

Regulatory Analysis Form

(Completed by Promulgating Agency)

INDEPENDENT REGULATORY
REVIEW COMMISSION

(All Comments submitted on this regulation will appear on IRRC's website)

(1) Agency
State Board of Education

2014 JUL - 8 AM 10: 54

(2) Agency Number: 006
Identification Number: 329

IRRC Number: 3064

(3) PA Code Cite: 22 Pa. Code Chapter 18 (Financial Recovery)

(4) Short Title: Financial Recovery

(5) Agency Contacts (List Telephone Number and Email Address):

Primary Contact: Karen Molchanow, Executive Director, State Board of Education, (717) 787-3787, kamolchano@pa.gov

Secondary Contact:

(6) Type of Rulemaking (check applicable box):

Proposed Regulation

Final Regulation

Final Omitted Regulation

Emergency Certification Regulation;

Certification by the Governor

Certification by the Attorney General

(7) Briefly explain the regulation in clear and nontechnical language. (100 words or less)

The proposed regulations identify criteria the Secretary of Education may consider in determining whether to place a school district in financial recovery status and provide guidance to the Secretary on whether a financial recovery school district will be deemed in either moderate or severe recovery status.

(8) State the statutory authority for the regulation. Include specific statutory citation.

The statutory authority for this chapter is Section 621-A(a)(2)(i) of the Public School Code (24 P.S. § 6-621-A(a)(2)(i)).

(9) Is the regulation mandated by any federal or state law or court order, or federal regulation? Are there any relevant state or federal court decisions? If yes, cite the specific law, case or regulation as well as, any deadlines for action.

Act 141 of 2012 added Section 621-A(a)(2)(i) to the Public School Code (24 P.S. § 6-621-A(a)(2)(i)), which directed the State Board of Education to promulgate regulations establishing additional criteria the Secretary of Education may consider in determining whether to issue a declaration that a school district is in financial recovery status and whether a financial recovery school district is deemed in either moderate or severe recovery status.

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(10) State why the regulation is needed. Explain the compelling public interest that justifies the regulation. Describe who will benefit from the regulation. Quantify the benefits as completely as possible and approximate the number of people who will benefit.

As noted in the response to question #9, Chapter 18 (Financial Recovery) was developed in response to Section 621-A(a)(2)(i) of the Public School Code, which directed the State Board of Education to promulgate such regulations.

(11) Are there any provisions that are more stringent than federal standards? If yes, identify the specific provisions and the compelling Pennsylvania interest that demands stronger regulations.

No

(12) How does this regulation compare with those of the other states? How will this affect Pennsylvania's ability to compete with other states?

In developing the proposed regulations, an Advisory Committee convened by the Board reviewed criteria used by the following states to identify school districts exhibiting signs of financial challenges: Michigan, California, Texas, Florida, Arizona and Illinois. The criteria identified by each state serve different purposes and are acted upon in different ways.

California's standards are used to guide the development of school district budgets and monitor districts' fiscal stability through required interim reports. In Texas, the state has established criteria that allow a district's own Board of Trustees to declare that the district is in financial exigency, in addition to other criteria that are used by the state to rate districts' financial management practices and review districts for circumstances that could lead to financial insolvency. Florida requires its state Auditor General to alert a district's local governing body if an audit unveils certain emergency conditions outlined in the sunshine state's statutes, and districts that fail to resolve or prevent the conditions are subject to greater state oversight.

In Arizona, the General Assembly granted the State Board of Education the authority to appoint a financial crisis team or receiver to oversee a school district that the State Board determines is insolvent or has grossly mismanaged its finances based on criteria identified in Arizona statute. Illinois' statute grants the State Board of Education the authority to establish a Financial Oversight Panel for a district the Board deems in financial difficulty based on state-established criteria, in addition to allowing a district itself to request that the State Board establish an oversight panel for the district. Finally, at the time this proposed rulemaking began its initial development phase, Michigan had in place a Local Government and School District Financial Accountability Act that included a broad set of factors that would allow the state to review a school district for indications of probable financial stress and potentially appoint an emergency manager to assume governance authority of the district.

Many of the criteria set forth in these other state policies were duplicative to criteria already identified for consideration by the Secretary in Pennsylvania's Public School Code and included in the Board's proposed rulemaking for completeness, including factors that account for missed employee payroll, missed bond payments, missed payments to other school districts, and various ways of assessing deficit spending.

(13) Will the regulation affect any other regulations of the promulgating agency or other state agencies? If yes, explain and provide specific citations.

Chapter 731 contains a Statement of Policy issued by the Department of Education comprising the Department's Early Warning System. The Early Warning System is designed to identify school districts that are demonstrating early indications of financial challenges and to support them with technical assistance.

Chapter 731 states that the Department may take into advisement the factors considered in issuing a declaration of financial recovery status as part of the analysis conducted under the Department's Early Warning System. However, Chapter 731 does not require that those factors be itemized and, therefore, does not necessitate an amendment to the Chapter to align with these proposed regulations.

(14) Describe the communications with and solicitation of input from the public, any advisory council/group, small businesses and groups representing small businesses in the development and drafting of the regulation. List the specific persons and/or groups who were involved. ("Small business" is defined in Section 3 of the Regulatory Review Act, Act 76 of 2012.)

As required by Section 621-A(a)(2)(ii)(A) of the Public School Code, the State Board of Education consulted with a stakeholders' Advisory Committee in the development of a draft proposed regulation. The Committee included representatives of school administrators, school directors, and school business officials, as well representatives from the Department of Education and the Governor's Office of the Budget. Further, the composition of the Committee was representative of urban, rural and suburban school districts across the Commonwealth. The Advisory Committee worked directly with a subcommittee of the State Board of Education during the drafting phase of regulatory development.

