
MEMORANDUM - UPDATE #3

TO: ROSE HERMODSON
FROM: LISA M. NEEDHAM
SUBJECT: SYNERGY RESIDENTIAL ACADEMY
DATE: 6/14/2012

INTRODUCTION

You asked me to examine the history of Synergy Residential Academy (hereinafter "Synergy"), one of the residential academies authorized under 1998 Minn. Laws Chap. 398, Art. 5 Sec. 46. Below, I discuss the provisions of the original grant to Synergy, key personnel, dates the facility was open, and post-closure concerns. This memo was amended from its original form considerably in light of the fact that it does not appear that the Department did not ever issue written consent to Synergy to close the facility.

I. THE ORIGINAL SYNERGY GRANT

In December, 1999, the state allocated \$6,159,190¹ to Special School District No. 1 (Minneapolis Public Schools) and Synergy Residential Academy to design, construct, furnish, and equip a residential academy.² The Grant Agreement specified that the allocated dollars could be used only to acquire a leasehold interest in real property, newly construct a facility, design, furnish, and equip a facility, and pay start-up costs for the residential academy.³

The Grant Agreement contained extensive information as to what constituted a default and what would transpire in the event of a default on the agreement.⁴ Many of the provisions, such as a failure to complete the project or a failure to fully pay for the project, are not relevant here. Of specific interest here are the provisions as to what would occur if the facility ceased to be used as a residential academy.⁵ The Grant Agreement states that a default would occur "[i]f, without the written consent of the State Entity, any part of the Real Property and, if applicable, the Facility, ceases to be used as a residential academy."⁶ The Grant Agreement also states that a number of other actions, such as leasing, selling, or conveying in any way the interest in the property and facility constitute a default.⁷

¹ Originally, the grant amount was less as 3, not 2, residential facilities were planned. However, one potential grantee dropped out before fiscal year 1999 and the money was reallocated to the remaining two grantees, Catholic Charities and Synergy. *See* "Residential Academy Program Report to the Legislature," Minnesota Department of Children, Families & Learning, May 2001 at page 3.

² *See* "General Fund Grant Agreement Construction Grant for the Synergy Residential Academy" at page 1.

³ *See id.* at pages 3-4.

⁴ *See id.* at pages 7-10

⁵ *See* Grant Agreement at page 7.

⁶ *Id.*

⁷ *Id.*

Synergy would be permitted to sell its interest in the property if the following conditions were met: (1) they determined, by official action, that the facility was no longer usable or needed as a residential academy; (2) the sale was made as authorized by law; (3) the sale was for fair market value; and (4) written notice of the sale was supplied to the state at least 30 days prior.⁸ In the event the facility or the interest in real property was sold, the state was to receive the first distribution of net proceeds.⁹

In brief, then, Synergy would have been required to repay the state any funds under the terms of the Grant Agreement if (1) if Synergy ceased operating as a residential academy and did not obtain the written consent of the state or (2) Synergy sold or otherwise transferred its interest in the real property or the facility.

Departmental inquiries have revealed that it does not appear that Synergy ever sought, or received, written consent, to cease operation or to transfer the property in any way. In the event the Department determines such consent was received, it would then have been permissible for the facility to have closed and ceased providing residential care, but it still would not have been permissible for Synergy to transfer its property interest without those funds reverting to the state. The latter issue is discussed at length in part III, below.

II. SYNERGY ACADEMY: KEY PERSONNEL AND DATES OF OPERATION

Synergy, Inc., a 501(c)(3) corporation, filed federal 990 forms for the tax years of 1999-2001.¹⁰ Synergy had its 501(c)(3) status revoked automatically for failing to file a 990 form for three consecutive years.¹¹ It is unclear Synergy ceased filing Form 990 after 2002 or in a later year.

Joyce Hayden, who also signed the grant agreement on behalf of Synergy, is listed as the only officer, director, trustee, or key employee each year.¹² Ms. Hayden received \$82,500 each year in that position. The 2000 990 Form 990 also reports Peter Hayden and Eric Mahmoud receiving \$68,750 as program consultants.¹³ Subsequent Form 990s do not list any other consultants or employees save for Ms. Hayden. The 2001 Form 990 provides a Board of Directors list:

- Eric Mahmoud, President and CEO of Seed Academy/Harvest Prep
- Vincent Hayden, President and CEO of Turning Point
- Dr. Bravada Garrett-Akinsanya, Brakins Consulting and Psychological Services
- Henry Crosby, Area Development Director, United Negro College Fund
- Bobby Joe Champion, Attorney
- Rev. Marchelle Hallman, Chaplain of Wayman AME Church
- Sandra Rowell, Retired Educator
- Joyce Stallings Hayden, Executive Director, Synergy.¹⁴

⁸ See Grant Agreement at page 11.

