

BHUSD MEASURE E CITIZENS' OVERSIGHT COMMITTEE

ANNUAL OVERSIGHT REPORT, Calendar year ending December 31, 2010

This Annual Report from the Citizens' Oversight Committee (COC) of Measure E is for the Beverly Hills Unified School District (BHUSD) Board of Education and especially to the tax paying citizens of Beverly Hills. Our last Annual Report was through March 2010 so this Report will cover the last three quarters of 2010 ending on December 31, 2010 since there was a Moratorium on Measure E spending by the BHUSD Board. We have tried to keep this Report brief and readable, but if more details are needed, please feel free to download any and all minutes from COC meetings from the website at www.bhusd.org (pull down menu at *About Us*, then select *Citizen's Oversight Committee*) or come to COC meetings as they are all open to the public, usually held monthly on the third Thursday of every month from 4-6PM in the BHUSD Board Room. Although the COC are the appointed members of the BHUSD, oversight is something that can and must be undertaken by the entire community. The COC's only role is to advise the community on Measure E costs, not to demand change.

LEGAL COMMITTEE REPORT

It is the COC's opinion that the February 3, 2011 memorandum from Charles Adams, Esq. of JONES HALL (copy of which is attached), does not justify spending Measure E bond proceeds on the Strategic Concepts litigation as the contract under which BHUSD paid millions of dollars sought to be recovered was made before the public voted for Measure E. It is the BHUSD position in its initial lawsuit against Strategic Concepts that its contract was illegal, void and unenforceable; thus, not arising under Measure E which was passed by voters in November, 2008 after that contract and its earlier iterations were made. Certainly the criminal action in which Quinn Emanuel is cooperating with the prosecutors at BHUSD expense cannot rise under Measure E, especially as it involves matters having no connection with the subsequently passed Measure E. The Adams memo does not specify how the criminal case relates to Measure E or how it would, if successful, support the civil lawsuit.

Through December 31, 2010, cumulative expenditures for these legal costs which have been charged to Measure E are \$1,093,806.00. Additionally, the costs for staff and consultants billed against Measure E that are spending a percentage of their time on the litigation are not quantifiable and detailed as the staff does not track their tasks in that manner. The COC has expressed a desire to have independent legal counsel advise on the necessity and the applicability and advisability of litigation to protect the Measure E funds from being spent on what appear to be unrelated legal expenses. The COC, once again, determined that litigation expenses regarding the Strategic Concepts disputes should not have been paid out of Measure E funds. The District claims to have an opinion from Bond Counsel supporting such payment with which the COC disagrees in whole. The Board of Education was notified of such COC determination at two separate meetings of the Board of Education.

The committee is also concerned that Measure E will have legal fees charged regarding the Metro Western route alignment.

MEASURE E PROJECTS

Due to the continuing moratorium on the expenditure of Measure E Funds, no projects were undertaken or completed during the first calendar quarter of 2010. The COC continues to voice its opinion that by placing a moratorium on the progress of the Measure E Program, there will be (1) a protracted delay in the completion of the Master Plan; and (2) the execution of the Measure E Program; and (3) a lost financial opportunity to reap any cost advantages during a downturn in the construction marketplace. In addition, any lingering delay could place our projects behind other school districts with the DSA (California Division of the State Architect) delaying the projects further and could risk IRS penalties due to potential arbitrage.

DISTRICT PERSONNEL CHANGES

Over the last Fiscal Year there were numerous changes to staff and hiring of consultants, including the project manager for the Measure E projects and an Interim Superintendent of Schools. This staff turnover creates an ongoing issue of legacy information and efficient distribution of information to the COC but by the end of FY 2010, staffing appears to have settled down with permanent staff, consultants and a range of competitive bids that were processed in early 2011.

MASTER PLAN

In the quarter ending December 31, 2010, the Board of Education was in discussions to move forward with a Master Plan bid process.

EXPENSES BILLED AGAINST MEASURE E

BHUSD adjusted the cost of the administrative staff passed through to Measure E and is now allocating 25% of admin. support for COC to the general fund. To date, the school district has passed a percentage of salary from consultants and administrative support to Measure E. The COC endeavors to continue to scrutinize expenditures to ascertain whether administrative expenditures are improperly paid from Measure E proceeds as stated in our previous report, pursuant to Education Code Section 15280(a).

