

SUMMARY REPORT

**TURKEYFOOT VALLEY AREA SCHOOL DISTRICT'S
TRANSPORTATION CONTRACT**

October 2002

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INTRODUCTION AND BACKGROUND

The Department of the Auditor General (the Department) conducts audits of Pennsylvania school districts pursuant to its authority and responsibilities under the Fiscal Code, 72 P.S. § 403.

In July 2001, the Department received complaints concerning alleged irregularities in the Turkeyfoot Valley Area School District (TVASD) transportation contract. The Office of Special Investigations (OSI) conducted an inquiry which included interviews of TVASD staff, the owner of the vendor providing transportation services and reviews of records of TVASD, the transportation contractor and third parties.

A summary of the draft results of the investigation was reviewed with the TVASD school board president, solicitor and the superintendent on July 11, 2002. A response to the draft summary was submitted by the TVASD solicitor on behalf of the school district on August 15, 2002, and has been incorporated into the final report.

SUMMARY OF FINDINGS

TVASD has made payments to third parties which lease vehicles to the school district's transportation contractor. While there was no evidence of misuse of school district funds in connection with the payments, the initial agreement to make the payments was made without school board authorization.

Changes were made to TVASD bus routes without a corresponding downward adjustment to payments to the transportation contractor as provided in the transportation contract. However, TVASD provided a justification for not making the downward adjustment.

RECOMMENDATIONS

1. TVASD should require school board authorization for all agreements to make payments to third parties in connection with the transportation contract, as well as any such agreements with other vendors. Such authorizations should be required separately from school board approvals of individual payments to vendors.
2. The school district's solicitor should review all such agreements in advance.
3. Responsibility for the administration of such payments should be assigned to a school district official or employee with no family, personal and/or financial relationships with the contractor to avoid conflicts of interest and the appearance of impropriety. If such assignments of personnel are not possible due to staffing limitations, the school district should ensure that there is adequate supervision and oversight by appropriate officials and the school board.

FINDINGS

Finding No. 1 – TVASD has made payments to third parties which lease vehicles to the school district’s transportation contractor. While there was no evidence of misuse of school district funds in connection with the payments, the initial agreement to make the payments was made without school board authorization.

TVASD’s transportation contractor is Turkeyfoot Transportation, Inc. (TTI), Confluence, PA. From 1995 to 2000, TTI was one of several vendors with which TVASD had separate contracts for school bus transportation routes. During the 1999-2000 school year, TVASD obtained bids from TTI and other contractors for a new bus transportation contract or contracts for the 2000-2001 school year through the 2004-2005 school year. According to the school district records, after a second round of bids the school board’s transportation committee recommended awarding the contract to TTI for all routes. The school board voted to approve the award of the contract to TTI.

Reviews of school district, TTI and third-party records disclosed that, beginning during the period of TTI’s previous contract with the school district, TVASD made payments to third parties that held leases on vehicles used by TTI. From September 1995 to the present, the school district has made payments related to five of TTI’s leases. The total payments made by the school district on the leases, as of May 2001, and the periods during which the payments were made, are shown below on Table No. 1.

Table No. 1 – Lease Payments Made by TVASD

	<u>Monthly Payment</u>	<u>Period</u>	<u>Amount</u>
Lease No. 1	\$2,855.80	September 1995 to January 2000 (41 payments)	\$117,087.80
Lease No. 2	\$1,715.77	September 1996 to May 2001 (45 payments)	\$ 77,209.45
Lease No. 3	\$1,511.95	September 1998 to November 2000 (21 payments)	\$ 31,750.95
Lease No. 4	\$2,046.00	October 1999 to (ongoing) (17 payments as of May 2001)	\$ 34,782.00
Lease No. 5	\$1,086.80	February 2001 to (ongoing) (4 payments as of May 2001)	\$ 4,347.20
<i>Total (As of May 2001)</i>			<i>\$265,177.40</i>

According to school district records, in some cases the leasing company’s invoices were sent directly to TVASD. For two leases, payment books were sent to, and maintained by, TVASD. Invoices sent by one of the leasing companies stated that there was a five-percent “late fee.” No record was found that the school district has been charged or has paid a late fee or other penalty in connection with the lease payments.

The lease payments were deducted from TVASD's monthly payments to TTI made pursuant to the transportation contracts. No evidence was found of overpayments to the contractor or the leasing companies in connection with the lease payments.

