
Audit of Student Transportation Services

A Report to the
Governor
and the
Legislature of
the State of
Hawaii

Report No. 99-1
January 1999



THE AUDITOR
STATE OF HAWAII

The Office of the Auditor

The missions of the Office of the Auditor are assigned by the Hawaii State Constitution (Article VII, Section 10). The primary mission is to conduct post audits of the transactions, accounts, programs, and performance of public agencies. A supplemental mission is to conduct such other investigations and prepare such additional reports as may be directed by the Legislature.

Under its assigned missions, the office conducts the following types of examinations:

1. *Financial audits* attest to the fairness of the financial statements of agencies. They examine the adequacy of the financial records and accounting and internal controls, and they determine the legality and propriety of expenditures.
2. *Management audits*, which are also referred to as *performance audits*, examine the effectiveness of programs or the efficiency of agencies or both. These audits are also called *program audits*, when they focus on whether programs are attaining the objectives and results expected of them, and *operations audits*, when they examine how well agencies are organized and managed and how efficiently they acquire and utilize resources.
3. *Sunset evaluations* evaluate new professional and occupational licensing programs to determine whether the programs should be terminated, continued, or modified. These evaluations are conducted in accordance with criteria established by statute.
4. *Sunrise analyses* are similar to sunset evaluations, but they apply to proposed rather than existing regulatory programs. Before a new professional and occupational licensing program can be enacted, the statutes require that the measure be analyzed by the Office of the Auditor as to its probable effects.
5. *Health insurance analyses* examine bills that propose to mandate certain health insurance benefits. Such bills cannot be enacted unless they are referred to the Office of the Auditor for an assessment of the social and financial impact of the proposed measure.
6. *Analyses of proposed special funds* and existing *trust and revolving funds* determine if proposals to establish these funds and existing funds meet legislative criteria.
7. *Procurement compliance audits* and other *procurement-related monitoring* assist the Legislature in overseeing government procurement practices.
8. *Fiscal accountability reports* analyze expenditures by the state Department of Education in various areas.
9. *Special studies* respond to requests from both houses of the Legislature. The studies usually address specific problems for which the Legislature is seeking solutions.

Hawaii's laws provide the Auditor with broad powers to examine all books, records, files, papers, and documents and all financial affairs of every agency. The Auditor also has the authority to summon persons to produce records and to question persons under oath. However, the Office of the Auditor exercises no control function, and its authority is limited to reviewing, evaluating, and reporting on its findings and recommendations to the Legislature and the Governor.



THE AUDITOR STATE OF HAWAII

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OVERVIEW

Audit of Student Transportation Services

Report No. 99-1, January 1999

Summary

This report was prepared in response to Section 46 of Act 116, Session Laws of Hawaii 1998 (the Supplemental Appropriation Act) which requested the State Auditor to conduct an audit of the student transportation program. This program provides subsidized school bus transportation services for eligible students traveling to and from public schools in grades kindergarten through 12th. The program also transports eligible special education students during the school day.

The audit focused on the Department of Accounting and General Services (DAGS), the agency responsible for procuring and delivering the services, and the Department of Education (DOE), the agency responsible for program oversight. We found that DAGS needs to improve the student transportation program. The methodology currently used to develop the base fare rate is questionable. The base fare rate is included in the State's contracted cost for each bus route. The internal controls are inadequate to assure that students are transported effectively and at least cost. For example, in FY 1997-98, the department's expenditures and encumbrances exceeded its authorized ceiling. This stemmed from the lack of adequate procedures to transfer and account for revenues from the pre-paid bus pass program. We also found instance of overpayments and outstanding encumbrances from appropriations that date back as far as 1986. We found that a weak internal control structure for the West Hawaii fleet operations, which consists of state-owned buses driven by state employees. Significant anomalies in the daily collections were never investigated and cash receipts and deposits do not reconcile. The department needs to develop procedures for recognizing and investigating irregular activities. We also found that DAGS uses a "50 percent" special provision that prevents true competition and violates the spirit and intent of Chapter 103D, HRS. The provision makes the program more costly for the State, has not been adequately reviewed, and may not be in compliance with administrative procedures outlined in Chapter 91, HRS.

We found that DOE needs to correct inefficiencies that are costing additional time and effort. The pre-paid bus pass program looks promising, but needs some improvement. Implementation varies among the pilot test schools, with some schools having serious accountability problems. The department needs to provide schools with better guidance on how to implement the program. We also found that DOE's efforts in the planning and coordination for student transportation could improve. DOE's failure to communicate changes in school calendars in a timely manner has created difficulty for DAGS but we recognize DOE is making improvements through the promotion of a complex-level calendar.

We also found that eligibility determination procedures were inefficient. Schools do not consistently verify eligibility, which may result in subsidizing transportation for unqualified students. The use of multiple forms for eligibility determination

program criteria is inefficient. The adoption of a single multi-use form to assist in eligibility determination for several subsidy programs should help efficiencies. We also note that the program could be more efficient by requiring forms to be filled out only for students requesting subsidy, rather than for all students.

Recommendations and Response

We recommend that the Department of Accounting and General Services (a) revise the base fare methodology to include control requirements already established under contract provisions and implement this methodology more frequently, (b) conduct a formal documented analysis of the "50 percent rule" to determine legality and feasibility, (c) improve personnel and fiscal accountability by implementing procedures for contract monitoring, investigations, and surveying contractor performance, and (d) improve the fiscal accountability of its West Hawaii fleet operations by implementing procedures for collections accounting and reconciliation.

We also recommend that the Department of Education improve (a) the fiscal and management controls over the pre-paid bus pass program by implementing policies and procedures outlined in the department's *User Policy Guide and Process Flow Manual*, (b) the procedures for reporting delays or service problems, developing projections of needed special education services, and requiring more timely submission of special education transportation requests, and (c) the controls over eligibility determination for full-subsidy ridership and bus pass processing.

The Department of Accounting and General Services noted that many of the operational accountability issues would be addressed once the pre-paid bus pass program is implemented statewide. DAGS agreed to review its investigative procedures and request a formal opinion relating to Chapter 91 compliance. However, we believe the issues revolve primarily around the procurement laws, Chapter 103D. While we generally agree that the pre-paid bus pass program offers some solutions to the problems discussed in the report, we caution that the program must have adequate internal controls in order to avoid creating other problems. The Department of Education expressed disappointment over an alleged lack of dialogue with DOE staff. Our records indicate such a deficiency to be untrue, especially in light of the legislative request for this audit. However, the DOE asserts that it will attempt to implement our recommendations even as it believes that our findings are "not necessarily consonant" with departmental directions.

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Submitted by

THE AUDITOR
STATE OF HAWAII

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Foreword

This report was prepared in response to Section 46 of Act 116, Session Laws of Hawaii 1998 (the Supplemental Appropriation Act) which requested the State Auditor to conduct an audit of the student transportation program (AGS 808). The budget act proviso requested the Auditor to analyze accounting procedures relating to the internal controls over the collection of student transportation fees, procurement practices, and fiscal and personnel accountability.

We wish to express our appreciation for the cooperation and assistance extended to us by the officials and staff of the Department of Accounting and General Services and the Department of Education whom we contacted during the course of this audit.

Marion M. Higa
State Auditor

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Chapter 1

Background on Student Transportation Services

Impetus for the Audit

The State's student transportation program provides both regular education students and special education students with bus services to schools in the state-run public school system. During the 1998 Regular Session, the Legislature expressed concerns about the student transportation program's efficiency and accountability. These concerns stemmed from the Department of Accounting and General Services' budget request of an additional \$700,000 for transportation services for the seven school days added to the regular school year. Furthermore, the department presented information about the pre-paid bus pass program which resulted in additional questions. Concerned about the adequacy of controls and program accountability, the Legislature questioned the program's operations and need for additional funding. The department was unable to justify its request to the Legislature's satisfaction.

As a result, the Legislature included in Section 46 of Act 116, Session Laws of Hawaii 1998 (the Supplemental Appropriations Act), a request that the Auditor conduct an audit of the student transportation program (AGS 808). The budget act proviso specifically requested the Auditor to analyze accounting procedures relating to the internal controls over the collection of student transportation fees, procurement practices, and fiscal and personnel accountability. The proviso also requested that the Auditor review the cost of the program and differentiate operating from non-operating costs and submit a report to the 1999 Regular Session.

Program Background

Prior to statehood in 1959, Hawaii first provided student transportation through the county governments. The counties' programs, however, varied greatly in regulatory standards, levels of service provided, and methods of acquiring services. For example, Hawaii County owned a fleet of buses while other counties contracted with private companies.

During the 1960s, the State assumed the function of providing student transportation services. Several laws were enacted that developed and implemented statewide safety standards for school bus transportation and transferred student transportation responsibilities to the State.

In 1970, the Department of Accounting and General Services and the Department of Education signed a memorandum of understanding that allocated student transportation responsibilities between the two agencies with guidance provided by the governor. The memorandum was amended in 1979 to include added responsibilities for the Department of Transportation and the Department of Personnel Services (now known as

the Department of Human Resources Development). The Department of Human Resources Development was to provide driver and first aid training to state-employed school bus drivers (this applies only to a small number of drivers who operate state-owned buses in West Hawaii). The 1979 memorandum assigned the primary responsibility of developing safety standards to the Department of Transportation, while the Department of Education was responsible for passenger safety education, developing relevant rules and regulations, and ensuring compliance. The Department of Accounting and General Services was responsible for contract administration, which included developing and enforcing contract provisions and requiring contractors to conform to rules, policies, and safety regulations. The memorandum was amended again in 1980 to clearly identify the Department of Accounting and General Services as the central source of public information for the student transportation program.

In 1983, the Legislature enacted Act 94, which was later codified as Section 286-181, HRS. This section codified the agreements developed in 1979. Despite some minor revisions since 1983 relating to vehicle safety, the responsibilities have remained unchanged. The four departments—the Department of Accounting and General Services, the Department of Education, the Department of Human Resources Development, and the Department of Transportation—continue to be involved in student transportation. Exhibit 1.1 outlines the major responsibilities of each department.

