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FOR RELEASE _____ September 8, 2009 _____

Auditor of State David A. Vaudt today released a special report on the Former Russell Community School District for the period July 1, 2007 through June 30, 2008. The Iowa Department of Education requested the Auditor of State's assistance in performing a final reconciliation by fund for all funds of the Former District, reviewing and testing the propriety of selected expenditures made by the Former District and determining whether an equalization levy is necessary.

As a result of the procedures performed, Vaudt determined the Former District transferred \$300,000 of local option sales tax revenue from the Capital Projects Fund to the General Fund and used the \$300,000 to pay salaries and other General Fund bills. Expenditures for salaries and most of the General Fund bills paid from local option sales tax revenue are not an allowable use of the local option sales tax revenue since these expenditures are not school infrastructure and, accordingly, would not meet the statutory requirements of Chapter 423E.1 of the Code of Iowa at the time of payment.

Pursuant to Chapter 11.15 of the Code of Iowa, copies of this report have been filed with the Lucas County Attorney for review and determination of further action, if any. Copies of the report have also been filed with the Great Prairie Area Education Agency and the Iowa Department of Management.

A copy of the report is available for review in the Great Prairie Area Education Agency Business Office, in the Office of Auditor of State and on the Auditor of State's web site at <http://auditor.iowa.gov/specials/specials.html>.

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FORMER RUSSELL COMMUNITY SCHOOL DISTRICT

**INDEPENDENT ACCOUNTANT'S REPORT ON
APPLYING AGREED UPON PROCEDURES**

**FOR THE PERIOD
JULY 1, 2007 THROUGH JUNE 30, 2008**

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Independent Accountant's Report on Applying Agreed Upon Procedures

To the Iowa Department of Education:

We have performed the following procedures, which were agreed to by the Iowa Department of Education (Department), for the Former Russell Community School District (Former District) for the period July 1, 2007 through June 30, 2008 and subsequent period, as noted, solely to assist you in performing a final reconciliation by fund for all funds of the Former District, to review and test the propriety of selected expenditures made by the Former District and to assist in determining whether an equalization levy is necessary. The Department requested our assistance as a result of the Department's action on or about March 11, 2008 to remove accreditation from the Former District. The Former District's management is responsible for compliance. This agreed upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the Iowa Department of Education. Consequently, we make no representation regarding the sufficiency of the procedures described below, either for the purpose for which this report has been requested or for any other purpose.

The procedures we performed are as follows:

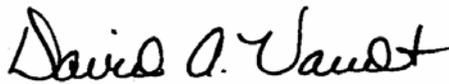
1. Reviewed Former District minutes from July 1, 2007 through June 30, 2008 to identify and/or determine contracts, agreements, obligations and other potential or contingent liabilities as of June 30, 2008.
2. Obtained and reviewed the Former District's Certified Annual Report (CAR) for the year ended June 30, 2008 prepared by Great Prairie Area Education Agency personnel.
3. Obtained and reviewed year-end fund balance reconciliations by fund for all funds of the Former District prepared by Great Prairie Area Education Agency personnel.
4. Confirmed all bank balances and investments of the Former District as of June 30, 2008 and as of February 24, 2009, the starting date of our field work.
5. Reviewed and tested selected expenditures for propriety and payment from appropriate funds of the Former District.
6. Obtained schedules and reviewed the Former District's receivables, short-term and long-term liabilities, including capital leases, judgments and claims, compensated absences and termination benefits, if any.
7. Obtained and reviewed the Former District's capital asset schedules and performed limited testing of the schedules.

Based on the performance of the procedures described above, we identified instances of non-compliance and have developed various recommendations for the Department. Our recommendations and the instances of non-compliance are described in the Detailed Findings section of this report. Unless reported in the Detailed Findings, no items of non-compliance were noted during the performance of the specific procedures listed above.

We were not engaged to and did not conduct an audit of the Former Russell Community School District, the objective of which would be the expression of an opinion on the financial statements of the Former Russell Community School District. Accordingly, we do not express such an opinion. Had we performed additional procedures, or had we performed an audit of financial statements of the Former Russell Community School District, other matters might have come to our attention that would have been reported to you. Pursuant to Chapter 11.15 of the Code of Iowa, copies of this report have been filed with the Lucas County Attorney for review and determination of further action, if any. Copies of this report have also been filed with the Great Prairie Area Education Agency, the Iowa Department of Management, the Iowa Public Employees Retirement System, the Internal Revenue Service and the Iowa Department of Revenue.

