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# Before School Districts Go Broke: A Proposal for Federal Reform

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# BEFORE SCHOOL DISTRICTS GO BROKE: A PROPOSAL FOR FEDERAL REFORM

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ABSTRACT

School districts across the country continue to face falling revenues and are scrambling to cut their budgets and adjust to leaner times. But districts have never had to make such drastic adjustments—and some of them are nearing a point of fiscal crisis. In fact, in summer 2011, we will see school districts hit what education law and policy experts call the "funding cliff": revenue from state and local sources will not have rebounded, and the federal stimulus funding approved in August 2010 will nearly have run out. A nation-wide solution is needed, and this Article proposes just that. First, the Article defines the problem, looking beyond the recession to examine the systemic and situational challenges in school finance that the recession has illuminated. Second, the Article searches federal and state statutes and regulations for legal mechanisms that are sufficient to deal with school districts' current and future fiscal crises and finds a substantial gap: in 19 states, *not one* legal mechanism is available to school districts in fiscal crisis (including federal municipal bankruptcy), and in the remaining 31 states, there is considerable variation in the utility of the authorized legal mechanisms. Third, the Article proposes that when Congress reauthorizes No Child Left Behind, which it is expected to do in 2011, it should include fiscal accountability provisions that require states to (1) help districts create immediate, additional cost savings, (2) publicly monitor districts' fiscal health and create a

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plan for escalating involvement when a district nears and reaches fiscal crisis, and (3) assist in stabilizing districts' revenues long-term.

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## INTRODUCTION

During 2009, more than 11,000 corporations filed for bankruptcy in the United States[2] and more than 1.41 million individuals did so.[3] Media reports on these topics abound. But, we have heard little about municipalities reaching a similar point of fiscal crisis—and until recently, we have heard little about school districts' fiscal crises in particular. In part, this is because municipal bankruptcy proceedings are very rare, and in fact only permitted in about half the states;[4] even from 2006 through mid-2010, during the recent recession, only 27 municipalities filed for bankruptcy[5] and no school districts did so. Yet, fiscal crises for local governments,

[2] 11,000 is the approximate total number of Chapter 11 filings. Nicole Bullock, *US Cities Forced to Consider Bankruptcy*, Financial Times, Apr. 29, 2010.
[3] Sara Murray & Conor Dougherty, *Personal Bankruptcy Filings Rising Fast*, Wall St. J., Jan. 7, 2010.
[4] Michael W. McConnell & Randal C. Picker, *When Cities Go Broke: A Conceptual Introduction to Municipal Bankruptcy*, 60 U. Chi. L. Rev. 425, 425 (1993); James E. Spiotto, *Introduction to Municipal Bankruptcy*, 378 PLI/Real 611, 613 (1992); Frederick Tung, *After Orange County: Reforming California Municipal Bankruptcy Law*, 53 Hastings L.J. 885, 886 (2002). Less than an estimated 600 municipal bankruptcy petitions have been filed since 1937. Stephen Henderson, editorial page editor for the *Detroit Free Press*, estimates that 10,000 corporate bankruptcy filings in a year are not unusual. Stephen Henderson, *Is Bankruptcy the Road to DPS's Comeback?*, Detroit Free Press, July 12, 2009; Nicholas B. Malito, *Municipal Bankruptcy: An Overview of Chapter 9 and a Critique of the "Specifically Authorized" and "Insolvent" Eligibility Requirements of 11 U.S.C.A. 109(c)*, 17 J. Bankr. L. & Pract. 4 Art 2, text accomp. note 2 (2008); Omer Kimhi, *Chapter 9 of the Bankruptcy Code: A Solution in Search of a Problem*, 27 Yale J. on Regulation 351, 360 (2010).
[5] David Porter, *Facing $20M Judgment, Pa. Town Seeks Bankruptcy*, ABC News, June 15, 2009, *available at* http://abcnews.go.com/; James Spiotto, *Municipal Bankruptcy Remains "Last Resort" Despite Troubled Economy*, June 8, 2010.

including school districts, are far from over.[6] The executive director of the American Bankruptcy Institute has speculated that a wave of municipal insolvency may be just around the corner.[7]

In December 2008, a *Wall Street Journal* article noted that "many school districts [were] facing the biggest cutbacks they've seen in decades."[8] A few months later, the 2009 American Recovery and Reinvestment Act infused nearly $49 billion into elementary and secondary education.[9] Even with that influx of stimulus money school districts laid off teachers, administrators, and staff; closed schools; and tried to cut costs wherever they could—sometimes even by draining swimming pools and thus eliminating the expense of chlorine, or asking parents to purchase boxes of tissue, copy paper, and garbage bags.[10] Congress intended the stimulus money to stretch over two years, but most states used the vast majority of those funds during Fiscal Year (FY) 2010.[11] As the beginning of FY 2011 neared, the National Association of School Boards anticipated that states' budget shortfalls for education "could be as much as $38