⁹ See *id.* Indeed, this is what transpired with Catholic Charities, who suspended operation of their residential academy in 2005 and subsequently sold the building. The net proceeds of that sale (\$775,000) were returned to the state. See "Minnesota School Finance," House Research Department, November 2011 at page 84.

¹⁰ See *generally* Form 990, Synergy, 2000; Form 990, Synergy 2001; Form 990, Synergy, 2002.

¹¹ See GuideStar Report for Synergy Residential Academy.

¹² See *generally* Form 990, Synergy, 2000-2002.

¹³ See Form 990, Synergy, 2000.

¹⁴ See Form 990, Synergy, 2001.

Synergy broke ground for the facility in January, 2000 and began serving students in early 2001.¹⁵ By April, 2001, the facility was serving 24 students, most of whom were children in the Hennepin County foster care system.¹⁶ Foster care funds assigned to those children were paid by Hennepin County to Synergy to help offset ongoing expenses.¹⁷

In August, 2003, news stories began appearing that Synergy would likely close.¹⁸ Hennepin County Commissioners Mark Stenglein and Penny Steele raised objections to continuing to fund the program.¹⁹ The facility did close in 2003 due to a lack of funding for noneducational costs.²⁰ The Legislature reported that since closing the facility has been used for early childhood services provided by Seed Academy.²¹ However, the Department noted in 2006 that the facility was used for housing charter schools as well.²²

III. POST-CLOSURE CONCERNS

Of primary concern to the Department, presumably, is the question of whether any money is recoverable from Synergy since it ceased operation as a residential academy. An ancillary question is whether there was anything improper in Synergy's grant contracting, construction, or closure of the facility. The answer to both questions is complicated.

The original Grant Agreement specified that a default under the grant would occur if Synergy ceased to operate as a residential academy without obtaining written consent from the state.²³ The original Grant Agreement also specified that a sale of the real property and facility was permissible if Synergy determined, by official action, that the facility was not usable or needed as a residential academy and funds from the sale reverted to the state.²⁴

Here, it appears that once Hennepin County ceased providing noneducational funds, Synergy determined it was unable to continue operating as a residential academy.²⁵ The record is unclear as to whether Synergy obtained written consent from the state to close, but there is no evidence that they obtained such permission. Department emails in 2002 show that Synergy was exploring the possibility of renting the facility, which was severely underutilized, as a homeless shelter.²⁶ At that time, the

¹⁵ See "Residential Academy Program Report to the Legislature," at page 4.

¹⁶ See *id.*

¹⁷ See *id.*

¹⁸ See, e.g., "Synergy May Close," *Insight News*, August 24, 2003. From internet searches, it appears that the StarTribune covered the issue as well, but full articles are no longer available.

¹⁹ See *id.* The news article frames it as an "objection to funding the program" but it does not appear that Hennepin County was responsible for funding the program. Rather, it appears that Hennepin County was responsible for providing funds for non-educational costs.

²⁰ See "Minnesota School Finance" at page 84.

²¹ See *id.*

²² See email from Morgan Brown to Chas Anderson, May 17, 2006, stating that first and third floors of Synergy were then being leased to Harvest Prep, and the second floor was being leased to Hmong Academy.

²³ See Grant Agreement at 7.

²⁴ See *id.* at 11.

²⁵ See "Minnesota School Finance" at page 84.

²⁶ See email from Audrey Bomstad to Barbara Yates, April 16, 2002, noting that Joyce Hayden, head of Synergy and the signatory on grant documents, had inquired of a legislative representative whether such use would be permissible.

