
Committee Meeting

of

SENATE EDUCATION COMMITTEE

AND

ASSEMBLY EDUCATION COMMITTEE

*“Testimony from representatives of the Department of Education
on the budget shortfall in the Newark School District”*

LOCATION: Committee Room 4
State House Annex
Trenton, New Jersey

DATE: February 24, 2000
10:00 a.m.

MEMBERS OF COMMITTEE PRESENT:

Senator Robert J. Martin, Co-Chairman
Assemblyman David W. Wolfe, Co-Chairman
Senator William L. Gormley
Senator Joseph A. Palaia
Senator Byron M. Baer
Senator Shirley K. Turner
Assemblyman E. Scott Garrett
Assemblyman Joseph R. Malone III
Assemblyman Jeffrey W. Moran
Assemblyman Gerald H. Zecker
Assemblyman Raul “Rudy” Garcia
Assemblyman Craig A. Stanley



ALSO PRESENT:

Darby Cannon III
Kathleen Fazzari
*Office of Legislative Services
Committee Aides*

Beverlyn Grissom
*Senate Majority
Committee Aide*

Carrie L. Mitnick
*Senate Democratic
Committee Aide*

***Meeting Recorded and Transcribed by
The Office of Legislative Services, Public Information Office,
Hearing Unit, State House Annex, PO 068, Trenton, New Jersey***

TABLE OF CONTENTS

	<u>Page</u>
David C. Hesper Commissioner New Jersey Department of Education	4
Elizabeth E. DeMatteo Business Administrator Newark Public Schools	5
Marion A. Bolden State District Superintendent Newark Public Schools	5
Michael Azzara Assistant Commissioner Division of Finance New Jersey Department of Education	11
John M. Sherry Assistant Commissioner Division of Field Services New Jersey Department of Education	38
APPENDIX:	
“Report on the Newark School Budget” submitted by David C. Hesper	1x
Statement submitted by Leo F. Klagholz Former Commissioner of Education	76x
Letter addressed to David C. Hesper from Beverly L. Hall, Ed.D. Former Superintendent Newark Public Schools	94x
lmb: 1-92	

SENATOR ROBERT J. MARTIN (Co-Chairman): We're going to start the hearing this morning that deals with the Newark School District and the budgetary shortfall. I'm Senator Martin, and I'm Chair of the Senate Education Committee. I note that all of our members are here. Senator Gormley is not in his seat, but I know he is out and about, around somewhere near here. He'll be joining us shortly, but Senator Baer, Senator Turner, Senator Palaia, and myself are here. The Assembly Committee members, with their honorable Chairman, Mr. Wolfe, is here. So I believe we have all members here from both Committees.

The purpose of this hearing is to ascertain some of what has happened in Newark. It's clear now that there's at least a shortfall of \$58 million in the operational budget. It will require probably some action by the Legislature. At least, there's been a request made that a certain amount of that shortfall will have -- is to be made up in the budget for this year's appropriation. So that is a matter that directly concerns the Legislature, and I think it's fair for us to say, before we provide any money to repair the current problem, we have a definite obligation and responsibility to find out what happened, as much as we can, and whether the problem has been fixed or whether there is still some serious mistakes.

In the interest of time, and I know the Assembly has a session, we're going to try to keep this as-- We'll allow the Commissioner to speak. He's brought other people here. Time permitting, we'll have as many questions as we can. I would ask you to keep it more, like, in the form of *Jeopardy*, at least from the Committee's point of view, that we put our issues in the form of a question to gather information. We anticipate that there will be

at least another meeting, based upon information gathered today, in which we will interview -- or at least, I guess, interview is an appropriate word -- other people with regard to this matter.

I will turn this over to Assemblyman Wolfe. I just want to make one point in the way that I've approached this. I ran across an article in the *New Jersey Reporter* that talks about the takeover districts, and it is concentrated on school performance and how well kids are doing in those districts, which is really, I think, when we cut through all the chase, that's really the bottom line of what we should be concerned about, how well are our kids being served. Unfortunately, we're not going to be dealing with that topic today, because we can't get there until we find out how our resources are being spent.

But there's a paragraph here written by a Francis Ann Burns (phonetic spelling) which says the following: "Across the country, 22 states have laws that authorize takeovers. State legislators, governors, and education departments have intervened in at least 19 districts, ranging from giant Chicago to rural counties in West Virginia. The new regimes have removed patronage jobs from the payrolls, uncovered fraud and mismanagement, and restored many districts to financial health." It goes on it talk about the fact that they may or may not have done the job in helping to improve student performance. But it seems to be fairly clear that in almost all of these takeovers throughout the country, at the very least, one could expect that you would be able to improve financial health.

I think all of us are shocked, dismayed, about the fact that the Newark School District hasn't even reached that level. The State takeover occurred in July of 1995. So this isn't something, I think, that we can say they

need, if they had a little time, that they needed for a turnaround. I think that deadline, whatever one would be liberal in granting it, has since passed.

So we are here to try to ascertain what's been going wrong, where has the money gone, and who may or may not be at fault from both an organizational point of view and an individual point of view.

Assemblyman Wolfe.

ASSEMBLYMAN WOLFE (Co-Chairman): Thank you very much, Senator.

I just would like to, very briefly I would say, reiterate some of the things you said, but also, perhaps, give the philosophical point of view that the Assembly is approaching in this particular hearing. This is rather unusual that we meet as a Joint Legislative Committee, which we do not do ordinarily. But, I think, the gravity of this situation warrants some investigation and some discussion of not so much what happened, but why did it happen, and what has been done, and what will be done to see that it does not happen again.

And Senator Martin, I think, said it quite eloquently -- words that our Assembly members have also discussed prior to our coming in here today, and that is the interest of the kids, whether it's in Newark or Madison, or wherever it is, is the number one priority. And I think that we do not have all the answers, but we're here to, hopefully, find out a little bit about how this situation arose. And I have to say, quite honestly-- I would ask the audience, who may have come here with a certain point of view, to put themselves in the place of us legislators. With the exception of Assemblyman Stanley, none of us represents Newark, but we all have had concerns expressed to us, as legislators, regarding the need for the comments for and the comments against

State takeover. The fact that this situation happened in a State-takeover district, I think, is even more serious than if it would happen in a nontakeover district.

And I'm quite dismayed, personally, when I received the copy of *The Star-Ledger* this morning, which was given to me, and then on the front page, there's a statement that, "Reports have been given to the Committee from former State officials regarding what happened in Newark." I received a report this morning that was faxed at 7:00 last night to the legislators. They did not see this report. This report appeared in *The Star-Ledger* this morning. Now, it's this type of game playing, I think, that has to stop. Legislators cannot stop this, but it's pointing fingers at people and making people look foolish, and I think we're here to get to the bottom of this. Whether we're leaking memos or undating memos, I think we really have to get to what happened, what had happened, and what can be done to see that it doesn't happen again.

Again, I want to thank the Senate and my Assembly members for being here.

And without further ado, I'd like to ask that Commissioner Hespe and his staff come on up.

SENATOR MARTIN: Commissioner, let me just tell you, that from what we understand in the transmittal, that anyone who speaks has to be on one of the -- in the first row. (indicating witness seats)

COMMISSIONER DAVID C. HESPE: One of the two front rows--

SENATOR MARTIN: No, actually--

COMMISSIONER HESPE: --or just this row? (indicating witness seats)

SENATOR MARTIN: --when they speak. It's only the front three microphones that we're able to mike.

COMMISSIONER HESPE: All right. I'll just have to repeat what they say, that's all.

SENATOR MARTIN: We did ask the Commissioner -- in just a preliminary meeting that Assemblyman Wolfe and I had with him last week -- to bring a number of people, including the current Superintendent, Business Administrator of Newark, as well as some of the key people in his office. So this is not-- He is not bringing a protective cover. (laughter) We asked him to have people here that if there were certain questions that he might not know, but somebody in his immediate supervisory level, that they would be here to assist us in getting to answers.

COMMISSIONER HESPE: Senator, may I introduce everyone?

SENATOR MARTIN: Yes, please.

COMMISSIONER HESPE: To my far left is Betsy DeMatteo, the Business Administrator for the Newark School District; to my immediate--

SENATOR MARTIN: Could you also indicate when they have -- their status, in terms of when they've been appointed?

COMMISSIONER HESPE: October--

ELIZABETH E. DeMATTEO: Twentieth.

COMMISSIONER HESPE: --20, 1999.

Marion Bolden--

MARION A. BOLDEN: July 21.

COMMISSIONER HESPE: --July 21, 1999. Marion is the current Superintendent in the Newark School District.

I'm David Hespe. I'm the Commissioner of Education, and March 26 -- very late March, I was sworn in.

Madeleine Mansier, my Chief of Staff. She arrived with me.

To my immediate far left, in the second row, is John Sherry, Assistant Commissioner, Division of Field Services, in the Department. September 1997, John arrived.

Mike Azzara, our Assistant Commissioner, Division of Finance, and Mike has been with the Department, in this role, since -- three years, which would take it back to 1996.

Ben Rarick, our Director of the Office of State-Operated Schools. He assumed that job in August -- six weeks ago. He was Acting Director -- sorry about that. That's right, Maria was. Yes, thank you -- January of '00. We have Anzella Nelms, Marion's Deputy Superintendent, who was appointed to that, along with Marion, about the same time.

And then Tom King, Director of the Office of Compliance, and Tom has been with the Department for a number of years.

SENATOR MARTIN: Now, you have a report that you are going to present in an oral form.

COMMISSIONER HESPE: Yes, we have-- I'm sorry, Senator.

SENATOR MARTIN: That's all right. Just go ahead.

COMMISSIONER HESPE: Senator, we have a report for you, which I will walk through orally. You also have an appendix of documents, which are referred to in that report. We are also providing the Committee

with two statements that we received yesterday, one from Dr. Klagholz, which we received late last night, which I think Assemblyman Wolfe was referring to, and--

SENATOR MARTIN: Just to make the record straight on that, too, as far as we can piece together, no legislator received this. The Office of Legislative Services received it this morning. Apparently, it might have been faxed late last night, but none of us have had a chance to read it. The most that we've-- It is available to all members. We asked to make it available in your packet. It will be made available to the public, but no one here has had a chance to digest it, other than what the article in the newspaper said.

COMMISSIONER HESPE: And we also have a statement, which we are providing to the Committee, from Dr. Hall, which we received on Tuesday.

I'd like to start the presentation, Senator.

Thank you, Senator Martin and Assemblyman Wolfe and the Committee members. I appreciate the opportunity to be here this morning. The subject of this hearing is not a pleasant one. I think this is a sad day for education, and as I make my report, I think you'll understand why. I know this issue has raised many concerns with you, with your colleagues, and with the public. I know it falls into question the ability of the Department to oversee the State operation in Newark and the other State-operated school districts, and in some respects, our ability to monitor all *Abbott* districts.

You alluded to the fact that we'll be looking for organizational, personal responsibility, and let me just begin with a clear statement regarding responsibility, and that is, that the Department of Education is my

responsibility. The State-operated district is ultimately my responsibility. And when you become Commissioner, I think you're responsible for not just what happens in the future, but also for everything that happened in the past and what your employees have done and not done in the past and that other people in your position have done and not done in the past.

It is my responsibility to come before this Committee to account for what happened, to take steps to assure you that this will not happen again, and most importantly to make sure that you're comfortable that the problem has been fixed, and fixed correctly to begin with, because this problem, as you know, has been going on for four and a half years. It's time it's been fixed, and I think we'll provide you assurances that it is being fixed.

And I hope, that when my presentation is concluded, you'll not only have a better understanding of what went awry in Newark, but what we have done to make sure that the public is comfortable with the expenditure of additional dollars for the Newark School District. That the Department is capable of ensuring that those dollars are going to the appropriate programs so that the children of Newark, as both you, Senator Martin and Assemblyman Wolfe had indicated, are what this hearing is really all about. We'll discuss a lot about the business of education, but rest assured the real reason for this hearing is to make sure the children at Newark have the programs that they deserve.

Today you'll hear a lot about what may have gone wrong. I only ask that while you listen you also keep in mind what has gone right in Newark and what the consequences could be for the more than 40,000 school children

in Newark if we do not act carefully and deliberatively to fix these issues. We must keep events in context.

And I will certainly start by saying that, I believe, State operation has not been a failure in Newark. Student performance is not where any of us want it to be at this point, but academically and in many other ways, I believe the Newark School District has made some great strides on the State operation. And I would also ask you to remember why the State took control in July 1995, and there are certainly statements in the report detailing findings by the Court on this issue. Also, I'm sure you have a copy of the Comprehensive Compliance Investigation.

When State operation commenced in 1995, the number one goal of Governor Whitman, Commissioner Klagholz, and District Superintendent Beverly Hall was the health, safety, and education of the children. The State's primary focus was to create a foundation upon which the district could build in the years ahead. In the four years that followed, significant progress was made. And in your packet, you'll see a list of these accomplishments of the schools of Newark and the people in these schools and, of course, Dr. Hall and Dr. Klagholz during State operation, that is attached to the report.

I would just like to also indicate that, although insight is a wonderful thing into these issues from a vantage point of the present, I think it's always easier to look back and say what should have been done in the past knowing what you know today. In hindsight, should more attention have been paid to the district's business office? On the district's business operations? Certainly, an answer to that is yes. But as we go through the chronology of events in Newark and the Department that led to our realization that there is

a \$58 million budget shortfall in the district, we should keep in mind what other pressures and challenges were in play. And we should ask ourselves whether the actions taken by the players were reasonable, at the time, given the contexts, of the events that were occurring around them.

I ask you to remember that an attempt was being made to turn around the school district with serious problems, the biggest school district in the State. We had to deal with ineffective bureaucracy in some areas, entrenched local opposition in others. You'll see from some of the news accounts that we've also provided, as to issues going on at that same time. Those are from the conclusions there. The magnitude of the problems that needed to be addressed were, in some aspects, enormous.

And you should also remember that there were many other issues at work on a State level, that the Department was gauged in Core Curriculum Standards assessment system, *Abbott* implementation, the new school funding formula, charter schools choice, and others. As I go through what we know about the events that led to the shortfall, I ask that you keep this larger picture in mind. All of us need to question whether the decisions that were made at the time were reasonable in the context of, also, that larger picture.