**Exhibit 1.1
Responsibilities of Departments Involved in Student Transportation**

Department	Responsibilities
Accounting and General Services	<ul style="list-style-type: none"> • Transports regular education and special education students to and from school. (Does not include field trips, excursions, or other school-related transportation needs.) • Draws up, puts out to bid, and awards contracts. • Monitors and enforces compliance with contract provisions.
Education	<ul style="list-style-type: none"> • Adopts rules governing passenger conduct, safety instruction, and disciplinary procedures. • Adopts rules related to supervision and administration of student transportation. • Provides transportation to and from school and for field trips. • Coordinates field trips and verifies student eligibility for fully subsidized transportation.
Human Resources Development	<ul style="list-style-type: none"> • Provides driver and first aid training for drivers of state-owned buses.
Transportation	<ul style="list-style-type: none"> • Adopts and enforces rules and standards relating to school vehicles, equipment, and drivers.

Source: 1980 Memorandum of Agreement between the Departments of Education, Transportation, Accounting and General Services, and Human Resources Development.

While each of these departments plays some role in student transportation, the focus of this audit is on the Department of Education and the Department of Accounting and General Services. These two departments form what is referred to in this report as the “student transportation program.”

Program Description and Operation

The student transportation program supports the Department of Education by providing subsidized school bus transportation services to all eligible public school students. The program provides bus transportation to and from public schools in all grades (kindergarten through 12th grade). In order to be eligible, a child must live at least one mile or more from the school. Those deemed eligible are issued passes.

Students who use these services pay a fare of \$0.25 per trip (Maui and Hawaii County children pay less because their counties further subsidize the fare). Some students are exempt from paying any fare and are given a special bus pass. Bus drivers monitor paying student passengers to ensure that fares are paid. Fares are collected and kept by the contractor.

In addition to the established program, a pre-paid bus pass program has been implemented at ten schools. Under this program, students pay a set fee for a bus pass that is valid for a certain time period. Individual schools are responsible for cash collection and program accountability and the revenues are disbursed in a variety of ways.

In addition, the student transportation program provides free transportation to and from school, between school and other sites, and in and around school for special education students.

Exhibit 1.2 presents cost information and the number of students participating in the statewide student transportation program for the 253 public schools.

Exhibit 1.2
Student Transportation Services for 253 Schools (School Year 1997-98)

	Total Number of Students	Total Number of Riders	Percent of Riders to Total Students	Estimated Annual Average Cost Per Rider
Regular education students	173,720	31,500	18.13%	\$337
Special education students	15,561	2,889	18.56%	\$2,785
Total (all students)	189,281	34,389	18.17%	\$542

Sources: Department of Education's Communications Office and the Department of Accounting and General Services' Student Transportation Branch.

The Student Transportation Branch of the Department of Accounting and General Services consists of ten positions, including one branch chief, one contract specialist, one clerk typist, and seven student transportation officers (three on Oahu, two on Hawaii, and one each on Kauai and Maui). Student transportation officers are responsible for administering and monitoring the private contractors, investigating complaints, and assessing routes and ridership. The neighbor island transportation officers receive direction for technical issues from the Student Transportation Branch but report to the department's district offices for day-to-day operations. The district offices' supervisors are responsible for all department functions for their island, including student transportation, and report directly to the comptroller.

The student transportation program is operated through contracts with private providers except for eight buses located in West Hawaii that are controlled by the department. The drivers for this state-operated program are custodians from the schools. The student transportation officer for the West Hawaii district is responsible for controlling and maintaining these buses. This small operation is a continuation of the county program from the late 1960s.

The department contracts with private vendors whose selection is based primarily on the lowest bid per route. The contracts run for six years and allow two biennial extensions. This contract length allows companies enough time to recoup the amount invested in the purchase of equipment, especially buses. The contracting procedure—issuing Invitations for Bid, processing submissions, and awarding the contracts—is staggered over several years so that all routes are not open for bid in the same year. Currently, 65 contracts cover approximately 785 routes statewide. For FY1997-98, the Department of Accounting and General Services expended approximately \$18.6 million for these contracts. The department has been appropriated \$20.3 million in general funds for FY1998-99. Exhibit 1.3 shows the total operating expenditures of the Student Transportation Branch by cost categories.

Objectives of the Audit

1. Review and assess management controls related to the procurement, management (including fiscal), and operations of student transportation services.
2. Review and assess planning and coordination efforts between the Department of Education and the Department of Accounting and General Services, as related to student transportation services.
3. Review, analyze, and report program expenditures.
4. Make recommendations as appropriate.

Exhibit 1.3**Operating Expenditures of the Department of Accounting and General Services, Student Transportation Branch (FY1997-98)**

Operating Expenditures by Category	Amount
Bus contracts (regular and special education routes)	\$18,650,449
Personnel	332,386
Repair, maintenance, and fuel cost (West Hawaii fleet)	56,032
Mileage reimbursements	46,113
Office supplies	5,329
Utilities	2,160
Postage	1,623
Travel	1,143
Furniture and equipment	356
Interest payment and others	228
Total expenditures	<u>\$19,095,819</u>

Source: Department of Accounting and General Services departmental report no. 445 and adjustments for previous encumbrances expended in the current fiscal year.

Scope and Methodology

The audit examined student transportation activities statewide at the Department of Accounting and General Services, Student Transportation Branch and the Department of Education. We reviewed procedures and practices related to the procurement, administration, and delivery of services. We assessed the controls established over the collection of student fees, coordination efforts between the Department of Accounting and General Services and the Department of Education, and other related issues. We also analyzed and reported the expenditures of the program. The Department of Transportation and its responsibilities relating to school bus safety fell outside the scope of this audit and therefore were not subject to review.

The scope of the audit included all contracts currently in effect. Since the duration of contracts can be up to ten years, current contracts include those from FY1987-88 to the present. However, the assessment of procurement practices was limited to contracts that were re-bid and executed or extended in FY1997-98. The fiscal review covered FY1997-98. Information on projected expenditures included information up to FY1999-00. Documents, files, and correspondence reviewed were from FY1997-98. All related audits, news articles, and reports were reviewed.

We used the following general methodology to accomplish the objectives of this audit: we interviewed staff at the Department of Accounting and General Services, the Department of Education, the Department of Transportation, the State Procurement Office, and the City and County of

Honolulu. The team also interviewed contractors and reviewed their documents related to state student transportation contracts.

We conducted walkthroughs of the program cycles (including contracting, receipts, disbursements, purchasing, and reporting) and evaluated the applicable internal and management controls over the processing and reporting of statistical and fiscal data to determine the extent and timing of procedures to be performed. Appropriate sampling methods for the compliance and/or substantive testing were used to fulfill the objectives of the audit.

Our work was performed from June 1998 through October 1998 in accordance with generally accepted government auditing standards.

Chapter 2

The Student Transportation Program Lacks Accountability

This chapter outlines our assessment of the management and operations of student transportation services. The State of Hawaii has been providing student transportation services for over thirty years—relying on privately contracted services established by the counties prior to statehood. We found that the Department of Accounting and General Services, the agency responsible for procuring and administering program services, needs to improve program controls to ensure greater accountability. We also found that the department is using a contract provision during the procurement process that appears to violate the spirit and intent of Chapter 103D, Hawaii Revised Statutes (HRS), and the administrative procedure established in Chapter 91, HRS. We found that the Department of Education needs to improve coordination and reduce costly operational inefficiencies.

Summary of Findings

1. The Department of Accounting and General Services' student transportation program needs to change its approach to rate setting, contract monitoring, and financial controls in order to strengthen accountability and efficiency.
2. A special contract provision violates the spirit and intent of the procurement laws. The department is accepting higher bids when the lowest bid contractor holds 50 percent or more of the routes within the district. This practice costs the State more money than necessary to operate the program. In addition, this provision was instituted without following administrative procedures.
3. The Department of Education needs to reduce inefficiencies and solve other costly problems with adequate guidance and controls.

The Department of Accounting and General Services' Student Transportation Program Needs Improvement

The operations and management of the Department of Accounting and General Services' student transportation program needs improvement. The department uses an unsound method for determining base fare rates and lacks the necessary internal procedures to adequately monitor contractors and contract compliance. The department also failed to develop adequate controls to ensure fiscal accountability. The lack of adequate controls has resulted in serious errors in managing the program's finances.

Unsound method is used in developing base fare rate

The department employs a "base fare" rate methodology that is unsound. The department uses the number of paying riders for a nine to ten working day period each October. This ridership, and therefore its revenues, is assumed to represent the average ridership for the entire school year. The estimated revenue constitutes the base fare rate for each route and each contractor. The department deducts the base fare rate from each contract payment rate and pays each contractor the balance throughout the year. The department thus eliminates having to collect fares itself but still benefits from the offset they provide. While the system appears to work well, the methodology used to calculate the base fare rate is questionable. Each company collects and keeps the actual fares paid by students. The base fare rate, which represents the average revenues, are reduced from the State's payment on the contracts. We find this methodology to be unsound because the procedures used to gather the information needed to calculate the base fare rate are not truly representative of the average ridership.

Some bus companies allege that the ridership used to calculate base fare rate is higher than the actual average ridership. If true, this results in lower contract payment to the bus companies. Legislators, on the other hand, were concerned that the base fare rate may be too low and that contractors were reaping profits because the program lacks controls.

In school year 1995-96, the department recalculated the base fare rate because of valid complaints by contractors regarding significant decreases in ridership. It determined that the daily total base fare rate for all contracts decreased approximately \$900 from October to February. The department attributed the decrease in ridership to the increased bus fare rate implemented during that year. Our testing suggests that the ridership decrease is due to seasonal variations rather than a single event such as a bus fare increase.

In order to determine the relative accuracy of the base fare rates, we compared the actual revenues collected by bus companies to the base fare rate being used by the department. Contracts were selected randomly from two bus companies. Information on fare revenues was requested for school years 1995-98. Both companies had significant difficulty fulfilling our request, even with several extensions. In fact, by the end of our fieldwork, one company still had not provided us with all the information requested.

From one bus company, we were able to obtain the total fare revenues collected for a two year period. We verified revenue amounts by reconciling the company's cash receipt logs with its deposit receipts and bank statements. We then calculated the total fares collected for the contract. We found that the base fare rate deducted from the contract

amount was greater than actual revenues collected. We found that the company was short approximately \$12,000 per year for these contracts. Exhibit 2.1 outlines the results of our examination.