REPORTING OF FINANCIAL EXPENDITURES BY BHUSD STAFF

The school district has had numerous changes of staff throughout the last year. However, one result of that has been the inefficiency in distribution of financial statements to the COC in a timely manner. Additionally, the formatting for the financial reporting has been varying in depth

and detail. The COC has had numerous meetings in which the financial reports were not distributed; hence, they were tabled to the next meeting. The financial reports were distributed without ample time to review prior to COC meetings, or without any details. Clearly the ability of the COC to oversee expenditures is limited by and to information provided.

ETHICS COMMITTEE

An Ethics Committee was established in late 2009. A four member committee was created and they issued a Report and Code which the COC approved and then issued in early 2010 when it was sent to the BHUSD Board; therefore, the Ethics Code was not implemented until six months later in June.

AUDITS

At its January 20, 2011 meeting, the COC heard a presentation from a representative of Christy White Accountancy Corporation (CWA) and reviewed CWA's financial and performance audit reports for Measure E for the fiscal year ending June 30, 2010 (2009/10). Following discussion between the Committee and CWA, the COC voted at the February 17, 2011 meeting to recommend that the District approve each of CWA's audit reports.

There were several important findings in CWA's audits which are summarized below, and the auditor's reports are presented in their entirety as an Appendix to this report.

FINANCIAL AUDIT HIGHLIGHTS

CWA delivered an unqualified opinion in its financial audit report. However, CWA identified certain deficiencies in BHUSD's internal control over financial reporting related to Measure E that CWA considered to be significant deficiencies. Under generally accepted auditing standards, a significant deficiency is defined as a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. These deficiencies included:

Audit Finding: Expenditure internal controls

- Of the 34 Measure E expenditures that CWA tested during its audit work, 11 had a purchase order dated after the invoice date and another 7 had no purchase order in place.
- A payment to a contractor made in 2009/10 was for a contract that had a series of change orders totaling approximately 78% of the original contract; the 13 individual change orders were individually below 10% of the contract amount, per Los Angeles County requirements, but in total exceeded 10% of the contract amount per Public Contract Code Section 20118.4.
- \$2.1 million in prior year (2008/09) expenditures CWA tested that were made from the Measure E Bond Building Fund to vendor Strategic Concepts had control deficiencies and questionable aspects (lack of itemization, no usage of purchase orders, contract not accurately monitored in payment history summary, relatively high level of fixed charges

early in the bond program, improperly coded items and relatively high levels of reimbursable items such as food and wireless bills.

Auditor Recommendations:

- Purchase orders should be created prior to Measure E expenditures to document authorization for expenditures and to properly encumber funds.
- Steps should be taken to limit construction contract change orders.
- The District is advised to undertake an investigation of payments made to vendor Strategic Concepts from the Measure E bond program. Any amounts recovered from Strategic Concepts should be reimbursed to the Measure E Bond Building Fund. Although the District has obtained a legal opinion stating that charging construction-related legal fees to the Measure E Bond Building Fund is permissible, the District is cautioned that the amount of legal fees paid be closely monitored so that Measure E funds can be maximized in their direct application toward facilities modernization and construction purposes.

District Response:

- The administration of the bond program has changed and stricter internal controls and processes are being put into place.
- The District is creating purchase orders for tracking the contract for projects under the Bond Funds.
- The Facilities Department is also using facility software to track the detail of each project, including change orders.
- The current administration is following the maximum change order amount of 10%.

COC Comments:

- On numerous occasions, the COC has expressed its concern to the District and the Board regarding the potential for internal control deficiencies due to high turnover and the lack of established procedures and processes in the District's business office; CWA's findings confirm that there have been significant deficiencies in internal controls.
- As stated elsewhere in this report, the COC believes that it is inappropriate to charge legal expenses related to the Strategic Concepts matter to Measure E.

Audit Finding: Interfund Borrowing of Measure E Bond Proceeds

- CWA noted that the District's General Fund borrowed \$4 million of Measure E bond proceeds in 2009/10, repaying \$2 million in February 2010 and repaying the remaining \$2 million in August 2010. Amounts were repaid with interest.
- The August 2010 repayment was not in compliance with Education Code Section 42603, which requires that interfund borrowings not made in the final 120 days of the fiscal year be repaid within the same fiscal year.