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[6] State revenues may not recover from recession for "several more years" Lesli A. Maxwell, *School Funding on Block Again As States' Fiscal Pain Continues*, Educ. Week, Mar. 3, 2010, at 3; Nicholas McGrath & Ji Hun Kim, *The Next Chapter for Municipal Bankruptcy*, Am.. Bankr. Inst. J. 14, 14 (June 2010).
[7] Alex P. Kellogg, *Detroit Schools on the Brink*, Wall St. J., July 21, 2009; Nicole Bullock, *US Cities Forced to Consider Bankruptcy*, Financial Times, Apr. 29, 2010; Associated Press, *Alabama School System Faces State Takeover in Crunch*, Montgomery Adviser, June 23, 2010, *available at* http://www.montgomeryadvertiser.com/article/20100623/NEWS/100623009/Alabama+school+system+faces+state+takeover+in+crunch?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+StatelineorgRss-Alabama+%28Stateline.org+RSS+-+Alabama%29. For a cautionary note on this point, see Spiotto, *supra* note 5; Kimhi, *Chapter 9*, supra note 4, at 352; *State Superintendent Releases Education Budget Cut Spreadsheet*, Mississippi Link, Jan. 22, 2009, at 8; Matthew Tolbert Smith, *How Today's Solutions Become Tomorrow's Problems*, Aspatore, Feb. 2010.
[8] Anne Marie Chaker, *K-12 Schools Slashing Costs*, Wall St. J., Dec. 11, 2008.
[9] U.S. Department of Education, *State Fiscal Stabilization Fund*, Mar. 7, 2009, *available at* http://www2.ed.gov/policy/gen/leg/recovery/factsheet/stabilization-fund.html; Erik W. Robelen, *'Funding Cliff' Fueling Worry Among States*, Educ. Week , Nov. 4, 2009, at 19; Nick Anderson, *Senator Harkin Proposes $23 Billion Bailout for Schools*, Wash. Post, Apr. 14, 2010; Tamar Lewin & Sam Dillon, *With Revenue Cut, Schools Are Warning of Huge Layoffs*, N.Y. Times, Apr. 21, 2010, at A12; Erik Hanushek, *Cry Wolf! This Budget Crunch is for Real*, Educ. Week, May 19, 2010, at 40.
[10] Anne L. Bryant, *NSBA Statement: Swift Action is Needed to Save Education Jobs*, Feb. 25, 2010, http://vocuspr.vocus.com/vocuspr30/Newsroom; Lewin & Dillon, *supra* note ; Michael Cooper, *Governments Go to Extremes as the Downturn Wears On*, N.Y. Times, Aug. 6, 2010; Kurt Eisele-Dyrli, *School Supplies on a Budget* (July 2008).
[11] Robelen, *'Funding Cliff,' supra* note 9; Anderson, *supra* note 9; Lewin & Dillon, *supra* note 9; Hanushek, *supra* note 9.

billion"[12] and others estimated the shortfalls could exceed $55 billion.[13] So, to address these gaps, in August 2010 Congress allocated an additional $10 billion of stimulus funds for public schools.[14]

Although the additional stimulus funding certainly tempered the educational funding cliff experts had predicted for FY 2011, the reality is that it has only delayed the inevitable.[15] As the clock ticks down to FY 2012, a small yet increasing number of school districts—sometimes major urban districts, often poorer districts, and perhaps especially rural districts that cannot merely raise local property taxes to survive the next few especially lean years[16]—are nearing the point where they may not be able to pay their bills and at the same time fulfill what state law requires of them regarding class size, length of school day or year, curricular coverage, and other

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[12] Bryant, *supra* note 10.
[13] Robelen, '*Funding Cliff,' supra* note 9; Anderson, *supra* note 9; Lewin & Dillon, *supra* note 9; Hanushek, *supra* note 9.
[14] Motoko Rich, *Given Money, Schools Wait on Rehiring Teachers*, N.Y. Times, Aug. 17, 2010. Sean Cavanaugh, *Federal Aid Adds Twist to Election*, Educ. Week, 1, Sept. 22, 1010 ("a number of state candidates explain that while they might normally oppose the federal spending that has gone to states this year and last, these are not normal times.").
[15] Government Accountability Office, *Recovery Act: Opportunities to Improve Management and Strengthen Accountability Over States' and Localities' Uses of Funds*, 20-22 (Sept. 2010); Bryant, *supra* note 10; Robelen, *'Funding Cliff,' supra* note 9; Anderson, *supra* note 9; Albert Bozzo, *States, Cities Likely to Slash Jobs as Stimulus Dwindles*, CNBC, Mar. 10, 2010; Lewis & Dillon, *supra* note 9; *Public Schools Facing Budget Holes as Stimulus Runs Out*, The Jacksonville Free Press, Feb. 18, 2010, at 3; Andrea Eger, *Union Public Schools To Cut More Than 90 Jobs*, McClatchy-Tribune Business News, June 30, 2010; Jennifer Bonnett, *Galt Elementary Board Approves Budget With Eye on Next Year*, McClatchy-Tribune Business News, June 25, 2010; Kerry Benefield, *Spring Sports Saved at Santa Rosa Schools*, McClatchy-Tribune Business News, May 27, 2010; Donald J. Boyd & Lucy Dadayan, *Revenue Declines Less Severe, But States' Fiscal Crisis is Far From Over*, State Revenue Report, Apr. 2010, at 1; Victor Rivero, *Tightening the Purchasing Process: Superintendents Get More Involved in Buying Policies* (Nov. 2009) ("public schools are often tied to revenues that take two to three years to react to any economic conditions [thus] they are the last ones... to see an upturn after the economy recovers."); Ben S. Bernake, *Speech at the Annual Meeting of the Southern Legislative Conference of the Council of State Governments*, Aug. 2, 2010, *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20100802a.htm ("state budgets will probably remain under substantial pressure for a while"); Stephen Sawchuk, *Slew of Layoffs May Be Linked to Overhiring*, Educ. Week, May 19, 2010, at 18; Rich, *supra* note 14.
[16] Associated Press, *Wealthier Districts Winning School Tax Hikes, Widening Divide, Experts Find*, Educ. Week, June 28, 2010. Associated Press, *Alabama School System Faces State Takeover in Crunch*, Montgomery Adviser, June 23, 2010, *available at* http://www.montgomeryadvertiser.com/article/20100623/NEWS/100623009/Alabama+school+system+faces+state+takeover+in+crunch?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+StatelineorgRss-Alabama+%28Stateline.org+RSS+-+Alabama%29; Melissa McKinney, *State Votes to Take Over Two School Systems*, WSFA, July 15, 2010, *available at* http://www.wsfa.com/global/story.asp?s=12809636 (discussing the state financial takeover of two rural Alabama school districts).

