

## #71 Anatomy of a Charter School Fraud

**Jennifer Berkshire:** Welcome to Have You Heard, I'm Jennifer Berkshire. Our topic, this episode is charter school fraud and our destination: San Diego. Now, if this were a regular episode and my cohost Jack Schneider was here, this is the point where I would surprise him with the information that I actually spent part of my childhood in San Diego. We'd reminisce, enjoy a little banter. Maybe I'd make a joke at his expense. But Jack remains on his lengthy summer getaway, which means that it's all business today on Have You Heard.

[News clip: San Diego County District Attorney]

**Berkshire:** That was the San Diego County District Attorney handing down an indictment against a charter school management company known as A3. Now, the scam that was carried out was so complex that even explaining it requires drawing complicated graphs and charts. Fortunately, I've got somebody here who's going to break it all down for us. Will Huntsberry is a reporter at the Voice of San Diego and has been covering the case of A3. Welcome, Will. That indictment we were just hearing about was 235 pages long. And I'm curious about what you thought as you started reading through it for the first time.

**Will Huntsberry:** Well, you know, I've not, I'm not used to being asked to put my feelings first and foremost as a reporter as the first question. But you know, when I saw the indictment, I think the thing that stuck out to me is like, I was shocked by how many people seem to be complicit in what was clearly a scam. You know, it's one thing for two or three people to be running one but it's another thing for a scam to be touching high school football coaches and some of them at least seeming to, like just, turn a blind eye and just roll with it.

**Berkshire:** So you did some really great reporting about this and just to give people a sense of the kind of ornateness of the scam you had to produce these elaborate charts, just showing how it all fit together. So give people the sort of big picture explanation of what was going on.

**Huntsberry:** Sure, sure. So Jason Shrock and Sean McManus are two guys who were at the top of this company called A3 Education that controlled a lot of charter schools with a lot of students in them, all around the state of California. It was operating in most of southern California, 20 counties down in our area going all the way up to Santa Cruz and then there was a little northern cluster of counties as well around Sacramento and Sonoma and that was 14 counties. And so A3 Education operated all these online charter schools and they could draw students from all of those counties. So we're talking many, many millions of California students.

And the way their organization works is, you know, in a way it's like a legitimate organization. You have kind of lieutenant figures under you in the corporate structure and then figures beneath them. And what it came down to is that all of these people were involved in opening up schools and enrolling more students and some of those students were very real and doing

online classwork and some of those students, according to the prosecutors in this case, we're very fake.

**Berkshire:** I think you referred to these students in one of your stories as ghost students. Explain what this means.

**Huntsberry:** That's right. Yeah, we could almost just refer to them pretty easily as fake students in the sense that they certainly weren't taking any classes and they weren't meeting with any teachers. These were students who McManus and Schrock and the A3 organization were managing basically to get their paperwork and they were capturing most of these students through summer athletic programs. So one of Schrock and McManus' lieutenants would approach a football team or a soccer team and say, 'hey, we can donate to your program if your kids sign up for this thing we're doing. And they'll sign up for our charter school for the summer, but they won't really have to do anything. Their whole curriculum will just be embedded in all the practice and all this stuff you are going to do. So just get them to sign this paperwork. We'll give you 25 bucks ahead and we'll call it a day.'

**Berkshire:** There is a lot about this case that is unusual. We're going to talk in a bit about why A3 was so focused on summer athletic programs. But there's also something very familiar going on here. Sean McManus and Jason Shrock were out to make money and they chose as their venture of choice online schools. Will: can you just walk us through why online schools in California make such an attractive and lucrative target?

**Huntsberry:** If you're like an entrepreneurial or an investor-type person and you're looking at the California landscape, I think the place you immediately look is online or semi-online schools, what we call non-classroom based schools. So McManus and Schrock were operating online schools only, which you know, if you are trying to run a big scam online schools is the place to be because you can still receive 100% funding from the state, the same amount of funding that a regular brick and mortar school would receive for this online system. You're running this obviously far, far, far less expensive [school] to run.

And you know, in California we also have independent study schools. These are places where a student might show up once a week to a storefront kind of class and receive a paper packet that they're supposed to go home and do. And then they're supposed to bring it back. That's another case where these schools can get 100% funding per child. As I'm sure your listeners know, each student comes with a dollar amount attached to their head in state funding and in California it's anywhere from like seven to \$10,000 and these schools, even though their overhead is so much less, can still receive 100% funding.

