

Ralph Campbell, Jr.
State Auditor

STATE OF NORTH CAROLINA
Office of the State Auditor

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July 28, 2003

Mr. Wade Hobgood, Chancellor
Office of the Chancellor
North Carolina School of the Arts
1533 South Main Street
Post Office Box 12189
Winston Salem, NC 27127

Dear Chancellor Hobgood:

The State Auditor's Hotline received a complaint via e-mail from a Contractor that alleged he performed services and provided equipment at the North Carolina School of the Arts (School of the Arts) and did not receive full compensation.

According to the Contractor, he agreed to provide services and equipment to the School of the Arts in exchange for equipment valued at \$50,000. The Contractor stated in his complaint, he signed a written agreement in July 2001 to the exchange. According to his e-mail, the equipment was delivered in December 2002, damaged and missing vital components. Additionally, the Contractor stated he requested the equipment be insured at its value of \$50,000. The Contractor stated the School of the Arts failed to insure the equipment and denied any knowledge of the missing parts. The Contractor also stated the School improperly packaged the equipment which caused the damage. According to the Contractor, he sold the equipment for \$1,200 but paid \$800 to ship the equipment to the buyer. According to an invoice provided by the Contractor, the total amount due for his services and storage of the equipment is \$54,129.99. The Contractor further stated he believes the School breached its contract as well as improperly traded the equipment.

According to the Dean of the School of Filmmaking at the NC School of the Arts (Dean of Filmmaking), in December 2001, the Contractor, who had previously worked for the School of the Arts, verbally agreed to perform services and provide equipment in exchange for an OmniMix and Screensound Digital Post Production Audio Editing System (OmniMix) valued at \$50,000.

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The Dean of Filmmaking stated prior to the verbal agreement, he determined the OmniMix to be obsolete, and purchased newer, current equipment for the school. He also stated the School of the Arts tried on several occasions to sell the equipment, but was unsuccessful. According to the Dean of Filmmaking, the company from which the OmniMix was purchased, suggested a trade-in value of \$50,000, which is how the value was determined. The OmniMix was originally purchased in 1995 for \$539,000.

The Dean of Filmmaking stated the Contractor did provide services and equipment totaling \$41,955. According to the School of the Arts records, a check in the amount of \$11,600 was paid to the Contractor for equipment that he provided. Thus, the remaining balance due to the Contractor was \$30,355. The Dean of Filmmaking stated the Contractor voluntarily agreed to the trade and the OmniMix was shipped prior the end of 2002 properly packaged. The Dean of Filmmaking said insuring the equipment was never discussed between the parties. In addition, the Dean of Filmmaking stated prior to the agreement, he inquired with the Head of Purchasing to confirm the OmniMix could be traded. He said he was told that equipment could be traded as long as it was no longer in use. The Head of Purchasing said she told the Dean of Filmmaking the equipment could be traded but she never indicated he could circumvent the surplus property procedures.

According to the trucking company that delivered the equipment, the OmniMix was not packaged in accordance with requirements set forth by the National Motor Freight Classification for this particular item.

Based on our review, the School of the Arts should have termed the equipment "surplus property" in accordance with the School's policies since it was no longer used. According to the North Carolina School of the Arts Resource Manual, Administrative Policies and Procedures state the following in regards to surplus equipment,

Occasionally, departments have in their possession equipment or furnishings which are no longer of use to them, and therefore, may be termed "surplus property". Rather than permitting such surplus items to set idle and occupy needed space, they should be disposed of in one of the following ways:

- 1. Transfer the items to another School department or office where they will be used. A department may sell to a department by budget transfer, but cannot sell directly to individuals.*
- 2. Sell the items through the North Carolina State Surplus Property Office.*

Disposal of all state-owned property must be coordinated through the Surplus Property Officer in the Purchasing office.

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It appears the School of the Arts violated the policy stated above when it agreed to exchange the equipment for services provided by the Contractor. Therefore, we recommend the School adhere to the surplus property policies when disposing of equipment. The complainant in his original e-mail, subsequent e-mails, and his website, has raised numerous allegations regarding this matter and the alleged breach of contract. In our opinion, these are legal issues relating to the alleged contract that should be resolved through the legal channels that are available.