Why don't I just walk you briefly, just so you have a feel for the structure of the report. Then, I'll get into some of the findings in the report. The first is you have a table of contents, then a brief introduction, background on school finance, and what was going on pertinent to background with the Newark budget. You also have a section on-- You'll then have a chart on the various budget information, which we'll go through in a second. Then, you'll have a background statement on State operation. Then, you'll come to a blue

sheet. After the blue sheet, you'll see a chronology of events concerning the business operations from '95 to '96, and then you'll see two additional sheets, one of what else was going on in the district at the time, what else was going on in the Department at the time, and that is repeated after each blue sheet for each year until the present.

At the end of those various years' chronology, towards the end of the report, you will come to conclusions and some recommendations. The last blue sheet in the book, these are conclusions that we've drawn based upon all the information we know as of yesterday and corrective actions that have been taken, and, most importantly, 10 recommendations regarding what else needs to be done to make sure you have that confidence, and we have that confidence, that this will never be repeated again.

With that said, let me start my overview with the numbers chart that is around four pages in. I'm going to ask-- Mike's not on a microphone. I was going to Mike Azzara to work through this with us.

If you could come up, Mike, and I'll let you sit in Madeleine's seat, and you can work through the fiscal chart.

ASSISTANT COMMISSIONER MICHAEL AZZARA: On the far left column, what you'll see is categories of expenditure, revenue, and fund balance related to the district's General Operating Fund, their Early Childhood Program Aid, and their Demonstratively Effective Program Aid. We're grouping those three together because up until '97-'98 at--

SENATOR GORMLEY: Excuse me. Where is it?

MR. AZZARA: The fourth page, in between the -- right after the budget.

SENATOR GORMLEY: Okay.

MR. AZZARA: Do you have it?

SENATOR GORMLEY: Maybe we'll number the next report, the pages.

MR. AZZARA: Sorry about that.

SENATOR GORMLEY: No problem.

MR. AZZARA: This is--

SENATOR GORMLEY: This is so easy to understand.

MR. AZZARA: Yes, I know. That's why we're walking-- It's very difficult to understand.

SENATOR GORMLEY: Thirty-three different chronologies.

MR. AZZARA: Yes, but they are grouped by years, and I think we can walk them through.

SENATOR GORMLEY: Okay.

MR. AZZARA: And by the way, we were going to group into one, but we found it to be even more muddled than grouping it into three. So we did actually combine them.

SENATOR GORMLEY: There's an initial perception of muddle.

MR. AZZARA: Okay. So we'll get back to this.

Up until '97-'98, the QEA had a category of aid called at-risk aid, which was part of the General Fund, which was then replaced by ECPA and DEPA, where it became restricted funds. So, in order for an apples-to-apples comparison from '95-'96 through '99-'00, we have to take a look at all three of these categories.

What you'll see in '95-'96 is that the district's expenditures in that year total \$505 million. The revenues that year were \$497 million, and their structural deficit, as we call it, in other words, where expenditures exceeded revenues, was 8.5 million. But you'll notice they also had a significant amount of surplus that year, and, in fact, had indicated they were going to spend 18.5 million of it. So, in fact, in '95-'96, while they had a structural deficit, they didn't even spend the full amount that they had budgeted, and, in fact, didn't use as much as 10 million of the surplus that they had planned to spend that year. What you'll see at the bottom is what they had left at the end of the year.

The undesignated fund balance is balance that they just kept in surplus, a rainy day fund. They had 13 million that year. The designated fund balance is the amount that they say that they're going to use the following year to balance that budget. Okay. So in other words, when they put their budget together, they said, "Our expenditures exceed our revenues by 29.894, and we're going to use surplus to cover that." The overall fund balance at the end of '95-'96, which is both the undesignated and designated, was 43 million in '95-'96.

We move on to '96-'97, and you'll see the expenditures of 497 million, with revenues of 520 million. That's a bit deceptive, because the 520 million revenue figure includes a \$26 million special appropriation that was given to the district at the tail end of that year and, in fact, was not budgeted for spending that year, but was to lapse into surplus for the future year. So, when you see the structural balance of 22.4, okay, it, in fact, without the \$26

million special appropriation, would have shown a structural deficit of about 4 million that year as well. Okay.

At the end of that year, you'll see that they had an undesignated fund balance. I mean, the rainy day fund shrunk from 13 million down to 3 million at the end of '96-'97. They designated, for the subsequent year's budget, '97-'98, \$44 million, okay, of which 26 million came from that special appropriation I talked about. In '97-'98 -- and this is where the financial problems really started to mount -- their expenditures were, roughly, \$535 million, the revenues were \$481 million. And that was the first year of CEIFA, and it was the first year we were going back to actual enrollment adjustments after a six-year hiatus. So the district had incurred about a \$34 million reduction in State aid because we had gone back to current year enrollments as the basis for funding districts, which was also one of the reasons that we gave them the \$26 million appropriation to help them phase that in over time.

You'll see that what happened, though, is at the end of the year they had a structural deficit of expenditures over revenues of \$53 million. And, in fact, they exceeded the appropriated surplus that they had been approved to spend by 9 million. So, despite the additional 26 million in surplus and the -- which led to a \$44 million appropriation of surplus, which is what they were approved to spend that year, they actually spent 53 million more than revenues, 9 million more than they were approved to spend in '97-'98. They ended up with an undesignated fund balance, and this is where it starts to get a little tricky.

SENATOR GORMLEY: It's been tricky so far.

MR. AZZARA: They ended up with an undesignated fund balance, a rainy day fund, that was in the red, minus 9 million. And the reason for that is because they designated-- In other words, when they put their budget together for '98-'99, they did not have the benefit of having closed records for '97-'98. They could not tell what their financial position was. They did not have an audit. They estimated that they were going to have about \$22 million available in surplus to balance the following year's budget. But when the audit finally came in, that was not the case. They only had about 12.8 million in surplus. So their budget, starting '98-'99, was technically in the red by \$9 million because they didn't have the surplus to support the appropriation they made.

In '98-'99, the structural deficit continued where their expenditures exceeded revenues by 28.3 million. Okay. The appropriated surplus you see there did not materialize, and in fact, right now, we are still working to reconstruct the '98-'99 school year and get an audit done. This number is soft. But based on information that we have available now, it looks like they may end up with a '98-'99 deficit of anywhere from 5 million to 15 million, and currently it looks about 11 million. But that number is soft, we're finding things daily that change that.

COMMISSIONER HESPE: You should also be aware that that number does not include approximately 9 million in unpaid bills from that year--

MR. AZZARA: Right.

COMMISSIONER HESPE: --which we have included in '99-'00, so that number would be higher.

MR. AZZARA: If we put the 9 million in unpaid bills that we found when we went in that were never recorded or paid, that deficit in '98-'99 could be as much as 20 million.

SENATOR MARTIN: I guess, just jumping to the chase, this information may be relatively new, but it's interesting that you pose this as they, in this period of time, when this, as you know-- As Assemblyman Wolfe said, this was a State-takeover district. This was being run by the Department of Education. So, I mean, I think that the most general question we all want to know was if this data wasn't available to you then, why was it not -- who was -- shouldn't there have been someone to at least-- We're not putting fault on where the spending is, but who is doing the budgetary analysis at the time? It seems to us that no business, whether public or private, would operate with a checkbook and not know what was in their account. It seems like there's just a spending pattern here where there is no tally as to what we have available.

Admittedly, in the beginning, there was a surplus. So maybe people could be a little sloppy, but what's, I think, disturbing -- what you just described, Mike -- is they got worse the longer the State was providing the takeover. It took to the second year to hit the \$53 million figure. So things were not getting better. They seemed to be multiplied, so maybe you could--

ASSEMBLYMAN WOLFE: I'd like to ask, along those lines. What you're showing us, I would say this -- not being funny -- but gross figures in total, but also, you could say, gross bad, but-- Well, looking at the total picture, but where -- will you talk later on to us about where or when the red flags first began to appear that something was wrong, or did it just continue to become cumulative?

COMMISSIONER HESPE: Actually, I was going to go from this to those very issues.

ASSEMBLYMAN WOLFE: Okay.

COMMISSIONER HESPE: Maybe 10 or 15 minutes more, if that's okay?

ASSEMBLYMAN WOLFE: Okay.

COMMISSIONER HESPE: Is there a question on the numbers?

SENATOR GORMLEY: Can I be honest with you? If I may make a suggestion because, believe it or not, some of us are having a problem keeping up with this.

COMMISSIONER HESPE: Okay. Do you want us to run through it again?

SENATOR GORMLEY: What I would suggest is start with the first problem, the person and the date, and we'll work backwards from the problem, because we're getting all this information thrown at us and then you'll expect that we will remember this. I'd like to know the first time, the first red flag, the first date that the first person who made a mistake.

SENATOR MARTIN: If I could, let him make his presentation. He's identified a problem. Now, there's a couple of things we want to know. How it happened? And we at some point, when I briefly talked to the Commissioner last week, I said, we're going to need an organizational chart to understand who is doing what in terms of the financial responsibilities as part-- I assume that that will be part of your presentation.

COMMISSIONER HESPE: That's part-- I'm trying to, believe it or not, approach this logically. So I think the first -- it's important to

understand what the dollar problem is, because this is substantially about dollars, and then move into the reasons that that occurred. And then we can, I guess, spend a great deal of time trying to get some -- to those issues that you have concerns with that I haven't addressed.

I just want to go back for a second--

SENATOR BAER: Mr. Chairman, may I ask, through you, if along with this explanation of what was happening within the Department, if the Commissioner knows, if he could also tell us how this ties in with any involvement to the State Office of Management and Budget and any information that alerted them or any role that they played relative to these events, because I think that's also relevant for us to know?

Thank you.

SENATOR MARTIN: We'll make sure that that part of it is asked.

Go ahead.

COMMISSIONER HESPE: Okay. Just a moment on financial requirements of school districts. As in the early '90s, all school districts had to have adopted the prescribed format of double-entry bookkeeping in New Jersey utilizing Generally Accepted Accounting Principles, which are known as GAAP. This practice allows the district to constantly track its fiscal position. The use of GAAP ensures, in bookkeeping practices, that anyone who comes into the district to review your books will know how you're going about it. They'll know what line items you're using. They'll know that you used a double-entry bookkeeping system. So that's the first requirement that, I think, we should understand.

The second requirement is that, in order to ensure fiscal accountability, each district, under the statutes, is required to have an annual audit. You'll see it sometimes referred to as a Comprehensive Annual Financial Report, or CAFR, which is more than the audit. It also has recommendations in there as well. The books for the prior fiscal year in that is due by November 1 of each year. State law requires that the district prepare a monthly financial statement and to have the Treasurer of School Moneys to compare a monthly statement, as well, regarding the monthly reconciliation and account balances. Those two forms -- those monthly forms -- are called A-148s and A-149s. You can see that there. (indicating report)

We also should keep in mind that any decision to implement reductions to the district's budget in needed programs and services would directly implicate the Supreme Court's order in the *Abbott V* decision. That decision requires the *Abbott* districts, of which Newark is one, to implement a number of new programs and services, Whole School Reform, early childhood education, and the State is required to fund the costs of those new programs to the extent that the district's budget cannot be reallocated or reprioritized to support those efforts.

Those additional State aid dollars are provided through what we call the *Abbott* Supplemental Funding Process. You'll see that, in order to cover the shortfall in '99-'00, we approved a 15 million supplemental request in the springtime, and that was contingent on our receipt of the '97-'98 audit. We said at the time that number might go up or down and, indeed, it did go up. In January, we approved another supplemental fund request of \$22 million. That's all pursuant to *Abbott*.

We should also be aware that this structural problem that Mike was referring to--

ASSEMBLYMAN WOLFE: Commissioner, could you say that again? Fifty-seven million when?

COMMISSIONER HESPE: No. Twenty-two million in January of '00, and 15 million in May of 1999.

ASSEMBLYMAN WOLFE: Okay, thank you.

COMMISSIONER HESPE: In the originals-- I'll get to the overall district supplemental funding requests in a second, but there were two pieces. The first one was a 15 million supplemental funding which we approved in May and then indicated that that number would grow or decrease based upon the '97-'98 budget. And of course, the '97-'98 budget was important because it would tell us not only what the status of the district's accounts were, but the status of its surplus, and if there's surplus available to the district, that 15 million figure might very well go down. Conversely, I don't think anyone foresaw this. The district's '98-'99 budget actually had an actual deficit where the bills were going unpaid, that number would substantially increase, as it did, as you saw.

Next, I'll get to some overview of some of the more important findings in this report, and this is directed to, I think, Assemblyman Wolfe's question about what's the order of our information on this. If you go to the first blue tab, you'll see the '95-'96 chronology. I think the first thing you should be aware of is, when the district was taken over by the State on July 12, the computer system that was used by the business office is an MSA system, a Dun and Bradstreet. That system was functional. It was capable of general

ledger and account balancing. However, it wasn't programmed for GAAP. It's not Y2K compliant, and it was to some degree unreliable, to some degree, I think I should--

The system that had been used by the schools for payroll was unique to the district. You should be aware that the two systems were not integrated at that time. At that point, as we have already indicated, the district had a General Fund balance going into that year. So that's the first snapshot, I think, you should get, that the district had a functional system, but it had -- it needed to be upgraded. I think that's the first snapshot.

If you go next to the next blue divider, you'll see the chronology for the '96-'97 school year. You'll see, on November 4 of 1996, a letter from the State Superintendent to the Department, and that letter, on November 4, indicates that the audited financial statement for the previous year, which was due in November, would not be available until late-- Three reasons were given for the delay: First, the financial systems, the computer systems that generate personnel transactions and payrolls, were not linked directly into the accounting system; grant administration was a problem; and also the inability of the Treasurer to supply the school system with timely reconciliations was also a problem.

If you go next to the next blue statement, we'll look at another snapshot. We just saw there that the '95-'96 CAFR was late, and the reasons for that. And then we'll see the '97-'98 year, and you'll see there that there's a letter dated June 20, from the district to the Department, which basically indicates that there is a late submission for parity aid transfers based upon -- it was a byproduct of delays.

We lost you. I think we lost you.

ASSEMBLYMAN WOLFE: Excuse me, Commissioner. We're looking for that. Where is that?

COMMISSIONER HESPE: June 30 of 1996. I'm sorry, '97-'98 actually, I was in.

ASSEMBLYMAN WOLFE: Starts with July 2 on our--

COMMISSIONER HESPE: Yes. Well, you've got to go to the end.

ASSEMBLYMAN WOLFE: Okay.

MR. AZZARA: Third page.

COMMISSIONER HESPE: Yes, bottom of the -- because we were right at the end of that fiscal year.