Advisory Committee on Financial Recovery Members

Amy Morton, Executive Deputy Secretary, PA Department of Education

Christine Baldini, Division Manager, Governor's Office of the Budget

Mike Kuhn, School Director, Lebanon School District

Dr. Margaret Billings-Jones, Superintendent, Lakeland School District

Dr. Alan Vandrew, CFO, Mechanicsburg Area School District

Dr. Charles Hughey, Adjunct Professor, Waynesburg University*

**former Superintendent, West Allegheny School District*

Jeanine McCreary, former School Director, Erie City School District

The Advisory Committee convened public meetings on September 6, October 18, November 14, and December 6, 2012. Opportunities for public comment were made available at each meeting. Additionally, updates on the development of the regulations were presented to the State Board at its public meetings on September 13 and November 15, 2012, and opportunity for public comment was made available at those convenings. Finally, the Board engaged in consideration of the proposed regulations at its public meetings on January 10, 2013 and November 14, 2013, and opportunity for public comment was a part of each meeting's agenda.

In recognition of the regulatory flexibility and economic impact provisions of the Regulatory Review Act specific to small businesses, on December 7, 2012, the State Board invited the National Federation of Independent Business (NFIB) to provide feedback on the draft proposed regulation's impact on small businesses. NFIB, which represents more than 15,000 small business owners in the Commonwealth, has expressed no concern with the proposed regulations.

(15) Identify the types and number of persons, businesses, small businesses (as defined in Section 3 of the Regulatory Review Act, Act 76 of 2012) and organizations which will be affected by the regulation. How are they affected?

The proposed regulations will affect the work of the Secretary of Education and staff of the Department

of Education assigned to collect and analyze school district fiscal information and administer the appeal process.

While the proposed rulemaking does not directly regulate school districts, up to nine districts at any time may be indirectly affected by the rulemaking through the Secretary's utilization of the proposed criteria to issue declarations of financial recovery status. A district subject to such a declaration will operate under a new governance structure to develop and implement a financial recovery plan.

(16) List the persons, groups or entities, including small businesses, that will be required to comply with the regulation. Approximate the number that will be required to comply.

The statutory foundation for the regulations, Section 621-A(a)(2)(i) of the Public School Code, provides discretion to the Secretary of Education in issuing declarations of financial recovery status to school districts. The proposed regulations will provide guidance for the Secretary in determining whether to issue such declarations.

While not directly regulated by the proposed rulemaking, up to nine school districts at any time may be required to comply with declarations of financial recovery status that may be issued by the Secretary based on criteria identified in the proposed rulemaking.

(17) Identify the financial, economic and social impact of the regulation on individuals, small businesses, businesses and labor communities and other public and private organizations. Evaluate the benefits expected as a result of the regulation.

The proposed regulations will provide greater transparency to school districts and the public in how determinations of financial recovery status will be executed by the Secretary of Education.

(18) Explain how the benefits of the regulation outweigh any cost and adverse effects.

Implementation costs to state government are required by statute insofar as Section 621-A of the School Code establishes a process by which the Secretary may place up to nine school districts in financial recovery status and directs the State Board to promulgate regulations identifying additional criteria to guide the Secretary in making such determinations.

(19) Provide a specific estimate of the costs and/or savings to the **regulated community** associated with compliance, including any legal, accounting or consulting procedures which may be required. Explain how the dollar estimates were derived.

The Board consulted with the Department of Education to identify the needs of the Secretary in implementing the proposed regulation. The Department will incur costs related to staffing and the development of systems to collect and analyze information relevant to the criteria identified in the proposed regulation, as well as costs related to staffing for legal procedures. Specifically, the Department anticipates the following implementation costs:

- \$399,500 to annually support 1-2 full-time equivalent employees, plus outside counsel, to support legal procedures associated with opinions, declarations, appeals, petitions, contracts and challenges.
- \$72,500 to annually support one full-time equivalent staff to coordinate and consolidate information, communications and procurement.

- \$77,080 to support staffing to conduct preliminary reviews, request and review information, produce summary reports and provide expert advice to the Department.

The Department previously incurred one-time costs of \$75,000 to develop, populate and reconcile models to be used for information pertinent to the Department's Early Warning System. Moving forward, these models also can be applied to criteria identified in the proposed regulation.

(20) Provide a specific estimate of the costs and/or savings to the **local governments** associated with compliance, including any legal, accounting or consulting procedures which may be required. Explain how the dollar estimates were derived.

The proposed regulations carry no anticipated cost for local governments. While a school district may incur a cost to appeal a designation of financial recovery status, the decision to appeal is at the discretion of the individual school district. Therefore, the proposed regulation does not impose a direct cost on districts as it does not mandate that a school district pursue an appeal. Further, the right to appeal does not constitute a newly-established provision by the Board, but merely reflects the right granted to school districts in Section 621-(A)(c) of the School Code and is included in the regulation for completeness.

(21) Provide a specific estimate of the costs and/or savings to the **state government** associated with the implementation of the regulation, including any legal, accounting, or consulting procedures which may be required. Explain how the dollar estimates were derived.

The regulated community in Chapter 18 is state government, specifically the Department of Education. Therefore, the costs to state government are the same as the costs to the regulated community reflected in question # 19.

(22) For each of the groups and entities identified in items (19)-(21) above, submit a statement of legal, accounting or consulting procedures and additional reporting, recordkeeping or other paperwork, including copies of forms or reports, which will be required for implementation of the regulation and an explanation of measures which have been taken to minimize these requirements.