such regulations.[17] In fact, earlier this year, the California Department of Education estimated that 12% of its 1,042 school districts could become insolvent by 2012.[18] As school districts approach FY 2012, once again they will be bracing for more cuts and hoping for yet another deus ex machina intervention.

It is a bad habit, to say the least, for school districts to expect an annual bailout when fiscal times are tough. Thus, in this Article, I offer a proposal to change the game. In Section I, I discuss the basics of school finance and budgeting and also explore the many roots of school districts' current and emerging fiscal crises. In Section II, I analyze the three statutory and regulatory remedies available to school districts in fiscal crisis: federal municipal bankruptcy (available to school districts in 24 states), state receivership (available to school districts in 2 states), and state fiscal takeover of a school district (available in 17 states). Neither bankruptcy nor receivership serve school districts' needs well and although state fiscal takeover is better able to address school districts' fiscal problems, there certainly are better and worse ways for a state to intervene. However, in 19 states *not even one* of these three imperfect legal mechanisms is available to assist school districts in fiscal crisis.

Therefore, because the federal government has a substantial interest in the existence of financially stable school districts across the country, in Section III I call for Congress to amend the Elementary and Secondary Education Act of 1965 (the ESEA, known best by the name of its most recent iteration, "No Child Left Behind"[19]) by adopting fiscal accountability provisions.

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[17] Associated Press, *Record Number of Calif. Districts Struggling to Pay Bills*, Educ. Week, June 30, 2010; Rich, *supra* note 14.
[18] Andrew Ward, *More California Schools on Fiscal Brink*, Bond Buyer, Mar. 24, 2010, at 1.
[19] The ESEA was initially passed in 1965 and has been reauthorized ever since; in 2001 its name was changed to "No Child Left Behind," however, the current Secretary of Education, Arne Duncan, intentionally has begun to call the legislation by its original name, ESEA. Remarks by U.S. Department of Education Charlie Rose at Education Law Association annual meeting in Louisville, Kentucky. October, 2009; No Child Left Behind Act, 20 U.S.C. §§ 1041–1044, 3427, 6052, 6053e, 6054b, 6055h, 6056a (2006) (amending the Elementary and Secondary Education Act of 1965, 20 U.S.C. §§ 6301–6578).

This proposal is especially timely because the Obama Administration is in the process of proposing that the ESEA be substantially restructured when it is reauthorized, which likely will happen in 2011, and again roughly every five years after that.[20] Specifically, I argue that as a condition of receiving federal ESEA funding, each state should create a plan that (1) helps districts create immediate cost savings, (2) monitors districts' fiscal health going forward and creates mechanisms for assisting districts as they approach and enter fiscal crisis, and (3) makes efforts to stabilize education funding long-term.

Before moving to this argument, though, it is necessary to clarify why this Article does not discuss school finance litigation in any great detail. After all, a great many law review articles about school districts and money focus on that topic,[21] and some school finance lawsuits have been prompted by state-level cuts made as a result of the recent recession.[22] Indeed, as one commentator has stated and countless others must have noted, state courts' deference to legislatures "leaves many schools underfunded and under-resourced in spite of successful adequacy litigation—a problem that is aggravated during times of recession."[23] I do not argue that the current way in which we fund public schools is just; although the disparities among districts are notably less than they were twenty, thirty, or forty years ago, shocking inequalities

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[20] ED.gov blog, *Reauthorization of Elementary and Secondary Education Act (ESEA)*, Mar. 13, 2010; Alyson Klein, *K-12 Policy Shifts Loom in Republican Surge* Educ. Week 18, 21 (Sept. 22, 2010); Donald M. Payne, *Reauthorization of the Elementary and Secondary Education Act: Challenges Throughout the Legislative Process*, 26 Seton Hall Legis. J. 315, 316 (2002).