ASSEMBLYMAN WOLFE: Okay.

COMMISSIONER HESPE: And there you have a letter from the -- June 30 from the district to the Department basically indicating a whole host of reasons for late submission of parity aid and indicated a whole bunch of problems with the business office at the time. They're not GAAP accounting, and school-based budgeting was also indicated.

I'm just running through just a couple of documents. You should definitely spend a lot of time in the chronology, because I do think it does paint a picture. The next statement--

SENATOR MARTIN: That was the year that they had a \$53 million deficit. They're also requesting that all their accounting and audits would be late being submitted.

ASSEMBLYMAN WOLFE: Could I ask a question on that June 30 memo? On the next page, it says, "Because of these circumstances, we are asking for a waiver of the requirements for preapproval of budget transactions prior to committing funds." Was this something that was typically done?

COMMISSIONER HESPE: Yes. This was applicable to all *Abbott* parity aid requests.

ASSEMBLYMAN WOLFE: Who would approve those? Who would, typically, approve those?

COMMISSIONER HESPE: The Department would approve those and then in all but the State-operated districts -- we had a group -- we had a team to do that.

ASSEMBLYMAN WOLFE: So in other words, the Superintendent is saying, despite these three problems that she cited, they're asking that no one approved what they're going to be doing?

COMMISSIONER HESPE: Yes, well, they're looking for a waiver of that.

Mike has a lot more history on that.

ASSEMBLYMAN WOLFE: Okay.

MR. AZZARA: She was basically asking to be able to spend as she wished, and us ratify it later.

SENATOR GORMLEY: Oh, okay.

ASSEMBLYMAN WOLFE: That's good.

Assemblyman.

ASSEMBLYMAN MORAN: What was the answer?

COMMISSIONER HESPE: The answer was yes.

ASSEMBLYMAN WOLFE: Yes.

COMMISSIONER HESPE: I guess that's a short answer.

Right, Mike.

MR. AZZARA: Yes. Yes.

COMMISSIONER HESPE: The next blue--

ASSEMBLYMAN MORAN: Mr. Chairman, if I could ask a brief question of Mr. Azzara?

Did any other school districts in the State request that waiver?

MR. AZZARA: No.

ASSEMBLYMAN MORAN: Thank you. If they did, would they have gotten it?

MR. AZZARA: No, and neither did Newark.

ASSEMBLYMAN MORAN: Okay. Thank you.

ASSEMBLYMAN WOLFE: Excuse me, you're saying they didn't get that waiver that they requested?

MR. AZZARA: No, they did not.

ASSEMBLYMAN MORAN: Newark did not get the waiver?

MR. AZZARA: No, we did not grant them that waiver.

ASSEMBLYMAN WOLFE: So, therefore, their expenditures were preapproved by the Department.

MR. AZZARA: No. No. They-- She asked for a waiver--

ASSEMBLYMAN WOLFE: Right.

MR. AZZARA: The waiver would have given her preapproval.

ASSEMBLYMAN WOLFE: Right.

MR. AZZARA: Okay. We refused to give it to her.

SENATOR GORMLEY: I think we're talking de facto.

MR. AZZARA: Okay.

ASSEMBLYMAN WOLFE: Okay.

MR. AZZARA: What led to this was the fact that they were submitting bills, okay, that had nothing to do with their plan for reimbursement, and we were rejecting them. She wanted-- The problem was they weren't spending consistent with their plan. And, in fact, as late as January of that year, they hadn't been approved. We hadn't approved one, single expenditure for their parity aid plan. She was worried they weren't going to spend the money, but we forced them to give us the explanations of why they were modifying their plan and prove to us that the expenditures they were modifying it with met the spending criteria for parity aid. She was not happy with that because she didn't think they'd be able to spend the money if they had to get preapproval, if they had to come to us first for approval, that they would not be able to spend it.

SENATOR MARTIN: Well, I guess what we're-- But they just went ahead anyway. They didn't get your approval or you didn't give them a waiver, but things just-- They more or less did what they did.

MR. AZZARA: Well, I think what happened on the parity aid plan was at the end, at the tail end, they started giving us some very big ticket items, capital expenditures, things like that -- that they would send us the letter telling us what it was they wanted to do. It met the expenditure criteria for the parity aid, and we would give them the approval to go ahead with the expenditures.

COMMISSIONER HESPE: So they were-- We did insist that they be new projects, but it appears that a lot of them may have been actually--

MR. AZZARA: And a lot of them, it appeared, probably were planned prior to this, not as part of the *Abbott* one, but they did meet the *Abbott* regulations, and we did approve them for the parity aid.

SENATOR MARTIN: Well, what's the difference in-- If they got a waiver, then they could go under DOE approval, but not receiving a waiver and spending money anyway, there were no repercussions, right?

MR. AZZARA: No. No. What happened was-- No. What they did, okay-- What they wanted was a waiver to go ahead and spend, and then submit the bills later for ratification. What we made them do is tell us what they were going to spend the money on before they spent it, approved it as consistent with the regulatory requirements for parity aid, and then they spent it. Now what it appeared was that some of these expenditures, although they met the *Abbott* parity aid requirement, they weren't part of the originally approved plan, but they requested modifications of the plan, which were allowed under the regulations. We did it for all the *Abbott* districts. As the course of the year went on, subsequent events, and things like that, they came back in with modifications. But they all had to prove that the expenditures that they were asking to modify the plan with were, in fact, consistent with the regulatory requirements for spending the money.

ASSEMBLYMAN WOLFE: Say that again.

SENATOR MARTIN: Let me ask you one point that's directly below that in the next paragraph. It says, "The Strategic Plan Annual Report for '97-'98 acknowledges that no reports were filed." The report acknowledges

that no reports were filed because the district did not have automated means of assigning staff to the appropriate budget accounts established to pay their salaries because changes in State law meant that large numbers of staff had to be transferred into new accounts. The fact that the Department knew that they weren't producing these kinds of reports -- wouldn't that, as an oversight responsibility, trigger somebody to say, "You've got to produce them, if not in this form, in some other form. If you don't have the personnel there, then you have to make some kind of shifting-- What happens? It seems like everybody is getting off the hook by writing a memo saying, "I got a problem," and just sending a memo to somebody else and then saying, "Well, don't blame me. I told you." Doesn't something happen when a memo like that gets reported?

COMMISSIONER HESPE: Well, I think, the answer to that is things were happening but, certainly, they were not effective. I have just one comment on that, and I'm going to take you to a memo earlier in that year and then to a second memo, which gives you a snapshot, I think, of what was happening. The first is that, in terms of the monthly financial reports, I don't think there's any question that the Department was well aware that they were not following those monthly financial reports. I think four or three were filed throughout the entire State operation. The reasons for that--

ASSEMBLYMAN WOLFE: Could you just stop right there? If you said these are monthly reports and only three or four were filed over a, I guess, you said four and a half years of State operation, then who or what would have been responsible to go back and demand that those reports be filed, be submitted as required by law?

COMMISSIONER HESPE: Yes. I think we-- If you could just hold the question for a minute, and we can get to this memo, I think you'll get a snapshot--

ASSEMBLYMAN WOLFE: Okay.

COMMISSIONER HESPE: --of an answer, and then I'll follow through on that.

If you go to '97-'98, February 2. If you just back up a couple of pages to February 2 and then -- which is in response to the January 8 memo you see above that (indicating) regarding problems -- these type of problems -- the memo basically indicates that the problems in carrying through on corrective actions really have two major components. The first and most serious was the lack of internal controls. Junior staff were not held accountable for implementing corrective action plans.

The second component of this problem was that communications with the Newark and various department offices are poor. Regarding solutions, the memo stated, "The group all agreed that the solution to this problem requires your personal communication with Dr. Hall on the seriousness with which you take this matter. This conversation can take one of three different approaches, wherein you would communicate to Dr. Hall one of the following three messages." There are three options there. (indicating report)

The memo explained each option and came through with a recommendation. On the recommendation is, "First, that this matter is urgent and has been overdue for a resolution for quite some time. Second, that a pattern of failure in compliance has developed over the past few years, and this

will not change unless specific incentives or specific consequences are used as leverage for change. And third, methods of collaboration and correspondence at our level have been exhausted, and you should talk with Dr. Hall personally to bring this matter to resolution.”

So at this point in time, we’re at February 2 of 1998, and this has now been brought all the way up the chain of command. Things are happening at this point in time -- there’s total inaction.

ASSEMBLYMAN WOLFE: Excuse me. This letter was sent by Ron Brady?

COMMISSIONER HESPE: Yes. Ron Brady to--

ASSEMBLYMAN WOLFE: Commissioner Klagholz.

COMMISSIONER HESPE: Ron Brady is the former director of the State-Operated Schools Office.

ASSEMBLYMAN WOLFE: And this went to Commissioner Klagholz.

COMMISSIONER HESPE: Yes.

SENATOR BAER: What incentives or consequences?

COMMISSIONER HESPE: For failure to comply with the letter? Well, if you go-- We certainly know that if you go to-- We’ll look at another memo, which is immediately-- If you go to the next blue divider--

SENATOR MARTIN: Just before you go there, I think those options are really interesting. Is there some place that there was some decision made as to what option they were getting?

COMMISSIONER HESPE: No. No one is aware of any options being communicated.

SENATOR MARTIN: Because the first one to Dr. Hall was, "You fix it, and I'm holding you accountable." The second one was, "Fix it, and here is how I want you to fix it." And the third one is, "Can we help you get this done? If so, then how?" I mean, that seems like an appropriate, sort of, posture to take, but you're not aware that anything happened other than discussing those as strategies?

COMMISSIONER HESPE: We know the district continued to struggle with corrective actions that were not effective, so that there were things going on to try to correct this problem. They were just not effective, but we don't know what -- certainly no one that we have been--

SENATOR MARTIN: None of those options were settled on as a policy that you're aware of that was--

COMMISSIONER HESPE: We have one of the draft letters that was setting forth a particular option which was never sent, and that's-- Junior staff do not know what the conversations were. So we're kind of at a dead end on that. We do know that the corrective actions continued from that point on, but they continued to be ineffective, and they became ineffective as a point that you see in September 1 of 1998, which is under the next blue chart. You have an E-mail from the County Superintendent, Mary Louise Malyska, to Ron Brady, and it follows up on a meeting they had the previous day with Newark business staff. She says, "Let me make one thing very clear. GAAP is the accounting code structure of business and industry, as well as every school system in the State of New Jersey, since this administration required the shift around five or six years ago."

SENATOR BAER: Where are you reading from?

COMMISSIONER HESPE: September 1, Senator, 1998, onto the next blue divider. It's the second entry in '98-'99. She says, "Let me make one thing very clear. GAAP is the accounting structure of business and industry, as well as every school system in the State of New Jersey, since this administration required the shift around five or six years ago. Every district had problems switching to GAAP, everyone complained, but by the next budget year, with a lot of pushing, mentoring, and just plain hardball, the Department had every business administrator in the State on board. Can it be that everyone in education has learned to accommodate, but it is unreasonable for us to expect that Newark can accommodate? We must have accurate and timely financials from these people or we invite theft, forgery, consistent (and potentially purposeful) mistakes, and more. It is critical that LK" -- and I assume that's Commissioner Klagholz -- "know about and correct this problem immediately."

So we could have a memo eight months later which very much indicates that this problem continues, and it continues at a very serious level.

SENATOR MARTIN: I know you know this, but just so we focus. One of the questions related to this, and it's raised in that particular memo, is whether the inability, slowness, difficulty in changing to GAAP in monthly accounting was because they didn't want revelation of the fact -- and I'm using they, we could say you -- but the Newark people didn't want to have a focus on where their financial balance was at the time. That's one of the conclusions one might very well draw. It isn't just a difficulty here, but it's a fact that having done so, we would all see that they -- the highest spending school

district in the State -- were still running millions of dollars higher than what the budget had anticipated.

COMMISSIONER HESPE: Yes. I would not make that conclusion. I think that there were efforts underway to try to resolve this problem. They were just highly ineffective. When they moved away from the original system that was in place at the time of State operation and moved to putting -- became committed to putting a new system in place, I think the difficulties with putting that new system in place put them in a very bad position. Normally, what you do is you run the old system at the same time you put the new system in place. You have parallel systems.

SENATOR MARTIN: This allowed them to buy some time, to be able to continue to not disclose the fact that they weren't operating under the budget that the State had provided.

COMMISSIONER HESPE: I don't think there was a conscious decision to say, "We're not going to prepare these monthly financial reports." I think it was a more of an inability to prepare them.

SENATOR MARTIN: Well, it seemed as though they serve another purpose.

You wanted to proceed.

COMMISSIONER HESPE: October 28 of that same year, you see a memo from Loren MacIver, who is the Business Administrator, to Leonard Hellenbrand, who is the Chief Operating Officer, and then to the State Superintendent, regarding continuing problems in the district. They're indicating that the change in the chart of accounts and GAAP coding, "Did not allow us to post accumulative payroll charges into the general ledger on a

regular accurate basis. The lack of fully posted ledgers meant that we were unable to produce, in a timely manner, the necessary A-148s” -- the monthly financial reports -- “and more importantly, the trial balances and other analytical documents on a monthly basis from the financial information systems.” It discusses the transfer of certain people in the district, and he indicates that they, “Made a conscious decision that we’re not going to interfere in their management and implementation of the PeopleSoft Project by constantly dragging them back in to be included in the day-by-day operations of their respective departments.”

And I think that’s important to know, because you can see them struggling to put in place this new system. I think that’s important because it demonstrates there was action throughout this period in time -- just the action did not correct the problem, and obviously, from the September 1 memo, above, was still very serious three years into the State operation.

SENATOR MARTIN: You don’t think that had they been able to somehow put GAAP into place, show a clear picture of their budgetary place at that point in time, that the Legislature would not have been outraged by the fact that they were running up structural deficits for -- ever since the State had taken over the district?

COMMISSIONER HESPE: Yes. Well, two separate issues. The first is, I want to demonstrate they were doing something. However, there is no excuse for this problem not to be corrected three years into State operation. So let me-- You should keep those two thoughts separate. They were struggling with something, but is there an excuse for this not being corrected three years in? I think the answer to that is no. There really isn’t an excuse

for that. It can be fixed, and there are other systems available, but there were bad decisions made in terms of what systems to use and how to go about implementing them. We'll get into that in a second.

I think the next--

ASSEMBLYMAN WOLFE: Excuse me.