The proposed regulation will cause the Department to undertake legal procedures related to opinions, declarations, appeals, petitions, contracts and challenges in issuing declarations of financial recovery status and administering appeals to such declarations. Additional accounting and consulting work will be required to develop procedures to conduct preliminary information reviews, request and review additional information, and produce summary reports.

The Department also will undertake new reporting and recordkeeping responsibilities related to procedures for issuing declarations of financial recovery status; complying with communication requirements of the School Code; providing expert advice to the Secretary; and coordinating and consolidating information.

(23) In the table below, provide an estimate of the fiscal savings and costs associated with implementation and compliance for the regulated community, local government, and state government for the current year and five subsequent years.

	Current FY Year	FY +1 Year	FY +2 Year	FY +3 Year	FY +4 Year	FY +5 Year
SAVINGS:	\$	\$	\$	\$	\$	\$

Regulated Community	\$0	\$0	\$0	\$0	\$0	\$0
Local Government	\$0	\$0	\$0	\$0	\$0	\$0
State Government	\$0	\$0	\$0	\$0	\$0	\$0
Total Savings	\$0	\$0	\$0	\$0	\$0	\$0
COSTS:						
Regulated Community*	<i>*State Government is the regulated community. Therefore, to avoid duplication, costs estimates are provided only once in the column for State Government below.</i>					
Local Government	\$0	\$0	\$0	\$0	\$0	\$0
State Government	\$549,080	\$549,080	\$549,080	\$549,080	\$549,080	\$549,080
Total Costs	\$549,080	\$549,080	\$549,080	\$549,080	\$549,080	\$549,080
REVENUE LOSSES:						
Regulated Community	NA	NA	NA	NA	NA	NA
Local Government	NA	NA	NA	NA	NA	NA
State Government	NA	NA	NA	NA	NA	NA
Total Revenue Losses	NA	NA	NA	NA	NA	NA

(23a) Provide the past three year expenditure history for programs affected by the regulation.

There are no historic expenditures to report as Chapter 18 constitutes a new regulation with new responsibilities for the Secretary.

Program	FY -3	FY -2	FY -1	Current FY

(24) For any regulation that may have an adverse impact on small businesses (as defined in Section 3 of the Regulatory Review Act, Act 76 of 2012), provide an economic impact statement that includes the following:

- (a) An identification and estimate of the number of small businesses subject to the regulation.
- (b) The projected reporting, recordkeeping and other administrative costs required for compliance with the proposed regulation, including the type of professional skills necessary for preparation of the report or record.
- (c) A statement of probable effect on impacted small businesses.
- (d) A description of any less intrusive or less costly alternative methods of achieving the purpose of the proposed regulation.

The proposed regulations will not have an adverse impact on small businesses.

(25) List any special provisions which have been developed to meet the particular needs of affected

groups or persons including, but not limited to, minorities, the elderly, small businesses, and farmers.

The regulated community for the proposed regulations is the Department of Education. The proposed regulations do not directly regulate specific groups including minorities, the elderly, small businesses or farmers.

(26) Include a description of any alternative regulatory provisions which have been considered and rejected and a statement that the least burdensome acceptable alternative has been selected.

Through its Advisory Committee and subsequent Board discussions, the Board considered additional criteria for inclusion in the regulation. However, through the course of its deliberations, it was determined that certain factors under consideration were duplicative and, therefore, unnecessary.

For example, the Board's Advisory Committee considered recommending that the Secretary consider criteria that account for sudden, unexpected costs experienced by school districts, such as costs associated with a natural disaster. The Advisory Committee determined that such criteria were unnecessary given a provision that already allows the Secretary to not issue a declaration of financial recovery status if circumstances facing a district were caused by an emergency within the past five years.

The Board considered including a factor that looked at whether a district in financial watch status did not show improvement as a result of that designation. However, this was not included in the proposed regulation as it is already part of the Department's decision-making process.

The Board also considered including factors to assess the stability of a district's tax base due to the loss of a major employer as measured by reductions in local real estate and earned income tax revenues. These criteria were not included in the proposed rulemaking as they represent circumstances outside the control of a school district and, in certain circumstances, the state already provides special aid to assist districts who experience a significant loss in local real estate taxes.

Further, the Board considered including a criterion for the Secretary to consider undisputed missed payments of social security or pension obligations. While such missed payments may represent a serious issue, the criterion was not included in the proposed regulation because the circumstances that led to such missed payments likely would be captured by other criteria already included in the regulation.

Additional discussion occurred over whether the regulation should include a concept allowing the Secretary to consider undisputed obligations owed to creditors in determining whether to place a district in Financial Recovery Status. That concept was not included in the proposed regulation due to concerns about the Department potentially being put into a position to serve as a broker for unpaid creditors, and questions as to whether the Department has the authority to determine undisputed payments between school districts and their vendors.

The Board also discussed including a factor that considered whether a district's non-instructional expenditures increased disproportionately to a district's instructional expenditures over a three-year period. The factor was not included in the proposed regulation due to concerns related to local control over budgeting.

Further, the Board discussed including a criterion to allow the Secretary to consider information related to financial challenges or irregularities provided by federal, state or local authorities. However, the criterion was unnecessary because the Department already receives school district audits from the state Auditor General and a system is in place to intervene if malpractice is identified.

Finally, the Board considered including a criterion that would allow the Secretary to consider whether a local school board had been removed from office due to neglect of duty related to its fiscal responsibilities. The Board did not include the criterion in the proposed regulation because the underlying issues that would lead to removal of a local governing board likely would be captured by other criteria already included in the proposed rulemaking.

