The Sacramento City Unified School District Board of Education Was Negligent in the Establishment and Oversight of the California Administrative Services Authority

Issue

The Sacramento County Grand Jury received a complaint asking for an investigation of the Sacramento City Unified School District and the propriety of creating a joint powers agreement (JPA) between the California Administrative Services Authority (CASA) and the Sacramento City Unified School District (SCUSD) to establish an alternative retirement program for a select group of employees. Among the allegations were possible misuse of public funds, conflicts of interest, and an inappropriate relationship between SCUSD employees and CASA.

The Grand Jury was primarily interested in how and why this alternative retirement program, which benefited a select group of SCUSD employees, and required them to leave the employment of the school district for that of a contracting agency, could be approved by the Board of Trustees. The Jury was also concerned about the ethics and process utilized by the school board in the establishment and operation of CASA.

Method of Investigation

Review of Documents:

- "Preliminary Investigative Report on the California Administrative Services Authority" by the Sacramento Leadership Coalition on Public Education, July 9, 2003.
- "Final Report Review of the California Administrative Services Authority Program" by MGT of America, December 16, 2003.
- California Public Employees Retirement System (CalPERS) memorandum dated March 5, 2004, entitled, "Summary: California Administrative Services Authority."
- "California Administrative Services Authority Employee Handbook" of September 2000 and revisions of September 2002.
- Agendas and minutes of meetings of the Sacramento City Unified School District Board of Education.

- Video tape of March 6, 2000, Sacramento Unified School District Board of Education meeting.
- News articles in The Sacramento Bee.
- CASA documents, including bylaws and operating agreements.
- Relevant district correspondence and memoranda.

Interviewed:

- SCUSD current Board Members serving since 2000.
- SCUSD former Board Member serving in 2000.
- SCUSD current Superintendent.
- SCUSD former Deputy Superintendent, Chief Financial Officer and unpaid Chief Executive Officer of CASA – retired CASA member.
- SCUSD current Chief Financial Officer – CASA member.
- SCUSD current Chief Personnel Officer – CASA member.
- SCUSD retired Chief Personnel Officer – retired CASA member.
- SCUSD current Internal Auditor – former CASA member, current CalPERS member.
- SCUSD current Director, Employee Relations – CASA member.
- SCUSD current Analyst, Personnel & Employee Compensation – CASA member.
- SCUSD former Analyst, Personnel & Employee Compensation – prior CASA member.
- Executive Director, Service Employees International Union, Local 790.
- President, Sacramento City Teachers Association.
- Executive Director, Sacramento City Teachers Association.
- Chairman, Sacramento Leadership Coalition on Public Education.
- Division Chief, Actuarial and Employee Services, California Public Employees Retirement System.
- Staff Counsel, California Public Employees Retirement System.
- Complainant.

Attendance at SCUSD Board Meetings

Background and Facts

In the late 1980s and early 1990s, the Sacramento City Unified School District (SCUSD) had been beset by serious educational, fiscal and governance problems. Student achievement was declining. There was frequent turnover in the superintendency, and unrest and dissatisfaction among employees. A split board of education provided little leadership or planning on how to address the situation. Sacramento's then Mayor spearheaded the election of a new board. A new superintendent and a new chief financial officer (CFO) were hired to bring educational direction and financial stability to the struggling district.

Sacramento City Unified School District made educational and financial progress under this new administration. The Superintendent provided the educational leadership that had been lacking and test scores improved under his educational reforms. The CFO brought stability and financial soundness to the District and gained the trust and confidence of the Superintendent and the Board of Education. According to those interviewed, her decisions and recommendations were rarely questioned by the Superintendent or the Board. However, her managerial style was described as intimidating and controlling. The CFO also assumed additional responsibilities by becoming the head of personnel, as well as maintaining her position as financial officer. This resulted in the centralization of significant administrative power in the hands of one person. For example, the District's internal auditor, budget manager and personnel manager all reported directly to the CFO. The CFO became the conduit of information to the Superintendent and the Board. As a consequence, there was a lack of checks and balances within the administrative units she supervised.