Commissioner, before you move on, in that same scenario on the 28th, at the bottom, it indicates difficulty of establishing a working relationship with the Treasurer of School Moneys. Who would that be at that time?

COMMISSIONER HESPE: The city of Newark had that employee. I do not know what the individual's name was.

ASSEMBLYMAN WOLFE: That would be a municipal employee, or a State employee?

COMMISSIONER HESPE: It was a municipal employee.

ASSEMBLYMAN WOLFE: Okay.

SENATOR BAER: Mr. Chairman?

SENATOR MARTIN: Yes.

SENATOR BAER: Previously, I asked about incentives and consequences that you referred to. You said we would get back to that.

COMMISSIONER HESPE: Okay. I'm sorry, Senator.

SENATOR BAER: I don't think we did get back to that, and I'd like to know what incentives and consequences were available to the Department? What incentives and consequences were threatened or communicated, and what incentives or consequences were applied?

COMMISSIONER HESPE: I think there are three main consequences that were available to the Department. No. 1, withhold State aid, and I don't think that serves a purpose because you're then just hurting the children in the end. Although I think to get someone's attention, it might have been useful to do that at some point. No. 2, you can direct corrective actions of a certain nature. And No. 3, you can direct that certain people be terminated. Those are your three options. I don't think any one of those three were exercised. The Department threatened withholding State aid a couple of times, but there was no follow-through on that.

SENATOR BAER: Was there also the option of making this public?

COMMISSIONER HESPE: Well, I think, through the annual reports, it was public. I think it was very public information that the district was not filing their monthly financial reports. Those are public documents, but in terms of -- and the question there is that's a very limited public document. I mean, people are going to read that -- that report. I don't have anything here which indicates that was an option that was considered.

SENATOR MARTIN: It seems, however, that there was no-- Although in some of these memos, it's expressed that there is some difficulty, perhaps, in the relationships of-- The Department was well aware, not the deficit, was well aware that they would not know what the school's financial picture really was because they weren't getting data that would confirm that.

COMMISSIONER HESPE: No. You're absolutely right. That is the connection between the shortfall and these failures in the budget office. Because without an accurate picture of your expenditures and your revenues

and the availability of surplus, you really are budgeting in the dark, and you're hoping that nothing bad happens.

SENATOR MARTIN: It's referred to here in the memo on October 28 (indicating report) that it's a structural unit. The internal audit unit -- my understanding is that is the Department's personnel placed directly at Cedar Street, where the Newark central headquarters is, to keep an eye on the financial goings on of the district. What role did they play in this process?

COMMISSIONER HESPE: Yes. Again, I think that's a good question. On the takeover law, there's a separate section which establishes an internal audit unit for each State-operated district. The function of that unit is to oversee the financial operations of the district and then to report findings to the Commissioner and to the State-operating superintendent. That was done. You'll see a host of memos from Tom King to various people indicating that reports aren't filed. As a matter of fact, if you want to -- just to see one-- In 1998, just look to November 30, which is late in the year, but you'll see the same type of memos being sent throughout the '96--'97--

SENATOR MARTIN: Where he says, "The district's failure to file it's CAFR on time for the third straight year is of serious concern."

COMMISSIONER HESPE: Yes, that's right. And he mentions the monthly financial report. So these are being-- The internal audit unit is flagging these things. What is lacking throughout is the ultimate follow-through, and I think that is a more of a structural and organizational issue.

I think the next document, and the last one that I'll refer to, is February 10 of 1999. I think this is a memo from Commissioner Klagholz to

Dr. Hall. The memo basically just reads that, "In recent weeks, I have become more concerned about the state of financial record keeping and the underlying operations-- As you know, I have endeavored to ensure that my staff in the Department provides you with the information and support you need to help you improve the district's shortcomings in these areas, shortcomings that I recognize existed." He indicates this is his statement, "That the shortcomings that I recognize existed prior to State operation. I fear, however, that these issues have not been resolved quickly enough and, thus, are becoming an unacceptable vulnerability for both you and for the Department." He has put together a team, and at the same time this happened -- you see on February 11, Ernst and Young, the consultants, are then hired.

So at this point, both Dr. Klagholz and Dr. Hall become very much engaged in fixing the business operations. You'll see--

SENATOR MARTIN: But this is after they have already both submitted their letters of resignation -- accepted other significant positions?

COMMISSIONER HESPE: It's almost-- Yes. Just a couple of-- A period of time-- It was around that period of time. That's right.

ASSEMBLYMAN GARRETT: Senator, may I just ask a question with regard to that memo that you just referred to?

COMMISSIONER HESPE: February 10?

ASSEMBLYMAN GARRETT: No. The November 30. I know it's hard to keep--

COMMISSIONER HESPE: I'm sorry. Yes, very well. I'm there.

ASSEMBLYMAN GARRETT: And this is all Greek to me. In that, it makes reference to the fact that Tom King is saying that certain reports

haven't been filed. So he's giving notice to Beverly Hall. And in some of the reports, it says, should have been "submitted to the county superintendent -- A-149 are prepared and submitted to the county superintendent of schools."

COMMISSIONER HESPE: That wasn't happening.

ASSEMBLYMAN GARRETT: Forgive me for not knowing all the procedures where these reports if somebody-- Another person involved in all this is-- These reports are also landing on the desk of the county superintendents or, in this case, maybe not landing on the desk.

COMMISSIONER HESPE: That's right. The county superintendent tracks these for-- If you were a typical district, the county superintendent would know if you were not filing these forms and would take some substantial action.

COMMISSIONER HESPE: John, do you want to--

SENATOR MARTIN: Just step up, if you would, to the mike.

ASSISTANT COMMISSIONER JOHN M. SHERRY:
I'm Sorry.

John Sherry, Assistant Commissioner, Division of Field Services.

Dr. Mary Louise Malyska was the County Superintendent of Schools for Essex County during this period of time. Dr. Malyska was aware of the fact that these reports were not being filed. She had corresponded that information to a number of people in the Department. It was very difficult for Newark to file those reports. If you did not have your CAFR report, if you did not have your fund balance, you don't have a starting point to do those reports. So, yes, we were aware of this. I think just about every office in

the Department was aware of the fact that this was a problem. It was very frustrating to Dr. Malyska.

ASSEMBLYMAN GARRETT: Okay. Thank you.

COMMISSIONER HESPE: That is a quick roll through the documents. I'll just spend a couple minutes on some findings and then some recommendations, and then I'll be done with the presentation.

SENATOR MARTIN: Let me just ask you one question. Were the millions of dollars that the State was engaged in giving Newark and then increasing that amount because of *Abbott* -- the fact that the accounting procedures were woefully deficient -- wasn't there any interest in trying to put together an auditing or accounting system that would make the picture reveal itself in a positive way?

COMMISSIONER HESPE: I think there certainly was the interest to do that. The whole host of memos during that period of time indicates that, yes, we need to get that done. It just never happened.

SENATOR MARTIN: I mean, I can only speak for myself, as a legislator, but if the Department said that there's one-- We were looking at a lot of different requests for financial assistance to Newark, as well as the other districts. But if somebody came here and presented this, we can't-- We don't know what Newark is spending or not spending because they don't have an accounting process or a computer system in place that will speak to that issue. I think we would have coughed up an additional million dollars, or so, or whatever the cost was, in addition to the other millions that we were obligated by the Court so we could have at least had some confidence as to where the money has gone. We still-- We haven't even gotten to the issue of where did

the extra money go, because we can't figure out how much-- I mean, we don't have a good accounting system, if I'm not mistaken.

Senator Turner.

SENATOR TURNER: Yes. This is very frustrating. I'd like to know why, within the five-year period of time the State had taken over Newark, why didn't our State auditor go in and conduct an audit?

COMMISSIONER HESPE: The State auditor is a legislative function. We have worked with them on a number of school districts, but I believe since the statutes call for a separate internal audit unit responsible for those functions that, I would gather, the State auditor would assume that that office is doing their job, when I think that's probably more of a question for the State auditor to answer. There is that statutory structure that there is supposed to be a State internal audit unit present in the school district in order to accomplish those goals.

SENATOR TURNER: The State auditor does not go into other districts?

COMMISSIONER HESPE: Sure they do.

SENATOR TURNER: But not into Newark?

COMMISSIONER HESPE: We're in Camden with them. I'm not aware of them being in Newark, but I think that's a better question for the State auditor. We certainly do collaborate on a number of occasions, and we have in the past.

SENATOR MARTIN: Senator Turner, I'm aware, from OLS, as well as having a short conversation with the State auditor the last year, that that may be, as long as we're casting blame, it could be a legislative fault. The

auditor doesn't audit school districts unless they receive 80 percent of their money as State aid. Newark school system, although we give them more money than any other district -- slightly more than 20 percent of their budget is paid for by local taxation, so the auditor was not obligated and did not audit the Newark School District. He has audited other districts, I believe, such as Camden, where the amount of State aid is somewhere, I think, 90 percent or so.

SENATOR BAER: Following up on that, if I may, referring again to the Office of Budget and Management, which is within the Executive department, as opposed to the auditor, which is the Legislature, I'm interested to know what role, if any, they have played here. First of all, I'm not sure whether they go over accounts that are managed by a department, but which are, like, this takeover, as opposed to accounts of the different departments themselves, which I know they provide oversight over every department. Do they do anything like that? Were they asked to do anything like that because, I assume, they have a great deal of resources and expertise in dealing with a variety of dilemmas?

COMMISSIONER HESPE: No. They were not.

SENATOR BAER: They were not--

COMMISSIONER HESPE: They did -- had no activity on this issue at all.

SENATOR BAER: Was any effort made to contact them or try to bring them in?

COMMISSIONER HESPE: I see nothing to substantiate that that was ever done.

SENATOR MARTIN: Assemblyman Moran.

ASSEMBLYMAN MORAN: Thank you, Mr. Chairman.

I have three brief questions.

I'm sorry, Byron.

SENATOR MARTIN: I thought you were done. Do you have another question?

SENATOR BAER: I paused too long.

Do you feel that since the State has responsibility for a lot of financial matters beyond those that are just spelled out in departmental budgets, whether it involves the management of the school district that's taken over or whether it involves oversight with an HMO that's in financial difficulty, over which this regulatory authority, whether Office of Management and Budget or some office within the Executive department, should provide this type of service to a department that has difficulties that they're struggling with?

COMMISSIONER HESPE: Yes. Definitely, I think that in terms of assistance to the district in putting together some computer systems and other payroll systems and accounting systems that there are resonant expertise in other State departments, for example, Treasury, which probably could have been useful but were not tapped into.

SENATOR BAER: Thank you.

SENATOR MARTIN: Assemblyman.

ASSEMBLYMAN MORAN: Thank you, Mr. Chairman.

I have three basic questions, if you could answer them in that order. Do we have the evidence in boxes somewhere of the '97-'98, '98-'99

budgets, so that we could restructure that into the GAAP system? Do we have records of the W-2s and 1099s for those years, so we could restructure those into the GAAP system? And are we presently using the GAAP system as we speak? And last of all, I've been personally involved, in our school district, with Tom King and his army of accountants, and I can attest to them that they're efficient and competent.

COMMISSIONER HESPE: They are indeed.

ASSEMBLYMAN MORAN: And I would suggest that maybe we send Mr. King's army to Newark to do those things that I've outlined if, in fact, they haven't been done yet.

COMMISSIONER HESPE: Yes. I think your use of the word army is probably appropriate, because I think in order to accomplish those things you would literally need an army.

I'll just ask Betsy if you could-- There are three questions I'm on-- Is it possible to load prior budgets into the GAAP format?

MS. DeMATTEO: But the audit for '97-'98 is in GAAP format. Basically, the auditor redid the financial records that he had available, and that's how the CAFR has to be submitted.

COMMISSIONER HESPE: And that's why it was 10 months late.

MS. DeMATTEO: The advertised budgets for those years are also in GAAP format, based on the State compliance. However, the information was then interpreted back into the financial system that the district had at the time. We are presently GAAP compliant.

ASSEMBLYMAN MORAN: So can we tell from the '97-'98 and '98-'99 where the overexpenditures occurred by line item, as per GAAP?

MS. DEMATTEO: Through the audit for, at least, '97-'98. The '98-'99 audit has not been completed.

COMMISSIONER HESPE: We're still reconstructing that budget. We'll probably be a little while longer before we're there. Not only are we continuing to find some bills, I think we're continuing to find unpaid bills, but we also need to reconstruct the expenditures. There was a tracking of expenditures.

SENATOR MARTIN: So we're clear on that point. It means that the \$58 million that you've identified as a deficit at this point could, in fact, be increased by additional bills, as found in the system.

COMMISSIONER HESPE: That's likely to occur.

ASSEMBLYMAN MORAN: Mr. Chairman, if I may go back to '97-'98? So do we have a pattern of the overexpenditures by GAAP for 1997 and 1998 that we've identified?

MS. DeMATTEO: I have not analyzed that, no.

ASSEMBLYMAN MORAN: And the W-2s and the 1099s, do we have records of all those for those years?

MS. DeMATTEO: Yes, we do.

ASSEMBLYMAN MORAN: And do we show any payroll accounts that show that there were duplications or misappropriations--

MS. DeMATTEO: Duplications, I'm sorry?

ASSEMBLYMAN MORAN: --where employees were paid more than once or contractors who were paying the 1099s more than once?

MS. DeMATTEO: Any duplications or-- I can only say they were identified at the time they were taken care of. I don't know if those records include duplications that they did not find.

ASSEMBLYMAN MORAN: Okay.

Thank you, Mr. Chairman. Thank you.

SENATOR PALAIA: Mr. Chairman?

SENATOR MARTIN: We'll just rotate back and forth.

Senator Palaia had-- If you want to ask some questions, you'll be next.

SENATOR PALAIA: Thank you, Mr. Chairman.

Commissioner, I'm sure if you're hearing these questions today -- and all very valid questions -- do you feel now there was a definite lack of coordinating the systems between the DOE and the takeover school system?

COMMISSIONER HESPE: Yes. I have set forth around 10 recommendations, and a lot of those focus on the organizational structure. We've already taken some steps. We've moved the Office of State-Operated Schools out from under the Commissioner and moved it to the Division of Field Services, so you have that communication with the county superintendent, which was mentioned here as an issue by Assemblyman Garrett. So we've also--

SENATOR MARTIN: What does that do, Commissioner?

