



TO: Nathan Mains, Executive Director

FROM: Stuart Knade, General Counsel

SUBJECT: Budget Impasse Cash Flow Issues

Date: August 21, 2015 (with footnote added August 27, 2015)

As you requested, I have examined the legality of two measures that it has been reported have been taken or are under considerations by our member school districts to deal with the growing cash flow challenges caused by the Commonwealth's long delay in adopting a budget. They are: (1) delaying payment of employer contributions to PSERS; and (2) delaying payment of the portion of charter school tuition otherwise owed that represents the proportion of total budgeted revenue received from the Commonwealth. As explained in more detail below, it is my opinion that both can be done consistent with statutory obligations, in recognition of a school district's overriding duty to try to meet the educational needs of school children in the short term notwithstanding the lack of a Commonwealth budget. However, when sharing my conclusions with our members is it important to stress that school districts considering these options should seek and follow the advice of their respective solicitors on these matters, as some local counsel may not completely agree with all aspects of my analysis.

Initially, it must be observed that once the Commonwealth has failed to adopt a budget by the deadline established by law, and consequently is not distributing the state and federal education funding upon which large portions of local school entity budgets are premised, we have moved into uncharted territory beyond the contemplation of most of the laws governing public school operations. In a situation our laws simply were not written to address, and in which timely compliance with all of those laws can become impossible as a practical matter, local public school systems are forced to fulfill their duties as best they can with the limited resources available and to prioritize in a way that best comports with legal obligations. In short, when the Commonwealth stops paying its bills, it is inevitable that school districts might have to put off paying some of theirs.

Employer Share of PSERS Contributions

Fortunately, the provisions of the Public School Employees Retirement Code contain a provision specifically intended for this kind of situation. Prior to June 30, 1995, the Commonwealth paid one-half of the total employer contribution determined to be necessary, directly into the retirement system fund. 24 Pa.C.S. §8327. Starting in July 1995, an amendment to Section 8327 meant that most school employers now are required to pay the entire amount directly into the fund, and then under a different section of the Code added at the same time (Section 8535), they are reimbursed by the Commonwealth for 50% or more of that amount (depending on aid ratio) as a part of their overall allocation of state subsidy. 24 P.S. §8535.

Section 8327 also establishes a subsidy payment intercept process, so that if quarterly payments of employer contributions are not made on time, they are deducted from subsidy payments otherwise due to the local school employer and paid directly into the fund. 24 Pa.C.S. §8327(b). However, pursuant to paragraph 3 of Section 8535, local school employers are not expected to pay the employer contribution into the system until five days after they receive the pertinent reimbursement from the Commonwealth. Section 8535 states as follows:

(3) School entities shall have up to five days after receipt of the Commonwealth's portion of the employer's liability to make payment to the Public School Employees' Retirement Fund. School entities are expected to make the full payment to the Public School Employees' Retirement Fund in accordance with section 8327 (relating to payments by employers) in the event the receipt of the Commonwealth's portion of the employer's liability is delayed because of delinquent salary reporting or other conduct by the school entities.

24 Pa.C.S. §8535(3).

Accordingly, local school employers have express statutory authority to delay payment of the *entire*¹ employer share of PSERS contributions for as long as the payment of the corresponding reimbursements for that obligation are delayed due to the budget impasse, plus five days. So long as payment is made within that five day period, there should be no need for the subsidy intercept to occur. However, this authority to delay payment does not apply to local employers' obligation to continue to make timely

¹ (Footnote added August 27, 2015): PSERS takes the position that this only applies to the portion of the employer contribution that is reimbursed by the Commonwealth, while recognizing that the wording of §8535(3) can be interpreted differently. In prior budget impasse situations PSERS has instructed employers to make partial payment of the employer share, and school employers should expect that similar instructions will be given this time. This underscores the importance of consultation with the solicitor.

deposit into the fund of employee payroll deductions for employees' contributions (no later than ten days after the close of the month in which deducted from pay). School employers do *not* have legal authority to delay remitting such payroll deductions.

