

VINCENT CRAPELLI, :
WILLIAM M. MOORE AND :
JOSEPHINE LEE, :
 :
 PETITIONERS, :
 :
 V. : COMMISSIONER OF EDUCATION
 :
 BOARD OF TRUSTEES OF THE : DECISION
 RED BANK CHARTER SCHOOL, :
 MONMOUTH COUNTY,¹ :
 :
 RESPONDENT. :

SYNOPSIS

Petitioners sought to invalidate a settlement that resolved lawsuits filed against the Red Bank Charter School (RBCS) by two creditors to recover monies owed in connection with the construction and renovation of RBCS's school facility, projects undertaken by the Red Bank Charter School Foundation (Foundation). Petitioners contended that the settlement effectively ratified a series of unauthorized actions on the part of former board trustees who acted on behalf of the separate Foundation, and that settlement will result in expenditure of funds in violation of school law. Petitioners filed a motion for emergent relief which was denied by the ALJ, who found no likelihood of success on the merits.

The ALJ found that: the salient facts and applicable law were outlined in his prior order denying emergent relief; the petition lacks merit, as boards of education enjoy wide discretion in the conduct of school affairs and the settlement at issue here falls well within that exercise; the RBCS Board of Trustees entered into the settlement on the advice of counsel that they had only poor defenses against the creditors' claims; the Board's decision to settle was not arbitrary or capricious. The ALJ ordered that the petition be dismissed.

The Assistant Commissioner, to whom this matter has been delegated pursuant to *N.J.S.A. 18A:4-34*, concurred with the ALJ and adopted the Initial Decision of the OAL with supplementation. The Assistant Commissioner found that: the respondent Board acted reasonably in voting to approve the settlement under the totality of the circumstances presented; the Foundation was never truly independent of the RBCS – having been created for the sole purpose of providing RBCS with a school building and financial assistance – and RBSC was subsequently responsible for the liabilities of the Foundation. The petition was dismissed.

This synopsis is not part of the Commissioner's decision. It has been prepared for the convenience of the reader. It has been neither reviewed nor approved by the Commissioner.
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May 15, 2008

¹ The New Jersey Department of Education, Office of Charter Schools was originally a named respondent but has been dismissed by agreement of the parties.

OAL DKT. NO. EDU 8821-07
AGENCY DKT. NO. 336-11/07

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RESPONDENT. :

Petitioners wish to undo a settlement reached between the respondent Board of Trustees of the Red Bank Charter School (RBCS or the Board), and Patock Construction Corp. (Patock), and Short-Term Money LLC (Short-Term), to resolve two lawsuits filed by the aforesaid companies to recover monies owed in connection with the construction and renovation of premises used as RBCS's school facility.³ Both parties requested summary disposition of the matter.⁴

The material facts of this case do not appear to be disputed. The Assistant Commissioner, to whom this matter has been delegated pursuant to *N.J.S.A.* 18A:4-34, has relied, in particular, upon facts presented 1) in an affidavit by Bruce Whitaker, current president of the RBCS Board of Trustees (Whitaker Affidavit), and 2) in various exhibits annexed to the

² The New Jersey Department of Education, Office of Charter Schools was originally a named respondent but has been dismissed by agreement of the parties.

³ An emergent application that had been filed with the petition was denied by way of a November 20, 2007 order of the Office of Administrative Law (OAL), which order was adopted by the Commissioner of Education (the Commissioner) on December 18, 2007.

⁴ No exceptions were filed by the parties.

petition, including the May 6, 2005 report of a compliance investigation conducted by the New Jersey State Department of Education (Exhibit I to the petition).

From these facts it is apparent that in 2000, a foundation was created (the Foundation) for the purpose of financing, purchasing and renovating a facility to be used as the Red Bank Charter School. In 2003, the Foundation received a loan from the New Jersey Economic Development Authority (NJEDA) and purchased property at 58 Oakland Street in Red Bank (58 Oakland). In September 2003, the Foundation entered into a contract in the amount of \$1,853,000 with Patock to perform renovations at 58 Oakland. In so doing, the Foundation did not observe the laws designating procedures to be followed when public entities contract for services. No resolutions approving the property purchase, the NJEDA loan, or the contract with Patock were passed by the respondent board of trustees of RBCS.