COMMISSIONER HESPE: What it does is before you had a separation of lines of authority between the Office of State-Operated Schools and the county. The Office of State-Operated Schools reported directly to the Commissioner and-- One of the problems is a failure to coordinate efforts in

the failure of communications regarding who's doing what and the failure to make sure that everyone from the county offices, through those with the technical expertise, are aware of what's going on in the district. In order to facilitate that, we made that one change residing that oversight into one division, the Division of Field Services. We also moved the-- And then we moved the internal audit unit into the Division of Finance in order to be able to tap into the expertise that's in the Division of Finance. As a matter of fact, the Division of Finance is now leading our efforts to work with the district to resolve these problems.

So those are two structural changes we've already made, and you should also be aware that that change from the Office of State-Operated Schools reporting to the Commissioner and then moving the Field Services, that was the situation before approximately 1997 and, certainly, coordination before that period of time was much better.

SENATOR PALAIA: Commissioner -- May I continue, Mr. Chairman? -- as you know, putting together a piece of legislation of this magnitude was not an easy job some 14, 15 years ago. It is obvious that a bill of this magnitude needs to be revisited quite often, and of course, sometimes out of something bad comes something good. In this case, I think we're, whether you believe in a takeover bill or you don't believe in it, something good is going to come out of this because, I think, we're going to strengthen the system of how we go into these districts and work with them.

Mistakes were made. That's quite obvious, quite obvious. And each takeover, by the way, as you know, is a little unique and a little different. So we're only addressing Newark today. I have to say, though, Commissioner,

that under your presentation today, under State operation, I hope we keep one thing in mind, and that's the bottom paragraph on Page 4.

I'm just going to read it. It's brief. It says, "The Newark School District became a State-operated district in July of 1995 based on the finding that the district was plagued by mismanagement, poor student performance, nepotism, cronyism, political intrusion, questionable spending practices, high dropout rates and crumbling facilities."

And this is the part, I think, that speaks volumes, "An administrative law judge" -- not the Governor, not the sponsor of the bill -- "indicated that the State would be 'derelict in its duty' if it did not take over the district. The Appellate Division" -- again, not the State -- "agreed, citing the 'undisputed fact' that the district was failing to provide its children with a thorough and efficient education." This was a grave mistake that's going on now, and it has to be corrected and should never happen again. There's enough blame to go around for everybody, including me, as the sponsor of the bill originally, by not having some of these stopgap measures in place, but you don't know that all the time.

As any of us who know, who draft legislation, you can't include everything and mean everything to everybody. But that paragraph speaks volumes about why we are there. We have to correct what's going on here and move on to what is the most important thing, and some have already said it, and that is the children of the district and making sure the moneys get to them. After today's session, if you would submit some of those recommendations so we can make amendments to the bill and move ahead with it.

Thank you, Mr. Chairman.

COMMISSIONER HESPE: Yes. You're absolutely right, Senator. We do need to focus on the reasons why we're there in the first place and the good things that have happened since then, and you'll see some Newark accomplishments in this report as well, things that the people of Newark and the students of Newark and the staff of Newark and administration at the Department and district have accomplished in that period of time which are very good things, very worthy things.

Also, you should be aware that I have included 10 recommendations regarding structural changes, communication issues, and other things, as well, for your review. I think it could serve as a discussion starter for us in that very topic that you mentioned of learning from this.

SENATOR PALAIA: I want to thank you and your staff for being upright about the whole thing and saying where you made mistakes, too.

COMMISSIONER HESPE: We've made a lot of them.

SENATOR PALAIA: And I think that's very important, and I think that's a big step in the right direction, instead of referring to people who aren't even here today to defend themselves, that maybe we should have been doing something along the way.

COMMISSIONER HESPE: I think that's right.

SENATOR MARTIN: I think Assemblyman Malone has a question, and we'll take both of you in a moment.

Assemblyman Malone.

ASSEMBLYMAN MALONE: Commissioner, I don't envy your position. I really don't. I guess a couple questions I have is, I just can't get in

my mind if we passed legislation requiring the GAAP system, that somebody had back four years ago, five years ago, said, "Look, it is mandatory that that system be in place in this school district as of a certain date." Now, if there's some slippage on a year or something like that, that's one thing. To let it continue to go, and whoever let it continue to go is, basically, really the person who is ultimately responsible for this and not yourself.

So it's nice for you to come and fall on the sword for other people, and I think that's commendable, but it really goes back to saying it should have been introduced -- that system -- when it was supposed to be. Regardless of what the obstacles were, no other district that I know of was allowed to get away with this, and the thing is, too, it has put us in this dilemma now. Really, nobody knows what's going on. I hate to say this.

Another question I'd like to ask before I get into some other ones here. Have you had enough time to really analyze what has happened and really prepare for this hearing today?

COMMISSIONER HESPE: Well, everything we know was as of yesterday, which was a fairly brief period of time from when we started digging into this, when we knew we were going to have to come and defend our actions and defend the numbers. I think we have our hands around this issue, comfortable that our recommendations are on target. Certainly, in terms of those personal responsibility issues, which you just discussed, we don't have the information. We probably never will have that information to be able to say this person or that person. We do know that given that there are unpaid bills that were not being logged, and there were expenditures that weren't being tracked, that we had some serious concerns of the chief operating officer of the

district, but we really don't have enough information to be able to say that those concerns are valid or not, but we definitely have them. It's hard to understand how something like that could occur, but I don't know if we ever would.

SENATOR MARTIN: Just to that point, and I think Assemblyman Malone might not have said it this way, but I think our frustration, in part, is if there was any district that needed to have GAAP, you would go to the highest spending one, the one that Senator Palaia just remarked had had a history of fiscal mismanagement. So that, in June of 1995, or July, when it was taken over, that's the district that you would seemingly want to put into an accounting system that was easily -- one would be able to detect problems. And the other part of that is if there was any district you would think that this Department could require putting into GAAP, it would be its own takeover district.

If Asbury Park, which is a district that's had some troubled history, gave you a hard time, that would be something you might have to resort to, by law, to get them to move more quickly. But a district that the State itself was taking over, one would think that you would have your own ability to do that through management. When I say you, obviously, I'm speaking to the Department.

I think you had some other questions, Assemblyman.

ASSEMBLYMAN MALONE: Yes. Just so I get it clear, as of what date are you completely GAAP compliant?

COMMISSIONER HESPE: Betsy.

MS. DeMATTEO: As of January 1, of this year.

ASSEMBLYMAN MALONE: So as of January 1, 2000, you are certified, sanctified, mummified, everything. If somebody walks in there, some accounting firm that's never done any business with anybody, walks in, they're going to know this system is totally in place with all the proper categories and the accounts are running with any encumbrances and the balances are left in every one of those accounts?

MS. DeMATTEO: We have some work to do, but yes, we have--

ASSEMBLYMAN MALONE: Okay. I am going to ask you one more time. Is it totally GAAP compliant as we speak today?

MS. DeMATTEO: We have GAAP compliant budget analysis reports. We have an A-148. We have -- all of our employees are GAAP coded as of January 1, and the payroll is being produced in GAAP format and posted.

ASSEMBLYMAN MALONE: And all you supply accounts and everything else?

MS. DeMATTEO: Absolutely.

ASSEMBLYMAN MALONE: Okay.

SENATOR MARTIN: She was brought in from the Morris School District. I know that she's a very, very good and competent person. If she says this, I have reason to believe her.

ASSEMBLYMAN MALONE: I think it's important that everyone know it's as of such and such a date. Henceforth, it's going to be a relatively easy process to keep track of the funds.

COMMISSIONER HESPE: There are still things that, for example, in '98-'99, still hasn't closed, Assemblyman.

ASSEMBLYMAN MALONE: I didn't ask that question.

COMMISSIONER HESPE: All right. You're just focused on that system.

ASSEMBLYMAN MALONE: Yes. Okay, now.

COMMISSIONER HESPE: If you're just focused on that system, I think the answer is yes.

ASSEMBLYMAN MALONE: Okay. The question I have-- For us to go back and reconstruct everything that has been done up to January 2000, it sounds like it's a monumental amount of work? What do you estimate that's going to cost us? How many millions is this going to cost?

MS. DeMATTEO: When you say a final cost, we have consultants, right now, who are reconstructing last year's information so that it can be audited. We brought in a new finance system. We suspended the finance system they were working on, too, because it was not going to be satisfactory. That costs additional funds. We have still a ways to go, but as far as a bottom line, I really can't tell at this point.

ASSEMBLYMAN MALONE: A ballpark figure?

MS. DeMATTEO: The new finance system cost about 400,000. The consultants-- We have Ernst and Young, which they have done, like I said, the '98-'99, and they are continuing with the first half of this school year. They will be helping us put together the first half of this year, because we only-- We brought over data from the first half of this year in a conversion program, so their contract is between 300,000 and 400,000, but they're not finished with their work.

ASSEMBLYMAN MALONE: So we could be talking \$3 million, \$4 million, when everything is done?

MS. DeMATTEO: I don't think it's going to be that high. I really don't.

COMMISSIONER HESPE: It's a considerable amount of money, though.

SENATOR MARTIN: I got other people on the line.

ASSEMBLYMAN WOLFE: Can I speak?

SENATOR MARTIN: You can.

ASSEMBLYMAN WOLFE: I know some folks are waiting to ask him--

Senator Martin and I both said, before we began, the number one concern was the education of the children in Newark schools. Senator Baer asked about, maybe a half hour ago, sanctions, what kind of sanctions. And I think maybe that's going to be part of your conclusion, but I think, as we sit here and we listen and we read and read and read about unmet deadlines and very few required reports coming in, if this were any other-- I don't mean this-- Well, if this were any other school district, they would really, literally, be hammered. I would get a call, or one of the legislators would get a call, that we didn't get something in on the 15th, and the Department is really coming down on us, can't you do something to have them relax? And probably, we would be unsuccessful, that the Department would come down pretty heavily on those districts.

I understand there's a financial concern that we're looking at here, millions of dollars, but I'm also concerned about the message that this sends to the other school districts in the state, that you can do whatever you damn well please and the hell with whatever the Department says. We've got

cronies, we've got a way, we can just do what we've done in the past, nothing is going to happen, and life will go on as usual. Now, maybe that's going to be something you're going to recommend, but I am very, very concerned about that if we have a State system.

COMMISSIONER HESPE: Yes. The recommendations are very self-critical. They get into those issues as to Department structure, our ability to communicate, and I think the message that we're trying to send by those recommendations is that we'll hold ourselves accountable, as well as local districts. And I think that comes through in this report.

ASSEMBLYMAN WOLFE: Okay.

SENATOR PALAIA: Mr. Chairman, just to piggyback off that one second. You know, one of your biggest problems is it's too much of talk, talk, talk, talk, but not enough action. It's the way we started the school takeover. When they don't comply, remember, for two years and three years, we say, "Please, please do this, and please, please, please," and eventually we take over. I think one of your -- the major fallacy in the whole Department is that you kept saying, "Please comply," when you should have taken action.

I'm sorry. The gentleman down on the end there -- the Assemblyman -- has been waiting--

SENATOR MARTIN: Assemblyman Stanley is going to speak.

SENATOR PALAIA: Yes.

SENATOR MARTIN: But with that, I think the options that were identified in 1997 to the superintendent to "either fix it and I'll hold you accountable, or fix it and here is how I want you to fix it, or can we help you

get this done, if so, than how,” are not bad, at least, approaches to consider as a way to deal with it.

SENATOR PALAIA: Yes.

SENATOR MARTIN: Assemblyman Stanley, who represents the city of Newark, as well as other municipalities in the area.

ASSEMBLYMAN STANLEY: Thank you, Mr. Chairman. I appreciate that.

Let me first start by saying maybe we ought to distinguish between the Newark School District and the State-operated district in Newark. I think the record should be reflective of the fact that we’re talking about a State-operated district in Newark. Sometimes when we say that this happened in the Newark district we, perhaps, maybe unintentionally vilify Newark or the people in Newark for what has happened, really, under State control. I think that’s one of the first issues I’d just like to raise.

The \$58 million surplus, when the State came in, I think that’s reflected in your information. Now we have a \$58 million deficit. I’m very concerned that, number one, that those figures are the same. I’d like to try to find out how we get to a \$58 million deficit, and also, in terms of that surplus, what that surplus was comprised of, were there bond dollars included in that surplus, was some of that money specifically designed toward construction, whether there were some dollars there that might have been misallocated during the course of that time span, when we find ourselves with a \$58 million deficit.

But even before I get those answers, I’d just like to touch on a couple of things that I’ve heard in terms of the monthly reports. Those were

not done under the State operations, and also, just add the fact that, under the Newark School District, under the Newark Board of Education, these monthly reports were, in fact, done, that the budgets were, in fact, done and audited. And also, that under the Newark operated -- the Board of Education in Newark -- what we had was a GAAP system since the early '90s. I think those things ought to be reflected. Now, the State came in subsequent to that. All of a sudden, we didn't have GAAP, we didn't have reports, monthly reports being generated and given.

It's very disconcerting because, as Senator Palaia said, one of the reasons we said that the State was going into Newark for was because the situation was such that children weren't being given a thorough and efficient education. Well, we didn't really need an administrative law judge to say that. We already had the Supreme Court saying that for the last 25 or 30 years. However, I am very concerned about the fact that some of these things were in place prior to takeover. Subsequent to takeover, they disappeared, and we have to really understand that this is a State-operated school district, that is school children in Newark.

I just want to finally say, for now anyway, that I don't know whether if we had a State-operated school district in any other municipality in the State of New Jersey that these types of safeguards and procedures would have been allowed to continue. I think that we have to really grapple with that and understand that as well. It wasn't a result of-- I don't think it was a result of just people, kind of, coming forward on their own, Senator, saying, "That we make a mistake or we've got some problems here." I think it was the fact

that we knew that without \$58 million we were never going to make that school district work for the rest of the year.

So I think that a lot of this is as a result of what was needed from the Legislature, and I commend Senator Martin and Assemblyman Wolfe for chairing this hearing because we need to find out, and we need to make sure that not only were the dollars spent -- and this \$58 million deficit is such that it doesn't hurt the students in the future, that we're not taking different programs and setting those programs aside because we want to make that \$58 million stick. We have to make sure that different things that maybe the Superintendent would have been able to do, could have been able to do, if we had not run into this mismanagement problem, that she will still be able to do it.

We also need to make sure that in your recommendation to us, as far as the dollars that you need, that we're able to do the type of accounting, the investigation, all these dollars that have been regarded and referred to, as far as how many more people or how much more time or whatever it's going to take to make the accounting system work now that that doesn't impact on the programs and things that we need to see done in the Newark schools for the children.