**Berkshire:** As you reported, it wasn't long before A3 was reeling in "mind blowing profits." I want you to go over some of the numbers for us, but you also point out that green in that money is really only part of the challenge. If you're running an operation like this, if the goal is to get that money into a personal bank account, you have to get very creative. Help us follow the money.

**Huntsberry:** Once the indictment came out, I started pulling their online tax documents because they're a nonprofit corporation. You have to post your tax documents. I pulled their 2016 tax returns for A3 Education, which they were saying is a consulting company that's working with all these online charter schools. That company brought in \$14.2 million but it only spent \$3.6 million. About a third of that was on McManus and Schrock' salaries. They seem to be the only two employees.

If you're running this kind of grift, what you have to figure out is 'I'm bringing all this money into a nonprofit corporation and how do I get it out of that nonprofit corporation and into my pocket?' And that is definitely a really difficult proposition that requires a lot of shady accounting and prosecutors say that make McManus and Schrock were able to divert about \$8 million into personal bank accounts and that they also bought a house for about \$1.6 million in San Juan Capistrano.

But the number they actually managed to get into their own bank account pales in comparison to what they were bringing in. A3 Education, for the years the prosecutors were looking at, brought in \$80 million. So that's not the full state funding. That's what came into consulting companies controlled by McManus and Schrock and, and you know, presumably if what prosecutors say is right, they were then the plan would be to try to figure out how do we get this \$80 million out of these companies we control and into our pockets? Cause I said it was \$80 million to A3 Education, but actually it was \$80 million to A3 and two other companies they controlled. One was called Mad Dog Marketing. Another is called Global Consulting, I think.

**Berkshire:** There were so many details in your reporting that I really didn't see other places. For example, you explained why Schrock and McManus were so focused on summer enrollment, and I'm going to do my best here to try to summarize. So the school year in California is 180 days long and a student with perfect attendance is supposed to be worth one unit of funding. But these guys figured out that by enrolling students in summer programs, they could get an extra 20% worth of funding that went straight to A3. That's where the recruiters come in, and a whole lot of paperwork. And there's one recruiter in particular that you're going to tell us all about.

**Huntsberry:** So one guy that wasn't charged comes up a lot in the indictment and his name was Luiz Rigney and he was an enrollment worker. His job was to go out to football programs, give them a presentation about what A3 could offer them—in this case it was \$25 a head—and what they had to do for that \$25, which was provide some paperwork. And you know, there's this amazing story in the indictment of Luiz Rigney in December of 2017 going to one of the corporate offices of A3 with like several suitcases stuffed with student records worth \$5 million because A3 had to get these records in so they could collect the money from the state. And there was a whole long back and forth about Rigney being able to get this paperwork into them in a way where it would satisfy state standards.

You know, it appears the indictment that Rigney had thought the parents could kind of date it whenever they needed to. And that was not the case at all. It had to be dated by July 1st for the scam to work right. For A3 to get the full funding they were trying to capture. And so we have text messages in the indictment from McManus talking to Rigney saying what date needs to be on the master agreements. And eventually he directs Rigney to backdate the paperwork and bring it in.

You know, a lot of the paperwork wasn't filled out completely. A lot of it wasn't filled out on the right date. Rigney sorted all that out. He brought it to the corporate headquarters and eventually he also got a really big check. These enrollment workers usually got paid per student. They enrolled and Rigney got \$25 per student he enrolled, and I think he alone enrolled 4,200 students, which accounted for almost a \$100,000 check to him.

**Berkshire:** Now to open all of these online charter schools, A3 needed somebody to authorize them. And one of the key details about this case is that you had superintendents from small California districts who were basically signing off on these schools and taking a cut of the proceeds. And now some of them have been indicted to explain to us how all of that worked.

**Huntsberry:** We have a lot of bigger districts here who feel that education has been undercut and subverted by the growth of charters. And they're not particularly keen on authorizing new ones. They're especially not keen on ones that aren't authorized in their district operating in their district anyway. And you know, here in San Diego County, that would be our biggest district, San Diego Unified and some of the mid-size districts, which I'm sure your listeners haven't heard of: Sweetwater, Grossmont.