(27) In conducting a regulatory flexibility analysis, explain whether regulatory methods were considered that will minimize any adverse impact on small businesses (as defined in Section 3 of the Regulatory Review Act, Act 76 of 2012), including:

- a) The establishment of less stringent compliance or reporting requirements for small businesses;
- b) The establishment of less stringent schedules or deadlines for compliance or reporting requirements for small businesses;
- c) The consolidation or simplification of compliance or reporting requirements for small businesses;
- d) The establishment of performing standards for small businesses to replace design or operational standards required in the regulation; and
- e) The exemption of small businesses from all or any part of the requirements contained in the regulation.

The proposed regulations will not have an adverse impact on small businesses.

(28) If data is the basis for this regulation, please provide a description of the data, explain in detail how the data was obtained, and how it meets the acceptability standard for empirical, replicable and testable data that is supported by documentation, statistics, reports, studies or research. Please submit data or supporting materials with the regulatory package. If the material exceeds 50 pages, please provide it in a searchable electronic format or provide a list of citations and internet links that, where possible, can be accessed in a searchable format in lieu of the actual material. If other data was considered but not used, please explain why that data was determined not to be acceptable.

Empirical data did not serve as the basis for the proposed regulations.

(29) Include a schedule for review of the regulation including:

- | | |
|---|--|
| A. The date by which the agency must receive public comments: | July 14, 2014 |
| B. The date or dates on which public meetings or hearings will be held: | July 9-10, 2014
September 10-11, 2014
November 12-13, 2014 |
| C. The expected date of promulgation of the proposed regulation as a final-form regulation: | September 2014 |
| D. The expected effective date of the final-form regulation: | February 2015 |

E. The date by which compliance with the final-form regulation will be required:

February 2015

F. The date by which required permits, licenses or other approvals must be obtained:

___N/A___

(30) Describe the plan developed for evaluating the continuing effectiveness of the regulations after its implementation.

The Board will review Chapter 18 every four years in accordance with the Board's policy and practice respecting all of its regulations.

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FACE SHEET
FOR FILING DOCUMENTS
WITH THE LEGISLATIVE REFERENCE BUREAU
(Pursuant to Commonwealth Documents Law)

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Copy below is hereby approved as to form and legality. Attorney General

Angela Elliott

BY: _____
(DEPUTY ATTORNEY GENERAL)

JUL 03 2014

DATE OF APPROVAL

Check if applicable
Copy not approved. Objections attached.

Copy below is here by certified to be a true and correct copy of a document issued, prescribed or promulgated by:

State Board of Education
(AGENCY)

DOCUMENT/FISCAL NOTE NO. 6-329

DATE OF ADOPTION: November 14, 2013

BY: *Karen McClane*

TITLE Executive Director
(EXECUTIVE OFFICER, CHAIRMAN OR SECRETARY)

Copy below is hereby approved as to form and legality. Executive or Independent Agencies.

[Signature]

MAY 28 2014

DATE OF APPROVAL

Deputy General Counsel
(~~Chief Counsel, Independent Agency~~)
(Strike inapplicable title)

Check if applicable. No Attorney General approval or objection within 30 days after submission.

PROPOSED RULEMAKING

STATE BOARD OF EDUCATION

[22 PA. CODE CH. 18]

Financial Recovery

The State Board of Education (Board) adopts Chapter 18 (Financial Recovery) as a proposed rulemaking to read as set forth in Annex A. The Board is acting under the authority of section 6-621-A(a)(2)(i) of the Public School Code of 1949 (24 P.S. § 621-A(a)(2)(i) (relating to issuance of declaration)).

Purpose

This proposed rulemaking establishes criteria the Secretary of Education may consider in determining whether to place a school district in financial recovery status and provides guidance to the Secretary in determining whether a district would be deemed in either moderate or severe recovery status.

Background

Act 141 of 2012 added section 621-A(a)(2)(i) to the Public School Code, which identifies 15 criteria the Secretary of Education (Secretary) may consider in determining whether to issue a declaration that a school district is in financial recovery status. That same section of the Public School Code directs the Board to promulgate regulations that establish additional criteria the Secretary may consider in determining whether to issue a declaration of financial recovery status and whether a financial recovery school district should be deemed in either moderate or severe recovery status.

In promulgating the regulations mandated by Act 141, the Board was required by section 6-621-A(a)(2)(ii)(A) of the School Code (24 P.S. § 621-A(a)(2)(ii)(A)) to convene and consult with a statewide Advisory Committee comprised of representatives of the Department of Education and the Governor's Office of the Budget, and a superintendent, school board member and school business official representative of urban, rural and suburban school districts. The Advisory Committee convened four times throughout the fall of 2012 to develop a draft proposed regulation for the Board's consideration. All Advisory Committee meetings were open to the public and public comment was invited at each convening.

From its first meeting on September 6, 2012, through the conclusion of its deliberations on December 6, 2012, the Advisory Committee worked in conjunction with the Board's Standing Committee on Financial Recovery. The full Board was kept abreast of the Advisory Committee's work through regular reports of the chairman made during the Board's bi-monthly public meetings.

In the early stages of its deliberations, the Advisory Committee reviewed its statutory charge and received a presentation on Act 141 so that Advisory Committee members had a comprehensive understanding of how their work fit into the broader system of supports for struggling school districts established by the General Assembly in the Act. This included receiving a presentation on the new Early Warning System developed by the Department of Education (Department) to identify districts that show indications of financial challenges and provide them with technical assistance early on in the hopes that their challenges may be addressed before a declaration of financial recovery status would become necessary.

In the next stage of its deliberations, the Advisory Committee reviewed approaches used by other states to identify school districts facing financial challenges and discussed whether criteria used by those states were factors that should be included in the Board's regulation. In total, the Committee reviewed relevant policies in Michigan, California, Texas, Florida, Arizona and Illinois. Finally, the Advisory Committee also reviewed other Pennsylvania laws concerning financially distressed entities to inform itself of the criteria used in other Commonwealth policies to classify distressed local governments.