A TVASD employee who works in the business office and who served as the school board secretary through the end of 2000 was responsible for the administration of the lease payments. Invoices from some of the leasing companies were sent directly to this employee at the school district. The employee is a relative by marriage (sister-in-law) of the owner of TTI. The employee also is listed as an emergency driver for TTI. According to the school board president, she is not paid for this work.

We received no information from the school district concerning how the agreement to begin making payments directly to TTI's leaseholder had come about. According to the owner of TTI, he obtained permission to have it done from the TVASD superintendent and the then-school board secretary. The arrangement or understanding took place before TTI obtained its contracts with the school district.

According to records of TTI's vehicle leases, TTI authorized the leasing company to send the monthly invoices for four of the leases (Nos. 1, 2, 3 and 5 on Table No. 1) to TVASD and to receive the monthly invoice payments directly from TVASD. The authorization in connection with the first lease (Lease No. 1 on Table No. 1) was made in July 1995, prior to the date of the school board's approval of the contract with TTI. The authorizations for the other three leases are dated after the date of the school board's approval of the transportation contracts. According to the owner of TTI, the leasing company from which the other lease (Lease No. 4 on Table No. 1) was obtained, did not request that direct payments be made by the school district. He stated that the invoices came to TTI; he gave them to the school district employee responsible for making the other lease payments to also make the payments on this lease (Lease No. 4) for accounting and record keeping purposes. As pointed out above, the school district employee is the TTI owner's sister-in-law.

The TVASD superintendent declined to be interviewed during the investigation. The superintendent was represented by the same attorney who represented TTI during the investigation. The attorney later informed us that the superintendent would agree to an interview if necessary. Information that was sought from the superintendent was provided by and through the president of the school board and the school district solicitor.

There is no evidence that the school board authorized the superintendent and the then-school board secretary to agree to make the lease payments. There is no reference to the lease payments in the TTI contracts. There is also no record that the school board's transportation committee was informed about the payments. According to the school board president, the school board was not aware of the TTI leases. According to the TVASD solicitor, the school board would have agreed to a proposal that it make such payments for any of the school district's bus contractors. The school district's monthly payments to the leasing companies were included in monthly expenditure reports submitted to the school board for approval. In the school district records, the payments are listed as "Contr Lease Pay," or "Contr Transp (Lease Pay)" or "Contracted Lease Pay." The school board approved the monthly payments.

TVASD has made payments directly to banks in connection with its bus transportation contracts with other contractors. Based on the records provided by the school district and information obtained from the contractors, it appears that the payments were direct deposits of checks made payable to the contractor into the respective contractors' bank accounts.

Conclusions and Recommendations

The Public School Code states that the affirmative vote of a majority of all the members of the school board is required to take action on entering into contracts "of any kind" where the amount exceeds \$100.¹ Regulations of the Pennsylvania Department of Education (PDE) state that the board of directors of school districts are responsible for all aspects of pupil transportation programs, including negotiation and execution of contracts or agreements with contractors.²

The TVASD school board approved the contract for transportation services. However, it did not authorize the initial agreement to make lease payments to third parties. **Given the requirements of the Public School Code and the PDE regulations, it appears that it is reasonable and prudent, if not mandatory, that the school board be informed of proposals to make payments directly to third parties and that board authorization be obtained before such arrangements are agreed to by the school district's staff.**

In this case, there was an informal and unwritten understanding or agreement involving three people, the transportation contractor, the TVASD superintendent and a school district employee. Responsibility for handling the payments was given to the above-mentioned school district employee, who is a relative by marriage of the owner of the transportation contractor. The number of payments and leases and the use of payment books also support an inference that the school district staff was performing an extraordinary service for the transportation contractor.

During the investigation, school district officials stated that arrangements for third party payments are common or at least not unusual. Leasing of vehicles by school district transportation contractors is not uncommon. Third party payments, when properly authorized, approved and documented, would not be questionable.

The complaints which led to the investigation alleged that the school district staff was unduly favoring the transportation contractor. During the investigation, the attorney who represented the transportation contractor and the superintendent stated that school board members who questioned the school district's transportation contract had personal and/or employment relationships with another transportation contractor. Information concerning possible personal and/or financial interests of those school board members may provide an explanation of possible motives for complaints. However, that information does not alter the facts concerning the actions of the school district staff which are the subject of this Finding.