Exhibit 2.1
Comparison of Fare Collection and Base Fare Rate

School Year	Fare Revenues Collected and Kept by Bus Company	Base Fare Rate Calculated and Subtracted by DAGS from Contract Amount	Difference (Contractor Short)
1995-96	\$127,120.45	\$140,092.15	(\$12,971.70)
1996-97	\$126,173.13	\$138,496.75	(\$12,323.62)

Sources: Bank deposit slips and contract billing statements.

We concluded that using the current methodology allows for too much variability from the actual collections. Our conclusions are based on recorded fare revenue collections provided by the bus contractors. The variances between actual collections and average collections create inequity in the payment to contractors. As previously noted, it appears that one contractor is losing a significant amount of revenues and is not realizing the full contract price. One way to overcome this inequity is to use a statistical method to determine average ridership. However, this would involve random sampling and require base fare rate adjustments back to the beginning of the contract period.

In the past, the department had a more accurate means of determining fares collected that was outlined in the contracts. Bus companies were required to establish separate revenue accounts for each contract, deposit receipts daily under separate collections, and submit deposit receipts to the department on a weekly basis. The information available from this process also allowed the department to determine, with more accuracy, the fares being collected. Although some of these older contracts are still in effect, the department has removed this provision from more recent contracts.

Contractors fail to comply with contract provisions

We reviewed the department's procedures for contract compliance and found inadequate controls. We requested information from contractors based on earlier contract provisions but, as noted earlier, neither company could readily provide the information. One company kept sufficient records, but failed to deposit moneys on a daily basis and oftentimes commingled its deposits. The other company simply did not provide all the information required.

Contract provision not enforced

A department official noted this provision was not enforced due to inadequate staffing. The department should require its contractors to comply with contract provisions. Its failure to do so raises the question of how monitoring is conducted and accountability maintained since sufficient information is not being provided and reviewed.

Inadequate controls result in problems

State law requires departments and agencies of the executive branch to establish and maintain an adequate system of internal controls. Section 40-2, HRS, requires that agencies ensure that their internal control systems continue to function as designed. The department failed to comply with this requirement. As a result, the department has exceeded legislative and administrative ceilings for expenditures and encumbrances, made overpayments, and failed to allow outstanding encumbrances on expired contracts to lapse to the State's general fund.

Expenditures and encumbrances exceed authorized ceilings

The department has expended and encumbered funds exceeding its legislative and administrative ceiling. During FY1997-98, the department collected approximately \$44,000 in revenues from the pre-paid bus program. However, the department failed to identify this and reduce its appropriation request to account for collection of revenues from the pre-paid bus program in its preparation of the program budget. As a result, the Legislature unknowingly appropriated general funds without deducting collections from the pre-paid bus program. Rather than depositing the cash to the state treasury, the department chose to use the revenues to reduce program expenditures. This had the effect of increasing the program's allotment from which it expends and encumbers funds. As a result, the department expended and encumbered over \$10,000 more than it was initially authorized.

Contractors are overpaid

In our review, we found two instances in which the department overpaid contractors. The total overpayment amounted to more than \$11,000 and was due to the lack of a timely review and communication with the schools and bus companies. The department receives a billing from contractors twice a month that is checked against contract and base fare information, then recorded in internal records. It is also checked against information supplied by the schools and the bus companies, such as changes in school schedules or ridership. However, the department fails to reconcile this billing to the State's accounting records generated from the Financial Accounting Management Information System (FAMIS), which reflects payment. Had the review of information and reconciliation occurred, the department would have noticed that it was current with its bus contract payments and an adjustment to the billing would be required.

Another indication of the weak review process was the difference between the department's internal records and the State's records. An effective system of internal controls includes appropriate review and reconciliation of financial transactions to safeguard assets from loss or misuse. The department lacks such a system.

Outstanding encumbrances for expired contracts not lapsed to general fund

Section 40-66, HRS, requires appropriations to lapse when funds are not expended during the fiscal period and where a contract for engagement has not been made and is not in effect. This is to ensure that unused funds are available for other programs the following fiscal year. We found that the Department of Accounting and General Services failed to lapse general funds amounting to more than \$11,000 for bus contracts that have expired. One expired contract had encumbered general funds from the 1986 appropriation, more than 11 years ago. In addition, funds from three other contracts totaling \$11,000, from FY1993-94 to FY1995-96, continue to be encumbered. Although these contracts are still valid, the years for which the encumbrances were made has long since passed and unexpended funds should be lapsed. The department explained that some of these encumbrances are for contractors who provided services but failed to submit a tax clearance. We urge the department to resolve the tax clearance issues and pay the remaining contract obligations. Any remaining encumbrances should be considered unused and lapsed to the general fund to become available for new legislative appropriations.

State fleet operations need improvement

In addition to procuring contract services, the Department of Accounting and General Services also operates eight state-owned school buses in the West Hawaii district. This program requires the department to collect student fares, much like the private contractors. As noted earlier, the department is required to establish adequate internal controls under Chapter 40, HRS, but has failed to do so. We found several weaknesses in the program's internal control structure. Procedures were not established to monitor and investigate anomalies occurring in revenue collection. In addition, the program's cash receipts did not agree with the total cash deposited.

Internal control structure is weak

The West Hawaii fleet operation has significant weaknesses in its internal control structure that have led to inconsistencies and deficiencies in the fleet's fiscal operations. The West Hawaii operation is geographically divided into three smaller operations with each operation handling collection and disposition of cash receipts differently. We were informed by department officials that West Hawaii operations involve placement of

cash collected by drivers in unsecured containers such as coffee cans and candy jars. We inspected the buses and confirmed that no secure fare boxes were present.

In the Ka'u area, the schools collect fares from the bus driver and give the driver a numbered receipt. The schools then disburse a check to the Department of Accounting and General Services for the total amount collected together with all the receipts issued to drivers. This operation has relatively strong controls in place. Adequate records are maintained that allow deposits to be traced to checks and the corresponding receipts of the cash collected.

In the Kohala area, schools also collect the student fares from the drivers. However, unlike Ka'u, the money is placed in an envelope with the daily collection amounts noted on the front of the envelope. No receipt is given to the driver. The cash collection is periodically taken to the West Hawaii transportation office, usually once a week. The internal controls for this operation are relatively weak. These collections, left in cash, are commingled with cash receipts from the Kona operation, which makes determining its origin difficult. In addition, numbered receipts are not maintained, making it impossible to reconcile the cash collected and deposited.

Cash collected from the third operation in Kona is usually remitted daily to the West Hawaii transportation office in Kona. However, receipts are not generated and the cash receipt logs do not include signatures of the drivers nor the receiver of the cash certifying the amount being submitted. In addition, the cash is not deposited on a daily basis.

Anomalies in daily collections not investigated

The weak internal control structure noted earlier has resulted in serious accountability problems. For example, the West Hawaii cash receipt log included a number of anomalies that remain uninvestigated and unexplained. Daily cash collections fluctuated significantly. For example, one route's collection ranged from \$13.65 to \$41.37. This represents a daily change in ridership of over 92 students on a single route. In addition, there were 16 instances in which one or more drivers had no deposit entries. No sufficient explanation was provided. The information contained in the log also indicated other amounts, not associated with drivers, again with no explanation. When asked about the discrepancies in collection amounts, a department official only replied that ridership can change. This does not adequately explain the wide range in collections and deposits. The recognition and resolution of anomalies are essential to maintaining accountability and the safeguarding of assets from loss or misuse.

Cash receipts and deposits not properly accounted for

We conducted additional testing to determine the extent of the problem with the cash receipt logs. Initially we tested several months of cash receipt logs to determine whether the cash deposited matched the totals for the amounts recorded in the logs. However, the West Hawaii transportation office inappropriately recorded Kohala's cash receipts as daily receipts when actually the cash was received weekly. This resulted in cash deposits not matching the cash received and recorded in the cash receipt logs, making it difficult to track discrepancies.

In order to further investigate this problem, we expanded our testing to include the entire 1997-98 school year. The test results indicate that the West Hawaii transportation office deposited an amount in excess of \$440 of that recorded in the cash receipt logs. West Hawaii officials could not explain the reason for the excess deposits. The problem could be attributed to inaccurate cash receipt logs or moneys from another program being incorrectly deposited to the credit of the student transportation program. Given the initial problems noted with the cash receipt logs and the excess deposits, we conclude that the amounts recorded in the cash receipt logs are unreliable and that the West Hawaii's fleet operations lack the basic internal controls needed to safeguard the cash collected. The Department of Accounting and General Services needs to address this serious issue.

Procedures for recognizing and investigating irregular activities are needed

The department, as the administrator of the student transportation program, should monitor contracts and contract related activities to ensure bus company practices comply with laws, rules, and contract provisions. An adequate system is not in place to accomplish this task. During our review, we found a number of incidences that were not directly investigated by the department. In cases where other agencies were involved, the department failed to gather sufficient documentation to make a determination about the status of the contracts involved. In addition, the department failed to develop and implement a consistent system to apply penalties for bus companies not in compliance.

Questionable indicators not investigated

Base fare collections, bidding patterns, and other indicators of anti-competitive practices are key areas that require monitoring. Base fare collections determine the amounts deducted from the total contract price. As noted earlier, monitoring of this area is weak.

We found that base fare collections fluctuated significantly from year to year. Of the 10 routes we reviewed, we found that the collections between years varied by as much as 58 percent. This variance resulted in a difference of approximately \$3,600 in fare collections.

Monitoring bid patterns and other contractor activities may indicate anti-competitive activities. We found two companies in the most recent bidding of contracts that did not compete for the same routes, even though one company is located in the area of the other company's routes. In another case, one company was charged with collusion by the attorney general, which resulted in a mutual settlement and a fine. However, the department did not have documentation relating to the case. These types of questionable situations should have been investigated by the department to formally assess and resolve the questionable practices. Unfortunately, the department lacks such procedures and as a result, possible misdeeds have not been sufficiently investigated.

Department lacks adequate enforcement procedures

The department failed to develop policies to establish consistent enforcement. Past incidents could have resulted in actions against bus companies for violating the provisions of the contract.