In January 2004, the president of the Board of Trustees signed documents on behalf of the RBCS in connection with the transfer to RBCS of the title to 58 Oakland and the liability for the NJEDA loan. The Foundation monitored the renovation project and, during the Spring of 2004, paid Patock over \$1,200,000. However, the Foundation purportedly requested more work – in the amount of \$453,495. The RBCS Board of Trustees did not formally approve this change order.

In May or June of 2004, the RBCS students were moved into the renovated 58 Oakland. At about the same time, the Foundation borrowed \$600,000 from Short-Term and paid same to Patock. A few months later, in August 2004, the Foundation sought to borrow an additional \$200,000 from Short-Term. In exchange, Short-Term asked for a second mortgage on 58 Oakland and an agreement that RBCS would assume the debt if the Foundation defaulted. The president of the RBCS Board of Trustees signed such an agreement, although the Board never formally approved same.

The Foundation was apparently attempting to secure another loan from Commerce Bank in October 2004. Representatives from Patock and Short-Term, whom the Foundation then collectively owed over \$1,300,000, appeared before the respondent Board to urge them to vote to approve the use of 58 Oakland as collateral for such a loan. In December 2004, after hiring special counsel, the Board formally approved the terms of the Commerce Bank loan.

In January 2005, the Office of Compliance Investigation of the New Jersey State Department of Education (OCI) was asked to review RBCS's records. Its findings in March of 2005 included a determination that 1) the Foundation and RBCS were not separate entities,⁵ 2) the Foundation incurred debt disproportionate to the value of the property it purchased and renovated, 3) the Foundation expected RBCS to take responsibility for debt that the trustees did not approve, and 4) the Foundation ignored public bidding laws. The OCI also noted that the former president of the board of trustees took actions independent of the rest of the Board.

A large penalty was imposed upon RBCS for the foregoing improprieties, and later reduced in a settlement with the RBCS. In addition, the OCI directed that RBCS implement procedures to limit debt, ensure that no debt or expenditures be incurred without board approval, and ensure that the Board be advised of all actions taken by the Foundation. The membership of the RBCS Board of Trustees subsequently changed and, by August 2005, all of the Foundation's board members had resigned.

In or about August 2005, Patock filed an action for the balance on its contract (and change order). RBCS's initial motion to be dismissed as a non-party to the contract

⁵ For instance, the Foundation's articles of incorporation and bylaws indicate that the sole 'member' of the Foundation was the RBCS; the RBCS trustees voted for the Foundation trustees; the RBCS trustees were responsible for approving and monitoring the Foundation's operating and capital budgets and approving the Foundation's strategic, business and/or long-term plans; and any amendments to the Foundation's bylaws and articles of incorporation had to be approved by the RBCS trustees.

between Patock and the Foundation was denied. Further, the judge who oversaw the pretrial mediation advised RBCS that its defenses to the litigation were weak. Short-Term filed a similar action against RBCS in April 2006.

After extensive consultation with counsel, the respondent Board voted to settle the two lawsuits by accepting responsibility for the outstanding debt owed to Patock and Short-Term. The Whitaker Affidavit recites that the trustees knew that RBCS's case was weak, and were concerned about the possibility that judgment creditors could possibly compel the sale of 58 Oakland. Whitaker also explained that the trustees were aware of resentment from several of the school's benefactors, who were unhappy with RBCS's handling of the Patock and Short-Term claims. Loss of benefactor support was a serious concern.

Settling the lawsuits clearly saved further costs of litigation and, just as importantly, the plaintiffs agreed to relieve RBCS from paying a prodigious amount of interest on its debts if it managed to pay the principal within a year. Further, approval of the settlement enabled RBCS to initiate discussions with Commerce Bank to refinance the first mortgage on 58 Oakland to absorb the settlement debt and allow for manageable long term payment of same.