Late in 1999, the CFO, on her own initiative, presented an alternative retirement program to the Superintendent to cover the three contract positions–the Superintendent, the CFO and the District's Legal Counsel. This plan also included approximately 100 non-represented (non-union) confidential and classified workers.

Implementing the plan required the establishment of a joint powers agreement (JPA), which required two or more public agencies to participate. Joint powers agreements are common in education, created to combine the resources of various agencies to provide services such as busing, insurance, purchasing, etc. This JPA would be unusual in that its sole purpose was to set up a retirement system. Only Long Beach Unified School District had established a similar program.

On March 6, 2000, the CFO proposed the formation of the JPA to the Board of Education. As presented to the Board, the rationale of the proposal was twofold: to develop a retirement program that would both encourage top administrators to stay with the district; and to enhance recruitment. The CFO strongly stated to the Board that the plan was "cost neutral." The presentation was made by outside consultants selected by the CFO. There was no consideration or discussion given to possible negative consequences. Unbeknownst to the Board but known to the CFO, there was pending legislation which could have jeopardized the cost neutrality of the JPA.

Two weeks later, the Board authorized the establishment of the new JPA, which was designated as the California Administrative Services Authority (CASA). The formation of CASA required the SCUSD Board of Education to appoint two representatives to the three-person CASA Board of Directors. The School Board, by resolution, delegated the responsibility to the Superintendent. This was in variance to the customary procedure followed in other district JPA appointments. The Superintendent allowed the CFO, who was also the Executive Director of CASA, to select the appointees. Neither of these appointees was affiliated with the District.

In June, the Yolo County Office of Education joined with SCUSD as a partner to form the JPA. The retirement program was implemented July 1, 2000.

Prior to implementation, the CFO went to the Board of Education on June 19, 2000, requesting new contracts for the top administration (Superintendent, Chief Financial Officer, and the District Legal Counsel). These contracts would convert expense money and travel allowances to salary and add ten additional years of service credit to retirement through the newly formed JPA. The Board viewed this action as a way to reward these employees for past services without a cost to the District. The Board unanimously approved these three new contracts.

The CASA retirement program is complex, but as described by the CFO, it offered enhanced retirement benefits to members of the new JPA. It involved increasing the computational CalPERS factor from 2.5 to 3 percent. For example, retirement benefits based on 2.5 percent of final compensation per year of service, with 30 years of service and a final annual compensation of $150,000, yields a pension of $112,500 a year for life. If the percentage-per year multiplier is raised from 2.5 percent to 3 percent with no other changes, the pension rises from $112,500 to $135,000. This is a 20 percent increase in retirement pay per year for life.

Approximately one hundred SCUSD employees who had joined CASA would leave the California Public Employees Retirement System and become members of CASA. They would be employees of CASA and their services would be contracted back to the District. The employees would hold the same positions, perform the same duties and receive the same salaries as they did with the District. They also retained all district benefits and all seniority rights. The CFO of Sacramento City Unified School District assumed the responsibility of unpaid executive director of CASA. In these positions, she oversaw the transfer of funds between the District and CASA and directed the retirement system, of which she was a member.

In order to make the retirement program work, approval by CalPERS and the Social Security Administration was necessary. CalPERS granted reciprocity to the CASA system, thereby allowing its members to leave the state public retirement system. Social Security officials also authorized withdrawal from its program.

In November 2001, approximately a year and a half after the founding of CASA, the CFO requested the Board of Education approve a pension obligation bond valued at $6.5 million dollars. The CFO stressed the low financial risk of the bond. The Board approved the bond with little discussion. In a memo to the Board, the CFO stated, that without the bond the CASA retirement plan is still actuarially sound, but “the bonding provides extra actuarial strength and security for participants in the new retirement plan.” According to the MGT report, the cost to issue the bond was $420,709.