Upon receiving the Advisory Committee's recommendation on Chapter 18, the Board's Standing Committee on Financial Recovery held a public meeting on January 9, 2013, and adopted amendments to further refine areas where the Standing Committee felt the Advisory Committee's recommendation needed greater clarity. The proposed Chapter 18, as approved by the Standing Committee on Financial Recovery, was then presented for additional comment to both the Board's Council of Basic Education at its public meeting on January 9, 2013, and the full State Board of Education at its public meeting on January 10, 2013. Both the Council and the Board provided an opportunity for public comment prior to approval of the proposed regulation.

Subsequently, the Board withdrew its proposed rulemaking to engage in continued discussion of the criteria identified for the Secretary's consideration. On November 14, 2013, the Board discussed and approved a revised rulemaking that removed criteria that were identified as being duplicative and, therefore, unnecessary. An additional opportunity for public comment was made available prior to the Board's

consideration of the revised proposed rulemaking at its public meeting on November 14, 2013.

Provisions of the Proposed Rulemaking

The regulations establish a new chapter – Chapter 18 – to address the requirements outlined in section 621-A(a)(2)(i) of the School Code. Major components of the regulation include:

Issuance of Declaration

Sections 18.4 and 18.5 address the issuance of a declaration of financial recovery status.

Section 18.4 (relating to issuance of declaration under section 621-A(a)(1) of the School Code). This section reflects statutory criteria that require the Secretary to place a school district in financial recovery status and is included in the proposed regulations for completeness. The section also contains, again for completeness, statutory provisions that allow the Secretary to decline to issue a declaration of financial recovery status to districts that meet the criteria established in section 621-A(a)(1) of the School Code if the circumstances facing a district were caused by an emergency that occurred within the past five years and that prohibit a district from being placed under such a declaration if its financial circumstances were caused by the failure of the Commonwealth to make timely payments of state or federal funds due to the district.

Section 18.5 (relating to issuance of declaration under section 621-A(a)(2) of the School Code). This section establishes criteria the Secretary may consider in determining whether to issue a declaration that a school district is in financial recovery status. Section 621-A(a)(2) of the School Code identifies 15 criteria that the Secretary may consider in

deciding whether to issue a declaration. Those 15 statutory criteria are included in the proposed regulation for completeness and are reflected in § 18.5(a)(1)-(6), (9)-(16) and (18).

The Board is proposing 3 additional criteria for the Secretary's consideration in determining whether to issue a declaration of financial recovery status:

Section 18.5(a)(7) and (8): The Board is proposing to include the criteria proposed in § 18.5(a)(7) and (8) because they are conceptually congruent to the criteria identified in section 621-A(a)(2)(i)(F) of the School Code (*this statutory criteria is reflected in § 18.5(a)(6) of proposed Chapter 18*). Section 18.5(a)(6) directs the Secretary to consider whether a district is subject to withholding of state appropriations because the district met statutory thresholds that allow for withholding due to missed bond payments. The Board is proposing that the Secretary take into consideration whether a district is subject to withholding of state appropriations because the district met other statutory thresholds that allow for withholding either due to missed payments to the State Public School Building Authority or missed SWAP payments.

Section 18.5(a)(17). The Board is proposing this criterion as a means for the Secretary to assess districts facing a deficit situation by directing the Secretary to examine whether a district is experiencing a deficit of 3 percent or more for three consecutive years that results in an annual reduction of the district's unassigned fund balance. The Board recognizes that there are circumstances where deficit spending may be appropriate, including situations where a district is tapping its fund balance to meet pension obligations or to avoid increasing taxes. To address the use of fund balance in such circumstances, the Board has focused the proposed criterion on comparing a district's deficit only to reductions in a district's unassigned fund balance, recognizing that these appropriate uses of fund

balance should have a dedicated purpose and not fall into the category of unassigned expenditures. Further, the Board crafted the criterion to look only at deficits of 3 percent or more that continue for 3 consecutive years to avoid identifying districts that are experiencing short-term circumstances that result in a deficit situation. The proposed regulation also includes a safeguard for districts experiencing circumstances outside of their control from being identified for a declaration of recovery status by including a provision in § 18.5(c) that would allow the Secretary to decline to issue a declaration if a district's challenges were caused by an emergency. This provision could prevent identification of districts that may need to tap unassigned fund balance to address extenuating circumstances.

Section 18.5(b). Section 621-A(b) of the School Code (24 P.S. § 6-621-A(b)) prohibits the Secretary from placing a school district in financial recovery status if the circumstances facing a district were caused by the failure of the Commonwealth to remit timely payments of state or federal funds owed to the district. This statutory limitation is included in the proposed regulations for completeness.

Section 18.5(c). Section 621-A(a)(1)(ii)(B) of the School Code (24 P.S. § 6-621(a)(1)(ii)(B)) grants the Secretary the discretion to decline to issue a declaration of financial recovery status to districts subject to a designation by section 621-A(a)(1) of the School Code if the Secretary determines that the circumstances facing a district were caused by an emergency that occurred within the past 5 years. The Board is proposing to extend this provision to districts potentially subject to a declaration of financial recovery status under § 18.5 to grant the Secretary discretion to decline to issue a declaration of financial recovery status in all situations where the circumstances facing a district were caused by an emergency that occurred within the past 5 years.

Section 18.5(d). The Board is proposing to require the Secretary to identify which criteria were used as the basis for issuing a declaration of financial recovery status when making such a declaration.

Limitations

Section 18.6(a). Section 621-A(a)(1)(ii)(A) of the School Code (24 P.S. § 6-621(a)(1)(ii)(A)) limits the number of school districts that may be in either financial recovery status or receivership at any one time to 9. This statutory limitation is included in the proposed regulations for completeness.