The Administrative Law Judge (ALJ) found that petitioners had failed to meet their high burden to show that respondents had abused their discretion in approving the above referenced settlement. First, he pointed out that boards of education – including boards of trustees for charter schools - enjoy wide discretion in the conduct of school affairs. The Assistant Commissioner notes that *N.J.S.A. 18A:11-2* specifically bestows upon such boards the authority to sue and be sued, and the ancillary power to settle litigation.

Further, when an administrative agency acts within its authority, its decision is entitled to a presumption of correctness and will not be upset unless there is an affirmative showing that such decision was arbitrary, capricious or unreasonable. *Thomas v. Morris Bd. of*

Educ., 89 *N.J. Super.* 327 (App. Div. 1965); *Kopera v. West Orange Bd. Of Educ.*, 60 *N.J. Super.* 288 (App. Div. 1960). No such showing may be harvested from the facts of this case. The respondent Board settled claims against which they had only poor defenses, according to their lawyers and a mediating judge. In so doing, they avoided further litigation costs, were forgiven a significant amount of interest payments, kept judgment creditors away and won back former benefactors. Such action was neither arbitrary nor unreasonable.

The petitioners urge, by way of contrast, that RBCS need not take responsibility for the illegal or *ultra vires* acts of the Foundation and the former president of RBCS' Board of Trustees. The ALJ aptly addressed this argument on pages 3-4 of his November 20, 2007 order denying emergent relief:

The Trustees do not deny that prior arrangements with the Foundation were problematic. The Department's Office of Charter Schools has already made this finding, imposed penalties, and directed corrective action

. . . .

Petitioners characterize the Trustees' action as ratification [of prior *ultra vires* acts] and then rely on principles that forbid governmental units from embracing illegal or *ultra vires* conduct, to conclude that the Board may not settle the Patock/Short-Term Money claims. **Yet, the matter does not rest alone on prior errors and misdeeds, but on the totality of circumstances before the trustees now.** . . .

(Emphasis added)

As the OCI found, the Foundation was never truly independent of the RBCS and was, in fact, created for the sole purpose of providing RBCS with a school building and financial assistance. In such situations the corporate veil will be pierced and the 'parent' corporation will be held responsible for the liabilities of the 'subsidiary.' *See, e.g. OTR Associates v. IBC Services, Inc.*, 353 *N.J. Super.* 48 (App. Div. 2002) (the basic finding that must be made to enable the court to pierce the corporate veil is "that the parent so dominated the subsidiary that it

had no separate existence but was merely a conduit for the parent," citing *State, Dep't. of Env'tl. Prot. v. Ventron Corp.*, 94 N.J. 473, 501 (1983)).

Further, RBCS was the beneficiary of the work that was requested of Patock, and the money that was borrowed from Short-Term. Neither law nor equity will countenance a recovery that would result in unjust enrichment. *Empire Box Corp. v. Delaware, L. & W. R. Co.*, 171 F. 2d 389, 390 (2d. Cir. 1948). See, also, *Donnelly v. Capodici*, 227 N.J. Super. 310, 313, (Ch. Div. 1987).

It is within the Commissioner's jurisdiction to find that the Board of the RBCS acted reasonably in voting to approve the settlement of the Patock and Short-Term lawsuits – under the totality of the circumstances set forth above – and the Assistant Commissioner sees no need to revisit the RBCS' former violations of school law, as those violations have been addressed by the Department of Education's OCI.⁶ Accordingly, the Assistant Commissioner adopts the Initial Decision of the OAL and dismisses the petition.

IT IS SO ORDERED.⁷

ASSISTANT COMMISSIONER OF EDUCATION

Date of Decision: May 15, 2008

Date of Mailing: May 16, 2008

⁶ The Commissioner of Education has no jurisdiction to adjudicate alleged criminal offenses; nor may the Commissioner supplant judgments or interfere with proceedings in the Superior Court of New Jersey.

⁷ This decision may be appealed to the State Board of Education pursuant to *N.J.S.A. 18A:6-27 et seq.* and *N.J.A.C. 6A:4-1.1 et seq.*