

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

(2) Agency Number: 006
Identification Number: 329

IRRC Number:

(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.

(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.