COMMISSIONER HESPE: A whole bunch of questions. If I could just start from the beginning. First, the 58 million, I believe, was undesignated surplus. I don't think any of that was designated for special program starting. It was all undesignated surplus. The second is that it was our understanding that the system in place prior to takeover was not GAAP

compliant. I guess someone will testify differently on that, but that was what we were told by people who had looked at that issue.

ASSEMBLYMAN STANLEY: The information I have from people who were in those positions before suggested that it was GAAP compliant.

COMMISSIONER HESPE: Okay. It's an issue, I think, we probably need to find more about. There is a chart of account issue, but we'll get some more information.

SENATOR MARTIN: But it does seem to be clear that they weren't overspending the amount they that were.

COMMISSIONER HESPE: No. It was a functional system. The system in place before the State operation was functional.

SENATOR MARTIN: But although the \$58 million happens to be a, I think, a coincidental figure, there's \$116 million if you combine the two of saying, "Where did the money go?" No one has answered that question. (applause)

COMMISSIONER HESPE: Okay. Actually, we're going to get there in a second.

Thirdly, I'm just trying to take all your questions, Assemblyman. Looking at Jersey City, looking at Paterson, their business operations are very good. Jersey City actually wins national awards for their business office. I agree with you, I don't think you can generalize to those two districts. Their operations are solid.

Now your last question that's on supplemental funding-- Where is the supplemental funding money going? I think it's time we heard from the Superintendent, and I'll hand it over to Marion.

ASSEMBLYMAN WOLFE: Excuse me, Assemblyman. Senator Turner wanted to speak, and I'll get right back to you.

COMMISSIONER HESPE: I think Marion is going to answer your last question on supplemental funding.

ASSEMBLYMAN WOLFE: Go ahead.

COMMISSIONER HESPE: Is that okay?

ASSEMBLYMAN WOLFE: Sure it is. Go ahead.

COMMISSIONER HESPE: Especially when I think we have an answer for Assemblyman Stanley, is that right?

ASSEMBLYMAN STANLEY: Yes.

MS. BOLDEN: Let me just say that on July 21, when I was appointed the State District Superintendent, we had an unapproved budget to the tune of \$104 million in supplemental requests, and certainly, given the magnitude of that request, we were told to make a case for -- show documentation and where the money was actually going to be spent. That was the problem. In fact, in terms of the discovery, we have spent the last five months with a consultant group that came prior to Betsy DeMatteo, trying to reconstruct where the budget that we submitted came from in terms of the \$104 million. So what we had to do was certainly pay her back any moneys that could not be defined clearly and show a rationale for.

What we discovered in many cases were budget lines that had -- for example, ECPA money was recorded in two different locations, \$5 million here, \$5 million there. It was, needless to say, an effort in itself just to bring that \$104 million down to something realistic. And this is not with just the Department of Education working with us, this is with the Newark staff as

well. In other words, we spent almost all of our time trying to reconstruct history, trying to figure out where moneys had been spent, and not compromise the educational program in our school district.

And so where we started with the \$104 million, there have been cuts, certainly, that have been made because they were not justified, and certainly, as a school district, you are accountable for showing that your finances are -- have some integrity. We were not in a position to do that. But through the efforts of both departments, working through, what we realized is that when we got to that \$50 million, as far as we were concerned, any additional cuts would have compromised the educational program. And we're talking about implementing the New Jersey Core Standards, as well as the new *Abbott* and the other mandates that are very expensive, that go with it.

And so, when you look at the \$50 million deficit or supplemental requests that we were asking for, if we had not gotten that, then we were talking about, perhaps, cutting teachers and which we cannot do. We were even looking at our custodial staff, and we don't have, right now, all of the resources that we would like to have to ensure that our buildings are absolutely clean. So when we got to the \$50 million, it was a consensus of opinion from the Department of Education and from the educational perspective that any further cuts would compromise the programs that we wanted.

You asked, also, whether or not there were some programs that we would not be able to fund. Well, necessarily, that's true. And I can only cite things like science labs that had been in the original budget that had to be deferred for another year. But in terms of those programs that were in place, we did not cut those.

ASSEMBLYMAN STANLEY: Let me just say, and I don't believe-- I believe everyone on this panel agrees that there should be not one program that should be deferred as a result of mismanagement under State control. I think every person on this panel agrees with that. I just ask you and the Commissioner and the superintendent to go back and to understand that this panel would not agree with sacrificing the students of the city of Newark for the improprieties or, perhaps, just poor management of the State-operated school districts.

SENATOR MARTIN: That's always the dilemma. Too frequently, the wrong people get hurt, but I don't think constitutionally, as well as morally, we can blame the students in the city of Newark for whatever errors that human frailty that maybe we're, in some way, responsible for -- the Department, the administration -- and others are responsible for. So I do agree with you there.

I believe Senator Turner wants to speak, and then we'll come back to the Assemblyman.

SENATOR TURNER: Yes. Thank you, Mr. Chairman.

The Commissioner indicated earlier that the most important thing now is for us to make sure that this never, never happens again. He also recommended that we take some measures to put some structures in place to assure that it never happens again, but I would have greater confidence that this will never happen again if we take it a step further, as a legislative body. When I raised the question about the State auditor auditing this district sometime over the past five years, it was indicated that we do not have a

mechanism in place because Newark does not receive more than 80 percent in State aid.

SENATOR MARTIN: I think it's just across the threshold.

SENATOR TURNER: They're just over the threshold.

COMMISSIONER HESPE: It just crossed.

SENATOR TURNER: Okay, but it would not have been possible last year.

COMMISSIONER HESPE: Prior to this, that's correct.

SENATOR TURNER: Okay, but I would like to say that this legislative body should make it a practice, or a requirement, that any district that the State takes over, we should automatically send in the State auditor to monitor that district.

SENATOR MARTIN: It's clear that some of the recommendations-- I know the Assembly has taken a lead on this to look at whether it should be an independent auditor or whether, perhaps, a State auditor or I've heard of some other means, but I think that one of the issues that we should address, if not today at some other time, whether independently as committees or jointly, is how we take on the responsibility of ensuring that we have a confidence level built in. It may require some -- I hate to say it but -- additional supervision, but we need a way to ensure ourselves that what is going on won't repeat itself in this way. So I think this is one suggestion, but we will look at that specifically.

SENATOR TURNER: Is the State auditor monitoring those other districts where the State has taken over?

SENATOR MARTIN: I think one of the persons we should call at some point is the State auditor and ask him if -- in fact, he's here today -- but we will ask him whether he thinks that's a role that he would feel confident in, in terms of giving us reliable information, whether he would support an independent auditor, whether there has been some suggestions that-- In the city of Newark, for example, they have graduate programs at Rutgers with an Office of Management and Public Administration and an Education Department, whether they have some experts that maybe could play a role, if not for the Legislature, for others. So there's been a number of different suggestions, at least, brought to me about ways in which there could be some control mechanisms put in place, but this is certainly one which would be the State auditor playing the central role.

SENATOR TURNER: Thank you.

COMMISSIONER HESPE: Those are some of the recommendations that you'll see are actually a call, a need, for others outside of the Department -- the Joint Committee, perhaps, the State Board, an auditor -- but offices that have the capability to actually follow these complex issues. And so there's probably a need for a capacity issue there, so that there are other entities following these issues because there is a need, Senator -- I agree with you -- but I would say that there's a need for some other entities to be involved. They just need not just be an oversight entity, but an entity with a capacity to get involved in these issues. Maybe it is an auditor, maybe something else, and I think that conversation has to happen.

SENATOR MARTIN: In the private sector, when you have auditors frequently, or at least accountants, they do play a hands-on role in

some ways of changing practices. So if it can be a consultant relationship as well as an auditing, but you just have to make sure that they don't become-- I think in the past you worried about certain consultants because they're being selected entirely, whether they lose their objectivity because their bread is being buttered by certain people, and they, sort of, want to make sure that they don't come down too hard on them, which can be a problem. We have to look at those kinds of mechanisms.

I think Assemblyman Garcia was next, and then we'll--

ASSEMBLYMAN GARCIA: Okay. Thank you, Senator Martin.

First of all, as a legislator who represents a takeover district in Jersey City, there is already a mechanism and the tools to prevent this type of tragedy from happening again. If we just make sure that GAAP was used, that the Comprehensive Annual Financial Reports were filed, that the Treasurer of School Moneys' monthly reconciliation reports were conducted, this would have never happened.

So one of the things that Senator Palaia -- took some blame that maybe he should have drafted this takeover law differently. I think there were mechanisms already in place--

SENATOR PALAIA: They weren't followed.

ASSEMBLYMAN GARCIA: --that just weren't followed. If you look at this entire report, it's just -- you can tell -- memos after memos of people covering themselves rather than taking action to implement the programs they were supposed to be implementing so we would have never had this problem.

COMMISSIONER HESPE: I think you cut to the chase on that one. (laughter) You didn't finish?

ASSEMBLYMAN GARCIA: No.

COMMISSIONER HESPE: You did finish. I think you cut to the chase on that issue very, very quickly. I think you're right. Are there mechanisms in place to prevent this? Yes, there's GAAP. There are monthly accountability reports. There is a need for audited financial reports. There is an internal audit unit, under statute, who is supposed to be accomplishing this. My recommendation is really focused on why those didn't stop it and changes that were made. And certainly, the one conclusion that you could draw is, we should have just done things right from the beginning, but I think it's incumbent to, perhaps, to maybe just make it-- If we want to make sure this never happens again, I think we have to take into account that there are going to be communication breakdowns, and there is always going to be structural problems and maybe we need to do something about.

Another accountability issue that we really just should take a second to focus on is the whole supplemental funding process; what happened last spring, when you hear Marion discuss that quite a bit, as to why that supplemental funding request was just diction. Her task of having to reconstruct that budget over the last months so that we had the picture that we could then approve that supplemental funding request. Because my commitment to this Legislature on supplemental funding is -- when I approve that, it is necessary for that district to deliver a thorough and efficient education, and this body should be able to rely upon that assertion, that I have worked with that district, and we have come to that conclusion.

I'm just going to hand it over to Marion because this is something that I think is very important for her to say.

MS. BOLDEN: I guess given what you just commented upon, I guess, is why I'm sitting here and struggling with the issue of auditors and procedures when my experience is that those procedures were in place all along. On July 21, when I was appointed, it was very clear to me what I needed to do when the Commissioner said, "You have a responsibility to go in and--" in essence say, "clean up." Because there has to be an A-148, there has to be a CAFR, and so, for five months, that's what we've been in the process of doing. So if you have to be in GAAP compliancy, then that's what we had to do. So the issue of-- You can put layers and layers and layers of auditors wherever you want to. It is the people, ultimately, who are responsible.

So what I don't want to be, this enduring image, is that Newark and its credibility is now so damaged by what has happened. When I say that, I say that as an educator who in all likelihood lost the opportunity to have an SNF grant because they're saying if you can't manage your finances, we're not going to give you a \$12 million grant. So it is very important for us to project ourselves as knowing what we're doing.

And Betsy DeMatteo has said that we are going to apply for a certificate of excellence, and that's what I'd like to be able to show you, that there is now, in working with the Department of Education and working with the people in our district and getting on board in terms of compliance and efficiency, that that is exactly what we are doing. So I think that, yes, you can have an auditor and probably there is no question that you should, but ultimately you see the series of memos that have gone back and forth. If

nobody acts on it, then it's just another layer of someone-- We could easily-- In fact, I don't think that this could happen any place else again. But at any rate, I said, the mechanisms were already in place, as far as my determinations.

ASSEMBLYMAN GARCIA: Let me just say, if I just may, to just follow up on my initial question, is that you're right. The people in Newark, and certainly the children in Newark, shouldn't be blamed for this problem, nor should their additional science classrooms that they were supposed to have filled this year have to be stalled until next year just so that we can make up the \$58 million that they, nor you, nor this Commissioner for that matter, had any responsibility or took part in any action that causes this problem.

So I think what's most important here is that we look at exactly how much the deficit was. It was left as a result of us, or -- we are all to blame, I guess, we may find that all of these systems were not used. We should really separate that to get that money from a supplemental pot of money that's now going to be taken away from other school districts, and really then implement what was required by the Core Curriculum Standards, what was required to improve the educational programming in that school district, and whatever that amount of money is should be incorporated as well. Because to punish the children, these actions should ultimately be placed upon the people that wrote all these memos, that didn't take any action, and not on the school system itself.

I'll end here, but I just wanted to commend the Commissioner and everyone here for really being forthright and stepping up and really trying to take control of the situation. I know it's a situation that was not created by

you, Commissioner, and I think you've been very forthright, and that's to be commended.

SENATOR MARTIN: Go ahead.

ASSEMBLYMAN MORAN: If I may, Mr. Chairman. Is it Betsy?

MS. DeMATTEO: Yes.

SENATOR MARTIN: Quick question, then Senator Baer.

ASSEMBLYMAN MORAN: When you were talking to Assemblyman Malone, you had talked about, effective January 1, we were in compliance or tentatively in compliance. This fiscal year going back to July 1, are we rebuilding back to July 1 so that come June 30 we can close the books and say, "We complied with *Abbott* for this fiscal year, and we can tell where our 201, 203, 204 accounts, moneys allocated, encumbered, balances exist?"

MS. DeMATTEO: This is, obviously, a transitional year. We had an old finance system that crashed as of December 31, so we have to do a lot of quick fixes before January 1. We have gone back. We've entered all receipts and identified receipts back to July 1. We have rolled over open encumbrances. We have aligned all expenses to the GAAP codes. We realigned the budget that we put together with the 58 million. We realigned all of the lines in GAAP compliance. We are getting budget reports analysis so that these schools and offices will be able to know what their available balances are. As I mentioned, we have an A-148 for the General Fund. So, again, it needs a little work to it, and we need to get the other funds on line as far as the A-148.

I have met with representatives from the Treasurer, and all the payrolls have been posted.

COMMISSIONER HESPE: That's the Treasurer of School Moneys.

MS. DeMATTEO: Treasurer of School Moneys, right.

All the payrolls have been posted, and part of the problem with the Treasurer of School Moneys' report is we were not able to give the Treasurer the information that he needed to produce the reports. So we are working to give him that information. I have asked for 149 as of April, and hopefully, we will be in communication to make sure that that happens.