Department opined, correctly, that such a use would be impermissible without written consent of the state and, if the facility were no longer a residential facility, the facility would be sold and the proceeds would revert to the state.²⁷

A related question is why the facility was only able to maintain operation for such a short time – approximately 30 months. The original legislation did not provide that grant recipients were show continued fiscal ability to operate a residential academy. Rather, the legislation specified that in awarding grants, the commissioner was required to consider the quality of the education program, the location, the composition of the board and governance structure, the extent of collaborative effort with other organizations, the extent of community involvement, and whether year-round services were provided.²⁸ Perhaps accessing the original Request for Proposal (RFP) that resulted in the grant to Synergy would be helpful in determining whether fiscal soundness was one of the criteria initially considered.²⁹

In 1999, the Legislature amended the authorizing legislation to note that all projects awarded grants were required to submit updated capital and operating budget plans to MDE, and the commissioner was required to approve all educationally and economically advisable plans.³⁰ It appears, therefore, that at some point in 1999 or 2000, the commissioner approved a budget for Synergy that showed that Synergy had sufficient capital and operational projections to continue operations for a reasonable period of time. There isn't sufficient information to determine if Synergy failed to use funds wisely, failed to obtain necessary supplementary funds, failed to find enough students for the facility, some combination thereof, or other unknown factors. All that is known is that in 1999 the commissioner presumed that Synergy's budget was sufficient, but by 2003 the academy was closed when Hennepin County funds were unavailable.³¹

It is not clear whether Synergy chose to sell the building or in other ways transfer its leasehold interest. As noted above, were written consent to close received, the closure itself theoretically would not have triggered the provision in the grant agreement that required a return of funds to the state, as that provision is only triggered in the event of a sale or transfer of interest.³² The other residential academy in Minnesota, run by Catholic Charities, chose to sell the facility and returned funds from the sale to the state.³³ However, the post-2003 arrangement described by both the legislature and MDE raises questions. The legislature reports that the facility is now used for Seed Academy³⁴ and MDE reported in 2006 that the facility is used for charter schools.³⁵ However, the entity known as "Synergy Residential Academy" is no longer a corporation in Minnesota, as it was involuntarily dissolved in

²⁷ See *id.*

²⁸ See "Residential Academy Report to the Legislature" at page 2 (citing 1998 Minn. Laws ch. 398, Art. 5, Sec. 46 subd. 5).

²⁹ See *id.* at pages 2-3 (mentioning RFP and explaining who received awards).

³⁰ See *id.* at page 3 (citing 1999 Minn. Laws. ch. 241, Art. 4, Sec. 26(b)).

³¹ The 2002 Form 990 for Synergy shows a fund balance in excess of \$4 million at the end of 2001 with program revenues in excess of \$500,000. It is unclear as to why such funding would have been insufficient to continue the academy absent Hennepin County support.

³² See generally Grant Agreement at 11.

³³ See "Minnesota School Finance" at page 84.

³⁴ See *id.*

³⁵ See Morgan Brown email.

2005.³⁶ Synergy was the Grant Recipient, pursuant to the Grant Agreement, but Seed Academy appears as the owner of the property from 1984—present.³⁷

Synergy's possessory interest in the building is murky at best. The original Grant Agreement stated that funds were to be used to acquire a leasehold interest in the real property and newly construct the facility.³⁸ It is possible that Synergy constructed a new facility, as contemporaneous reports discuss "breaking ground" on the planned academy.³⁹ However, Synergy does not appear to have acquired title. Rather, they were the lessor of the real property from Seed Academy. The facility, however, was constructed by Synergy.

Attachments A and C of the original Grant agreement provide some clarity. Attachment A states that Synergy obtained a lease for the property and that the lease needed to remain in effect until all grant restrictions were complied with or a written release was received by the Minnesota Commissioner of Finance.⁴⁰ Attachment C states that Seed agreed to lease the property, as improved by the building of the residential academy, to Synergy for 50 years.⁴¹ Therefore, Synergy did obtain an interest in the property. However, Synergy's interest was somehow transferred, at some point, to Seed Academy, the owner of the property at 1300 Olson Memorial Highway, where Synergy was located and where Seed Academy, Best Academy, and Harvest Prep continue to be located. There is no record of this transfer in Department materials. It is unclear how Synergy could revert the lease to Seed Academy, as such a transfer would still require the funds be returned to the State.⁴² It may simply be that no one at the Department or State was made aware of the transfer of interest, which would be a default under the Grant Agreement.