Then in San Diego County we also have really, really tiny, tiny school districts that might serve 150 people. And what A3 realized was that if you can reach out to these small school districts and you can get them to authorize you, you'll still be able to pull students from the entire county you're in and every adjoining county. So in this case they were authorized by Deheza Elementary School District with 150 students, but they had access to more than a million students in Riverside County, Orange County, Imperial and San Diego County.

Just from that one authorization on top of that the school district did, Deheza gets enrollment fees where, which you are oversight fees, which you mentioned, I think, and they can collect one to 3% of the charter school's revenues. So these small districts, they don't have a lot of money. They're bringing in 3% on tens of millions of dollars that they can have extra teachers with that, they can pay themselves more with. They can do whatever they want with it. So there is this kind of unfortunate incentive for small school districts to authorize these charters. And that's what happened all around the state. It was a small school district that authorizes them here in San Diego County. And that was true in LA. That was true in Sonoma. That was, that seemed to be the crux of how they did business.

**Berkshire:** I played a clip at the start of the episode of the courtroom scene with that dramatic footage of some of these people we've been talking about being led away in handcuffs. I want you to fill us in on the state of the legal case, but also what's going to happen to A3's schools.

**Huntsberry:** Ten of those people have pleaded not guilty, but Sean McManus has not entered a plea and that's because he appears to be on the run in Australia, which is his home country. So the authorities have not tracked him down. He doesn't appear to have turned himself in. And the people involved face anywhere from, you know, I think 40 something years in jail to just two or three.

In the case of Deheza's superintendent here in San Diego County, she was charged with abetting all of this stuff that was going on, and she faces two to three years. As far as the schools go some of them are slated to close, but so you know, you'll know that in California and probably most other states, school districts have some kind of responsibility for overseeing the charters that they authorize. And so they're supposed to be checking in on them every few years, see how well they're doing, educating students, making sure their finances are all in order, and then the charter will come up for renewal. Maybe they'll renew it, maybe they won't.

One of the schools that was authorized by Deheza, and there were three online charters that were authorized that were A3 charters, one is already slated to close and was already that was already in the works before this indictment came out. And that's because they had such a poor graduation rate and such poor outcomes with students. The future of the other schools is uncertain. There's been a receiver assigned in the case who I think kind of has control of the company. The schools are still functioning. There are still many, many students enrolled in them. And it remains to be seen if, if they will stay open and A3 will continue to be a functioning entity.

**Berkshire:** One of the most poignant parts of your reporting is the letters from real people, teachers, parents, guidance counselors who were part of a three's operation but didn't realize that it was a money-making scam.

**Huntsberry:** Yeah, it is really strange. And I don't know what to make of it because I think these people feel protective over these institutions that they're tied to, but I'm sure they also feel very betrayed, you know. I got letters passed onto me from the lawyers representing A3, from guidance counselors and teachers and parents.

And you know, there absolutely are some parents and students who need education options that fall outside a typical brick and mortar school. And I think when you're serving as many families as A3 was serving, you're inevitably going to have many, probably many real cases like that of maybe a student with autism who doesn't do well with a lot of people around them or you know, a student with anxiety or a student with a physical disability. And I did hear from people like that who, who want a program that is online and gives them flexibility. And I heard from, you

know, guidance counselors and teachers who said they were absolutely trying to do the best they possibly could with their students.

**Berkshire:** I'll include links to your stories on the Have You Heard blog, but I'm wondering if there are any other details from the case that you'd like to see get more attention.

**Huntsberry:** Well one thing we didn't talk about, which is maybe a small detail, but you know, so Sean McManus, he has roots here in California in terms of being involved in charter schools. And I'm not quite sure how far that got back, but they go back to at least to 2010 or 2011, opening up schools around the state. A3 started in 2015 and it started because a man named Steve Van Zandt was able to orchestrate the sale of a school between A3 and a school that already existed and was authorized here in Deheza and I think that's kind of an interesting part of the tale.

You know, this is a nonprofit online school that is authorized by Deheza. It's called Mosaica and it's connected, I believe, to a company out of Colorado. But it's a nonprofit company and yet they're still selling the school for \$1.5 million to A3 who's like looking to get in the business in 2015. I'm still not totally sure how you sell a nonprofit and what happens to the assets thereafter and if people actually end up profiting off that sale.