Delay in Payment of a Portion of Charter School Tuition Payments

Media sources have reported that the board of the Bethlehem Area School District has decided that until the Commonwealth resolves its budget impasse and begins making subsidy payments, the district will withhold a portion of the amounts otherwise due to charter schools on account of resident students attending those schools. The portion the district intends to withhold is based on the portion of overall school district budgeted revenue that is derived from estimates of state and federal subsidies or reimbursements. Stated in the converse, the district intends for now to pay currently only the percentage of tuition payments that reflect the proportion of total revenues derived from local sources, and delay payment of the remainder.

The Charter School Law does not have provisions specifically addressing delays in the Commonwealth's payments of subsidy allocations or reimbursements. Nonetheless, it is my opinion that the partial payment delay in charter school tuition planned by the Bethlehem Area School District is a fair and reasonable (if not necessary) stop-gap cash flow management measure that is not inconsistent with the requirements of the Charter School Law (24 P.S. §17-1701-A et seq.).

The Charter School Law, at 24 P.S. §17-1725-A, requires school districts to pay each charter school an amount for each district resident enrolled in that charter school calculated based on the district's total budgeted expenditure, from which is subtracted the budgeted amounts for several specified expenditure categories including transportation and special education, with the resulting total divided by the district's average daily membership of enrolled students to arrive at a per pupil amount to be paid to the charter school on account of each non-special education student. For each special education student attending the charter schools, the tuition to be paid includes that plus an additional amount based on the district's budgeted special education expenditures divided by 16% of the district's average daily membership. 24 P.S. §17-1725-A(a). These amounts are calculated for each district using a form known as "PDE 363". That same section of the Charter School Law also establishes a subsidy intercept procedure if a district fails to pay charter school tuition as required.

This mechanism cannot work as intended in a situation where the amounts of state and federal subsidy allocations are not certain because the Commonwealth has not yet adopted a budget and appropriated those allocations. Funding provisions of the Charter School Law and other statutes governing the finances and budget processes for public

schools are premised on the assumption that prior to adoption of a final school district budget, or at least prior to completion of PDE 363 and payment of tuition to charter schools, the actual amounts of each district's state and federal allocations will be known, and not merely estimated.

Until those amounts are known based on actual appropriations, the portion of budgeted expenditures dependant on those remains purely notional and subject to change.² When those amounts become known, a school district may need to reopen its budget to increase or decrease the amounts of its revenues and expenditures pursuant to Section 616.1 of the School Code, 24 P.S. 6-616.1. It is unlawful for a school district's budgeted expenditures to exceed available funds. 24 P.S. 6-687(b).

It is my opinion that until the amount of state and federal subsidy allocations for each school district is known for certain and authorized for payment, it is entirely consistent with the intended operation of the Charter School Law and other statutory provisions governing public school finances and budgets that the amounts of any budgeted expenditures dependent on those revenues be regarded as purely hypothetical and properly excluded from the calculation of amounts paid to charter schools until resolution of the Commonwealth's budget impasse. Those amounts are not yet "real money". One cannot imagine that the General Assembly could have intended the Charter School Law to operate in a manner that would exempt charter schools from bearing a share of the same fiscal impacts the current budget impasse is causing for the students of traditional public schools, or force school districts to hand over hypothetical subsidies they are not actually receiving.

Accordingly, paying only that percentage of charter school tuition equaling the percentage of total estimated revenues derived from purely local sources, and delaying payment of the remainder until the budget impasse is resolved is a fair, reasonable and lawful stop-gap cash flow management measure in this time of abnormal fiscal constraints. Charter schools payments would be merely delayed, and when paid will be in amounts that accurately reflect what is allocated in the Commonwealth's budget. Charter school advocates are fond of defending the current charter school funding mechanism with the dubious catch-phrase, "the money follows the child". Dubious or not, if the money hasn't arrived, it most certainly cannot follow.

² It is noteworthy that as of the date this memo was written, the PDE web page where official school district PDE 363 tuition amounts normally are posted does not yet include the list for the current fiscal year. See, http://www.portal.state.pa.us/portal/server.pt/community/charter_school_funding/8661.