The audit for '99 will be completed mid-May, so that will be out of the way, and we are looking to close our books on June 30 and have the auditors back to do this year and have it audited on time. We will go into next year, and that will be the year that we have a budget that is responsible to the State, approved prior to the school starting, and we will move forward. That's what we want to do is move forward.

SENATOR MARTIN: Senator Baer.

SENATOR BAER: Thank you.

Relative to your recommendations, I see many things here that are very worthwhile and valuable. They speak of analysis and coordination and leadership and visibility and reassessment. I don't see anything here that specifically addresses what I think you've indicated you would like to see and most of the people here have indicated that they would like to see involved more and that is something relating to consequences, something relating to actions. Do you think that we should have something or that you would want to add to these recommendations something that indicates clearly that there would be consequences where there is a problem with compliance so that these

are not just set forth as objectives, which could be as easily ignored as the objectives which were previously set forth but which depend on, in some cases, having the ultimate application of consequences?

COMMISSIONER HESPE: I agree with you. I tried to encapsulate part of that in Recommendation 3, regarding effective ways to communicate key operational expectations. But you're right, there is no consequence to the failure of this follow-through team, which I have referred to, to correct the problem. I think you're right, there needs to be a sentence after that. It would say that appropriate consequences must be provided for failure to follow through.

SENATOR MARTIN: Senator Baer, I think it's important to note that a couple of years ago -- I think Marilyn knows the name of the way it's referred to -- but a statute was passed that essentially provides that there is a criminal action if somebody is so negligent, grossly negligent. I'm not sure of the exact wording of the statute, but essentially you're responsible in their duties, that there's criminal sanctions. Maybe you could-- It has not been ruled out. This is not the forum for it, but there is conceivably some potential that individuals might fall within the sanctions of that particular statute with Newark now and in the future. So there is something in place now.

COMMISSIONER HESPE: It's case law. There is, I guess, a Superior Court case on that issue and that, basically, lays out-- It was an event coming out of Eddie Moore at the--

SENATOR MARTIN: Yes. I was referring to the so-called Eddie Moore law, where if you intentionally overspend, it is a criminal sanction that is imposed. That's not easy to show. I mean, in certain circumstances, we're

not suggesting anything here. I haven't heard anything that identifies it, but there is some level where this actually crosses over into criminal if somebody knowingly and willingly spends money that they're not authorized to do so.

SENATOR BAER: I understand, but I also understand the Commissioner referred earlier to administration actions that could be taken regarding personnel that were not doing their job. I would assume that something -- I wasn't thinking of a criminal nature -- I assume that would only come into place where there was even defiance in the face of something that the Commissioner referred to, but apparently the record does not show this has been applied.

I also wanted to ask whether you thought that it would be appropriate somewhere in this group of recommendations to have something that indicates this, not precisely like a regulation would, but indicates that there is an appropriate point at which these things should be disclosed more fully publicly and that merely a technical and fragmentary disclosures, which perhaps a researcher could construct into a whole in a month of research, would not be sufficient. But there's a point at which the import of these things should be disclosed publicly, and that that ought to be something important to be encompassed within the recommendations because the accountability to the public is always a mechanism that helps to bring about compliance.

COMMISSIONER HESPE: No. I agree. I think if this issue had been debated publicly at some point, I think we probably would have seen a greater concerted effort to make sure that it actually happened. So I think there is some agreement on my part that that's right.

SENATOR BAER: And lastly, although I noticed that many of these recommendations are directed to a specific entity, like a Department or like a Division of Finance or the internal audit unit or district or the Treasurer of School Moneys, but there are five places of which these recommendations are directed to the State. I wanted to know if you thought that there should be more specificity in terms of who that involves, what entities or individuals, or multiple entities and individuals, should be identified there as a means of having these recommendations more effective?

COMMISSIONER HESPE: Depending on the context, sometimes the State refers to the Department, but in a number of times it actually refers to outside of the Department. I think it's a joint committee. The State Board have valuable functions to play. Also, I think that raised earlier was -- and I think you raised it earlier, Senator -- that there was resonant expertise outside of the Department of Education in some of these more highly technical issues, and shouldn't we tap into that coordination as well. And I think that's what we're trying to get at here. I think the issue you raised earlier was right on the point.

SENATOR BAER: I'm not suggesting limiting--

COMMISSIONER HESPE: You just want to be more specific?

SENATOR BAER: --how that should be more specifically identified--

COMMISSIONER HESPE: Okay.

SENATOR BAER: --but I'm asking whether you thought, perhaps, it should be identified, as specifically as it could be, so that the intentions would be more fully understood?

COMMISSIONER HESPE: We could certainly do it. The purpose was just to provide that starting step in terms of this discussion on changes and not to be the end-all and be-all, but certainly, I think, if it's unclear, we can certainly bring some more specificity to it, if you wanted us to do that.

SENATOR BAER: All right.

The last thing I wanted to ask, and it doesn't require any details here. Since you will be getting us additional material, perhaps, including relating to that which I've discussed, and since earlier in your testimony you referred a number of times to things that were being done without specifying what that was, could you provide the Committee with a detailed listing of what those things were that played a factor at those times?

COMMISSIONER HESPE: I guess just to-- I have listed corrective actions which were taken once, in the winter of '99. Everyone got focused and said, "Yes, we want to fix this problem." So we have a list of those corrective actions. I think you're referring to what happened prior to that one. I'm saying, like, after this memo, certain things are occurring, and I think mainly those focused around the putting in place a new payroll system, putting in place that people saw a payroll system, and the technical problems and the complex problems the district is dealing with in order to try to put those new systems in place, which in the end -- at least that's to the accounting piece that Betsy had to abandon even at that new system that they were trying to put in place-- But that's what I'm talking about. They're trying to put new systems in place during that period of time and are having a great deal of difficulty doing that.

SENATOR BAER: Thank you.

I assume as usual--

ASSEMBLYMAN WOLFE: Before we continue--

Go ahead.

SENATOR BAER: --through the Chair -- if there are any follow-up questions submitted in writing within a reasonable time--

COMMISSIONER HESPE: I'd be glad to.

SENATOR BAER: Thank you.

ASSEMBLYMAN WOLFE: As Co-Chairman, I'd like to exercise my prerogative and allow the Commissioner to complete his testimony. The Assembly has a voting session in 25 minutes. Before we do that, though, Assemblyman Stanley and Assemblyman Malone have some questions, so I'm going to ask them very quickly if they can be very concise.

SENATOR MARTIN: I think Assemblyman Garrett had asked to speak, and he hasn't spoken yet, so we want to give him an opportunity.

ASSEMBLYMAN WOLFE: Okay. Again, I would like to ask that my colleagues be very brief in their questions.

Thank you.

ASSEMBLYMAN GARRETT: Forty-five seconds? Okay. I'll be brief, to forty-five seconds. One is a comment, and the other is a question. The comment is in reference to other comments that are made by the members of this Committee, that everyone on this panel looks to make sure that the childrens' interests are protected and, yes, we all agree on that. But there's an implication being made that there's this missing \$58 million, that that necessarily is affecting student programming, affecting the kids, and at the end

of the day the State has the obligation to step up and reimburse the school districts for that \$58 million.

I, as a legislator representing a portion of the State that does not receive the largest of the State, as far as the amount of money going into our school districts, look at this as how is this going to impact upon students, not only in this school district, but how is this going to impact on students in our school districts and have the same concerns as, "Well, there goes more money being pumped into those school districts, that we always wondered where the money was going into even before the State took them over." We remember that there was a reason why the State took these school districts over and remember, also, that prior to taking these school districts over, there was a period of years, I guess, that the State gave these school districts the opportunity to adjust their financial dealings and the way they handled their finances.

So, as a legislator from another portion of the state, I just have those concerns, how all the kids in the entire state may be affected by all this according to how you do, pouring this money back into the system.

COMMISSIONER HESPE: I think the two answers-- First is we have an obligation under the *Abbott* line of court cases to ensure that Newark has the fiscal funds necessary to put in place the programs the Court has ordered. The second one is that, I think, in terms of other districts in the state, that this was a very good State aid distribution. It was one of the largest in the State's history, and I think is probably one of the better ones in the State's history, as well, in terms of getting dollars to local districts. So I think this was a very good year for all districts.

ASSEMBLYMAN GARCIA: Mr. Chairman, I think we should be careful and not blame the victims here.

SENATOR MARTIN: Well, we'll take that under advisement, Assemblyman Garcia. This is an open forum and--

Assemblyman Garrett, did you have another question?

ASSEMBLYMAN GARRETT: I guess the issue is I find your report interesting reading, although I can't, to be honest with you, comprehend it as I sit here and try to hear your testimony as well. At the end of the day, the real question is, does this \$58 million necessarily impact upon educational programming or may we find out that, yes, the \$58 million was spent up and above of what they should have been spending. But it may have, for all I know at this point, and I guess everyone here knows, maybe it has gone into other educational programming that was beneficial, either within lying their programs, not necessarily within lying with their programs, but still beneficial to the educational quality of the schools. And today we really don't know that, do we?

COMMISSIONER HESPE: The one thing that certainly we do know is that there was a very much -- a program intensive effort in State operation for those four years. The State was there. They were focusing a lot of energy. The Superintendent was focusing a lot of energy on educational programs in that district. They were funding those programs, however, through the use of surplus, which eventually became depleted, and that's the reason for these fiscal troubles. Those programs are solid programs, and we've determined those are necessary programs.

SENATOR MARTIN: Well, I think the general question -- one we've posed several times -- let's try and make it clear. I think Assemblyman Garrett would concur with this, if not with all the sentiments expressed by all of us throughout the course of this hearing. But we are concerned about the \$116 million that was the 58 million surplus, the 58 million deficit. We don't know where it went, and unless we have an indication -- I think Assemblyman Moran asked earlier about the GAAP and the specific line items -- we would ask you to identify that and make some judgment as to whether that was for worthwhile programs or whether it was spent in some ways that don't seem to show any benefit, which I think is what Assemblyman Garrett was concerned with, until we have some understanding of where the money went.

And I don't think it's just-- We're not doing this to be as vindictive as-- First of all, we have an obligation to find out where \$116 million went. We'd like to know whether does Newark -- at least, is Newark making a claim that they absolutely need that money in order to meet thorough and efficient. And if they are making that claim, we should have a judgment, at least, an independent review as to whether we think that's appropriate. But we don't know the answers to that because we don't know whether that money just, sort of, was filtered out into the wind or whether it was directed as some specific program.

You did indicate that every single program, presumably, that they had programmed under the *Abbott* Court order was reviewed and approved or not approved by the Department. So I don't know that they could have spent it on other programs, but I really-- I'm still at a loss as to know where the

money went. Is somebody going to make a case that it was justifiable? And then, we should have an opportunity to review that.

Assemblyman Zecker hasn't been heard from yet.

COMMISSIONER HESPE: Senator, could I just follow up on that just one minute?

SENATOR MARTIN: Let the Commissioner answer my question.

COMMISSIONER HESPE: Assemblyman Zecker, is that okay if I take 30 seconds?

ASSEMBLYMAN ZECKER: Yes. Why don't you call him at home tonight and explain it to him. (laughter)

COMMISSIONER HESPE: That's a very fair request. The Department has approved a supplement, because it basically says this money is necessary to accomplish *Abbott*. In consultation with Marion, we've made that decision. You want the justification for that decision, we'll get it to you.

SENATOR MARTIN: Assemblyman Zecker.

ASSEMBLYMAN ZECKER: I haven't read all of this, but I will. If you try to read this and listen to what you're saying-- And you don't have page numbers on there or tabs so--

COMMISSIONER HESPE: Yes. These were put together and, unfortunately, we just didn't have time to get it to a bookbinder.

ASSEMBLYMAN ZECKER: I'm not saying they're confusing, but boy if I wanted to confuse the legislator -- no page numbers, no tabs-- So you've been referring--

SENATOR MARTIN: They've done a good job trying to put this together.

ASSEMBLYMAN ZECKER: I'm teasing you.

COMMISSIONER HESPE: Just point to a blue page.

ASSEMBLYMAN ZECKER: The first blue tab.

COMMISSIONER HESPE: The first blue page is the way we've been referring to it.

ASSEMBLYMAN ZECKER: Right at the beginning, January 16, that would be 1996, right? Are we on the same page?

COMMISSIONER HESPE: January 16, that's right.

ASSEMBLYMAN ZECKER: Okay. "A new organizational chart for NPS executive staff is issued. Leonard Hellenbrand, who was hired by Beverly Hall and who is not certified in New Jersey as a school business administrator, is Director of Management and Budget, reporting directly to Beverly Hall." That's correct?

COMMISSIONER HESPE: I believe he got conditional certification.

Mike, he never got certified?

MR. AZZARA: He never got certified as a business administrator. That's correct.

SENATOR MARTIN: They hired a business administrator underneath him to be able to handle the--

ASSEMBLYMAN ZECKER: That's what the next sentence says, "No one has the title of School Business Administrator."

COMMISSIONER HESPE: Not until Loren MacIver is hired, no.

ASSEMBLYMAN ZECKER: And then it goes on, his name is mentioned. I think a lot of this report has a lot of paper, but maybe when you

go back through this, you can give this Committee from genesis, when he started, what his actions were with the State, because these reports, and I'm not saying it's accurate, lean towards the possibility that there were two sets of books kept. That's what some of the newspapers have been saying, too; that Hellenbrand was reporting to you one set of books, and yet had his own set of books that he was operating Newark under. Now, if we could get our hands on his set of books and find out what -- exactly what he was doing, I'm sure this Committee will get all the answers we want. Do I have some merit in my question?

COMMISSIONER HESPE: Yes. Well, there's merit in your question, absolutely.

ASSEMBLYMAN ZECKER: Do you think he was keeping a second set of books?

COMMISSIONER HESPE: We're not positive of that. We do know that the '98-'99 approved budget was overspent substantially, by 50 million, was it, approximately? No, the approved '98-'99 budget was overspent substantially, put it that way, and we're not clear how that happened without some understanding -- without having some way to track it, which wasn't the approved budget. So those are issues with a lot of merit, and we've actually been investigating--

ASSEMBLYMAN ZECKER: But I think if you zero in-- There's a lot of data here. If you can get this Committee what he did, from when he was there until the day that he left. These other memos are back and forth, but zero in, follow the dollars. All right. Apparently, he had a lot of control over the dollars. He was telling you or giving you what you were asking him

for, but he was doing something that was only known by him, or were there people close to him that knew what he was doing, and can we find out if they're still working in Newark? Maybe they can help us recreate the budget that Newark was actually working under -- a second set of books maybe.