At root, information on the transfer of the property interest is inherently incomplete. All that is known is that one entity – Synergy – received funds to acquire a leasehold and build a facility on land owned by Seed Daycare. In August, 2003, Synergy ceased to operate the facility and the facility closed. At some unknown point after that, Synergy ceased to exist. At another unknown point in time, Seed Academy, a separate organization⁴³ began (or perhaps continued) operating the facility as a daycare and became the landlord and lessor for several charter schools. It is therefore unclear as to how Synergy ceased to have an interest in the land or building without selling or transferring that interest to Seed Academy. The Grant Agreement prohibited a sale of the interest without charging fair market value.⁴⁴ However, no record of Synergy selling its interest to Seed Academy is available.⁴⁵

³⁶ See Business Record Details from Minnesota Secretary of State for Synergy Academy.

³⁷ See City of Minneapolis Property Info for Seed Daycare.

³⁸ See Grant Agreement at pages 3-4.

³⁹ See "Residential Academy Report to the Legislature" at page 4.

⁴⁰ See Attachment A to Grant Agreement at page 1.

⁴¹ See Attachment C to Grant Agreement at page 1.

⁴² Seed's 2004 Form 990 reflects that Seed acquired "rights in previously owned property" in the amount of \$4.7 million. This amount may reflect the transfer of Synergy's leasehold interest to Seed. See Seed Daycare 2004 Form 990

⁴³ The Department's report notes that the original award was made to "Urban Consortium," consisting of Seed Academy, Harvest Prep, Turning Point, and Save our Sons. See "Residential Academy Report to the Legislature" at page 3. However, the grant award was to Synergy Residential Academy, a non-profit corporation. See Grant Agreement at page 1. It does not appear from the Form 990 filings of Synergy, Inc., that Seed Academy was considered an affiliate of Synergy, but there may be other documents that explain the official relationship between the nonprofits.

⁴⁴ See Grant Agreement at page 11.

⁴⁵ The Department is in the process of encumbering funds for a title search, which should provide additional information.

CONCLUSION AND NEXT STEPS

There are a number of additional pieces of information that would assist in determining what transpired as regards Synergy:

- What the 1999 budget, approved by the commissioner, contained in terms of discussions of ongoing financial viability of the project.
- Whether the MDE issued, and retained, written consent to allow the facility to close.
 - Related, if MDE did not issue consent, whether the then-Department of Finance issued consent to close.
- Whether Seed Academy was a related nonprofit to Synergy.
- If Seed Academy was a related nonprofit, whether the transfer of property interest from Synergy to Seed was permissible.
- Whether Synergy filed any post-2002 Form 990s that reflect the transfer of interest or reflect that the organization no longer retained a \$4 million fund balance, as Seed's 2004 Form 990 reflects the acquisition of rights in previously owned property in the amount of \$4.7 million.
- Whether the transfer of property interest from Synergy to Seed involved payment.
 - Related, if the transfer did involve payment, did the Department of Finance receive the proceeds?
- What Minneapolis' role in the construction, operation, and dissolution of the residential academy was, and at what point, if any, that role terminated.

Obtaining some or all of this material will greatly assist in future discussions as to what occurred. Unless the successor to the Department of Finance, the Minnesota Office of Management and Budget (MMB) can provide documentation showing written consent to close, it appears that the closure of Synergy did constitute a default under the Grant Agreement. Though Hennepin County's refusal to fund the noneducational costs triggered the closure, it does not appear that MDE ever consented to the closure, but MMB may have. Additionally, significant questions remain as to what property interests Synergy acquired and how, if at all, those property interests were transferred to other entities, likely Seed Academy. In the event there was a transfer of interest, MMB may possess information showing that the transfer was proper and that money reverted to the state as required. In the event MMB does not possess such information, it appears that any transfer of interest was a breach of the grant agreement and state money should be recovered.

A final note: MDE personnel, like all government officials and employees, are obliged to report evidence of missing funds or public property to the Office of the State Auditor. Government personnel are also required to notify local law enforcement. *See* Minnesota Statutes section 609.456 subdivision 1. In the event MMB does not have documentation showing Synergy received written consent to close and has no information regarding the transfer of property interests, it appears MDE would have to consider reporting the matter.

Please feel free to contact me directly if you have further concerns or questions.