In June 2003, the Sacramento Leadership Coalition on Public Education, comprised of local education organizations and community members, gave to the President of the

School Board, a document entitled, “Preliminary Investigative Report on the California Administrative Services Authority.” He referred it to the Superintendent. The report questioned CASA’s operations and activities and the relationship between CASA and the District. In response to the report, the Superintendent sent a letter to the coalition, which was critical and dismissive.

On July 9, 2003, the coalition held a press conference challenging the legality and propriety of CASA’s establishment and made its investigative report public. In response to the press conference and to the report, the SCUSD School Board added a discussion of CASA to the District’s workshop agenda of September 15, 2003. At that time the Interim Superintendent, appointed in July 2003, recommended an independent, outside fiscal and programmatic audit be performed immediately, and a separate review of all legal issues by an independent, outside attorney. The School Board approved a $40,000 contract for a 230-hour/two-month management audit by the national consulting firm of MGT of America. In addition, the Interim Superintendent engaged the services of Lozano Smith for the legal review.

On December 8, 2003, MGT of America presented its findings and recommendations to the District and the School Board. The MGT report was highly critical of both the establishment and operation of CASA. The report cast serious doubt that the alternative retirement system was “cost neutral.” A key question was, who was the actual employer of the classified employees–SCUSD or CASA? The report concluded that, if it was determined that the District was indeed the employer, the District could be responsible for significant financial obligations to CalPERS, the State Department of Education and Social Security accruing from July 1, 2000.

The report also concluded that once CASA was authorized, neither the Superintendent nor the Board provided appropriate oversight. The Board did not require periodic reports or yearly audits of CASA. The Board delegated to the Superintendent its authority to appoint two SCUSD representatives to the CASA Board. The Superintendent accepted the CFO’s recommendations for these positions of individuals who had no affiliation with the District. The MGT of America report stated, “By doing so, the District board and the former superintendent failed to ensure the district’s representatives on the CASA board understood the District’s direction and priorities, and were committed to protecting the best interests of the District.” The report also stated that the only communication between the CASA Board and the SCUSD Board was through the CFO. This situation permitted actions, such as allowing CASA to receive advances, charge indirect fees and change its bylaws without authorization from the District. Such actions by the CFO gave the appearance of conflict of interest.

In March 2004, CalPERS sent a memorandum to the District that contained results of its investigation of CASA to see if reciprocity with regard to CalPERS benefits had been appropriately granted. That investigation found that CASA employees were in fact employees of SCUSD and therefore did not have the right to opt out of CalPERS membership. It further found that CASA did not qualify as an agency with which

CalPERS could establish reciprocity. The report states, “CalPERS was not aware of any of these facts at the time we approved reciprocal retirement status and health benefits and would not have granted reciprocity if these facts had come to light.”

At its April 1, 2004 board meeting, the Board of Education unanimously voted to withdraw SCUSD from the JPA effective July 1, 2004. At its April 29 board meeting, the trustees voted to end the District’s relationship with any outside attorneys, financial advisors and other consultants who previously advised them regarding CASA. The Grand Jury recognizes that many of the issues and concerns raised by the MGT report are already being addressed. The Grand Jury encourages the District to continue in this positive direction.

Conclusion

The Sacramento City Unified School District Board of Education failed in its oversight responsibilities. It was negligent in its responsibility to protect the interest of all its constituents, including voters, students, parents, taxpayers and employees by authorizing a joint powers agreement ostensibly for retirement purposes. Inasmuch as Board members make decisions in complex areas, they depend on district administrative staff for advice and recommendations, including school finance, curriculum, student safety, personnel practices and facility use. In the case of the establishment of CASA, the Board did not receive or request a complete and balanced picture. By their own admissions, they were convinced by their administrative staff of the efficacy of a unique retirement program—a program that ultimately proved to be flawed, and a liability to the District.

Although the Grand Jury reviewed the conduct of Sacramento City Unified School District, some of the recommendations could apply to the administrative functions of all school districts within Sacramento County. In order to strengthen the integrity of the administrative functions of school districts, the Grand Jury respectfully requests all school districts within Sacramento County consider the report’s recommendations.