Section 18.6(b). The Board is of the opinion that declarations of financial recovery status should be based on the most current information available to the Secretary. To provide guidance to the Secretary in executing decisions based on the criteria proposed in § 18.5(a), the Board is proposing that the Secretary not use information related to the criteria that is more than 5 years old. The Board is proposing a 5-year period based on a provision in the underlying statute (section 621-A(a)(1) of the School Code) that allows the Secretary to consider a 5-year period in determining whether circumstances facing a district were caused by an emergency.

Moderate and Severe Recovery Status

Section 18.7. This proposed section would provide guidance to the Secretary in determining whether a financial recovery school district will be deemed in either moderate recovery status or severe recovery status. The Board is proposing that such decisions be guided by whether a district is unable, or is reasonably unlikely to be able, to access enough revenue to complete the current school year or to fulfill the required amount of instruction to complete the forthcoming school year. The proposed regulations would guide the Secretary

to issue a declaration of severe recovery status to districts that would not be able to access enough revenue to complete the required instruction.

Appeal

Section 18.8. Section 621-A(c) of the School Code (24 P.S. § 6-621-A(c)) provides for declarations of financial recovery status to be subject to appeal under the Administrative Agency Law (2 Pa.C.S. §§ 501-08, 701-04) and is included in the proposed regulation for completeness.

Affected Parties

The proposed rulemaking would guide the decision-making of the Secretary of Education and affect work of the Department's staff.

Cost and Paperwork Estimates

The proposed rulemaking establishes new responsibilities for the Secretary of Education and staff of the Department of Education to collect and analyze information, as well as to support certain legal procedures. State government incurred one-time costs of \$75,000 in the 2012-13 fiscal year to develop, populate and reconcile models to be used by the Department for information collected relevant to the Department's Early Warning System and criteria identified in the proposed regulation.

Beginning in the current fiscal year, the Department estimates it would incur an annual cost of \$549,080 to support staffing necessary to carry out the requirements of the proposed rulemaking. Specifically, the Department anticipates the following implementation costs: \$399,500 to annually support 1-2 full-time equivalent employees, plus outside counsel, to undertake legal procedures associated with opinions, declarations, appeals, petitions, contracts and challenges; \$72,500 to annually support one

full-time equivalent staff to coordinate and consolidate information, communications and procurement; and \$77,080 to support staffing to conduct preliminary reviews, request and review information, produce summary reports and provide expert advice to the Department.

Effective Date

The proposed rulemaking would become effective upon final publication in the *Pennsylvania Bulletin*.

Sunset Date

The Board will review the effectiveness of Chapter 18 every 4 years in accordance with the Board's policy and practice respecting all of its regulations. Thus, no sunset date is necessary.

Regulatory Review

Under section 5(a) of the Regulatory Review Act (71 P.S. § 745.5(a)), on July 8, 2014, the Board submitted a copy of this proposed rulemaking and a copy of a Regulatory Analysis Form to the Independent Regulatory Review Commission (IRRC) and to the Chairpersons of the House and Senate Committees on Education. A copy of this material is available to the public upon request.

Under section 5(g) of the Regulatory Review Act, IRRC may convey any comments, recommendations or objections to the proposed rulemaking within 30 days of the close of the public comment period. The comments, recommendations or objections must specify the regulatory review criteria that have not been met. The Regulatory Review Act specifies detailed procedures for review, prior to final publication of the

rulemaking, by the Board, the General Assembly and the Governor of comments, recommendations or objections raised.

Public Comments and Contact Person

Interested persons and individuals affiliated with small businesses are invited to submit written comments, questions, suggestions, commendations, concerns, or objections regarding this proposed rulemaking to Karen Molchanow, Executive Director, State Board of Education, 333 Market Street, Harrisburg, PA 17126, ra-stateboardofed@pa.gov. Comments must be submitted to Board within 30 days of publication of this notice of proposed rulemaking in the *Pennsylvania Bulletin*.

Persons with disabilities needing an alternative means of providing public comment may make arrangements by calling Karen Molchanow at (717) 787-3787 or TDD (717) 787-7367.

KAREN MOLCHANOW,
Executive Director

Annex A

TITLE 22. EDUCATION

PART I. STATE BOARD OF EDUCATION

SUBPART A. MISCELLANEOUS PROVISIONS

CHAPTER 18. FINANCIAL RECOVERY

§ 18.1. Statutory authority

The statutory authority for this chapter is section 621-A(a)(2) of the Public School Code of 1949 (24 P.S. § 6-621-A(a)(2) (relating to issuance of declaration; criteria)).

§ 18.2. Purpose

Consistent with the requirements of section 621-A(a)(2) of the School Code (24 P.S. § 6-621-A(a)(2) (relating to criteria)), the purpose of this chapter is to establish criteria that the Secretary may consider in determining whether to issue a declaration that a school district is in financial recovery status, and whether a school district in financial recovery status is in moderate or severe recovery status.

§ 18.3. Definitions

For the purposes of this chapter, the following terms shall have the following meaning, unless the context clearly indicates otherwise:

Average daily membership – The final average daily membership of a school district as most recently determined by the Department in accordance with procedures established by the

Secretary under section 2501(3) of the School Code (24 P.S. § 25-2501(3) (relating to definitions)).

Claim – As defined by section 602-A of the School Code (24 P.S. § 6-602-A (relating to definitions)), a right to (1) payment, whether or not the right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured; or (2) an equitable remedy for breach of performance if the breach gives rise to a right to payment, whether or not the right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured or unsecured.