I mean, Steve Van Zandt is also a really interesting figure. He was a former superintendent in another small school district called Mountain Empire and he was authorized as superintendent of that small school district, he was authorizing of a lot of charters and he was making a percentage of the revenue that they brought in. That was in his contract as a superintendent of a public school district. He ended up being charged with some crimes. Now he's working as a consultant and he has these ties to A3 in kind of helping them get going and creating the empire that they were ultimately able to create between 2015 and now.

**Berkshire:** Well Will Huntsberry, I want to thank you for your great reporting and for explaining so clearly how this scam worked. In fact, I sometimes worried as I was reading your stuff that it could function almost like a how to guide for would-be fraudsters in other states. Did you ever think about that?

**Huntsberry:** Yeah, I think that certainly if you're, if you're an investor, maybe you kind of get excited at the thought of all this. I don't know. It depends what state you're in, obviously. But states like Florida, Ohio, Arizona, I think there definitely are states with looser regulations where people are paying attention to this and either expanding their industry or getting involved in it. I think there are wide profit margins to be made and I think some people see that and they say, 'how can I push the limits of the legality and do it and technically stay within the law?' I think in the case of A3 from the indictment, it appears that they knew they were far outside the boundaries of the law, but I think there are some people who are absolutely trying to push it to the max and hopefully not break it. You know what I mean?

**Berkshire:** I think we all know what you mean. That was Will Huntsberry. He's a reporter at the Voice of San Diego. Look for him at [voiceofsandiego.org](http://voiceofsandiego.org) and you can find all of his great reporting on this and other topics. And while you're there, subscribe to his newsletter, the Learning Curve. And I will be right back with another special guest who has something to say about the topic of charter school fraud.

[Music]

**Berkshire:** I want to bring in somebody who knows a lot about the sort of charter school fraud that we've just heard so much about. Preston Green is a professor of educational leadership and law at the University of Connecticut and he has written extensively and ominously about the key ingredient in the California charter scam, what are called related party transactions. Preston, explain what that means.

**Preston Green:** Related party transactions are business arrangements between companies with close relations. An example is one where between two companies or managed by the same group. Now it's important to understand that related party transactions are legal, but they can create severe conflicts of interests and as a result, taxpayer money can be wasted. So it's really important to create, for states to have regulations in place to guard against waste, fraud or mismanagement.

**Berkshire:** Now even if you don't know this term 'related party transactions,' you've seen what can happen when they go spectacularly wrong. I'm thinking of course about Enron, the infamous Texas energy company that went from being an emblem of innovation to a synonym for corporate fraud. Preston, I'm curious as you've been following the San Diego case, did you see anything familiar?

**Green:** What really stood out to me was just how much this look like Enron. This is as Enron-ny as it gets so far in charter school land where you had these really complex relationships between a nonprofit, a charter school management company, along with these for profit related parties that these folks had control, that these people had control with. And even the names, even that, some of the names were very Enron-like. I think that Mad Dog Consulting was very much like the Raptors of the Enron saga.

So I think that the complexity of these arrangements, the opaqueness and also just the amount of money that was being bandied about in the indictment. I think we've, we're talking about about \$80 million and it's just really amazing that you can see in \$80 million fraud in in a public school situation. But this is like these are large numbers and it's really stunning in an Enron-like way.

**Berkshire:** One thing that really concerns Preston is that because charter schools are so heavily concentrated in urban areas, communities of color end up bearing the brunt of the kinds of fraud that we heard about in this episode. In fact, he argues that charter school expansion is

starting to look like the subprime mortgage crisis and that there's basically a charter school bubble forming in a number of cities.

If you want to know more, you can join us in the special extended play version of the show that we call In the Weeds. All you have to do is go to [Patreon.com](https://www.patreon.com/HaveYouHeard) search for Have You Heard. A small monthly contribution gets you cool extras, like a reading list for each show, and entrance into the weeds, which is where Preston Green and I are headed right now to talk about charter school fraud. And Enron and subprime mortgages and how they all go together. How can you miss that?

This is usually the spot, of course, where Jack leaps in and reminds you that there are many ways to support the show that don't cost money, like recommending us to your friends or leaving us a five star review. But Jack is not here. So until next time, I'm Jennifer Berkshire and thanks for listening to Have You Heard.