¹ 24 P.S. § 5-508.

² 22 Pa. Code § 23.4.

We found no evidence of wrongdoing in connection with the actual payments. However, given the amount of the transportation contract and the relationships and interests of the parties, the school district should improve its procedures.

It is recommended that school board authorization be obtained for all proposals to make payments to third parties in connection with the transportation contract, as well as any such agreements with all other vendors, prior to making any payments and that such agreements be reviewed by the solicitor in advance. It is also recommended that, to avoid conflicts of interest and the appearance of impropriety, responsibility for administration or monitoring of payments to contractors, including third-party payments, should be given to a school district official or employee with no family, personal and/or financial relationships with the contractor to avoid conflicts of interest and the appearance of impropriety. If such assignment of personnel are not possible due to staffing limitations, the school district should ensure that there is adequate supervision by appropriate officials and the school board.

Finding No. 2 – Changes were made to TVASD bus routes without a corresponding downward adjustment to payments to the transportation contractor as provided in the transportation contract. However, TVASD provided a justification for not making the downward adjustment.

The contract between the school district and TTI contains a daily rate and a “bus specification” (the year of the vehicle’s manufacture and the number of passengers) for each bus route. The amount the school district pays the contractor for student transportation on regular bus routes is determined by adding the daily rates for each route and multiplying the total by the number of school days in the school year.

The contract contains requirements that the school board will approve the mileage for each route prior to the beginning of each school year and that adjustments to routes, i.e., changes consisting of either increases or decreases in mileage, shall be made at the rate of \$1.25 per mile. The contract states that “payment otherwise to be made to the CONTRACTOR shall be based upon approved mileage times the mileage rate set forth above and shall be adjusted upward by \$1.25 per mile for increase in mileage resulting from changes made during the school year, and shall be adjusted downward \$1.25 per mile for decreases in mileage resulting from changes made during the school year.”

The contract also states that the contractor shall submit all information required to make adjustments to the school district’s business office three times a year, i.e., 60 and 120 “pupil transport days” after the beginning of the school year and at the end of the school year. According to the contract, the adjustments would then be made, and the school district would then pay any additional sums due to the contractor and offset money due the school district against payments due to the contractor.

According to school district records, in August 2000 the school board approved adjustments in the mileage for the bus routes. Most of the changes were minor. However, the mileage adjustment for the bus used on Route No. 8 was from 85 miles per day, the distance stated in the contract, to 33.8 miles per day, a decrease of about 51 miles each day. There is no documentation or other evidence that a corresponding downward adjustment was made in the school district’s payments to TTI, as the contract appears to require. According to the terms of the contract, the amount of the adjustment would have been about \$63.75 per day (51 miles x \$1.25) or \$11,347.50 (\$63.75 x 178 school days) for the 2000-2001 school year. It should be noted that, according to the school district’s records, the contractor was paid a combined rate of \$233 per day for use of a bus and a van on Route No. 8 during that school year. Therefore, the above figures may require further adjustment to take into account any changes to van mileage on the routes.

When this matter was first discussed with school district officials during our inquiry, we were told that, (1) the contractor is paid on a daily basis for regular bus routes, not on the basis of mileage and, (2) that payment adjustments only need to be made when the school district makes or initiates the changes. The first part of the statement appears to be inconsistent with the wording of the contract. In regard to (2), since the adjustment in the bus mileage was approved

by the school board, it appeared to be clear that, since the school district made the mileage adjustment, the payments should have been adjusted accordingly.

During the investigation, additional documentation discrepancies concerning vehicles were noted: school district records showed that vehicles used on one or more routes are different from the vehicles described in the original transportation contract. The records appear to be inconsistent with information in other school district records. However, no evidence was found to suggest that incorrect information concerning vehicles has been submitted by TVASD to PDE in connection with the state transportation subsidy.

In TVASD's written response to our draft findings, the school district solicitor submitted the following:

Since the contract was entered into in November of 1999 and did not begin until the fall of 2000, and because of circumstances that the Board became aware of during the 1999-2000 school year, the Board Transportation Committee and the contractor discussed changing the route and providing different equipment. The equipment would actually have been more expensive to the contractor than the equipment that he was contractually obligated to provide. The Board approved this change with the minutes clearly reflecting that the Board was aware that there was no proposal to change the cost or price. It is within the discretionary authority of the Board to determine when it makes a change because of safety issues, where the contractor volunteers to provide equipment which he was not otherwise obligated to provide, and where the Board determines that the new equipment is better for the students and concludes that it is willing to allow the contractor to provide the new equipment and to pay the same price that it would otherwise have provided.