[21] *See, e.g.*, Scott R. Bauries, *Is There An Elephant in the Room? Judicial Review of Educational Adequacy and the Separation of Powers in State Constitutions*, 61 Ala. L. Rev. 701 (2010); John Dayton & Anne Dupre, *Blood and Turnips and School Finance Litigation: A Response to Building on Judicial Intervention*, 36 J.L. & Educ. 481 (2007); Preston C. Green, III., Bruce D. Baker & Joseph O. Oluwole, *Race-Conscious Funding Strategies and School Finance Litigation*, 16 B.U. Pub. Int. L.J. 39 (2006); Susan Pace Hamill, *The Vast Injustice Perpetuated by State and Local Tax Policy*, 37 Hofstra L. Rev. 117 (2008); Michael Heise, *Litigated Learning, Law's Limits, and Urban School Reform Challenges*, 85 N.C. L. Rev. 1419 (2007); James E. Ryan, *Schools, Race, and Money*, 109 Yale L.J. 249 (1999); Vinay Harpalani, *Maintaining Educational Adequacy in Times of Recession: Judicial Review of State Education Budget Cuts*, 85 N.Y.U. L. Rev. 258 (2010) (note).

[22] *See infra* Section I.B.2.b.

[23] Harpalani, *supra* note 21, at 258; Sonja Ralston Elder, *Standing up to Legislative Bullies: Separation of Powers, State Courts, and Educational Rights*, 57 Duke L.J. 755 (2007) (note).

remain.[24] But, whether a school district is fiscally stable and whether the education provided to students in that district or state is constitutionally adequate are separate issues. They are connected because fiscal stability is one necessary component among many in determining whether educational adequacy exists, but fiscal stability is certainly not a proxy for educational adequacy. This Article focuses on the complex problem of fiscal stability alone.

# I. SCHOOL FINANCE BASICS

The reforms proposed in this Article are tailored to address school districts' existing and future fiscal crises. These crises are more complicated than perhaps assumed, and they are not limited to or fully explained by the recent recession. This section is devoted to explaining those causes. First, it briefly explains how school districts operate, financially. Then, it discusses the many variables that can contribute to districts' fiscal crises.

## A. Money Comes In, Money Goes Out

### 1. School Districts' Major Sources of Revenue

Of the $584 billion in all U.S. public school districts' revenue columns during FY 2008, 8.2% was provided by the federal government, 43.5% by local governments, and 48.3% by state governments.[25] Of course the relative shares of federal, local, and state contributions vary from

[24] *See, e.g.*, JAMES E. RYAN, FIVE MILES AWAY, A WORLD APART (2010); Kristi L. Bowman, "A New Strategy for Pursuing Racial and Ethnic Equality in Public Schools," 1 Duke F. for L. & Soc. Chg. 47 (2009).
[25] Lei Zhou & Frank Johnson, *Revenues and Expenditures for Public Elementary and Secondary Education: School Year 2007-2008*, 2 (May 2010), *available at* http://nces.ed.gov/pubs2010/2010326.pdf.

state to state and district to district[26]—and the variation among districts in per capita levels of property wealth can be shocking[27]—but these are the national averages.[28]

Over the past few years, school districts' revenues have fallen sharply. The decreases have varied by source, however: federal funding for education has remained constant during the recession, and if one considers the stimulus money targeted for education during this time, federal funding has actually increased.[29] But, since 2008, state funding for elementary and secondary education has fallen in 33 states and the District of Columbia.[30] Thirty-four states expect new cuts in FY 2011.[31] These reductions have many causes, but the most immediate causes are that states' income tax revenue has been hit hard by job losses; local and state property tax revenue has fallen sharply because home values have been dropping as the real estate bubble burst and tax delinquencies and home foreclosures rose; and state sales tax revenues have decreased because of substantial drops in consumer spending.[32] Plus, states' and

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[26] BRUCE D. BAKER, PRESTON GREEN & CRAIG E. RICHARDS, FINANCING EDUCATION SYSTEMS 48, 53 (2008) (presenting a graph comparing relative portions of state, federal, and local contributions to education across all 50 states; and, listing the relative share of property tax, sales tax, and income tax to state and local education revenues across all 50 states).

[27] Cynthia A. Baker, *What Do We Expect?: An Introduction to the Law, Money, and Results of State Educational Systems*, 42 Ind. L. Rev. 317, 319 (2009) (describing one difference in Texas, from $14 million of property wealth per student in the most affluent district to $20,000 per student in the poorest); Benjamin Michael Superfine, *New Directions in School Funding and Governance: Moving from Politics to Evidence*, 98 Ky. L. J. 653, 654 (2010).

[28] A notable exception to this formula is in Michigan, in which education is financed by a combination of sales taxes, property taxes, lottery revenue, general funds, and stimulus funds. Kathy Barks Hoffman, *Cutbacks Stir Debate Over Funding System for Michigan Schools*, Educ. Week, Nov. 11, 2009, at 16.

[29] Stephen Sawchuk, *Slew of Layoffs May Be Linked to Overhiring*, Educ. Week, May 19, 2010, at 1.