Auditor Recommendation:

- The District should take steps to comply with Education Code Section 42603 requirements for interfund borrowing in the future. Amounts borrowed from the Measure E Bond Building Fund should be kept to a minimum, to fully comply with statutory and local ballot language prohibitions on usage of bond funds for administrative purposes.

District Response:

- Staff processed the reimbursement to the General Fund, including interest, as part of the year-end processing. Procedures to make the repayments in time have been implemented.
- The District will use the property tax payment cycles to repay the temporary cash borrowing and remit interest at the same time.

COC Comments:

- The COC has raised the issue of interfund borrowings in meetings with District personnel and has been assured that such borrowings are a common practice of municipalities and that all amounts would be repaid by the end of the fiscal year; in the case of the 2009/10 interfund borrowings, this did not occur.
- The COC is concerned that future interfund borrowings would increase the possibility that Measure E bond proceeds may not be available, if even temporarily, as needed.
- Therefore, the COC recommends that the District find alternative sources of funds to manage its liquidity.

PERFORMANCE AUDIT HIGHLIGHTS

CWA also conducted a performance audit of the Measure E Bond Program's compliance with California Proposition 39, as incorporated in Article 13A of the California Constitution and Education Code Section 15264 et seq., during 2009/2010. In CWA's opinion, the Measure E Bond Program complied, in all material respects, with the aforementioned requirements during 2009/2010, except as noted in their accompanying schedule of audit findings which are summarized below:

Performance Audit Findings: Expenditure internal controls and Interfund Borrowing of Measure E Bond Proceeds

- CWA's findings and recommendations were identical to the Financial Audit (see above).

Performance Audit Finding: Interfund Borrowing of Measure E Bond Proceeds

- CWA's findings and recommendations were identical to the Financial Audit (see above).

Performance Audit Finding: COC Activities

- Their findings and recommendations were identical to the Financial Audit (see above).
- CWA identified two areas for potential improvement in the area of Measure E Citizens' Oversight Committee (COC) activities, which include, the timely posting of COC

minutes, and adding a representative from a bona fide taxpayers' association (as required by the Education Code).

Auditor Recommendation:

- CWA recommended that the District post the minutes of the COC to the District website immediately following the approval of the minutes and that the District should appoint a member to the COC that represents a bona fide taxpayers' association.

District Response:

- Administration will begin posting approved meeting minutes for all COC meetings. Hard copies of the approved meeting minutes are available for review in the Facilities office.
- The District is actively looking for a representative to fill the bona fide taxpayers' association position on the COC as required by Education Code.

COC Comments:

- While required by the Education Code, the COC is unaware of any applicants representing a bona fide taxpayers' association.

FINANCIAL REPORT

Available on the District website at www.bhusd.org (pull down menu at *About Us*, then select *Citizens' Oversight Committee*, then select *Measure E Performance & Financial Audits*).

CONCLUSION

The Committee relies exclusively on information provided by the District staff and its consultants, members of the public who attend the COC meetings, as well as the BHUSD Board of Education and their independent accountants. Therefore, the scope of the COC is limited to its reliance on these information sources under State Law and the Brown Act rules. In early 2011, the BHUSD solicited and then appointed new COC members in February 2011.

The COC does not have any staff of its own, and relies entirely on the BHUSD support staff provided by the district to maintain minutes, announce meetings and financial data. The BHUSD gave limited information on the legal case with Strategic Concepts et al. that was held in strictest confidence. Despite this limitation, and based on the information the COC has received from District Staff and others for the period of this report, April 1, 2010 to December 31, 2010, the COC believes that, except as noted above, the actual expenditures and commitments of Measure E Bond Funds appear to fall within the parameters of the bond measure, which were expended and/or committed solely for construction, reconstruction, rehabilitation or replacement of school facilities, except as noted in this report.

As of December 31, 2010 the COC's officers and members were as follows:

Les Bronte

Rudy Cole, Chair

Woodrow W. Clark II, PhD., Vice-Chair

Steve Hendry, CPA

Ana LaDou

Linda Lewis

Todd Okum

Martin Perlberger, Esq

Joe Safier, CPA

Julie Steinberg

Shirley Zaragoza, MBA