COMMISSIONER HESPE: One of the problems that we had is that he kept the budget very much to himself. He ran the budget himself, and I don't think actually was functioning the way you would see a chief operations officer and a business administrator functioning. I think for that reason you really don't have the ability to track down much in terms of that issue.

I'll just ask Betsy or Mike to -- if they know anything about that.

ASSEMBLYMAN ZECKER: Then tell us how he was allowed to do that for so many years and why?

SENATOR MARTIN: Are you talking about Mr. Hellenbrand?

ASSEMBLYMAN ZECKER: Yes.

SENATOR MARTIN: Correct me if I'm wrong, but Dr. Hall, when she was hired, she brought in Mr. Hellenbrand, who was a high-level financial person within the New York City school system, to operate her system of finances. He is no longer in New Jersey. He's back, I believe, in Brooklyn. We have advised him that there was this Committee meeting, as we did with Dr. Hall and with former Commissioner Klagholz, and I think there might have been one or two others. I think Mr. MacIver was told, who was the business administrator operating under Mr. Hellenbrand, and at least informed him of this meeting and told them that if they -- they were certainly welcome to come. We wouldn't probably be calling them today, but that they may be, at some point, asked to testify.

I can tell you just, even with subpoena power, we wouldn't have the authority to be able to call-- They wouldn't have to respond to our request if they're out of the State of New Jersey. I believe Dr. Hall and Mr. Hellenbrand are outside the state. Whether they would honor a request, remains an issue.

ASSEMBLYMAN MORAN: Mr. Chairman, let me just ask one more thing. You know, I can remember sitting in this Chamber 13 years ago when Assemblyman, at the time, Palaia was walking around twisting arms to vote for this legislation. I believe, Assemblyman Bob Martin at the time was a co-prime sponsor of that bill, if I'm not mistaken.

SENATOR MARTIN: I don't think so. (laughter)

ASSEMBLYMAN MORAN: I think so. I remember getting my arms twisted.

SENATOR MARTIN: I supported the legislation.

ASSEMBLYMAN MORAN: And I did not, and sometimes I regret not supporting it, Joe, and I apologized many a time to you for that. But I can remember a number of things being debated during that piece of legislation right in this room here. A number of the issues was that making sure that all of our administrative staff in Newark, and in this particular case during the debate was Jersey City, were certified. We had the Superintendents Association of New Jersey, the Supervisory Administrative Council from New Jersey in arguing the point that everybody, in fact, was certified, and we found out later on during the evaluation that, in fact, it was not true. I don't think that they intentionally misled us, but I think they were misled themselves.

And we also made a point during the debate, I can remember, to make sure that all the school teachers were certified. We found out in many cases the teachers teaching in our urban school districts were, in fact, not certified. I can remember, Assemblyman, at the time, Palaia, Senator Palaia today, arguing the point that we must have all certified people. And the argument came up -- is that you're absent more than 21 days, were we going to let that lapse. We agreed that we weren't going to let that lapse, we were going to fight it. We were going to make sure it was done right, and that each and every youngster in New Jersey, especially in those youngsters in the urban school districts, are given at least a fair running start with certified people.

With all of that said, I find it extremely hard to believe that the second in command from the Superintendent of Schools, being Beverly Hall, which I had the pleasure of meeting on a number of occasions visiting Newark and going through the schools, and after her being Superintendent for three months, I think I visited more schools than she did in the Newark School District. I was more familiar with the Newark School District than she was after her 90-day tenure.

And I also found it interesting that Leonard Hellenbrand was not certified. We have an issue in New Jersey today -- is that each and every one of us, in central administration of public schools, have to go through the fingerprinting, you have to go through the certification, and we find it extremely difficult, on occasion, to find certified people. What we do is we advertise throughout the state, throughout the area, and around the country, and we're trying to encourage our State colleges and our private colleges in New Jersey to incorporate some of those programs so that we can get the

certified people. But here we are a school district, a State-operated school district, in the city of Newark, and I'm not calling it the Newark School District because it's the State of New Jersey School District.

To emphasize my point, Commissioner, I have to commend you and your staff for standing at the plate, going to the plate, and recognizing what's wrong, trying to put the pieces together, and making sure that the youngsters in this particular community are not hurt. I know what it's like to be audited, and let me tell you, it's not a pleasant experience. But when I get audited, I have something to lose. I have my certificate. I have my license. I have my job. But I find it interesting is when the State comes in and audits or when the State hires an auditing team, as Senator Martin very well said, coming in and being very, very careful about what they say because they'd like to get the next contract that comes down the pike, I think it's interesting that when they come in they audit us, or me, or my school district that I'm employed by, is that we shake in our pants, and we get nervous, and we break out into sweats. And that's a school district that complies to the law. That's a school district that has all licensed, certified people. We do the GAAP system, and we're extremely careful about each and every purchase order we do, each and every employee that we hire, because we all have something to lose.

I think if there's anything, and I think Byron Baer said it best before in the recommendations, I think we've got to be extremely careful. And if it means we've got to go back, and we've got to look at Newark. We've got to look at Paterson. We've got to look at Jersey City. We've got to look at all school districts through the County Superintendent's offices to make sure that

each and every person in his or her position is certified, is licensed. Because if there's nothing to take away from these people, if there's nothing but slapping on the wrist and going off to Atlanta or going back to New York and getting another job, we are not going to be serving the youngsters in New Jersey well.

I think if there's anything that we should go back and look at, Senator Palaia in due respect to you, to make sure that that particular piece of legislation that we passed 13 years ago, which said that every teacher has got to be certified and licensed, every administrator is going to be certified and/or licensed, there's going to have to be something there that we could take unbecoming. We can bring people up on charges and have something other than money to take away from that.

And I think if there's anything from this whole report that I read through briefly, and I listened to what the speakers were saying, as well as going through it, is that we found here -- is that everybody and anybody was pointing fingers. Nobody necessarily wanted to take responsibility. Those people, in my estimation, in my brief reviewing of it and reading all of the records that we've gotten in the last three or four weeks on this, is that everybody that is responsible packed up and left town and left you with the bag. And I commend each and every one of you and your staff. And most of all, I commend the people of the city of Newark because they recognized and they're standing up-- And from what I've been told, that they're standing shoulder to shoulder with you to recognize that there's a problem, but they're also impressed with the fact that there is somebody standing up and making

sure it gets resolved and the youngsters do not get punished in the city of Newark.

I have to stand with my colleagues here and say whatever it takes to make sure that youngsters in Newark, Camden, Jersey City takeover school districts are treated as fairly as those youngsters in the communities in which I represent in Ocean County, I think we've got a responsibility. I think those youngsters have a right, and I think we must stand up to the plate with you and your staff to make sure that that, in fact, is done.

Thank you, Mr. Chairman.

SENATOR MARTIN: We're going to try to wind down.

I know Senator Turner has been waiting. I think Assemblyman Stanley is waiting. So we'll try and-- We want you to be heard, but--

SENATOR TURNER: Okay. I'll be brief. I'm still trying to increase my level of confidence that this will never happen again. It seems as if you have an awful lot on your plate in the State Department of Education given the fact that you're operating three urban districts now. Also, you are supposed to be monitoring and overseeing the infusion of supplemental funds to 30 *Abbott* districts, as well as implementing Whole School Reform. And then on top of that, you're supposed to be monitoring the new school construction program. Given all of that, do you feel that you have sufficient staff to make sure that all of these things are not only going to be done, but be done effectively and efficiently?

COMMISSIONER HESPE: Well, I think the real bottom line is that Marion and I have an excellent relationship. Marion and I have the full confidence in Betsy DeMatteo, who is one of the top people in the State. I

don't think we could have found a better person to go into Newark. So the answer to that is when you have the right people, that's not an issue. And we have the right people in here.

SENATOR TURNER: But if you have problems monitoring one district, how can you monitor over 600 with the current staff, and you have all these additional responsibilities? You're saying you don't need any additional staff, that you can handle and keep all of these balls in the air at one time and not have any of them, again, hit the ground.

COMMISSIONER HESPE: I think it's not a quantity issue as much as it's a quality issue. I think if you have the right people in place, you can get the job done. I think we're very lucky in Newark to have the right people in place.

SENATOR MARTIN: You need very good jugglers.

SENATOR TURNER: Yes, indeed.

SENATOR MARTIN: I think, Assemblyman Stanley.

ASSEMBLYMAN STANLEY: Thank you, Senator. I'll be as brief as possible.

There are a number of people in Newark who are very, very much concerned with what we're doing here today. I think that we probably need to have, at least, one additional hearing. We've got Councilwoman Betsy Walker here, who came to testify. I know Eugene Campbell, former superintendent, is here. John Caverna (phonetic spelling) from the Newark-North Jersey Committee of Black Churchmen. And I know that John Aberdon (phonetic spelling) from the NCU, who has been very instrumental in really alerting the district to problems that, I know, some other legislators

as well, as to some of the problems in the Newark district before they really came out to the light, and I know he probably would like to testify also. I'd just like to, of course, commend you and urge you, and Chairman Wolfe, to convene another hearing of this type.

I just wanted to ask one final question of the Commissioner, and that is, do we know for a fact -- and this could have been asked already, and I apologize if it was -- that there is absolutely no criminal activity? I mean, could you or anybody say that there was no criminal activity involved? Fifty-nine million dollars is an awful lot of money. It's an awful lot of money. And then when you talk about the surplus, you're taking about 118 million, sometimes we look at it that way. I mean, a million here and a million there-- Are we confident beyond any doubt that all those moneys were spent on school issues?

COMMISSIONER HESPE: We're comfortable that we have not seen anything, yet, that would indicate that to us, but we have to audit these-- As these audited budgets come back, we have to review them. Our compliance unit is going to look at them. Our Federal units are going to look at these, and get that comfort level. In terms of criminal activity, we haven't come across any indications that anyone actually knew that this deficit was occurring, but I think we need to-- As information comes about to us, we're going to have to reassess that issue, and we're going to have to discuss it with the Attorney General's Office, because certainly-- You're right. These things don't happen. And if we say to ourselves, "This happens, oh, well," we're fooling ourselves. We have to make sure that we make that decision, but at this point we have not been able to conclude that that happened.

ASSEMBLYMAN STANLEY: Nor can we conclude that it didn't happen at this point either?

COMMISSIONER HESPE: I agree with you. That's right.

ASSEMBLYMAN STANLEY: Okay. Thank you.

SENATOR MARTIN: Just also -- since part of that was directed towards myself and Assemblyman Wolfe, Assemblyman Stanley, we did, as far as today's meeting, we tried as best we could to advise people that it was unlikely we would have an ability to have other testimony. I know the mayor of Newark also asked to-- And Senator James had asked to speak, as well as a number of other people. We said it was not likely today, especially with the voting session of the Assembly. However, we, at least between ourselves, assuming our leadership will go along with, do wish to have another meeting where people who think they can shed light on either past faults or make recommendations would be given an opportunity to speak, and certainly, that would be members of the Newark school community, as well as public officials.

ASSEMBLYMAN STANLEY: I think that would be--

SENATOR MARTIN: So we will plan to do that. I think it would be appropriate to wait until the Department, unless they can't get this in some reasonable point-- We'd like to have it at a time when they've released, as best they can, some financial picture of where the money went. We're still sort of in that mysterious vacuum of not knowing whether the money was appropriately spent, because we don't know where it went.

ASSEMBLYMAN STANLEY: Some of these people may be able to shed light on that, Mr. Chairman.

SENATOR MARTIN: Also, in fairness to Mr. Hellenbrand, although the request was made, an address was not found for him. So a letter did not go out inviting him to this meeting. If he read the papers, I'm sure he was aware of it, but we did not directly communicate to him. We did communicate to the other folks.

COMMISSIONER HESPE: We have not been able to reach him either. We have reached out to him a number of times.

SENATOR MARTIN: Don't hold your breath.

SENATOR TURNER: Mr. Chairman?

SENATOR MARTIN: Assemblyman Malone wanted to make a comment.

ASSEMBLYMAN MALONE: We had talked about that, and you had mentioned about an organizational chart in the past. Is there a current organizational chart for the school system and are there names associated with those positions, their background, and expertise in that position, and how the State interacts in each one of those positions?

COMMISSIONER HESPE: There is an organizational chart for both the State and the Department for the various kinds of State takeover, along with the chart, indicating the people who have held those positions, and for what times, in the Appendix.

ASSEMBLYMAN MALONE: Okay. But a current one-- Is this current?

COMMISSIONER HESPE: And current, yes. And current, past and current.

ASSEMBLYMAN MALONE: Okay.

COMMISSIONER HESPE: And if you have any questions after looking at that, we'll certainly fill in anything you need.

ASSEMBLYMAN WOLFE: Before we leave, I know the Senator also wants to speak, but, Commissioner, coming back to what Senator Martin just said, having some type of preliminary data would indicate some semblance of insurability where that money had gone. Do you have any time table of when you think that might be available for us?

COMMISSIONER HESPE: If you could allow us just this afternoon or tomorrow morning, and we'll give you a time frame.

ASSEMBLYMAN WOLFE: Okay. Thanks a lot.

SENATOR TURNER: I would just like to request that we receive copies of all written communications and memos regarding this entire situation be provided to us before we meet again.

COMMISSIONER HESPE: What was that?

SENATOR TURNER: All written communications and memos?

COMMISSIONER HESPE: Yes, you have everything we referred to in the report in this Appendix. There are other documents as well, and if you want, we will sit down with the various staff members and we'll go through those with them and see what other ones you would like. But everything we referred to in the report is here in the Appendix.

SENATOR TURNER: There are no other documents?

COMMISSIONER HESPE: There are plenty other documents, but these are the ones that we found to be critical. But I think in order-- If you want to get a fuller picture of that, I think the best way to do it is have

your staff sit down with those in the Department who actually did this, and they can review the whole universe of what's available for you.

SENATOR TURNER: Okay.

SENATOR MARTIN: Commissioner, many of the memos that you refer to here, and I think you've abstracted what you thought was the appropriate part, but if Senator Turner wanted to see that in more completeness, that would be--

COMMISSIONER HESPE: They're all in the Appendix. Each memo in its entirety is included here in the Appendix.

SENATOR MARTIN: Senator Gormley, last, last--

SENATOR GORMLEY: Just a comment. If I were ever to have left a troubled situation, I would hope that you would be my successor.
(laughter)

SENATOR MARTIN: Meeting adjourned.

(MEETING CONCLUDED)