Findings and Recommendations

Findings for the Board of Education:

Finding 1. The Sacramento City Unified School District Board of Education did not fully explore, question nor understand the joint powers proposal presented by the Chief Financial Officer and supported by the Superintendent.

Finding 2. In approving the JPA, the Board authorized transfer of district classified employees to CASA.

Finding 3. The SCUSD Board, once CASA was established, paid little attention to issues of oversight and management of the JPA. For example:

a. The Board did not appoint representatives to the CASA board but delegated the selection to the Superintendent.

b. The Board did not require periodic reports or yearly audits of CASA.

c. The Board allowed CASA bylaws to be amended without approval.

d. The Board allowed the CFO to assume the position of Executive Director of CASA while serving concurrently as the District CFO.

Finding 4. The Board opted to reward its three contract employees (Superintendent, Chief Financial Officer, Legal Counsel) by giving them inflated retirement benefits. For example:

a. Granting 10 additional years of service credit which was excessive and unprecedented for public service positions.

b. Granting mileage allowances, travel expenses, and vacation pay to be included in the final compensation calculation for retirement was inappropriate.

Finding 5. The CFO and the outside consultants she selected appeared to mislead the Board with incomplete information and strong assurances of cost neutrality of the CASA plan.

Finding 6. The Board authorized the issuance of an unnecessary $6.5 million pension obligation bond and incurred financial liability with little or no discussion or understanding of the possible financial impact to the District. The $420,709 cost to issue the bond could have been applied to educational purposes.

Finding 7. The Board of Education and top administrators were dismissive of community concerns regarding the JPA and CASA.

Recommendations to the Board of Education:

Recommendation 1. The Board needs to fully investigate and research all proposals that incur financial obligations and have fiscal ramifications. A discussion of the pros and cons should be publicly presented with adequate provision for public input.

Recommendation 2. Future attempts of the Board to compensate district individuals for outstanding service should be within the limits of what is generally given to people in education.

Recommendation 3. The Board should monitor and control all agencies or entities that the school district creates and for which it assumes liability. The Board should not delegate its oversight responsibilities to others. The Board should demand timely reports and audits.

Recommendation 4. The Board of Education must guard against appearances of potential conflict of interest whether ethical or legal.

Recommendation 5. The Board should establish a process to assure that community and constituent concerns are heard and addressed.

Findings for District Administration:

Finding 1. The Superintendent allowed the CFO to control the central office without necessary checks and balances. For example:

a. The Internal Auditor reported directly to the CFO rather than to the Superintendent and the Board.

b. The transfer of funds between the District and CASA went unsupervised by the Superintendent and the Board.

Finding 2. The centralization of power in the hands of the CFO created a climate of intimidation and coercion within the administrative offices. For example, employees were discouraged from questioning the CASA plan and some stated they felt pressured into joining.

Finding 3. The proposed retirement program and the enhanced retirement package put forward by the CFO for herself, the Superintendent and the Legal Counsel were self-serving.

Finding 4. The appearance of a conflict of interest occurred when the CFO of the District served as the unpaid Executive Director of CASA.

Recommendations to the District Administration:

Recommendation 1. Community concerns regarding district administration actions or policies need to be fairly and openly addressed. A community oversight committee could be established to directly monitor the response to these concerns.

Recommendation 2. The Superintendent must actively oversee the business administration of the school district, as well as the educational program.

Recommendation 3. It is one of the responsibilities of the Superintendent to establish and maintain a positive climate within the district office. Communication lines should be structured in such a way as to encourage and permit employee access to the Superintendent, enabling all opinions to be heard.

Recommendation 4. The Superintendent is responsible for assuring that a system of checks and balances is maintained so no one person or a group can bring undue or unfair influence on decisions.

Recommendation 5. The internal auditor should be autonomous and responsible and accountable to the Superintendent and report directly to the Board on a quarterly or bi-annual basis.

Response Required

Penal Code Section 933.05 requires that specific responses to both the findings and recommendations contained in this report be submitted to the Presiding Judge of the Sacramento Superior Court by September 30, 2004 from:

- **Board of Education, Sacramento City Unified School District**