses to counselors, social workers, and dean of students that are not instructional expenses and are not allowed by statute to receive CSF.
6. Classroom Site Funds cannot supplant existing funding according to ARS 15-977. As ASU as downsized the number of teachers in 2020, the percentage of teachers’ salaries paid for by CSF doubled. For example, 12% of Phoenix Elementary teacher salaries were paid for with CSF in 2019. In 2020 that percentage doubled to 24%. $57,418 was awarded in CSF performance pay to 24 teachers at Phoenix Elementary in 2019 for an average of $2,392/teacher. $125,490 was awarded to 19 teachers in 2020, a $6,604/teacher average. Phoenix Elementary, and all ASU Prep schools, used fewer existing funds for teacher salaries by supplanting with Classroom Site Funds in 2020, a violation of law.

ASU Prep is required by ARS 15-183(E)(6) to provide annual audits to its University sponsor. ASU has consistently failed to verify the accuracy of these audits in their regulatory role. ASU Prep 2018 and 2019 audits failed to disclose $21 million in loans provided by the University and the existence of a $6 million receivables loan from Charter School Capital. ASU’s General Counsel approved these loans as a member of the ASU Prep Board of Directors, but the University failed to notice their absence in audit documents. (Loan details are on page 5)

**The ASU Prep Board of Directors failure to manage the schools, allowing the inappropriate financial and managerial role ASU maintains in the operations of ASU Prep**

The failure to disclose financial transactions with ASU in ASU Prep audits raises major concerns regarding the blurring of roles between the operation and finances of ASU Prep and the University, in conflict with ASU’s role as a sponsor/regulatory agent and ASU policies on relationships with affiliated entities. For example:

1. According to ASU Prep board meeting minutes on March 16, 2017, ASU loaned ASU Prep $9 million at 2.5% interest to remodel ASU Prep Poly High School. The loan has never been disclosed on audits or annual financial reports and no payments have been made on the loan.
   1. ASU actually contracted and built Poly High School in 2018, not ASU Prep. (See Exhibit 1) There is no indication in ASU Prep audits that the loans were canceled or that ASU is leasing the new Poly HS to ASU Prep.
2. On May 1, 2018 the ASU Prep board approved” *the debt service on the internal loan from ASU in the amount of $12M in support of ASU Prep Digital expansion. The terms of the loan are 15 years at 2.5% interest.”*
   1. ASU Prep Digital opened August 2017 and reportedly had 1,200 students in the first month of school. The 2017-18 budget for Digital submitted by ASU Prep was $562,582 but they ended up spending over $6 million by the end of the school year, while receiving only $288,000 per pupil from the state. ASU Prep Digital did not receive the $12 million loan until the end of the 2018 school year. The University obviously was operating ASU Prep Digital throughout the 2018 school year and belatedly funded it through a questionable loan to ASU Prep after the school year was over.
   2. ASU opened ASU Digital Prep in 2017 -2018 primarily using University funds with no involvement from the ASU Prep or their Board of Directors. According to the Digital 2018 AFR, $3.8 million in equipment was purchased, 49 teachers were hired, and $3.8 million was spent on administration – all with no involvement from the ASU Prep Board.
   3. There is no disclosure of the ASU loan to ASU Prep Digital on any audit or annual financial report 2018-2020.
3. ASU policy FIN 130 defines the services the university can provide to affiliated entities – providing loans and operating the affiliated entity is not included:

*“Services may include use of university space, equipment, furniture, and administrative/financial services and staff in the performance of the affiliated entity’s functions and such other rights, services, or benefits that ASU may authorize.”*

1. The Board of Directors of ASU Prep represents both the corporate board and the school board for the schools (7/9/13 Board minutes) yet the Board hires no employees for ASU Prep, including the Managing Director (superintendent) and CFO.
   1. The Managing Director of ASU Prep is Julie Young, a vice president of the Educational Outreach and Student Services division of ASU.
   2. The Chief Financial Officer of ASU Prep is ASU employee John Kemper
   3. The Head of Schools for ASU prep Digital is Amy McGraph, an ASU VP of Educational Outreach
2. The ASU Prep board has discussed their role in hiring in a board meeting held on October 1, 2013, expressing concerns that the Board had no control over hiring:

*"Discussion took place when Jose Cardenas (ASU General counsel and ASU Prep board member) asked if it is necessary that this Board approve staffing-related items. Beatiz Rendon explained that the prior Governing Board used to approve staffing decisions; Deborah Gonzales suggested that possibly the authorizing agent was to approve. Beatiz confirmed that staffing is not the responsibility of the authorizer; however, she will look into what role the current Corporate Board has with regards to staffing. George Dean suggested that the item be moved to the information section. Review will take place and the Board will be updated. Motion carried 8-0*

Since that meeting, all staff hiring has been presented to the board only in the information section of board meetings. The University hired Julie Young to run the affiliated entity without approval from the ASU Prep Board of Directors.

