

# HOUSE BILL REPORT

## SHB 1431

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### As Passed Legislature

**Title:** An act relating to addressing financial insolvency of school districts.

**Brief Description:** Addressing financial insolvency of school districts.

**Sponsors:** House Committee on Education (originally sponsored by Representatives Anderson and Haigh).

#### **Brief History:**

##### **Committee Activity:**

Education: 2/1/11, 2/3/11, 2/17/11 [DPS];

Education Appropriations & Oversight: 2/18/11, 2/21/11 [DPS(ED)].

##### **Floor Activity:**

Passed House: 3/4/11, 97-0.

Senate Amended.

Passed Senate: 4/8/11, 49-0.

House Concurred.

Passed House: 4/13/11, 96-0.

Passed Legislature.

#### **Brief Summary of Substitute Bill**

- Requires the Superintendent of Public Instruction to convene the Educational Service Districts to analyze options and make recommendations for a clear legal framework and process for dissolution of a school district for financial reasons.
- Provides that the act is null and void if funding is not specified in the budget.

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### HOUSE COMMITTEE ON EDUCATION

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 21 members: Representatives Santos, Chair; Lytton, Vice Chair; Dammeier, Ranking Minority Member; Anderson, Assistant Ranking Minority Member; Ahern, Angel, Billig, Dahlquist, Fagan, Finn, Haigh, Hargrove, Hunt, Klippert, Kretz, Ladenburg, Lias, Maxwell, McCoy, Probst and Wilcox.

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

**Staff:** Cece Clynch (786-7195).

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## HOUSE COMMITTEE ON EDUCATION APPROPRIATIONS & OVERSIGHT

**Majority Report:** The substitute bill by Committee on Education be substituted therefor and the substitute bill do pass. Signed by 18 members: Representatives Haigh, Chair; Probst, Vice Chair; Anderson, Ranking Minority Member; Dammeier, Assistant Ranking Minority Member; Dahlquist, Frockt, Hargrove, Hope, Maxwell, Nealey, Orwall, Reykdal, Rolfes, Santos, Seaquist, Sells, Short and Stanford.

**Staff:** Ben Rarick (786-7349).

### **Background:**

After experiencing severe financial problems, Vader School District No. 18 (Vader) was dissolved and annexed to Castle Rock School District No. 401 in 2007. Prior to that event, it had been almost 25 years since the last school consolidation in Washington took place.

In November of 2009, Jon Molohon, Educational Service District (ESD) 113 Assistant Superintendent for Fiscal Services, ESD Fiscal Officer, and the Administrator of Vader Binding Conditions, published a report about the process, *The Vader School District Closing In Retrospect*. Primarily, the report identifies and makes recommendations to address the lack of a clear legal framework and process for dissolving a school district for financial reasons, including the lack of clear legal authority for the Office of the Superintendent of Public Instruction (OSPI) or an ESD Regional Committee to determine and manage the myriad financial and practical issues that such an event presents.

### Current Washington Law: School District Dissolution.

Current laws emphasize voluntary and negotiated reorganization of school districts:

- Boundary changes and consolidations can be initiated by agreement between the school boards of the affected districts, or by a petition from one board or a group of citizens.
- If a petitioned district does not agree with the proposed change, a Regional Committee appointed by the ESD has decision-making authority.
- Consolidations and transfers of territory that affect 10 percent or more of the student population require voter approval.
- Regional Committee decisions can be appealed.

After a reorganization, the Regional Committee is charged with the reallocation of assets and liabilities, including levies and bonded indebtedness. A new district can result from a consolidation or reorganization of all, or parts of two or more, current districts, but not a division of a single current district into separate ones.

There are only two references to "dissolution" of a district in statute:

1. School district boundaries may be altered by the dissolution and annexation to an existing district of a part or all of another district.
2. A Regional Committee is required to dissolve any school district that, in the prior year:

- has an annual enrollment of fewer than five K-8 students; or
- has not made a reasonable effort to provide the minimum 180-day school year.

No statutes provide for dissolution of a school district in any other fashion or for any other reason. The dissolution of Vader occurred under the second of the two laws referenced above, but only because the district agreed not to make up some days missed in the prior year due to an emergency closure in order to fall under the provisions of this statute.

Current Washington Law and Practice: School District Financial Problems.