Currently, a standard contract provision imposes a fine for liquidated damages of \$50 per day for specific violations. However, the application of this provision is inconsistent. The department has not developed a schedule of fines to ensure consistency in applying the fines. Department officials noted that all cases are treated separately and that the chief of the Student Transportation Branch makes the final determination. However, one bus company has questioned the status of fines imposed on another company. While we were unable to substantiate any claims of inequitable treatment, we determined that a process is lacking to ensure that companies are treated fairly.

Given the competitive nature of the student transportation industry, the Department of Accounting and General Services should develop a policy outlining penalties for contract violations to ensure equitable treatment. Implementation of investigative and enforcement policies and procedures would ensure that bus companies are clear on the consequences of violating laws, rules, and contract provisions.

Special Provision in Contract Specification for Procurement of Student Transportation Services Violates Spirit and Intent of Procurement Laws

The 1993 Hawaii Public Procurement Code, or Chapter 103D, HRS, applies to all contracts entered into after July 1, 1994. The intent of the law was to increase competition, ensure fairness, and establish greater uniformity in the purchase of goods and services. We found that the department's special provision for awarding contracts, the so-called "50 percent rule," violates the intent of fair and open competition. The special provision is inefficient, inconsistently applied, and is costing the State thousands of dollars. Also, the special provision could be a violation of the administrative procedures established in Chapter 91, HRS. If the special provision was deemed to be necessary, it should have been put into

effect as a rule or policy, using the correct administrative procedures, rather than using contract language to implement the provision. Such was not the case.

50 percent provision prevents true competition

In 1978, the department established a special provision commonly referred to as the “50 percent rule.” The provision, which is outlined in the Invitation for Bids for awarding student transportation contracts, was originally intended to prevent companies from monopolizing school bus services in any one county in the state. The provision requires any bidder with more than 50 percent of the routes in a county to bid at least 10 percent less than the second lowest bidder in order to be awarded the contract. Consequently, contract awards have not been awarded necessarily to the lowest bidder, but at times to the second lowest bidder. The provision appears to violate the spirit of fair and open competition established by Chapter 103D, HRS and Chapter 122, Subchapter 5, Hawaii Administrative Rules, which govern state procurement practices.

Provision circumvents lowest bid award and equal treatment

Section 3-122-33, Hawaii Administrative Rules, establishes the requirement that the State award contracts based on the lowest responsive bid and on criteria established in the Invitation for Bid. This section of the rules also states that all factors used for bid evaluation and award must treat all bids equally and that:

all specifications shall seek to promote overall competition, shall not be unduly restrictive, and provide a fair and equal opportunity for every supplier that is able to meet the state’s needs.

Under the department’s special provision, contractors who have over 50 percent of the routes are not evaluated equally because they are required to submit a lower bid in order to compete for the contracts.

Provision is inconsistently applied

The student transportation program provides bus services for both regular education and special education students. Transportation for regular education students to and from schools uses designated bus stops near the student’s home. In some cases, special education students can ride with the regular education students. However, when the child has special needs that prevent the use of regular transportation, the State provides free curb-to-curb transportation service. The State contracts for each type of service separately. However, both types of contracts must comply with the same procurement laws and are processed in a similar manner through the State Procurement Office.

Currently, one contractor holds 58.5 percent of all regular education and 65.7 percent of all special education routes statewide. If the department's rationale that the 50 percent provision was developed to prevent one contractor from monopolizing the market, one would assume that the provision would also apply to special education contracts. However, this is not the case because the "50 percent rule" is currently applied only to regular education contracts.

Department officials have stated that, historically, there has been no economic advantage for bus companies to control the special education transportation market. However, expenditures for special education transportation were approximately \$8 million for school year 1997-98—representing over 40 percent of the total appropriation for the student transportation program. In addition, special education expenditures for FY1998-99 show an increase of approximately \$434,000 from the previous year.

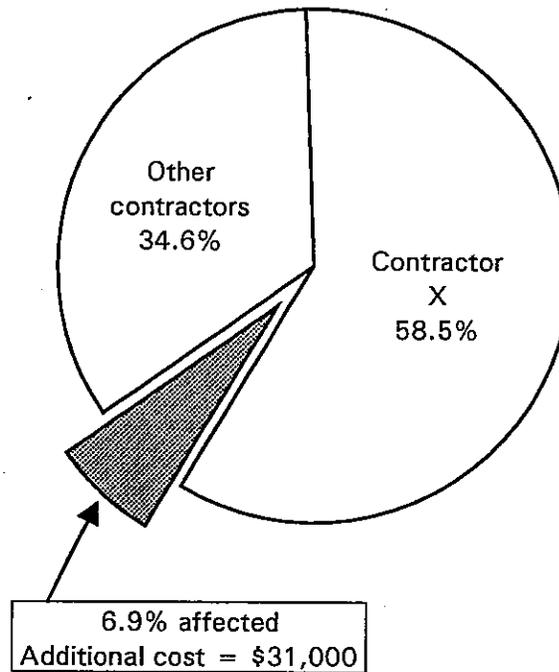
Under the Individuals with Disabilities Education Act and the *Felix* consent decree, the State is required to provide services, including transportation, if it is identified as necessary for a student's education. This makes special education transportation services an attractive market for bus companies, as noted by the current 65.7 percent of the routes held by one bus contractor. Yet the department's position is that special education transportation is not lucrative and not prone to a monopoly by one contractor. The department's inconsistent application of this provision raises the question as to whether the rationale used by the department is sound, and whether such a provision is truly necessary and in the best interest of the State.

***Implementation costs
the State more money***

Department of Accounting and General Services officials note that the "50 percent rule" saves the State money in the long run by keeping a larger number of competitors in the market. More contractors increase competition, giving the State more options and better prices. Department officials note that this is a long-term view of saving money for the State.

While the department's approach is theoretical, an analysis of the "50 percent rule" shows that thousands of dollars in State funds have been wasted. During the past three years, the provision was applied to three Invitations for Bid where the lowest bidder did not receive the contract. The resulting three contracts cost the State an additional \$31,000 per year. In total, with contract extensions, the provision could cost the State an additional \$310,000. Exhibit 2.2 presents the impact and added costs of the "50 percent rule." As shown on the exhibit, 6.9 percent of the contracts were awarded to higher priced contractors because the lowest bid contractor was unable to meet the lower price requirements under the "50 percent rule." It is questionable whether the additional \$31,000 per year will result in any long term cost savings to the State.

Exhibit 2.2
Effects of 50 Percent Provision



While the cost for implementing the special provision is available, the “savings” gained from the special provision is arguable. The Department of Accounting and General Services assumes that companies that are currently in the industry cannot survive without the special provision. While the department may eventually justify the special provision, it has failed so far to conduct sufficient analyses and documentation to warrant the continued use of the provision. It should develop a cost/benefit analysis to justify how the State will save money paying the higher prices. In addition, the department should comply with administrative procedures in developing and implementing the special provision.

***Lack of legal review
leaves provision open
to challenge***

The “50 percent rule” was developed and implemented over 20 years ago but no documentation shows that an adequate legal review was conducted. The department reports that a previous branch chief worked with the Department of the Attorney General in developing the provision, but the department was unable to provide any documentation to substantiate this claim. In any case, the procurement laws have changed significantly since 1976. Chapter 103D, HRS, establishes open competition, fairness, and uniformity. As noted above, the special provision appears to violate the intent of the current law. Given the questionable nature of this special provision, the department should seek a contemporary legal opinion regarding the use of the special provision.

Implementation of provision may violate Chapter 91, HRS

The “50 percent rule” is also open to challenge as an “unofficial” rule, violating Chapter 91, HRS. The “50 percent rule,” while hidden in contract language, essentially establishes the departmental policy relating to the evaluation of bids for student transportation. It also establishes a practice that affects the awarding of bids. Policies and practices fall under the definition of “rule” in Chapter 91 as a statement by the agency that “implements, interprets, or prescribes law or policy, or describes the organization, procedure, or practice requirements of any agency.”

Chapter 91, HRS, requires that rules go through a public hearing process to ensure that all rules are available for review before being implemented. This helps ensure that policies and practices implemented by the departments are fair, equal, and consistent in the treatment of all parties affected by the rule. The department’s inclusion of the “50 percent rule” within student transportation contracts changes the treatment of private contracts based on the contractor’s market share. The regular practice of using the special provision for evaluation of contracts and award of bids raises concern that the department may be in violation of the public review process established in Chapter 91, HRS.

The Department of Education Needs to Correct Inefficiencies

The Department of Education provides guidance to the student transportation program through policies, procedures, and rules. We found that guidance is lacking and results in inefficiencies that impact program operations. Decisions by the Board of Education, the Department of Education, and the schools can impact student transportation operations and related program costs. To be effective, these decisions need to be coordinated with the program administrator and the Department of Accounting and General Services. However, we found such coordination to be lacking.

Pre-paid bus pass program looks promising but needs improvement

The Department of Education, together with the Department of Accounting and General Services, developed a pre-paid bus pass pilot program that allows parents to pay for student transportation at the beginning of the school period. The Department of Education initiated this program to reduce potential discrimination between students with full-subsidy passes and those paying the \$0.25 partial subsidy fare. Students fully subsidized get a colored pass, while others get a white pass and pay the bus fare. The Department of Education noted that the issue was not about the color of the pass, but the distinguishing of students who place money in the fare box from those who do not.

The pre-paid bus pass program also has other advantages. Collecting the fares ahead of time eliminates problems associated with parents having to find correct change, lost or stolen bus fare, and non-paying students. It also improves program operations by placing fare collection under state

rather than contractor control. The major disadvantages are the additional work for schools at the beginning of the school period and the cost of supplies.

However, our assessment of the pilot program indicates that much more planning and guidance is needed. Schools vary significantly in their implementation and cash receipt processes. In addition, the two departments need to develop a better infrastructure to support the program.

School fare implementation significantly varies

The pre-paid bus pass program was first initiated as a pilot project in the fourth quarter of school year 1995-96. Since then, nine other schools have implemented the program.

In March 1997, the Department of Education's Office of Business Services developed guidelines for schools interested in implementing the program. The guidelines, however, provide very little information for schools except a basic framework. The department noted that "there is no one single-agreed-upon system" and schools are allowed to experiment. This lack of clear guidelines has resulted in schools developing varied procedures with inequitable impact on students.