With respect to Route #8, the Board approved the changes, and even though there would have been mileage on each piece of equipment, the Board approved the changes without changing the amount of the contract, which the Board had a legal right to do.

The school district's response included copies of the minutes of the March 13, 2000, meeting of the TVASD school board transportation committee in support of the solicitor's statement.

Conclusions and Recommendations

The school district provided documentation showing the reasons for not making a downward adjustment to payments to the transportation contractor after a decrease in mileage on the bus route. Based on the documentation, we have no basis to question the school board's decision.

TVASD'S RESPONSE

The school district's solicitor sent a lengthy and detailed response to the summary of the report's draft findings and recommendations. Due to the response's length, we have edited portions of it as noted below:

Finding No. 1

The School District vehemently disagrees with the statement that the School District staff agreed to make payments without authorization by the School Board and with the statement that payments were made under circumstances that give the appearance of impropriety and lack of appropriate controls.

It is the position of the School District that once the transportation contract was approved, the contractor had the legal authority to assign the payments to be made to him under that contract or to direct how those payments were to be made even without the consent of the School District. It is further the position of the School District that while staff may have discussed such payments with the contractor, no such payments were in fact made until they were submitted to and approved by the Board of School Directors.

While it is true that a relative of the bus contractor was a clerical employee of the School District, that employee had no authority to and did not in fact make any payments and could not make any payments. All checks were manually signed by the School District Treasurer, who was not a relative of the bus contractor or the clerical employee, and were signed only after review by the Chairman of the Finance Committee of the Board, an unrelated party, after submission of an account to the Board prior to Board approval, and after actual Board approval at a public meeting. Any accusation of an "appearance of impropriety" is unwarranted. Appropriate controls were in place as evidenced by the fact that the audit found no evidence of overpayments or that third parties received School District funds to which the transportation contractor was not entitled.

It is difficult enough for small school districts to operate and to obtain and retain competent staff. Neither the School District nor its staff should be criticized just because in a small community there may be a relationship between a clerical staff member with no decision-making authority and someone from the community who contracts with the School District.

The response discussed the transportation contractor's legal authority under the Uniform Commercial Code to assign the right to payment and stated:

To summarize, no consent or approval of any School District official or the Board of School Directors was required to acknowledge or comply with the contractor's direction to make payments to third parties. Formal action of the Board may have been required to refuse to comply because the School District had an option to refuse which it could exercise if it chose to do so, but no formal

action or approval was required to recognize the contractor's instructions and to abide by them, even though, in fact, as discussed below, such formal approval was given by the Board in this case.

Having said all of the foregoing, given the concern that has been raised in connection with this practice, the solicitor has recommended that the School District include the provision set forth on Exhibit A in future contracts and that it require a contractor or vendor to complete the written assignment set forth on Exhibit B and get specific Board approval therefor, except in those situations where the Board cannot refuse to approve under applicable law. The proposals may go beyond what the law technically permits, but I believe they are reasonable and so it is likely that parties contracting with the School District would abide by them. The School District is expected to approve the recommendation.

Note: Exhibit A consists of a proposed standard contract provision stating that a contractor/vendor shall request assignment of the right to receive payment in writing, submit an assignment form (Exhibit B) and that school board approval of the assignment is required, "after official Board action at a public meeting."

The school district's response also described in detail the school board's approval of specific third party payments.

The most that the School District staff could have done was to have acknowledged receipt of the instructions from Turkeyfoot Transportation to make payments to the leasing companies. There is nothing illegal or inappropriate about them acknowledging that the request had been made, and the School District staff did nothing until authorized to do so by the Board approval of the bills and the computerized bill payment list which every Board member had available.

The response stated that there was no appearance of impropriety or lack of controls, pointing out the following:

The Business Secretary could not have made any payment to anyone, relative or not, without Board approval and without the manual signature of the Board Treasurer, who is not related to the people involved in these transactions.