[30] National Governors Association & National Association of State Budget Officers, *The Fiscal Survey of States*, 4 (June 2010); Nicholas Johnson, Phil Oliff & Erica Williams, *An Update on State Budget Cuts*, Center on Budget Policy and Priorities, Aug. 4, 2010., (funding has fallen in Alabama, Arizona, California, Colorado, Connecticut, Delaware, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Maine, Maryland, Massachusetts, Michigan, Mississippi, Missouri, Nebraska, Nevada, New Jersey, North Carolina, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, Utah, Virginia, Washington, and the District of Columbia).

[31] Jacob E. Adams, Jr., *Where's the Smart Money in a Great Recession?*, Educ. Week 36, Sept. 15, 2010;

[32] Chaker, *supra* note 8; Michael Prombo, Ares G. Dalianis & Scott R. Metcalf, *Identifying and Mitigating Sources of School Revenue Erosion*, Sch. Bus. Affairs 14, 16 (Sept. 2009); Diane Rado, *Tax Cap Puts Lid on School Budgets*, Chi. Trib., Mar. 5, 2009; Orrick, *Municipal Restructuring and Insolvency*, http://www.orrick.com/practices/public_finance/municipalRestructuring.asp; Sara Behunek, *Three American Cities on the Brink of Broke*, May 28, 2010, http://money.cnn.com/2010/05/28/news/economy/american_cities_broke.fortune/index.htm; Kimhi, *supra* note 4 at 376.

municipalities' safety net—the bond market—has been so unprecedentedly unstable that the federal government intervened during both 2009 and 2010 to make billions of dollars in bonding authority available to states and major school districts, money which would not have been available otherwise.[33]

### 2. School Districts' Major Expenditures

In FY 2008, public elementary and secondary schools across the country spent nearly $597 billion to educate roughly 49 million students.[34] School districts' largest expenditures are salaries for teachers, staff, and administrators, totaling approximately $360 billion in 2006 and constituting 69% of all expenditures that same year.[35] During FY 2008, this was followed by roughly $58 billion (11% of all expenditures) spent on the maintenance and acquisition of equipment and facilities, and almost $16 billion spent on interest (2.6% of all expenditures) for $322 billion of outstanding debt.[36] Nationally, this averages out to spending an average of about

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[33] U.S. Department of Education Press Release, *Treasury and Education Announce 2010 School Bond Allocation*, Mar. 17, 2010, *available at* http://www2.ed.gov/news/pressreleases/2010/03/03172010a.html; Orrick, *supra* note 32; *'Build America' Bonds Could Boost School Construction*, Apr. 29, 2010, http://www.schoolgrants2009.com/content/%E2%80%98build-america%E2%80%99-bonds-could-boost-school-construction; Recovery.gov, *Build America & School Construction Bonds*, Mar. 17, 2010, http://www.recovery.gov/News/featured/Pages/BuildAmericaBondsUpdate.aspx; U.S. Treasury Press Release, *Treasury Releases Guidance on Build America Bonds and School Bonds*, Apr. 3, 2009, http://www.ustreas.gov/press/releases/tg80.htm; William Selway, *Build America Bonds Extended Under Jobs Bill Passed by House*, Bloomberg Businessweek, May 28, 2010; Lisa Anne Hamilton, *Canary in the Coal Mine: Can the Campaign for Mandatory Climate Risk Disclosure Withstand the Municipal Bond Market's Resistance to Regulatory Reform?*, 36 Wm. Mitchell L. Rev. 1014, 1018 (2010).

[34] Zhou & Johnson, *supra* note 25, at 16.

[35] U.S. Census Bureau, *Table 252. Public Elementary and Secondary School Finances by Enrollment-Size Group: 2005 to 2006.* During 2007, public elementary and secondary schools employed nearly 2.5 million full-time teachers plus 2.1 million administrators, nurses, social workers, clerical staff, custodial staff, bus drivers, and other staff. U.S. Census Bureau, *Table 251. Public School Employment: 1990 and 2006.* In small communities especially, the role of the public school system as a major employer is especially obvious; Kristi L. Bowman, *Rebuilding Schools, Rebuilding Communities: The Civic Role of Public Schools After Hurricane Katrina*, in Children, Law, and Disasters: What We Have Learned from Katrina and the Hurricanes of 2005 (2007).

[36] Zhou & Johnson, *supra* note 25, at 2.