Deficit – As defined by section 602-A of the School Code (24 P.S. § 6-602-A), the excess of expenditures over revenues, calculated as a percentage of revenue, during an accounting period, and which calculation includes all governmental fund types and all proprietary fund types, but excludes all fiduciary fund types of the school district.

Expenditures – As defined by section 602-A of the School Code (24 P.S. § 6-602-A), reductions in fund equity, including current operating expenses that require the use of fund equity, debt service and capital outlays. The term shall not include interfund transfers.

Financial Recovery School District – As defined by section 602-A of the School Code (24 P.S. § 6-602-A), a school district declared by the Secretary to be in financial recovery status under section 621-A of the School Code (24 P.S. § 6-621-A (relating to issuance of declaration)).

Fixed costs – Expenditures for utility services, insurance-general, communications, energy, and debt service, as defined in the *Manual of Accounting and Related Financial Procedures for Pennsylvania School Systems*.

Proposed Regulation #6-327 – As approved by the State Board of Education on November 14, 2013

Fund equity – As defined by section 602-A of the School Code (24 P.S. § 6-602-A), excess of assets of a fund over its liabilities. The term shall include a fund balance.

Revenues – As defined by section 602-A of the School Code (24 P.S. § 6-602-A (relating to definitions)), additions to fund equity other than from interfund transfers, proceeds of debt and proceeds of disposition of general fixed assets.

School Code – The Public School Code of 1949 (24 P.S. § 1-101—27-2702).

School district – As defined by section 602-A of the Public School Code (24 P.S. § 6-602-A), a school district of the first class A, second class, third class and fourth class and a Financial Recovery School District. The term does not include a school district of the first class.

Total annual expenditures – Reductions in fund equity (including current operating expenses that require the use of fund equity), debt service and capital outlays (including all governmental fund types and all proprietary fund types), but excluding all fiduciary fund types of the school district. The term shall not include interfund transfers.

Unassigned fund balance – Amounts available for any purpose within the general fund only, as defined in the *Manual of Accounting and Related Financial Procedures for Pennsylvania School Systems*.

§ 18.4. Issuance of declaration under section 621-A(a)(1) of the School Code

(a) As provided by section 621-A(a)(1) of the School Code (24 P.S. § 6-621-A(a)(1) (relating to criteria)), the Secretary shall issue a declaration that a school district is in financial recovery status when either of the following applies:

Proposed Regulation #6-327 – As approved by the State Board of Education on November 14, 2013

(1) The school district has an average daily membership greater than 7,500 and receives an advance of its basic education subsidy at any time.

(2) The school district receives an advance of its basic education subsidy at any time and either of the following applies:

(i) The school district is subject to a declaration of financial distress under section 691 of the School Code (24 P.S. § 6-691 (relating to when district distressed)).

(ii) The school district is engaged in litigation against the Commonwealth in which the school district seeks financial assistance from the Commonwealth to allow the school district to continue in operation.

(b) As provided by section 621-A(a)(1)(ii)(B) of the School Code (24 P.S. § 6-621-A(a)(1)(ii)(B)), the Secretary may decline to issue a declaration that a school district is in financial recovery status where the Secretary determines that the school district, within the previous five years, has faced an emergency that caused the occurrence of a circumstance set forth in subsection (a).

(c) As provided by section 621-A(b) of the School Code (24 P.S. § 6-621-A(b) (relating to failure of Commonwealth to make payment)), no school district shall be declared in financial recovery status if the circumstances enumerated in subsection (a) have been caused by the failure of the Commonwealth to make any payment of money due to the school district at the time the payment is due, including payment of any Federal funding that is distributed through the Commonwealth.

§ 18.5. Issuance of declaration under section 621-A(a)(2) of the School Code

(a) Consistent with section 621-A(a)(2)(i) of the School Code (24 P.S. § 6-621-A(a)(2)(i) (relating to criteria)), the Secretary may consider the following criteria when determining whether to issue a declaration that a school district is in financial recovery status:

(1) The school district receives at least 85 percent of its per pupil funding from the Commonwealth and collects less than 50 percent of local taxes levied to fund the school district.

(2) The school district's unreserved fund balance has declined for 3 consecutive years and is less than 5 percent of the school district's annual expenditures. As used in this paragraph, a school district's unreserved fund balance shall mean the school district's unassigned fund balance.

(3) The school district's fixed costs are at least 30 percent of the school district's total annual expenditures.

(4) The school district's total outstanding debt is greater than the school district's total annual expenditures.

(5) The salaries of any teachers or other employees of the school district are unpaid at least 15 days after payment is due.

(6) The school district is subject to withholding of its State appropriation under section 633 of the School Code (24 P.S. § 6-633 (relating to reports to the Secretary of Education; withholding state appropriations)).

(7) The school district is subject to withholding of its State appropriation under section 785 of the School Code (24 P.S. § 7-785 (relating to failure to pay rent or make payments; withholding appropriation)).

(8) The school district is subject to withholding of its State appropriation under section 8283(c) of the General Local Government Code (53 Pa.C.S. § 8283(c) (relating to failure to pay by school districts)).

(9) The school district has defaulted on the payment of a debt due to any school district, intermediate unit or charter school that remains unpaid on or after January 1 of the year following the school year it was due and there is no dispute regarding the validity or amount of the claim.

(10) The school district's assigned and unassigned total fund balance is less than zero in the school district's general fund.

(11) The school district's assigned and unassigned total fund balance in the school district's general fund as a percentage of total expenditures is less than 3 percent.

(12) The school district experiences a delinquent tax rate of more than 10 percent.

(13) The assessed valuation of taxable real estate in the school district, as certified by the State Tax Equalization Board, has not increased over the previous 5 years.

(14) Any amount due a joint board of school directors under a joint board agreement remains unpaid beyond the due date specific in the joint board's articles of agreement.