This report, a public record by law, is intended solely for the information and use of the Iowa Department of Education and the officials, employees and citizens of the Former Russell Community School District and other parties to whom the Former Russell Community School District may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the assistance extended to us by personnel of the Iowa Department of Education and the Great Prairie Area Education Agency. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.



DAVID A. VAUDT, CPA
Auditor of State



WARREN G. JENKINS, CPA
Chief Deputy Auditor of State

August 13, 2009

Detailed Findings

Former Russell Community School District

Detailed Findings

For the Period July 1, 2007 through June 30, 2008

- (A) Personnel Records – We requested access to the Former District's personnel and payroll records. However, according to Great River Area Education Agency personnel, the records obtained from the Former District did not include any individual employee personnel files or individual employee contracts. Also, according to Great River Area Education Agency personnel, all employees were paid in full as of June 30, 2008. Due to the missing personnel files and individual employee contracts, we were unable to test and/or verify the propriety of wages paid to employees of the Former District, including allocations of wages and related benefits charged to various categorical funding programs of the Former District.

In addition, due to the absence of contracts for certified staff or other documentation, we were unable to verify or determine the propriety of the \$37,481 reserved for teacher quality and \$978 reserved for teacher mentoring at June 30, 2008.

Recommendation – The Former District was responsible for compliance and for maintaining complete and accurate financial records to properly account for the receipts, disbursements and balances remaining, if any, for all funds of the Former District. The Former District has not demonstrated compliance with the receipt and expenditure of categorical funding by the Former District and we question the propriety of the \$37,481 reserved for teacher quality and \$978 reserved for teacher mentoring. The Department should review and determine the proper disposition of this issue, including consulting legal counsel regarding the propriety of the amounts reserved for teacher quality and teacher mentoring.

- (B) Superintendent's Compensation – According to the invoices and related payments, the Former District paid Robert McCurdy on a contractual basis for serving as the Former District's Superintendent. From July 1, 2007 through November 30, 2007, Mr. McCurdy received \$750 or \$1,350 per month for professional services, a total of \$5,500, which was paid to Sharon and Associates, an entity controlled by Mr. McCurdy's wife. A December 2007 check for \$1,350 was voided. We were unable to determine the reason for the variance in monthly check amounts or why the December 2007 check was voided. In addition, the Former District paid \$13.94 each month during this six month period, a total of \$83.64, for long-term disability and life insurance for Mr. McCurdy.

In January 2008, the Former District began paying \$1,376.39 per month for long-term disability, life insurance and family health insurance coverage for Mr. McCurdy in lieu of the monthly professional services payments of \$750 or \$1,350. Payments of \$1,376.39 were made from January 2008 through June 2008, a total of \$8,258.34. **Exhibit 1** summarizes the payments made on behalf of Robert McCurdy.

The monthly payments to Sharon and Associates for professional services were included in the list of bills payable. However, the Board minutes of the Former District did not include documentation of the Board's approval of the agreement(s) with Mr. McCurdy, including payment as an independent contractor or the amount(s) approved, Board approval to pay long-term disability and life insurance

or the change to pay monthly family health insurance in lieu of professional services payments. As previously noted, personnel records, including employment contracts, were not available.

Recommendation – Chapter 279.20(1) of the Code of Iowa states, in part, “The board of directors of a school district may employ a superintendent of schools for a term of not to exceed three years.” Chapter 279.23(1) of the Code of Iowa provides “Contracts with administrators shall be in writing” and the contracts shall include certain specified terms and conditions.

While we do not question whether Robert McCurdy provided professional services to the Former District, according to the Internal Revenue Service (IRS) and IRS Form SS-8, individuals typically may not be paid as "independent contractors" while also receiving "employee benefits". We were unable to determine the propriety of the payments made to Sharon and Associates, an entity controlled by Mr. McCurdy's wife, for professional services provided by Robert McCurdy as an independent contractor during the period July 1, 2007 through December 31, 2007 while the District also paid employee benefits for long-term disability and life insurance. Due to the unclear nature of Mr. McCurdy's employment status with the Former District, we also question the propriety of payments made by the Former District on behalf of Robert McCurdy for long-term disability, life insurance and family health insurance during the period January 1, 2008 through June 30, 2008. As a result, copies of this report have been filed with the Internal Revenue Service and the Iowa Department of Revenue.