We evaluated five schools and found significant variations in the implementation of the program. Some schools developed sound policies on lost passes, fare collection procedures, and pre-qualification. Other schools lacked basic controls needed to maintain accountability. Even schools that developed good procedures had a number of inconsistencies.

The determination of the price to the parent(s)—flat rate—for the pass varied by school. Some schools based the price of the pass on the cost per day and the total number of school days in the period. Other schools discounted the total price, assuming students would not ride every day. For example, three schools charged a flat rate of \$20.00 per quarter. The flat rate represented a 5 percent discount. The two other schools charged rates based on the number of days in the period. Three schools had a "no refund" policy; the remaining two did not. Prorating policies for students who were enrolled some time after the period began varied among schools. Lost pass charges also varied significantly, from \$1.00 to \$5.00 for the first lost pass up to \$20.00 for a third lost pass. These varying practices result in inequity to parents, who are being charged different rates for similar services. The Department of Education should review the various methods and develop consistent policies and procedures for the schools to implement.

Handling of cash receipts is inconsistent

The handling of cash collections also varied among schools. Some schools have developed a system based on the department's *User Policy Guide and Process Flow Manual, Section VII, Accounting for Collections*, that describes collection procedures. These schools used numbered receipts, cash logs, and had relatively good controls to safeguard the cash collected. Other schools, however, did not use receipts and failed to document amounts collected, the number of passes issued, or the names of the students issued passes. These schools did not have an adequate system to safeguard cash receipts. Most schools we reviewed had some weaknesses in their pre-paid bus pass program collection process.

While we found a majority of schools used receipts and other control documents, one school kept the cash collection box in an unsecured area. Schools also failed to deposit cash on a regular basis. We found one school had collected over \$3,000 before it made a deposit. The funds were kept in a safe for over three weeks. Another school did not use collection accountability procedures outlined in the department's manual, such as use of numbered receipts for money collected, documentation of student participation, and sufficient segregation of cash receipt duties.

Improvements, however, are expected. The Department of Accounting and General Services' review of their cash collection process in October 1997 resulted in several recommendations that have yet to be implemented. We urge that the Department of Education require schools using the pre-paid bus pass program to use control procedures established in the department's manual. Schools should already be familiar with these procedures as they are applied to the collections of other school-related fees.

No procedures established for handling revenues

The pre-paid bus pass program usually collects payments for bus passes for a school period such as a quarter or a semester. We found that the two departments have yet to develop a system to regularly transfer the revenues collected. This was due primarily to a lack of policy on accounting for the revenues and a general lack of understanding of the budget process.

The revenues collected from the programs varied from approximately \$4,000 to \$17,000 per school year. In March 1997, the Department of Education provided some guidelines indicating that schools should deposit the cash in their own accounts until the Department of Accounting and General Services sent a bill for the revenues collected. However, the deposit procedure was not always followed. Of the five schools we reviewed, two schools gave fares collected directly to the bus companies.

Other schools followed the required procedure and deposited the revenues in their accounts until billed by the Department of Accounting and General Services.

The Department of Accounting and General Services has not developed a system to regularly bill schools for the revenues collected. In some cases, schools have waited over two years for billing. In addition, the department does not know how much to bill schools and simply asks the school for the amount collected without verifying the amounts collected.

The Department of Accounting and General Services' student transportation program made its first collection in February 1998. The department collected \$44,762 from five of the schools on Oahu. However, as of the completion of our fieldwork, the department had yet to bill the schools on Maui and Hawaii. In addition, Oahu schools have not been billed for the last two quarters.

The delay between billing times could be more costly if additional schools implement the program because the State will lose interest earnings on uncollected revenues. If 20,000 regular paying students used pre-paid passes, the total revenues collected would be approximately \$1.8 million and simple interest earnings at 5 percent would represent a potential loss of \$90,000 per year.

The Department of Accounting and General Services and the Department of Education need to develop a schedule for transferring revenues collected under this program. The Department of Accounting and General Services should also develop a tracking and accounting method for these revenues.

Planning and evaluation component lacking

The pre-paid bus pass program has received strong support from the Office of the Superintendent which has stated that the pre-paid bus pass program would be implemented statewide by August 2002. While strongly supported by management, school personnel have serious concerns about the program and its implications. This is largely due to the Department of Education's failure to adequately plan and evaluate the program, and address the concerns of school personnel.

Schools have serious concerns about the impact on the workload required and the additional costs involved. These details need to be resolved before the program can be viable for statewide implementation.

One school has opted not to fully implement the program because some families have difficulty paying the up-front cost. Another school, located in a higher socio-economic area, has fully implemented the program because cost is not an issue.

Another concern is the cost to implement the program. The Department of Accounting and General Services has offered to compensate schools for administrative expenses. However, there is no definite compensation rate and there is some question as to whether compensation is appropriate for already established clerical positions funded through appropriations. Also, one school official noted that the funding offered by the Department of Accounting and General Services is not guaranteed. In the event of budget restrictions, the department could easily amend or cancel its offer.

Administrative costs reflecting the program workload vary. One school charged the Department of Accounting and General Services \$720 for administrative expenses. Another has not charged at all because the impact on operations was minimal. The impact on the school's workload varied according to school officials. One school said that it took very little time to incorporate into the school's operation because there were few riders. Another noted that it took a part-time person about 10-20 hours a week for several weeks. The key variable was the number of students being transported.

The issue of clerical support is a big concern for school officials. Many feel that schools are already short of clerical and administrative support staff and the pre-paid bus pass program would be an additional burden. As noted above, this may not be true depending on the number of students using transportation services.

The Department of Education needs to address the problems and variations identified if the program is to be further implemented. Schools need to be assured of adequate support and resources. Schools need clearer guidelines to avoid the pitfalls some schools have already experienced. In April 1997, the superintendent announced discussions would be held regarding a statewide implementation plan for the pre-paid bus pass program. In November 1997, the superintendent reported that the Office of Business Services, the Office of Information and Telecommunications Services, and the Office of Accountability and School Instructional Support were working to design an infrastructure to support the program. The superintendent also noted that the Office of Business Services would be reissuing guidelines and providing direction. Since that time, no additional guidelines or training have been provided.

***The department's
planning and
procedures need
improvement***

The Department of Education should improve coordination of regular and extended school calendars and the school-level procedures for transportation services. Taking into account the trend toward year round schools and the requirement for the extended school year, the department should coordinate with the Department of Accounting and General Services. Better school-level procedures for special education are also needed.

Irregular school calendar requires more coordination

Variations in the school year due to implementation of year round calendars and its attendant impact on the extended school year for special education significantly affect the provision of student transportation, especially for the Department of Accounting and General Services. Contractors oftentimes use a single bus for several trips to several schools, elementary through high school. If schools within the route are all on the same school year schedule, then pick-ups and drop-offs are not a problem to coordinate. However, not all schools are on the same schedule. An increasing number of schools have begun a year round school calendar that runs independently of other schools in the area. As a result, schools significantly vary in their times for things such as breaks and early release. The department is making some improvement through the promotion of several school complex calendar models:

Generally, in April the department provides the school calendars to the Department of Accounting and General Services so that schedules can be developed to best meet the area needs. However, not all schools provide calendars and some list dates as "TBD" (to be determined). As a result, last minute changes must be made as the information becomes available, costing additional time and money because not all buses are put to full use.

Another scheduling problem results from the extended school year for some special education students. As the number of year round schools increases, fewer facilities are available to hold special education extended school year classes. Developing extended school year schedules has become a complex task as special education students attend one school during the regular year and need to be transported to another school that is available for the extended school year. The routes become longer as more children attend fewer available schools. Scheduling problems and the day-to-day complaints received by the Department of Accounting and General Services hinder its ability to take proactive measures to ensure contractor accountability.

School level procedures need improvement

The education department needs to improve school level procedures relating to reporting of violations, responsibilities for dropping off students and requesting special education transportation. We found a number of cases in which school officials were not clear about their responsibilities due to poor training or lack of procedures. These concerns need to be addressed to increase accountability and improve the services provided.

In our review of 22 schools, we found several in which school staff were not clear about their responsibilities. School level staff collect bus

transportation applications, verify requests for fully subsidized transportation, and ensure that contractors provide the required services. We observed officials calling the bus companies directly when there were problems with bus arrivals. The proper procedure is to call the Department of Accounting and General Services to report problems. In most cases, the school staff lacked knowledge or training despite the education department's established policies.

Schools that do not properly report problems with student transportation services hinder the Department of Accounting and General Services' ability to improve the quality of the services. When school officials work directly with the contractor, the Department of Accounting and General Services is unable to accurately assess the services being provided. In some cases, direct violations of contract provisions for which the department can fine the contractor "liquidated damages" of up to \$50 per day were not directly reported. School officials need to know their role in monitoring and reporting service quality.

Policies relating to drop-off of special education students also need improvement. Under the Individuals with Disabilities Education Act, the Department of Education is required to provide related services to special education students to ensure they benefit from their education. Curb-to-curb transportation and mid-day transportation are considered related services. For curb-to-curb service, a contractor transports the child from home to school and back at the beginning and end of the school day. For mid-day service, the contractor transports the child to and from locations during the school day. Under current operations, the contractor has no drop-off guidelines when responsible adults are not present. The private contractor is responsible for the child until the child is turned over to a responsible adult, usually a teacher or the parent/guardian. The contractor may drop the child off unattended under certain situations but cannot do that for a severely disabled child.

Upon reviewing the school year 1997-98 driver complaint files for Oahu, we found 55 complaints due to no adults being present. Neighbor islands had considerably fewer complaints. In all cases, there is no official policy and the driver is usually forced to make a decision. The driver could wait, drop off other children along the route and return at a later time, or in extreme cases, return to the school or the bus company's base yard. In the event of a driver error or injury to the child, both the State and the contractor could be held liable. In 1995, the department developed a draft policy that it attempted to coordinate with other agencies such as the Honolulu Police Department and the Department of Human Services. However, this policy remains in draft form. To minimize the potential liability, we believe that the department should establish a formal policy that relieves the contractor and driver from making these decisions and to reflect the State's efforts in protecting the child.