The indication in the present case is that the principal owner of Turkeyfoot Transportation, Inc., is a brother-in-law of the Business Secretary of the School District. There is no conflict of interest unless a public employee uses the authority of her employment "for the private pecuniary benefit of a business with which a family member is associated," and the private pecuniary benefit must be something having more than a "de minimis economic impact."

The Business Secretary was the person responsible for gathering together and preparing the requests for payments of bills to the School Board. Turkeyfoot Transportation was one vendor out of many. The Business Secretary had no authority, either as a Business Secretary, or as Board Secretary during the time that she was a Board Secretary, to confer any benefit on Turkeyfoot Transportation. She performed a clerical duty of preparing the bill list showing Turkeyfoot Transportation's request that part of its payment go to its leasing company. She had no authority to make that payment. As a purely ministerial act, she participated in the preparation of checks, but even when her signature was affixed by facsimile as Board Secretary, a situation which no longer exists, she had no authority to issue a check without approval of the Board and without the co-signature of an unrelated party, the Board Treasurer, who had to manually sign each and every check.

Even if the Business Secretary had the authority, which she did not, to authorize the payment to leasing companies of sums due Turkeyfoot Transportation, these payments could hardly be classified as anything but "de minimis economic impact."

There is no evidence to suggest that the same courtesy would not have been afforded to another vendor or contractor had it been requested or that it was not afforded in the past when requested.

Each and every Board member had an opportunity to raise a question if they thought the bill list contained an improper item. The Finance Committee Chairman of the Board reviewed each statement prior to recommending its approval and could have raised a question if there was a proposed payment that he or she deemed improper. Each Board member had before it the list of bills to be approved. The Board Treasurer, was required, after Board approval, to affix her manual signature to each check. It is respectfully submitted that the checks and balances constitute sufficient controls to prevent improper payments being made.

While it is true that the Board could assign someone else to look over the shoulders of this or any other employee, that is neither administratively nor economically feasible since checks are already provided in the above-mentioned form of review. In addition, there is the informal control existing by virtue of the fact that the Superintendent is ultimately responsible for the presentation of matters to the Board and exercises an informal, if not formal, role in reviewing the bill lists and requests for payment presented to the Board.

This is not the only circumstance in the Turkeyfoot Valley Area School District where the School District deals with people in the community who are undoubtedly related to the employees of the School District with whom they are dealing. It is impractical to appoint a separate individual to handle clerical or administrative functions in every case of such an imaginary conflict, and it is

indeed imaginary if the employee has no discretionary authority to actually confer a benefit on a related party.

DEPARTMENT OF THE AUDITOR GENERAL'S COMMENTS

Finding No. 1 of the report does not question a vendor's right to assign payments to third parties after a transportation contract is approved. In this case, the superintendent and a school district employee reached an understanding or arrangement with the contractor that the school district would make the contractor's lease payments. The arrangement was made before the contracts were approved.

The school district's response noted correctly that an assignment of payments should not "materially increase" the school district's obligations. In this case, as of May 2001 the arrangement had resulted in approximately 128 payments by the school district to two different leasing companies on five leases, in addition to the payments made directly to the vendor. The school district also kept the vendor's payment books for two of the leases and made payments on a lease for which there had been no agreement to do so.

Given all of the circumstances, the activities of the school district's staff relating to the leases appear to have been extraordinary and more than ministerial.

We disagree with the school district's view that school board approval of such an arrangement is not required under the Public School Code and PDE regulations. In any case, the procedure proposed by the solicitor appears to be sufficient to address the Finding and accomplish the purposes of Recommendation Nos. 1 and 2.

In regard to the issues of conflict of interest and appearance of impropriety, conflict of interest questions are ultimately to be resolved by the State Ethics Commission. In this case, it appears to us that the Board Secretary's role was more than merely ministerial and that the relationships of school district staff with the transportation contractor, as well as the relationships of school board members with other bus contractors, present a situation in which the school district should take steps to maintain public confidence in the basic fairness of its procedures by adopting our Recommendation No. 3, or some equivalent procedure.

In regard to Finding No. 2, the school district's response addressed the issue presented in our proposed draft Finding and provided an explanation for the failure to make a downward adjustment to the payments to the transportation contractor.

REPORT DISTRIBUTION LIST

This report is being distributed initially to the school board, solicitor and superintendent of Turkeyfoot Valley Area School District and to the following:

Department of Education
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Secretary of Education
Harristown 2, Tenth Floor
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Governor's Office of the Budget
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