School districts must annually submit a budget to the OSPI when expected expenditures for the upcoming school year do not exceed expected revenues from all sources. If a school district cannot submit a balanced budget, it can petition the OSPI to be allowed to include revenues from a future school year (in other words, borrow against future state apportionment payments) only if the district agrees to certain binding conditions that are intended to improve the district's financial condition.

There are nine ESDs in the state. The ESD Financial Officer for the ESD in which the school district is located is assigned to be the administrator of the binding conditions. This role has limited authority and primarily serves as a consultant to the school district for how to improve their financial situation. The presence of a third party, even if somewhat symbolic, acts as a motivating factor for districts and their boards. According to a Joint Legislative Audit and Review Committee analysis, there have been 12 districts in binding conditions at some point over the last 10 years. Most resolve their finances in one to two years. All but two of these districts have had fewer than 2,000 students.

Report Recommendations.

The recommendations made in the Vader report can be summarized as follows:

1. authorize the OSPI or a school district to initiate the dissolution of a district due to financial insolvency and authorize the Regional Committee to make the determination and oversee the dissolution;
2. address various financial and legal issues associated with dissolution, including determining what is the appropriate length of time to permit a district to solve its own problems without outside intervention; and
3. make technical amendments to other laws dealing with district reorganization, including, but not limited, to dissolution of a district.

**Summary of Substitute Bill:**

The Superintendent of Public Instruction (Superintendent) is tasked with convening the ESDs for the purpose of analyzing options and making recommendations for a clear legal framework and process for dissolution of a school district on the basis of financial insolvency. The analysis must include:

- a definition of financial insolvency;
- a timeframe, criteria, and process for initiating dissolution of a district;
- roles and responsibilities of various entities, including the OSPI, the ESDs, and regional committees on school district organization; and
- recommendations with respect to various issues such as terminating staff contracts, liquidation of liabilities, and dealing with bonded indebtedness.

In conducting the analysis, the ESDs must consult with individuals with legal and financial expertise. The ESDs may recommend a financial early warning system for consistent, early identification of school districts with potential fiscal difficulties. The recommendations must address amendments to current law as well as propose new laws as necessary.

The Superintendent must submit a final report and recommendations to the Governor and the fiscal committees of the Legislature by January 5, 2012.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect 90 days after adjournment of the session in which the bill is passed. However, the bill is null and void unless funded in the budget.

**Staff Summary of Public Testimony (Education):**

(In support) This issue arose after the Vader School District failed. It was extremely challenging. The report describes the challenges that were faced as well as how the problems were ultimately resolved in that case. Included in the report was a recommendation that the laws need to be amended to address the situation of a district that is failing financially. There is a need for a thorough analysis and recommendations about how to amend the law to make it workable and capable of addressing financial insolvency. A safety net is needed. Because there are so many moving parts, the SBE has been put in charge.

(In support with concerns) There is a need for a process to be put in place. At the same time, there is concern that the SBE is not the appropriate entity and that the timeline is too short.

(With concerns) While the SBE is open to assisting, the SBE does have limited staff and resources. Additionally, the timeline is too short.

(Opposed) None.

**Staff Summary of Public Testimony (Education Appropriations & Oversight):**

(In support) What happened with the Vader School District and the subsequent report that documented the process by which the district was closed is the subject of this bill. Currently, there is a legal muddle with respect to school districts facing financial problems. This situation needs to be addressed. It is an extremely emotional situation when a school district must close. Some school districts are being put on the verge of financial crises due to the current economic situation. Most schools that do face the specter of closing have arrived at that juncture due to the fact that they have aged buildings, for which the upkeep is too expensive or impossible. They may have no place else to house students, and they cannot pass the necessary bonds to build facilities. Providing money for the work that must be done under this bill is the right thing to do.

(Opposed) None.

**Persons Testifying** (Education): (In support) Representative Anderson, prime sponsor.

(In support with concerns) Dan Steele, Washington Association of School Administrators.

(With concerns) Brad Burnham, Washington State Board of Education; and Marie Sullivan, Washington State School Directors Association.

**Persons Testifying** (Education Appropriations & Oversight): Representative Anderson, prime sponsor; Representative Haigh; and Dan Steele, Washington Association of School Administrators.

**Persons Signed In To Testify But Not Testifying** (Education): None.

**Persons Signed In To Testify But Not Testifying** (Education Appropriations & Oversight): None.