(15) The school district has contracted a loan not authorized by law.

(16) The school district has accumulated and operated with a deficit equal to at least 2 percent of the assessed valuation of the taxable real estate within the school district for 2 successive school years.

(17) The school district experiences a deficit of 3 percent or more for 3 consecutive school years, resulting in a reduction of unassigned fund balance each year.

(18) A new, merged or union school district has been formed and one or more of the former school districts which compose the merger or union school district was a distressed school district under section 691 of the School Code (24 P.S. § 6-691 (relating to when district distressed)) or a financial recovery school district under Article VI-A of the School Code (24 P.S. §§ 6-601-A—6-693-A (relating to school district financial recovery)) at the time of the formation of the new, merged or union school district.

(b) As provided by section 621-A(b) of the School Code (24 P.S. § 6-621-A(b) (relating to failure of Commonwealth to make payment)), no school district shall be declared in financial recovery status if the circumstances enumerated in subsection (a) have been caused by the failure of the Commonwealth to make any payment of money due to the school district at the time the payment is due, including payment of any Federal funding that is distributed through the Commonwealth.

(c) The Secretary may decline to issue a declaration that a school district is in financial recovery status where the Secretary determines that the school district, within the previous five years, has faced an emergency that caused the occurrence of a circumstance set forth in subsection (a).

(d) When the Secretary issues a declaration that a school district is in financial recovery status, the Secretary shall specify the criteria set forth under this section that placed the school district in financial recovery status.

§ 18.6. Limitation

(a) As provided by section 621-A(a)(1)(ii)(A) of the School Code (24 P.S. § 6-621-A(a)(1)(ii)(A) (relating to criteria)), no more than 9 school districts may be under a declaration of financial recovery status or in receivership at any time.

(b) The Secretary may not use information that is more than 5 years old when considering criteria under § 18.5 (relating to issuance of declaration under section 621-A(a)(2) of the School Code).

§ 18.7. Moderate and severe recovery status

(a) *Moderate recovery status* – The Secretary shall issue a declaration that a Financial Recovery School District is in moderate recovery status if the Financial Recovery School District is not declared by the Secretary in severe recovery status.

(b) *Severe recovery status* – The Secretary shall issue a declaration that a Financial Recovery School District is in severe recovery status if the financial conditions of the school district indicate that the school district is unable, or is reasonably unlikely to be able, to fulfill the 180 days of instruction for pupils requirement provided by section 1501 of the School Code (24 P.S. § 15-1501 (relating to minimum number of days; school month)) for the present school year or for the following school year due to the lack of existing revenue sources and additional revenue sources as are provided by and allowed under law, including the Taxpayer Relief Act (53 P.S. §§ 6926.101-6926.5006).

§ 18.8. Appeal

As provided by section 621-A(c) of the School Code (24 P.S. § 6-621-A(c) (relating to appeal), a school district may appeal the Secretary's declaration of financial recovery status under the Administrative Agency Law (2 Pa.C.S. (relating to administrative law and procedure)).

DRAFT



COMMONWEALTH OF PENNSYLVANIA
STATE BOARD OF EDUCATION

July 8, 2014

Mr. David Sumner
Executive Director
Independent Regulatory Review Commission
14th Floor, 333 Market Street
Harrisburg, PA 17101

Dear Mr. Sumner:

Enclosed is a copy of a proposed regulation approved by the State Board of Education (22 Pa. Code, Chapter 18 – Financial Recovery, #006-329) for review by the Commission pursuant to the Regulatory Review Act. The regulation also is being delivered today to the House and Senate Standing Committees on Education and the Legislative Reference Bureau.

The State Board of Education will provide the Commission with any assistance it requires to facilitate a thorough review of these proposed regulations.

Thank you for your consideration.

Sincerely,

A handwritten signature in blue ink that reads "Karen Molchanow".

Karen Molchanow
Executive Director

cc: Acting Secretary Carolyn Dumaesq
Gregory Dunlap, Esq.
Aaron Shenck

**TRANSMITTAL SHEET FOR REGULATIONS SUBJECT TO THE
REGULATORY REVIEW ACT**

I.D. NUMBER: 6-329
 SUBJECT: Chapter 18 (Financial Recovery)
 AGENCY: State Board of Education

TYPE OF REGULATION

- Proposed Regulation
- Final Regulation
- Final Regulation with Notice of Proposed Rulemaking Omitted
- 120-day Emergency Certification of the Attorney General
- 120-day Emergency Certification of the Governor
- Delivery of Tolled Regulation
 - With Revisions Without Revisions

2014 JUL -8 AM 10: 54

RECEIVED
IRRC

FILING OF REGULATION

<u>DATE</u>	<u>SIGNATURE</u>	<u>DESIGNATION</u>
		<u>HOUSE COMMITTEE - Education</u>
<u>7/8/14</u>	<u>Eileen Kuch</u>	MAJORITY CHAIR <u>Clymer</u>
<u>7/8/14</u>	<u>April Edwards</u>	MINORITY CHAIR <u>Roebuck</u>
		<u>SENATE COMMITTEE - Education</u>
<u>7/8/14</u>	<u>Janet King</u>	MAJORITY CHAIR <u>Folmer</u>
<u>7/8/14</u>	<u>Risa Spolli</u>	MINORITY CHAIR <u>Dinniman</u>
<u>7/8/14</u>	<u>Steph F. Hoff</u>	<u>INDEPENDENT REGULATORY REVIEW COMMISSION</u>
		<u>ATTORNEY GENERAL (for Final Omitted only)</u>
<u>7/8/14</u>	<u>Courne Mant</u>	<u>LEGISLATIVE REFERENCE BUREAU (for Proposed only)</u>