The head of ASU’s Educational Outreach Division is James Rund, who is also on the ASU Prep board. It appears that he and his vice presidents, along with the University’s chief counsel, have control of ASU Prep hiring, and perhaps all operations – as well as the conflicting regulatory role as sponsor.

1. According to Prep audits, ASU donated $6 million in 2018 and $13,317,656 in 2019 to ASU Prep, in addition to $6,177,297 in-kind expenditures. The ASU Prep board never acknowledged the donations.
   1. The ASU Prep governing board approved submission of revised 2019 budgets on April 30, 2019 – the end of the school year. The revised budgets declared total local revenue of $53,150 but actual 2019 local revenue was reported as $21,281,378 (including the ASU donations) in the schools’ Annual Financial Reports. Total M&O spending in the revised budgets was $26,281,378 while actual M&O expenditures totaled $45,595,114 in the AFRs.
      1. The Board approved 2019 revised budgets that had no relationship to actual spending and did not budget for the additional $13 million, despite the presence of the university general counsel and the VP in charge of sponsorship on the Board.
   2. The $13.3 million donation in 2019 is significant, amounting to half of all ASU Prep budgeted expenditures in 2019. Safford Unified District, with the same enrollment as ASU Prep, only expended $17 million total for M&O in 2020. ASU Prep spent $45 million with the addition of the ASU donation.
   3. ASU Prep recorded the highest administrative expenses of any district or charter school in the state fueled by massive ASU donations in 2019. ASU Prep spent $4,596/pupil on total administration in 2019, up from $1,596/pupil in 2017 while the state charter average was $1,620/pupil and the district average was $778/pupil for administration in 2019.
   4. In 2019 enrollment increased by 433 students (16%) from 2018. The number of employees, according to IRS 990 submissions, increased by 169 (41%) over 2018.
   5. The infusion of $21 million in donations by ASU in 2018 and 2019 went primarily to administrative spending.
      1. Administrative spending was $3,000/pupil more in 2019 than in 2017
      2. Instructional spending only increased by $885/pupil in the same time period
   6. The creation of ASU Prep Digital required extensive start up costs but excluding Digital expenses, administrative spending still increased $2,360/pupil 2017-2019 as a result of the ASU donations
   7. The ASU Prep central office had 29 people in March 2020 including a Student Wellness Director, 9 finance and 2 public relations staff members serving a system of 3,100 students. Safford Unified has the same enrollment and have just 13 district level employees.
   8. The Safford Unified superintendent made $118,037 in 2019. ASU Prep had six administrators making over $100,000, averaging $159,000/year. The ASU VP Director in charge of the schools made $260,000 and the ASU VP Head of Schools made $207,927 in 2019.
   9. ASU Prep spent $13,502,246 for purchase services according to their 2019 AFRs. The 2019 ASU Prep consolidated IRS 990 submission listed five companies where they purchased over $100,000 in services totaling $2,060,066. The only other source for the remaining $11 million in purchase services is from ASU. It seems ASU Prep spent the majority of the $13.3 donation from ASU by buying unspecified services from the University that were not disclosed in the 2019 990 submission.
   10. Despite the infusion of millions of dollars by ASU in 2018-19, the ASU Prep Board sought out a receivables and payments loan from Charter School Capital for $6 million on November 15, 2018, with the initial $3 million in funding to be used to pay off the current line of credit at Chase Bank. This type of loan uses the monthly state aid payments as collateral and is typically used by charters in dire financial difficulty – a “payday loan “for charter schools that have exhausted their lines of credit. If ASU Prep had access to any of the $13.3 million in ASU donations there would be no need for such a desperation loan. This loan was not disclosed in the 2019 ASU Prep audit.

ASU Prep is an “affiliated entity” by ASU definition and not a subsidiary of the University. ASU policy FIN 130 states that ASU may pay affiliated entities for services or make goods or services available on an in-kind basis, but may not transfer ASU funds to the affiliated entity:

***ASU Services for Affiliated Entity***

***“Affiliated Entity—ASU Monetary Transfers*** *All transfers of funds between the affiliated entity and ASU must be pursuant to written policy. Except for transfers for appropriate consideration and other transfers permitted by law, there will be no transfers of funds by ASU to the affiliated entity.”*