$10,000 on each public school student every year.[37] The inequalities among states and districts are great, however: per student spending ranged from the highest state average of $14,824 in New Jersey to the lowest state average of $6,060 in Utah, and the average per-pupil spending difference between a district at the 5th percentile and the 95th percentile in any given state is nearly $4000.[38]

State and local governments usually lag behind the private sector by a year or two in feeling the effects of a recession and having to cut their budgets,[39] but even by now it is old news that most school districts have been cutting back—postponing orders for new equipment and textbooks, cutting programs such as arts and athletics.[40] However, the cuts stretch beyond regular belt-tightening: at least two-thirds of school districts laid off teachers and staff for the 2009-2010 school year and 75-90% expected to do so before or during the 2010-2011 school year.[41] Because of the second round of stimulus funding, the number of teachers laid off in fall 2010 did not reach the 100,000-300,000 previously predicted, but 60,000 teachers still lost their

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[37] U.S. Census Bureau, *Table 253. Public Elementary and Secondary Estimated Finances, 1980 to 2007, and by State, 2007.*

[38] Professors Goodwin Liu and Derek Black both have written persuasively about the incredible level of education inequalities across states because of these funding disparities. Both Liu and Black also argue that Title I of ESEA perversely exacerbates these inequalities. Goodwin Liu, *Education, Equality, and National Citizenship,* 116 Yale L.J. 330, 397-98 (2006); Goodwin Liu, *Interstate Inequality in Educational Opportunity*, 81 N.Y.U. L. Rev. 2044 (2006); Goodwin Liu, *Improving Title I Funding Equity Across States, Districts, and Schools*, 93 Iowa L. Rev. 973, 973 (2008); Derek Black, *The Congressional Failure to Enforce Equal Protection Through the Elementary and Secondary Education Act*, 90 B.U. L. Rev. 313, 317-318 (2010). *School Finance,* Educ. Week 48, Jan. 14, 2010, (documenting the per-pupil spending difference).

[39] Bozzo, *supra* note 15.

[40] Rado, *supra* note 15; Amanda Paulson, *On National Teacher Day, Unions Rail Against Cuts*, Christian Science Monitor, May 4, 2010; Anthony Rios, *Cash-Strapped Districts Shift to Pay-to-Play Sports*, Educ. Week July 6, 2010; Ethan Stewart, *To the Bone*, Santa Barbara Indep. Feb. 25, 2010, at 11 (a board member noted, "we trimmed the fat a long time ago...").

[41] Anderson, *supra* note 9; Erin Richards, *Bill in Congress Could Supply $400 Million to Save State Educators' Jobs*, Milwaukee Journal Sentinel, May 12, 2010 ("Cleveland Public Schools, with about 50,000 students, is expecting to lay off 545 teachers and 100 principals. In Atlanta, the 90,000-student Fulton County School System might have to cut about 1,000 jobs, including close to 500 teaching positions.... Milwaukee Public Schools, with about 85,300 students, has proposed comparatively more layoffs than any other district in the state: 850 employees, including around 150 to 200 teachers.").

[41] Richards, *supra* note 41; Dakaria I. Aarons, *Report Says Stimulus Spending Staved Off Layoffs*, Educ. Week. (July 15, 2010). Reading and math specialists sometimes are cut disproportionately, thus removing crucial academic support for students who need it acutely; Danny Hakim, *School Districts Scramble After Albany Delays Aid*, N.Y. Times, Dec. 15, 2009; Bryant, *supra* note 10.

jobs.[42] Additionally, almost two-thirds of school districts expected that they would be consolidating most students into larger classes by fall 2010.[43] More than a third of school districts also evaluated whether to eliminate summer school programs;[44] others have been closing sometimes massive numbers of schools: 16 in Cleveland, 33 in Detroit, 28 in Kansas City;[45] reducing the length of the school day, week, or year;[46] eliminating early-childhood education;[47] closing alternative schools;[48] cutting back employees' health care benefits;[49] reopening collective bargaining agreement negotiations before the end of the term;[50] moving to a 401(k) retirement savings plan rather than a pension system;[51] charging students to ride the bus

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[42] NBC Nightly News, Apr. 21, 2010, http://www.msnbc.msn.com/id/21134540/vp/36699211#36699211; Charles Lane, *A Teacher-Layoff Crisis? Let's Do the Numbers*, Wash. Post., June 20, 2010; Pat Wingert, *Chicago's Lesson in Layoffs,* Newsweek, July 17, 2010; Arthur Delaney, *States Lay Off 58,000 Teachers in September Despite $26 Billion Aid Package*, Oct. 8, 2010, available at: http://www.huffingtonpost.com/2010/10/08/states-lay-off-58000-teac_n_755965.html.

[43] Hakim, *supra* note 41; Bryant, *NSBA Statement, supra* note 10; Anderson, *supra* note 9; Maxwell, *supra* note 6 at 3, 18.

[44] Anderson, *supra* note 9; Erik Robelen, *Financial Problems Force Districts to Cut Summer School,* Educ. Week, July 13, 2010.

[45] The Cleveland Public School district plans to close 16 schools by fall 2010. Dakari I. Aarons, *School Transformation Efforts Accelerate*, Educ. Week, Mar. 17, 2010, at 1. To avoid insolvency, the long-troubled Kansas City, Missouri public school district plans to permanently close about half its schools over the summer of 2010. Susan Saluny, *Board's Decision to Close 28 Kansas City Schools Follows Years of Inaction*, N.Y. Times, Mar. 11, 2010; Aarons, *School Transformation*, *supra* note 45, at 1, 12; Detroit Public Schools, *Final Decision Regarding Building Closures, Repurposing of Buildings, and Program Changes 2010 Through 2012*, http://www.michiganradio.org/media/docs/DPS_final_closure_list.pdf.