We are presenting our findings for your review and written response. The purpose of the response is to allow you the opportunity to outline any corrective actions taken or planned. We request the delivery of your written response by August 11, 2003.

General Statute §147-64.6(c)(12) requires the State Auditor to provide the Governor, the Attorney General, and other appropriate officials with written notice of apparent instances of malfeasance, misfeasance, or nonfeasance by an officer or employee. In accordance with the mandate, and our standard operating practice, we are providing copies of this special review to the Governor, the Attorney General and other appropriate officials.

If you have any questions or wish to discuss this matter further, please contact us. We appreciate the cooperation received from the School of the Arts staff during our review.

Sincerely,

Ralph Campbell, Jr., CFE
State Auditor

Auditor's Note:

The North Carolina School of the Arts' response to the management letter states there are several facts that need to be corrected. We disagree. We have reviewed the management letter and stand by the findings and recommendations. The statements given by employees of the North Carolina School of the Arts were given in oral interviews and/or written statements and are accurately reported in the management letter.

Management letters and responses receive the same distribution as audit reports.

NORTH CAROLINA

SCHOOL OF THE ARTS

July 30,2003

Mr. Ralph Campbell, Jr.
State Auditor
Office of the State Auditor
2060 I Mail Service Center
Raleigh, NC 27699-0601

Dear Mr. Campbell:

Thank you for sharing with me your preliminary draft regarding a violation of policy in the disposal of surplus property. I have discussed your findings with the parties involved. It is apparent that the North Carolina School of the Arts did indeed fail to follow stated policy in disposal of surplus property; however, several facts noted in your report need to be corrected.

- Contrary to the claim of Jerry Panza, there was never a written agreement, signed in July 2001, or any other time, documenting the agreement to trade services for the OmniMix.
- As the Panza emails immediately following delivery of the OmniMix demonstrate, there was not a problem with damage from shipping, and no vital components whatsoever were missing. All existing parts of the OmniMix were included in the shipment.
- While Jerry Panza asked that we insure the OmniMix, we never agreed to pay such insurance, only to list the value of the equipment as \$50,000 on the bill of lading, which Panza agreed to at the time of the verbal commitment. The auditor's report is not accurate in saying that Dale Pollock said the issue of insurance was never discussed. What was discussed with Panza was our intention to list the value of the equipment at \$50,000.
- We have no independent knowledge or confirmation of what Panza subsequently sold the OmniMix for, or what costs were associated with the later sale.
- If the trucking company felt that the OmniMix was not packaged in accordance with requirements set forth by the National Motor Freight Classification, that was never communicated to David Spencer, who packed the equipment. He was assured by the trucking company that the OmniMix was properly packaged.
- Dale Pollock acknowledges that he did not follow proper state procedures in disposing of surplus property. He and his staff are now well versed in proper state procedures for disposing of surplus property, and assure us that the same mistake will not be made again.

Office of the Chancellor
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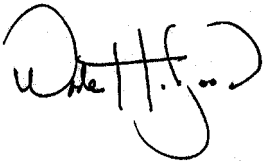
An equal opportunity constituent of the University of North Carolina

- Correction to auditor's letter: Page 2, line 3 should read:
"He also stated the School of the Arts tried on several occasions to **trade** (not "sell") the equipment, but was unsuccessful."
- Correction to auditor's letter: Page 2, par. 2, 3rd line from the end: "He said he was told that the equipment could be traded for something for equal or more value (words added) as long as it was no longer in use."

NCSA admits fault and apologizes for this violation. We have implemented a review of our policies to assure that this infraction will not occur again.

I regards to allegations made by the contractor, we have been in contact with the Attorney General and are reviewing our options. Thank you for bringing this matter to my attention.

Sincerely,

A handwritten signature in black ink, appearing to read "Wade Hobgood". The signature is stylized with a large initial "W" and a long, sweeping underline.

Wade Hobgood
Chancellor