1. **ASU stopped donations to ASU Prep in 2020. As a result, school instructional spending was cut in half in 2020, declining from $5,203/pupil in 2019 to $2,595/pupil in 2020. Administration spending also plummeted in 2020 decreasing by $3,293/pupil. ASU Prep spent $9.5 million more on administration in 2019 than in 2020 – while enrollment increased by 700 students. Discounting the high costs at ASU Digital, administration spending in 2019 was still $5 million more than in 2020.**
2. **When the 2020 budgets were adopted at the June 25, 2019 board meeting, CFO John Kemper only informed the Board that revenue would be $37.6 million and expenditures would be $37.4 million, with a 5% expected increase in enrollment. There was no mention in any ASU Prep board meeting minutes during the 2018-19 school year of how to spend the huge windfall donation of $13.3 million from the University. Likewise, 2019-20 Board minutes never addressed the drastic reduction in instructional spending, cutting the teaching staff from 211 teachers to 158 teachers, or cutting $9.5 million in administrative costs caused by the withdrawal of University donations. Not a word.**

**ASU Prep spending $9.5 million more in administration in 2019 than in 2020 points to possible fraud. Since the ASU Prep Board of Directors acted as if the $13.3 million ASU donation did not exist, it brings into question how ASU came to have such a large sum to donate and if the funds were actually spent on behalf of the charter schools or were comingled with ASU operations.**

**The ASU Prep board appears to have no role or interest in the actual operations of ASU Prep. The real management of ASU Prep is conducted by the University in conflict with ASU policy FIN 130 on affiliated entities and is an inappropriate role for a charter school sponsor as a regulatory body.**

***No Agency, Partnership, or Joint Venture*** *The affiliated entity is not the agent of ASU and shall not represent or imply that it operates under an agency, partnership, or joint venture relationship with ASU. Although ASU has approved the nonprofit corporation as an affiliated entity and the purposes of the affiliated entity, and although ASU may pay the affiliated entity for services or make ASU goods or services available on an in-kind basis, the affiliated entity is not controlled by ASU and the affiliated entity has no authority to act for or to obligate ASU. All contracts and other relationships with third parties will be solely in the name of the affiliated entity.*

The transfer of $13.3 million dollars to ASU Prep in 2019 as a donation that was never acknowledged by the Board of Directors, is in violation of ASU policy, and could be considered a money-laundering operation between the university and its sponsored affiliated entity – perhaps providing administrative jobs that overlap both entities. It is inconceivable that 169 new employees were hired at ASU Prep in 2019 based on a one-time donation. University financial statements and audits do not detail revenue and expenditures for associated entities, so the $13.3 million is basically unaccounted for and may have been misappropriated.

ASU loans of $21 million to ASU Prep that were never disclosed and now seem to have disappeared. The funds were apparently used by the University to create a digital platform that benefitted the ASU program and to build a new ASU building on the Polytechnic Campus in Mesa. The ASU Prep Board of Directors had no role in either of these projects.

The only transparency in the supervision (or lack of) by ASU and the operations of ASU Prep are in the Board of Director meeting minutes that are available on the Prep website. (<https://asuprep.asu.edu/governance>). Annual audits required by law are not available online from ASU Prep and public records requests dating back to March 2020 have been ignored. (See Exhibit 2)

ASU Prep is required to operate independently from ASU and the University is required to provide supervision, transparency, and regulation for the charter schools they sponsor. The failure to achieve these ends is resulting in the mismanagement of public funds and violation of state statutes and University policies.

Recommendations:

1. The ASU Audit and Advisory Services department and the Auditor General need to conduct a complete audit of ASU Prep finances in 2018 and 2019 to determine if University funds were misallocated:
   1. Determine how $14.5 million was spent on administrative costs in 2019 for a charter school system of 3,100 students.
   2. Determine how over $9.5 million in administrative costs were eliminated in 2020.
   3. Examine the two loan documents between ASU and ASU Prep for the construction of ASU Prep Poly HS and ASU Prep Digital expenses to determine, if they exist, why they were not disclosed on financial statements and why repayment has not begun.
   4. Determine why the ASU Prep found it necessary to take out a $6 million receivables loan despite the $13.3 million ASU donation in 2019 and why that loan was never disclosed in financial statements.
   5. Determine why 2018 and 2019 ASU Prep 990 submissions did not include purchase services paid to ASU and why $21 million in loans from ASU and the $6 million receivables loan were not disclosed.
2. The Provost Office needs to investigate the ASU Educational Outreach Division to determine:
   1. If there are policy violations regarding the transfer of $13.3 million in University funds to an affiliated entity.
   2. Examine ASU’s financial relationship with an affiliated entity they are supposed to regulate as a charter sponsor.
   3. Determine if the Educational Outreach Division is regulating ASU Prep as a sponsor or if it is acting as an unauthorized charter management company – making all operational decisions for the charter schools.
3. The Arizona State Board of Regents needs to establish policies and procedures for universities that sponsor charter schools and the monitor sponsor’s regulatory activities. Rules and regulations like those of Title 7 Chapter 5 of the Administrative Code are needed to assure that university charter schools are fulfilling the requirements of state law.
4. The Arizona State Legislature should pass HB2149 that would require all charter schools to be sponsored by ASBCS based on the total lack of regulation currently provided by university sponsored charter schools.
5. The Arizona Ombudsman needs to require ASU Prep to respond to public records requests as required by law.