[46] Chris Herring, *Schools' New Math: the Four-Day Week*, Wall St. Journal, Mar. 8, 2010; Tamar Lewin & Sam Dillon, *With Revenue Cut, Schools Are Warning of Huge Layoffs*, N.Y. Times, Apr. 21, 2010, at A12. The Mississippi Senate approved a bill which reduced the number of required school days by five and also permitted school districts to require their employees to take five days of unpaid leave per year. *Mississippi Senate OKs Shorter School Year*, Educ. Week, Mar. 10, 2010, at 4; Louis Freedberg, *School Year Shrinking as Budget Crisis Grows*, California Watch, July 19, 2010. For a discussion of the ramifications of a four-day week, see generally Katharine Baird Silbaugh, *Sprawl, Family Rhythms, and the Four-Day Work Week*, 42 Conn. L. Rev. 1267 (2010).

[47] Amanda Paulson, *On National Teacher Day, Unions Rail Against Cuts*, Christian Science Monitor, May 4, 2010.

[48] Carla Rivera, *Students Face Closure of Alternative Schools Because of L.A. County Budget Cuts*, L.A. Times. June 27, 2010.

[49] Hoffman, *supra* note 28.

[50] Hoffman, *supra* note 28; W. Richard Fossey & John M. Sedor, *In Re Copper River School District: Collective Bargaining and Chapter 9 Municipal Bankruptcy*, 6 Alaska L. Rev. 133, 136 (1989). Not surprisingly, teachers react very negatively to this. In Illinois' Lake Bluff School District 65, for example, teachers are responding to the district's efforts to reopen negotiations by wearing black and refusing to talk with the district's central administration. Conversation with Todd Fraley, Aug. 23, 2010.

[51] Hoffman, *supra* note 28.

to school or selling ads on school buses;[52] and outsourcing transportation and cleaning.[53] Some school districts have been able to draw on their reserves to minimize cuts, but others, especially smaller, rural districts, went into the recession without any safety net.[54]

Some states have also been trying to help school districts create cost-savings. Hawaii closed schools across the entire state for 17 Fridays during the 2009-2010 school year.[55] Mississippi Governor Haley Barbour proposed consolidating the state's 152 public elementary and secondary school districts into 100 districts for potential savings of millions of dollars.[56] The idea of district consolidation also has been discussed in Michigan, which is facing difficult times.[57] Additionally Mississippi enacted a measure reducing the required school year by five days and allowing districts to furlough their employees for another five days.[58] Idaho enacted a measure which would allow a school district to declare itself in fiscal emergency and cut salaries as needed, regardless of existing contractual or other obligations.[59] I am not aware of proposals in any state to raise the caps on class size or reduce curricular requirements in an attempt to conserve costs, but these sorts of ideas are the next logical steps for states to take.

[52] Winnie Hu, *Big, Yellow, and Ripe for Budget Cuts*, N.Y. Times, Aug. 9, 2009, at MB1; Donna Gordon Blankinship, *Could School Bus Ads Save School Budgets?*, Spartanburg Herald-Journal, Mar. 19, 2010; Sue McMillin, *Budget Cuts Mean School Bus Fees in Woodland Park*, June 17, 2010.
[53] Hoffman, *supra* note 28.
[54] Hakim, *supra* note 41.
[55] Michael Cooper, *Governments Go to Extremes as the Downturn Wears On*, N.Y. Times, Aug. 6, 2010.
[56] Alyson Klein, *Mississippi Governor Drawing Opposition on School-Cuts Plan*, Educ. Week, Dec. 9, 2009, at 16 (this is an especially dramatic suggestion in a state in which the school districts reflect a high degree of racial isolation, which is not coincidental); *See* Bowman, *The Civil Rights Roots of Tinker's Disruption Tests*, 58 Am. U. L. Rev. 1129, -- (2009).
[57] Hoffman, *supra* note 28, at 16 (this is similar to school districts' older municipal sibling, cities); Omer Kimhi, *Reviving Cities: Legal Remedies to Municipal Financial Crises*, 88 B.U. L. Rev. 633, 637 (2008); Sharif Shakrani, *School District Consolidation Study in 10 Michigan Counties*, Sept. 3, 2010, available at: http://www.epc.msu.edu/documents/School-District-Consolidation-Study-Sharif-Shakrani-Sept-2010.pdf.
[58] House Bill 1170. http://billstatus.ls.state.ms.us/2010/pdf/history/HB/HB1170.xml.
[59] Brad Iverson-Long, *'Financial Emergency' Provision Added to Schools Budget at the 11th Hour*, IdahoReporter.com (Mar. 3, 2010), available at: http://www.idahoreporter.com/2010/financial-emergency-provision-added-to-schools-budget-at-the-11th-hour/.

## B. The Causes of School Districts' Present Fiscal Crises

It might seem as though school districts should be fairly stable, in a financial sense—their income mainly is derived from state and local taxes, and their major expenditures are predictable employee salaries and benefits, capital expenditures, and debt service.[60] Yet, as we have seen recently, fiscal instability sometimes becomes inevitable. The general economic crisis clearly is the dominant, immediate trigger of most school districts' current fiscal crises; undisputedly, districts' revenues have dropped substantially in the past few years and districts have been unable to adjust their expenditures without substantial pain.[61] Other factors also have contributed to school districts being ill-prepared to deal with fiscal challenges, however.[62] This section first reviews the perennial, common systemic factors that contribute to many school districts' fiscal crises and then discusses the current and future situational factors, varying substantially over the course of time and from one district to another, which will cause substantial fiscal stress for many districts.