In addition, because of the potential implications pertaining to Mr. McCurdy's retirement benefits, a copy of this report has also been filed with the Iowa Public Employees Retirement System.

- (C) Transfer – According to the Former District's "Unofficial" Board minutes dated June 19, 2008, the Former District Board of Education approved a "Resolution to transfer funds from PPEL and SILO fund(s) to General Fund for the amount of what is needed to pay all salaries and bills by July 1, 2008." As a result, the Former District transferred \$300,000 from the Capital Projects Fund (local option sales tax) to the General Fund in June 2008. Effectively, this transfer created an interfund loan.

Local option sales tax may only be used for school infrastructure.

Chapter 423E.1 Code of Iowa applicable for fiscal year 2008 states, in part, "*school infrastructure*" means those activities for which a school district is authorized to contract indebtedness and issue general obligation bonds under section 296.1, except those activities related to a teacher's or superintendent's home or homes. These activities include the construction, reconstruction, repair, demolition work, purchasing, or remodeling of schoolhouses, stadiums, gyms, fieldhouses, and bus garages and the procurement of schoolhouse construction sites and the making of site improvements and those activities for which revenues under section 298.3 or 300.2 may be spent. A school district that uses local sales and services tax moneys for school infrastructure shall comply with the state building code in the absence of a local building code. Additionally, "*school infrastructure*" includes the payment or retirement of outstanding bonds previously issued for school infrastructure purposes as defined in this subsection, and the payment or retirement of bonds issued under section 423E.5."

Expenditures for salaries are not an allowable use of the local option sales tax revenue. In addition, payment of most other General Fund bills, including instruction, maintenance or other operational expenditures, would also not be allowable since these would not meet the statutory requirements of Chapter 423E.1 of the Code of Iowa during fiscal year 2008.

We are not aware of any statutory basis for the District to authorize a transfer or change the legal use of local option sales tax revenue since expenditure of local option sales tax revenue is governed by the requirements of Chapter 423.E of the Code of Iowa and the referendum approved by the voters of the Former District.

The Former District's individual fund balance reconciliations as of and for the years ended June 30, 2007 and June 30, 2008 are included as **Exhibit 2**. The fund balance reconciliation and Certified Annual Report for the year ended June 30, 2008 were prepared by Great River Area Education Agency personnel. The fund balance reconciliations in **Exhibit 2** are not affected by the interfund loan from the Capital Projects Fund to the General Fund as of June 30, 2008. As of June 30, 2008, the Former District had a General Fund negative fund balance of \$309,907.

Recommendation – The Department should consult legal counsel and determine the proper disposition of the transfer of local option sales tax from the Capital Projects Fund to the General Fund.

- (D) Auction Proceeds – In July 2008, an auction was held to dispose of various assets of the Former District. According to the auctioneer's statement, the auction proceeds totaled \$14,461.00, resulting in a net check, after payments for advertisements, commissions and other expenses, of \$11,630.25. The net auction proceeds were deposited by the Chariton Community School District rather than in the bank account of the Former District. As such, the auction proceeds have been reflected as accounts receivable from the Chariton Community School District in the Former District's fund balances at June 30, 2008, consisting of \$10,943 in the General Fund and \$987 in the School Nutrition Fund.

Based on our analysis of the summary of sales provided by the auctioneer, the auction proceeds totaled \$14,839.60, resulting in a variance of \$378.50. We were unable to determine the reason for the variance.

Recommendation – The Department should review and determine whether the Department or recipient districts (Chariton CSD, Wayne CSD and Albia CSD) should pursue and request reimbursement for the apparent underpayment of \$378.50 from the auctioneer. In addition, the Department should ensure the net auction proceeds are appropriately distributed to the recipient districts based on the percentages calculated by the Iowa Department of Management.

- (E) Disbursement Testing – Based on testing thirty-two disbursements, the following findings and concerns were identified regarding disbursements by the Former District:
- Seven instances where invoices could not be located.
 - Three instances where check amounts did not agree with the amounts approved.
 - Three instances where check amounts did not appear on the approved list of bills.
 - One instance where the disbursement was charged to the wrong fund.

The Former District purchased a 2007 Ford Taurus for \$12,200 on August 23, 2007 with resources from the General Fund. No invoice was available and the payment was not included on the approved list of bills.