Schools need to be more timely in their requests for special education transportation services. Schools submit their requests to the Department of Accounting and General Services for processing by early August. The request forms are reviewed and coordinated with contractors to provide coverage for the special education students, which is considerably more complex than providing for regular education students.

Since special education transportation is curb-to-curb service, adding a single child increases travel time and impacts other children's pick-up and drop-off times. Due to the individualized nature of their services, the school requests need to be timely. Every year, the Department of Education reminds schools to request services early. For school year 1997-98, the deadline was August 8, 1997 to ensure transportation for the upcoming school year.

In our review of requests for Oahu for the period May 1997 through May 1998, we found a significant number of late requests as demonstrated in Exhibit 2.3. A large number of requests arrived in May 1997, some of which were early requests for the next school year. However, a majority were requests for extended school year services which require greater coordination. The number of requests remained relatively high during June through July, reflecting late extended school year requests. The requests then increased during August through September, reflecting late requests. The Department of Accounting and General Services staff confirmed that late requests are a problem and hinder their ability to plan and coordinate special education transportation. The transportation was provided in most cases largely due to the cooperation of the contractors. However, services were delayed in other cases. The Department of Education needs to improve its coordination efforts and procedures to provide more efficient transportation services.

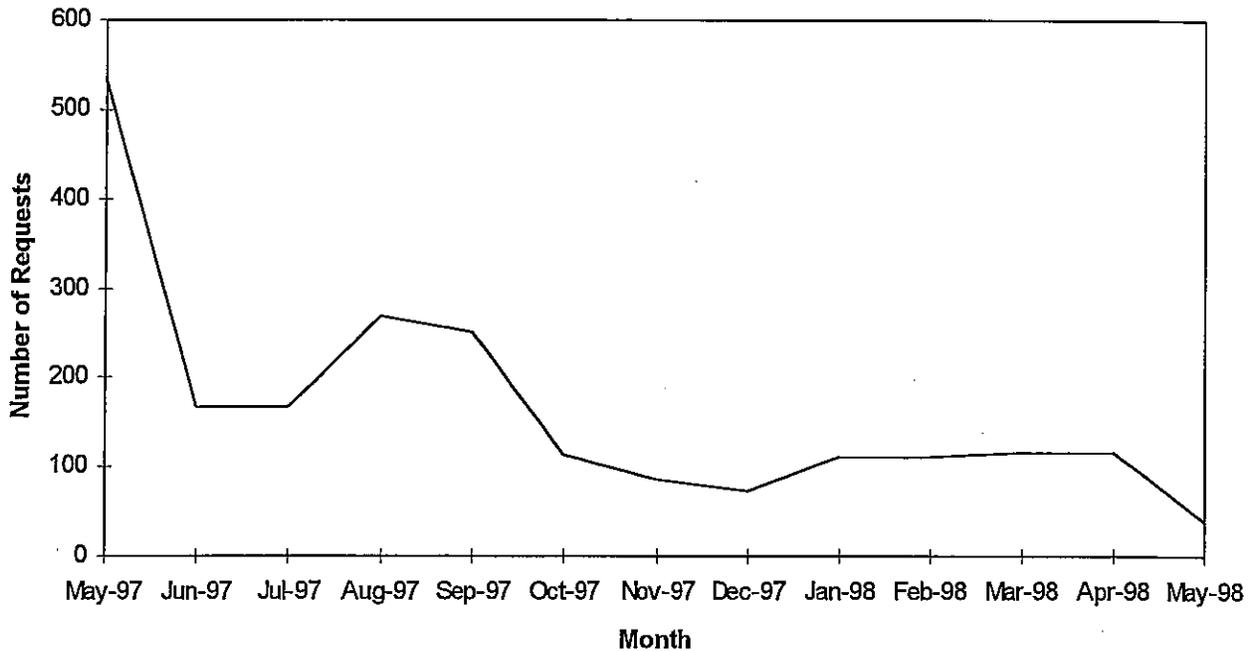
***Eligibility determination
needs improvement***

The process of determining eligibility for full or partial subsidy of student transportation is based primarily on the parent's ability to pay for the service. Fully subsidized transportation reduces fare revenues by approximately \$1 million per school year. We found that as much as \$210,000 for free services to ineligible students could be subsidized due to inadequate verification instructions and procedures.

Eligibility determination has weak instruction and verification is inconsistent

The department's procedures used by schools to verify eligibility fail to instruct schools on gathering information for verification and as a result, schools determine their own procedures. Without verification, the State is at risk of authorizing subsidized fares for ineligible riders.

Exhibit 2.3
Turn-in of Special Education Transportation Requests for Oahu, School Year 1997-98



We tested the accuracy of the eligibility information provided by parents for full-subsidy transportation from a sample of 22 schools (541 student files). We found that 80 percent of the schools were not verifying the claims and simply relied on the information provided by the parents.

In order to qualify for full-subsidy transportation, one of the following conditions must be met: the family is receiving welfare assistance, the family income level is below the Poverty Income Guidelines for Hawaii, the family has more than three riders paying for school bus transportation (fourth rider), or the students are affected by consolidation, grade transfer, or department-directed attendance.

We tested full-subsidy applications for reliability of information by matching information with the department's National School Lunch program. From our 541 application sample, we found numerous cases where information relating to income, number of family members, and welfare status did not match. A majority of discrepancies were related to income reporting where parents reported different income levels under each program. Other discrepancies related to the number of family members reported. The number of family members reported affects income level eligibility. In some cases, the discrepancies were such that

the student would not qualify for full-subsidy transportation. As much as 22 percent of the applications for full-subsidy transportation contained information from parents that did not match the National School Lunch Program Information which could have resulted in ineligibility. Based on this, the total loss of fare revenue could be as much as \$210,000 per year.

The department is making improvements

While the lack of a standardized verification process is troubling, the department has taken steps to improve verification procedures for all subsidized programs. A recently developed multi-use form requests parents' consent to use the information from the free and reduced lunch program to verify eligibility for summer school attendance, After School Plus (A+) program enrollment, and school uniform purchases. While the form does not include verification for full-subsidy bus transportation, the department still has the option of including it. We urge that the department add bus transportation verification to the multi-use form and develop a standardized procedure for all program verification. Controls such as cross-matching of program information for eligibility should be in place. Combining program eligibility efforts will be more efficient than the current separated efforts.

Program eligibility determination can be combined for efficiency

The department's verification effort for the student transportation program is redundant and inefficient. A standardized process to cross-match program eligibility information within the school would be more efficient. Various programs have similar criteria that could be applicable. The student transportation program also includes a "fourth rider" criterion that is difficult to verify and is applied inconsistently. The department should evaluate these areas to help improve overall efficiency.

Single criterion may be more efficient. The department's school lunch, After School Plus (A+), and student transportation programs all use income information as a basis of determining eligibility for subsidized or reduced fees. If all three programs used the same criteria, then establishing sufficient controls for one program would provide reliable information to verify the other two. This system is already used for the After School Plus (A+) program, which uses a formula based on the National School Lunch program criteria to determine eligibility and the amounts parents are charged. The student transportation program, however, uses a lower income scale to determine subsidy eligibility. A comparison of the three programs is shown in Exhibit 2.4.

**Exhibit 2.4
Comparison of Eligibility Requirements**

Eligibility Criteria	Student Transportation Program	National School Lunch Program	After School Plus (A+) Program
Welfare recipient	Receive full subsidy	Receive free lunch	Receive free after school care
Income qualification	100% of the poverty guidelines	130% of the poverty guidelines	130% of the poverty guidelines
Reduced rate for services	None	185% of the poverty guidelines	185% of the poverty guidelines
Number of children enrolled in the program	Fourth child is free	None	Reduced rate based on number of children

In order for the verification process to be more efficient, the department should evaluate the possibility of using the same eligibility criteria.

Fourth rider criterion rarely used and inconsistently applied. One eligibility criterion, the fourth rider, applies only to student transportation services. It is rarely used and schools have difficulty with verification. Schools also vary in their determination of eligibility using this criterion.

The fourth rider allows parents with more than three children paying bus fare to have free service for their fourth child. However, our sample of schools and student files reviewed found a low 1.5 percent, or eight applications, on full subsidy based on fourth rider eligibility alone. School officials noted that verifying a fourth rider is difficult and time consuming. If children are attending elementary, intermediate, and high school, school officials must contact individual schools to verify fourth rider eligibility. One school instituted a policy in which families qualify for the fourth rider subsidy only if all four children are in the same school. Other schools allow students to be in different schools. However, follow-up verification is rare.

The department was not able to provide information relating to the initiation of this criterion. It could be presumed that the fourth rider criterion reduces cost to parents. However, under this criterion, parents can qualify for a free fourth rider regardless of their income level. Most schools that had families applying for full-subsidy using income eligibility and fourth rider applied income eligibility as the primary criterion, rather than fourth rider. Fourth rider was used only in cases where it was the only criterion on which to base the application. The department needs to evaluate the need for this fourth rider eligibility criterion based on the small number of qualified students, the difficulties in verification, and the lack of correlation with parents' income levels.

Redundant information is collected, creating more paperwork

The procedures to apply for student transportation are inefficient, redundant, and create further administrative burden for those involved. Processing partial-subsidy riders involves collecting information that is readily available from other sources. Collecting information from paying families wastes time and resources.