A complaint regarding the failure to disclose ASU loans and the Charter School Capital loan in 2018 audits by auditor Fester and Chapman of will be submitted to the Arizona State Board for Accountancy.

Jim Hall

Arizonans for Charter School Accountability

CC:

* Lisa Grace - Executive Director ASU Audit and Advisory Services
* James Rund - Senior VP ASU Educational Outreach
* Cheryl Hyman - VP for ASU Academic Alliances
* Joanne Anderson - ASU Director of Fiscal Operations
* Dena Clark - ASU Director of Business Operations
* John Arnold - Executive Director Arizona Board of Regents
* Helen Baxendale - Board of Regents Director of Academic Affairs and Policy
* Donna Miller - Office of the Auditor General Director of Financial Audits
* Michelle Udall - Chairman House Education Committee
* Paul Boyer - Chairman Senate Education Committee
* Public Monies Complaint - Arizona Office of the Attorney General

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**Exhibit 1 – Design RFP for Design Services for ASU Prep Poly High School**

Graphical user interface, text, application, email

Description automatically generated

**Exhibit 2 - Public records requests filed on ASU Prep website on March 21, 2020 and January 8, 2021 by Arizonans for Charter School Accountability**

ASU Preparatory Academy via ASU Preparatory Academy <eoss@asu.edu>

Submitted on Saturday, March 21, 2020 - 12:06pm

Submitted by anonymous user: 70.166.126.184

Submitted values are:

First name: Jim

Last name: Hall

Address: 10057 N 39th Ave. Phoenix, AZ 85051

Email:: arizcsa1000@gmail.com

Records requested: :

Arizonans for Charter School Accountability requests:

- 2018 and 2019 Audits for ASU Preparatory Academy (second request)

- Transfer contract between ASU Prep and Phoenix Collegiate Academy

- Charter application and contract for ASU Prep Digital approved 07-01-2017

- Five-year reviews for ASU Prep Phoenix Elementary, Middle, and High School

pursuant to ARS 15-183(H)(3)

- Academic, operational, and financial performance framework for ASU Prep

Phoenix Elementary 2018

- Copy of the letter sent to parents and the ASU Board minutes documenting

the submission of an improvement plan by ASU Prep South Phoenix High School

when receiving a 2019 "D" grade pursuant to ARS 15-241.02 C.

- ASU policies and procedures for sponsoring charter schools

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| Submitted on Friday, January 8, 2021 - 9:39am Submitted by anonymous user: 2001:579:8014:8b:b9e4:45c0:cd40:9697 Submitted values are:  First name: : Jim Last name: : Hall Address: : 10057 N. 39th Ave. Phoenix, AZ 85051 Email: : [arizcsa1000@gmail.com](mailto:arizcsa1000@gmail.com) Records requested: : The following records were requested by Arizonans for Charter School Accountability on March 21, 2020 that were never received and the request was not acknowledged. We are also requesting a copy of the ASU Prep 2020 audit. If these records are not provided in a timely manner, The Ombudsman Office will be contacted.  ASU Preparatory Academy via ASU Preparatory Academy  Submitted on Saturday, March 21, 2020 - 12:06pm Submitted by anonymous user: 70.166.126.184 Submitted values are:  First name: : Jim Last name: : Hall Address: : 10057 N 39th Ave. Phoenix, AZ 85051 Email: : [arizcsa1000@gmail.com](mailto:arizcsa1000@gmail.com) Records requested: :  Arizonans for Charter School Accountability requests:      - 2018 and 2019 Audits for ASU Preparatory Academy (second request) - Transfer contract between ASU Prep and Phoenix Collegiate Academy - Charter application and contract for ASU Prep Digital approved 07-01-2017 - Five year reviews for ASU Prep Phoenix Elementary, Middle, and High School pursuant to ARS 15-183.H.3 - Academic, operational, and financial performance framework for ASU Prep Phoenix Elementary 2018 - Copy of the letter sent to parents and the ASU Board minutes documenting the submission of an improvement plan by ASU Prep South Phoenix High School when receiving a 2019 "D" grade pursuant to ARS 15-241.02 C. - ASU policies and procedures for sponsoring charter schools |