In addition, the Former District wrote a check from the Physical Plant and Equipment Levy (PPEL) Fund to the General Fund for \$25,886 on January 24, 2008. According to Great River Area Education Agency personnel, the Former District wrote the check to cover a General Fund payable. The only documentation provided was a payable from fiscal year 2005 for \$18,386 and a payable from fiscal year 2007 for \$7,500, totaling \$25,886, with the notation "auditor." The payment was not included on the approved list of bills.

We contacted the Former District's independent auditor who represented "The \$18,386 represent(s) correction of errors, which took place through the years (incorrect recording of property tax). The additional \$7,500 in 2007 represented \$7,500 received from Pepsi for an exclusive vendor contract, which was recorded in the PPEL Fund, but should have been recorded in the Former District's General Fund."

Recommendation – The Department should review and determine the proper disposition of these disbursements, including consulting legal counsel regarding the propriety of the disbursements.

- (F) Equalization Levy – Several factors affecting the determination of whether and to what extent an equalization levy should be imposed remain unresolved until the Department reviews and determines the proper disposition of the various items noted in this report. Of particular concern is the potential negative effect of the distribution of the negative General Fund balance of \$309,907 and the \$300,000 of local option sales tax transferred to the General Fund and used for the payment of salaries and other expenses without apparent legal authority to do so.

Recommendation – The Department should review and determine the proper disposition of the various items noted in this report, including consulting legal counsel as noted. The Department should investigate all possible legal remedies to avoid adversely impacting the General Fund financial condition of the recipient districts.

Former Russell Community School District

Exhibits

Former Russell Community School District

Former Russell Community School District
 Payments on Behalf of Robert McCurdy, Superintendent
 For the period July 1, 2007 through June 30, 2008

Month	Professional Services*	Employee Benefits**	Total
2007:			
July	\$ 750.00	13.94	763.94
August	1,350.00	13.94	1,363.94
September	1,350.00	13.94	1,363.94
October	750.00	13.94	763.94
November	1,350.00	13.94	1,363.94
December	-	13.94	13.94
Total 2007	5,550.00	83.64	5,633.64
2008:			
January	-	1,376.39	1,376.39
February	-	1,376.39	1,376.39
March	-	1,376.39	1,376.39
April	-	1,376.39	1,376.39
May	-	1,376.39	1,376.39
June	-	1,376.39	1,376.39
Total 2008	-	8,258.34	8,258.34
Grand total	\$ 5,550.00	8,341.98	13,891.98

* - Paid to Sharon and Associates

** - Long-term disability and life insurance for July through December 2007 and long-term disability, life insurance and family health insurance for January through June 2008

Former Russell Community School District

Fund Balance Reconciliations
(Unaudited)

For the years ended June 30, 2007 and June 30, 2008

	General	Capital Projects	Management Levy	Student Activity	PPEL
Balance July 1, 2006	\$ (121,353)	192,347	(325)	27,789	16,279
Revenues and transfers in	1,846,076	126,276	49,397	55,350	24,665
Expenditures and transfers out	1,864,488	14,188	30,202	53,957	22,459
Balance June 30, 2007	\$ (139,765)	304,435	18,870	29,182	18,485
Balance July 1, 2007	\$ (139,765)	304,435	18,870	29,182	18,485
Revenues and transfers in	1,862,887	121,749	44,808	55,230	27,081
Expenditures and transfers out	2,033,029	36,364	31,752	67,768	22,380
Balance June 30, 2008*	\$ (309,907)	389,820	31,926	16,644	23,186

* Fund balances reported at June 30, 2008 in this Exhibit include a \$300,000 interfund loan from the Capital Projects Fund to the General Fund.

Debt Service	Total Governmental	School Nutrition	Total
-	114,737	29,464	144,201
6,992	2,108,756	62,595	2,171,351
6,992	1,992,286	68,797	2,061,083
-	231,207	23,262	254,469
-	231,207	23,262	254,469
20,558	2,132,313	64,962	2,197,275
20,558	2,211,851	77,529	2,289,380
-	151,669	10,695	162,364

Former Russell Community School District

Staff

This agreed upon procedures engagement was performed by:

Susan D. Battani, CPA, Director
Nancy F. Curtis, CPA, Senior Auditor II
Daniel W. Henaman, Assistant Auditor

A handwritten signature in black ink that reads "Andrew E. Nielsen". The signature is written in a cursive style with a prominent initial "A".

Andrew E. Nielsen, CPA
Deputy Auditor of State