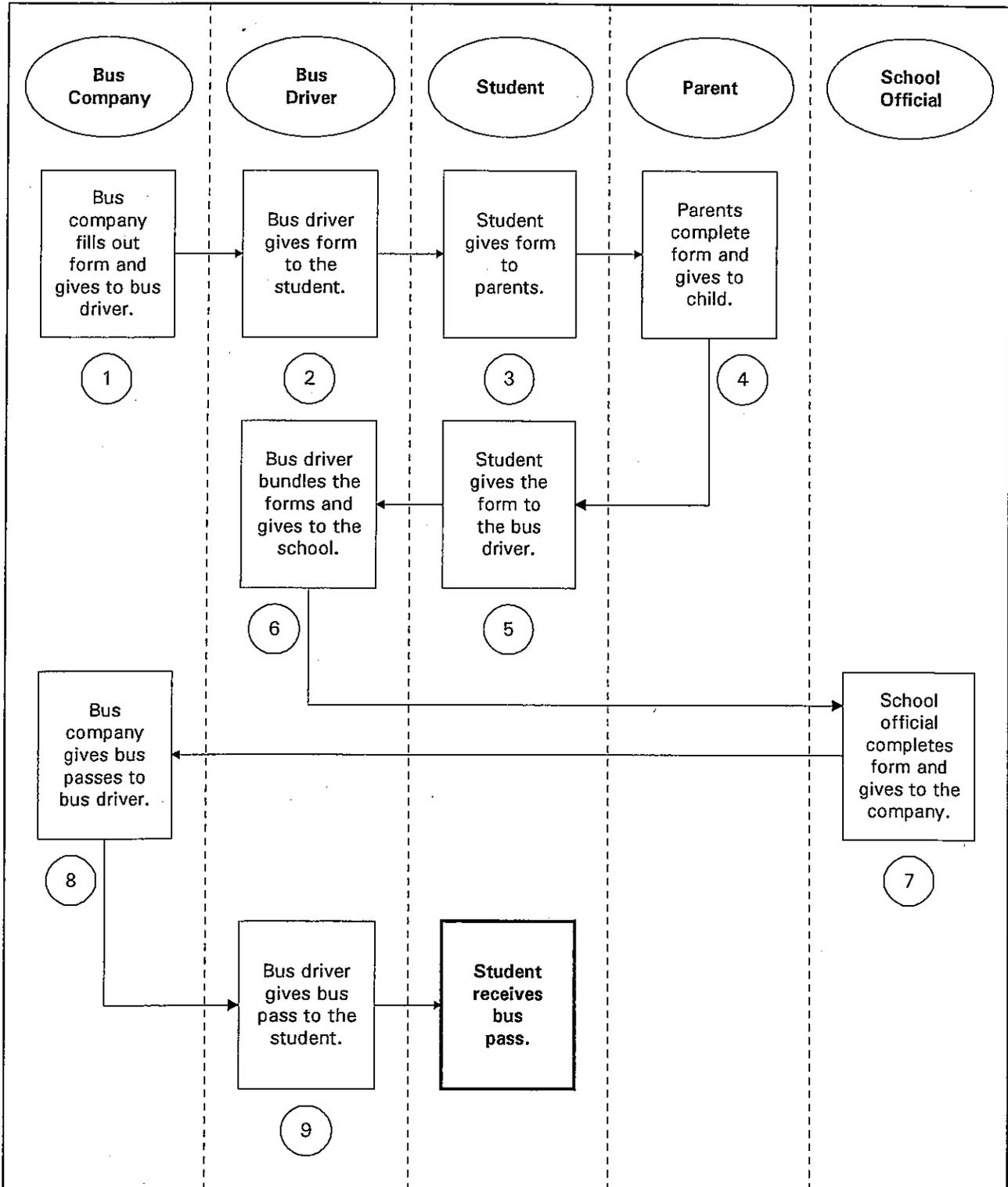
The student transportation program requires parents to fill out a form to request school bus services which the school uses to determine whether the child lives at least one mile from the school or is eligible for full subsidy. Bus companies use part of the form to process the bus pass. In contrast, the National School Lunch program requires parents to apply only when requesting free or reduced lunches for their children. Paying students do not submit applications.

The processing of the application is unnecessarily complex and time consuming. The bus application form is exchanged between the student, parent, bus driver, bus company, and school as many as nine different times before the student finally receives a bus pass. In some cases, it takes four to six weeks for the student to receive a bus pass. The bus pass application procedure is shown in Exhibit 2.5.

The form serves no useful purpose for paying students. Schools report that the forms are simply filed and never used again. One school processed, categorized, and filed over 700 forms and the department, as a whole, processed over 20,000 forms for school year 1997-98 for all paying students.

The schools already have basic student information to determine the one-mile distance for bus services before the school year begins. This information could easily be inputted and updated in the department's computerized School Information System that already has a specific module for student transportation. The module includes pre-set fields for bus number, routes, stops, and schedule times and open fields for customizing the module. Schools could easily use this module to generate a report to the bus companies for the preparation of bus passes. The arduous process for bus applications for paying riders can be eliminated. This would streamline bus pass processing by eliminating needless administrative work for the schools.

Exhibit 2.5
Bus Pass Application Process



Conclusion

The State has been providing student transportation for over 30 years. During this time, little has changed in the operations and management of the student transportation program. Much of the system inherited from the counties still remains. We found a lack of fiscal and operational procedures and internal controls that resulted in a lack of accountability. Both the Department of Education and the Department of Accounting and General Services need to coordinate and improve their efforts for the conditions we identified.

Recommendations

1. We recommend that the Department of Accounting and General Services:
 - a. Revise the base fare methodology to include control requirements already established under contract provisions and implement this methodology more frequently;
 - b. Conduct a formal documented analysis of the “50 percent rule” to determine legality. If the department feels that the provision is warranted, it should develop a cost/benefit analysis and follow appropriate administrative procedures to establish the provision as a formal rule;
 - c. Improve personnel and fiscal accountability by implementing procedures for contract monitoring, investigations, and surveying contractor performance. It should also develop a consistent method of applying fines and penalties; and
 - d. Improve fiscal accountability and its West Hawaii fleet operations by implementing procedures similar to those outlined in Accounting for Collections, Section VII, *User Policy Guide and Process Flow Manual* (DOE). The department should also reconcile student transportation expenditures and encumbrances to FAMIS reports monthly to ensure the program does not exceed its authorized ceiling and lapse unused encumbered funds for expired contracts.
2. We recommend that the Department of Education improve:
 - a. Fiscal and management controls over the pre-paid bus pass program by implementing policies and procedures outlined in the department’s *User Policy Guide and Process Flow Manual*;
 - b. Procedures for reporting delays or service problems, developing projections of needed special education services in light of school

year variations, and require more timely submission of special education transportation requests; and

- c. Controls over eligibility determination for full-subsidy ridership and bus pass processing.

Responses of the Affected Agencies

Comments on Agency Responses

We transmitted drafts of this report to the Department of Accounting and General Services (DAGS) and the Department of Education (DOE) on December 16, 1998. A copy of the transmittal letter to the Department of Accounting and General Services is included as Attachment 1. Its written response is included as Attachment 2. The response of the Department of Education is included as Attachment 3.

Overall, both departments generally agreed with our comments and are committed to making improvements. DAGS noted that it would review the need for including control provisions in the older contracts and obtain a formal legal review of the "50 percent rule" to determine compliance with Chapter 91, Hawaii Revised Statutes. The department also noted that it would implement controls where necessary, within its constrained resource. The department disagreed with our assessment that the program expenditures and encumbrances exceeded its authorized ceiling. However, it noted that it would be investigating the need and the requirements to establish a special fund.

While we note that DAGS has responded positively to the major areas of concern, we need to make two points. The department's focus on Chapter 91, the Administrative Procedures Act in obtaining a legal compliance review should be directed instead at Chapter 103D, the Hawaii Public Procurement Code. Simply complying with Chapter 91 is insufficient. Also, the department asserts that a number of internal control issues, especially those related to fare collections, would be resolved through the implementation of the pre-paid bus program. While we generally agree, we believe that the internal control problems of the pre-paid bus pass program itself must be addressed to assure that the program is fair and that all funds are collected and accounted for.

While the DOE asserts that it will do its best to attempt implementation of our recommendations, it also asserts that our findings are "not necessarily consonant with . . . departmental directions." This resulted, the department maintains, from inadequate dialogue between the department's state-level staff and our audit team. The department also asserts that the report contradicts some recommendations made by us in past reports.

We challenge the DOE's contention of our inadequate dialogue with state-level program staff. The legislative request was to audit the program operated by DAGS, AGS 808 and review financial areas that impact program costs. As a result, much of the work was performed at DAGS. However, revenues for the pre-paid bus pass program are collected and

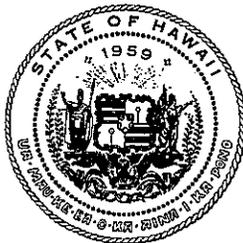
eligibility for subsidized transportation is determined at schools, requiring our review at the schools and selected staff-level offices. Staff at the Office of Accountability and School Instructional Support and the Office of Information and Telecommunication Services, the Board of Education, and the parent volunteer organization were contacted. A specific staff member was contacted on at least six occasions.

We disagree with the DOE's contention that the audit recommendations are not consistent with prior audit recommendations relating to decentralized decision-making. The recommendations in this report address the need to improve controls and procedures over various functions at the schools as they relate to student transportation. These improvements will help to ensure accountability, efficiency, and equity among those affected. The issue of decentralized decision-making and these recommendations in this report are separate issues. Decentralized decision-making can occur with the application of consistent procedures.

The DOE argues that it would stifle innovation by mandating procedures. But our recommendation focuses on the need to evaluate how schools currently implement the pilot program from development to distribution to other schools, avoiding the errors made during the pilot phase of the program. The department maintains that we were remiss in not discussing the planning and evaluation component with its staff. We reiterate that we did contact the staff at issue, as well as others, and all confirmed that there was no evaluation and no actual plan for implementing the pre-paid program.

As to the department's contention that it lacks the resources to carry out our recommendations, it nevertheless controls the prioritization of non-instructional resources and needs to give greater attention to the program that gets students to and from school.

STATE OF HAWAII
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917



ATTACHMENT 1

MARION M. HIGA
State Auditor

(808) 587-0800
FAX: (808) 587-0830

December 16, 1998

COPY

The Honorable Ray Sato
State Comptroller
Department of Accounting and General Services
Kalanimoku Building
1151 Punchbowl Street
Honolulu, Hawaii 96813

Dear Mr. Sato:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *Audit of Student Transportation Services*. We ask that you telephone us by Friday, December 18, 1998, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Monday, December 28, 1998.

The Department of Education, Governor, and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

A handwritten signature in cursive script, appearing to read 'Marion M. Higa'.

Marion M. Higa
State Auditor

Enclosures

BENJAMIN J. CAYETANO
GOVERNOR



CS-99.054

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING
AND GENERAL SERVICES
P. O. BOX 119
HONOLULU, HAWAII 96810-0119

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OFF. OF THE AUDITOR
STATE OF HAWAII

December 28, 1998

Ms. Marion M. Higa
State Auditor
Office Of The Auditor
465 S. King Street, Room 500
Honolulu, Hawaii 96813

Dear Ms. Higa:

We thank you for the opportunity to provide comments on your draft report entitled "Audit of Student Transportation Services." Our response is divided according to the recommendations cited in the report.

Recommendation 1(a.)

Revise the base fare methodology to include control requirements already established under contract provisions and implement this methodology more frequently.

Comment

The program has investigated alternatives to the concerns identified in this audit recommendation. In order to address the recommendation, we will review the benefits and impact of including control provisions that currently exists in older contracts. However, the program views the need for a pre-paid bus pass system as the longer term solution. In this respect, we will work with the Department of Education and its schools to accomplish implementation in accordance with the Superintendent of Education's directive which requires full compliance by the year 2002. Through this system, both rider anonymity and greater control over base fare counts and collections can be maintained.

Recommendation 1(b.)

Conduct a formal documented analysis of the “50 percent rule” to determine legality. If the department feels that the provision is warranted, it should develop a cost/benefit analysis and follow appropriate administrative procedures to establish the provision as a formal rule.

Comment

In order to clarify matters, a formal opinion on how this special provision relates to Chapter 91, HRS will be requested from the Attorney General. It is our position that this rule has proven effective in preventing the monopolization of the school bus industry in Hawaii. As the largest consumer of school bus services, it is necessary for the State to preserve competition within the industry. Historically, the consequences of having inadequate competition can only lead to higher prices over the long term.

Recommendation 1(c.)

Improve personnel and fiscal accountability by implementing procedures for contract monitoring, investigations, and surveying contractor performance. It should also develop a consistent method of applying fines and penalties.

Comment

The program will revisit its existing procedures as they relate to this recommendation. Within available resources and where ever appropriate, necessary controls will be implemented through written procedures to address the Auditor’s concerns.

Recommendation 1(d.)

Improve fiscal accountability and its West Hawaii fleet operations by implementing procedures similar to those outlined in Accounting for Collections, Section VII, User Policy Guide and Process Flow Manual (DOE). The department should also reconcile student transportation expenditures and encumbrances to FAMIS reports monthly to ensure the program does not exceed its authorized ceiling and lapse unused encumbered funds for expired contracts.

Comments

The implementation of a statewide pre-paid bus pass program will reduce much of the concerns over accounting and proper internal controls for base fare collection. During the interim, the program’s existing procedures will be reviewed and modified as needed to assure the necessary level of control.

Additionally, the program has proposed to the Department of Education that State-operated busses in West Hawaii be eliminated by June 2000.

With respect to expenditures and encumbrances:

1. The program will work with its Administrative Services Office to assure the timely reduction of contract encumbrances at the end of each contract period. Only those contracts for which a tax clearance for final payment has not been submitted will be kept open. However, in these situations, the program will aggressively pursue resolution.
2. We believe that your assessment of "expenditures and encumbrances that exceed authorized ceilings" has been misunderstood. Although the program is appropriated funds by the Legislature, it is NOT fully budgeted through appropriation. Thus, the practice of applying fare collections towards contract costs is understood by the Department of Budget and Finance (B&F) and Legislature. This is evidenced by B&F's reduction of the program's Fiscal Year 1996 budget in anticipation of an increase in fare rates from 10 cents to 25 cents. In summary, fare collections are necessary to adequately cover contract costs.

In order to clarify your concern, we have consulted with our Administrative Services Office. For the present time, we will continue to treat pre-paid bus pass collections as a program reimbursement. Simultaneously, we are investigating the need and requirements to create a special fund to collect and disburse these funds.

Should you require further information on our response, please have your staff contact Mr. George Okano at 831-6739.

Sincerely,


RAYMOND H. SATO
State Comptroller

c: DAGS-Central Services

BENJAMIN J. CAYETANO
GOVERNOR

PAUL G. LeMAHIEU, Ph.D.
SUPERINTENDENT



STATE OF HAWAII
DEPARTMENT OF EDUCATION
P.O. BOX 2360
HONOLULU, HAWAII 96804

OFFICE OF THE SUPERINTENDENT

December 28, 1998

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OFFICE OF THE AUDITOR
STATE OF HAWAII

The Honorable Marion M. Higa, State Auditor
Office of the Legislative Auditor
465 South King Street, Room 500
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

Thank you for the opportunity to respond to your report entitled, "Audit of Student Transportation Services." Our comments on your recommendations for the Department of Education (DOE) are listed on the attached page.

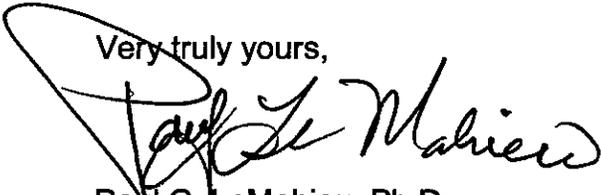
Please be informed that we were disappointed that an adequate dialogue between our staffs did not transpire regarding the merits and shortcomings of the program. Consequently, the findings of your audit are not necessarily consonant with our departmental directions. Additionally, your office has made recommendations in the past proposing more decentralized decision-making at the school level which are consistent with our general direction but ironically dichotomously offer several recommendations for standardization of procedures and program implementation in this audit.

The reality of dwindling resources and the large increase of duties placed on school staff due to decentralization have forced us to make difficult decisions regarding the allocation of resources. Since our priorities are concentrated on

The Honorable Marion Higa
Page 2
December 28, 1998

classroom needs, we have not been able to provide additional funding for non-classroom related tasks such as refinement of the management of student transportation services. It is difficult for you or the public to realize the strain under which school offices must operate. Nevertheless, we will do our best to attempt implementation of the auditor's recommendations and will continue to work closely with the Department of Accounting and General Services, Central Services Division, to improve the program in all facets noted by your audit.

Very truly yours,



Paul G. LeMahieu, Ph.D.
Superintendent of Education

PLeM:jl

Attachment

cc: S. Fernandes, CSD/DAGS
A. Suga, Supt's Office

DEPARTMENT OF EDUCATION'S RESPONSE TO AUDIT OF
STUDENT TRANSPORTATION SERVICES

Recommendations and Department's Responses to Recommendations:

- 1) **Fiscal and management controls over the pre-paid bus pass program by implementing policies and procedures outlined in the department's "User Policy and Process Flow Manual."**

The department will review the "User Policy and Process Flow Manual" to determine how proper fiscal and management controls can be implemented. It should be noted that there has been no complete evaluation of the pre-paid bus pass program which needs to be carried out. While there are inconsistencies related to the allowance of schools to experiment with procedures, you have pointed out that some schools developed sound policies for some matters. If the department had mandated the procedures, some of the innovations might not have surfaced. The department can implement those procedures which the auditor found to be sound, if provided with a list of those items, and can eliminate undesirable practices which have occurred. Your assistance in obtaining the good policies and procedures from your viewpoint would be appreciated. The department will work with the Department of Accounting and General Services (DAGS) to implement a pre-paid bus pass program with the assistance of staff in the Office of Business Services such as the school support section or the internal auditor.

The DOE will continue to promote the pre-paid bus program despite some organizational support and personnel problems. We support your statement on page 22 that the issue of clerical support is a big concern for school officials. The pre-paid program will definitely be a burden on many schools and should be noted as a concern of the department since the staffing standard for clerical staff has not been reached over a long period of time, nor does there seem to be any support for the improvement of this problem.

The DOE plans to improve the training of school staff including administrators and clerical staff to implement the pre-paid bus pass program despite inadequate training funds and personnel. Inadequate training funds decreases the opportunities for the department to properly instruct all staff on the procedures, problems, and solutions to handling the pre-paid bus pass system. Hence, there will inevitably be differences in operations considering the number of schools in the system. It is difficult to assure schools of adequate support and resources when they don't always exist.

The department is working with the DAGS in the development of guidelines for schools to implement the pre-paid bus pass program to include accountability for collections and more uniform procedures.

- 2) **Procedures for reporting delays or service problems, developing projections of needed special education services in light of school year variations, and require more timely submission of special education transportation requests.**

The department will review current procedures for reporting student transportation concerns to the DAGS. The department will also work with school administrators and clerical staff to understand the proper reporting procedures of problems with student transportation services to allow the DAGS to make appropriate improvements in service. However, we do not agree with your assessment that coordination and planning between the DAGS and the department "to be lacking." Your staff did not interview the state specialist in charge of student transportation regarding his observations of the program and relationship with DAGS.

You acknowledge that the department is making improvements in promoting several school complex models and this direction was initiated due to the cooperation and concerns of both the DAGS and the department. As long as there is some allowance for school decision making, which the auditor supports, there will be coordination problems to work out with DAGS related to school schedules and bus transportation schedules and contracts.

The matter of developing projections of special education services is more difficult than you describe. There are many cases in which services are determined to be required during the summer months due to new arrivals of students, new certification of students eligible for services, and the transfer of students from one school site to another. The department will continue to

seek the most efficient means to determine bus transportation services required, train new personnel serving the special education population, and coordinating the voluminous paperwork required.

3) **Controls over eligibility determination for full-subsidy ridership and bus pass processing.**

The department is currently working toward similar qualification criteria for all department programs which require payment of fees. There is a desire to simplify the verification process for full ridership eligibility. However, you do mention that the department has taken steps to improve the procedures for all subsidized programs. Within the limits of staff time and staff allocations, and your acknowledgement that there are differences in eligibility criteria for the school lunch program and the student transportation program, the department will make further attempts to consolidate, where possible, the criteria guidelines and introduce common application forms. Should the school bus eligibility criteria for free bus ridership be aligned with the school lunch program free and reduced lunch price eligibility criteria, higher student transportation costs may be realized as more students are expected to be qualified for free bus ridership.

The department needs to assess your suggestion that information related to the one-mile distance from school can be determined through the School Information System. If the suggestion truly eliminated administrative work for schools in a simple manner without creating additional work for schools to input other information, this recommendation can be pursued.

The department will work with the DAGS and schools to expedite the processing of school bus applications. The department will also strongly consider your recommendation not to require non-paying students to submit an application form. The major concern will be if this process creates another problem of identifying and labeling those students who are not able to pay for the services, thus creating a problem similar to the one which eliminated identification of free school lunch subsidized students by passes.