### 1. Systemic Factors

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[60] Kimhi, *Reviving Cities*, *supra* note 57, at 637; U.S. Census Bureau, *Table 252*, *supra* note 35.

[61] Kimhi, *Reviving Cities*, *supra* note 57, at 638; Charles K. Coe, *Preventing Local Government Financial Crises: Emerging Best Practices*, 68 Pub. Admin. Rev. 759, 763 (2008), *citing* Mackey; Beth Walter Honadle, *The States' Role in U.S. Local Government Fiscal Crises: A Theoretical Model and Results of a National Survey*, 26 Int'l J. of Pub. Admin. 1431, 1458-59 (2003).

[62] Sara Behunek, *Three American Cities on the Brink of Broke*, May 28, 2010, http://money.cnn.com/2010/05/28/news/economy/american_cities_broke.fortune/index.htm, ("Rampant unemployment, tepid consumer spending, and deeply underfunded public pensions are the leading causes of the balance sheet issues cities are having today. But years of political chicanery and poor financial decision-making by city officials are what led to this problem.").

The systemic factors contributing to districts' fiscal crises generally fall into two categories: management and politics.[63] First, management problems could come in the form of outdated accounting methods,[64] a lack of "specialized knowledge in analytical tools developed to help local governments assess their fiscal health,"[65] a general lack of sophisticated fiscal expertise among school districts' financial officers,[66] dated and inflexible budgetary procedures,[67] and a sense of planning year-to-year rather than having a long-term fiscal plan that includes having sufficient money in reserves.[68] One example of mismanagement and short-sightedness is as follows: school districts hired aggressively between 2000 and 2008 in response to NCLB and the general push for accountability, decreasing class sizes and adding teaching coaches, instructional mentors, ELL instructors, special education teachers, and others who specialized in focused instruction. In fact, between 1999 and 2008, the public school student population grew 5% and the number of classroom teachers grew 11%.[69] Yet, when school districts were hiring these additional employees, they probably did not anticipate that their funding might decrease a little, let alone a lot.

Second, the problems of politics are obvious, if stubborn and complicated: as John Chubb and Terry Moe argued in 1990, when education policy is made at the local level by elected officials and those who report to them, it becomes influenced by interest groups who bring to the table concerns extending beyond the education of children; the interest groups' power can lead to

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[63] Kimhi, *Reviving Cities*, *supra* note 57, at 638.
[64] Coe, *supra* note 61, at 763 (citing Mackey); Honadle, *supra* note 61, at 1458-59.
[65] Honadle, *supra* note 61, at 1434.
[66] Gretchen Morgerson, *Exotic Deals Put Denver Schools Into Debt*, N.Y. Times, Aug. 5, 2010.
[67] Coe, *supra* note 61, at 763 (citing Mackey); Honadle, *supra* note 61, at 1458-59; Erik Hanushek, *Cry Wolf! This Budget Crunch is for Real*, Educ. Week 40, May 19, 2010 (this is not unique to school districts, though—as the Pew Center on the States notes, "as many as 17 states project only one or zero years beyond the current budget cycle."); The Pew Center on the States, *Long-Term Fiscal Planning*, *available at* www.pewcenteronthestates.org/initiatives_detail.aspx?initaitive.
[68] *Id.*
[69] Sawchuk, *supra* note 29, at 18.

policies that do not match the educational needs of children in the district.[70] Consider the inertia for the present system of budgeting: According to Marguerite Roza, a school finance expert, "[school] districts tend to think of everything in terms of fixed costs . . . stabilizing a budget would mean that a smaller share of the budget would be tied to committed or escalating costs, including salaries."[71] However, school districts have not adjusted to the model Roza proposes.[72] Many school district budgets are besieged by interest groups wielding political power,[73] complicated by power dynamics between and among government officials,[74] and obscured by many stakeholders' interests in making the financial situation seem better than it is because of the general unpopularity of options for dealing with fiscal crisis.[75] On top of all of this, some school districts also are weakened by corrupt government officials who embezzle, or coordinate the embezzlement of, millions of dollars annually (as in the Detroit and New Orleans public school districts).[76] Ahhh, politics.

2. Situational Factors

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[70] John E. Chubb & Terry E. Moe, Politics, Markets & Public Schools (1990) (for example, a decision about laying off teachers is not a debate about the research about the effect of larger class sizes; especially in poorer communities, it becomes a powerful local political issue if the school district is a major employer); Aaron Saiger, *Disestablishing Local School Districts as a Remedy for Educational Inadequacy*, 99 Colum. L. Rev. 1830, 1858-59 (1999) (note).

[71] Sawchuk, *supra* note 29, at 18.

[72] Many school districts covered much of their FY2010 shortfalls with stimulus funding, thus avoiding substantial amounts of layoffs or other programmatic changes. *See, e.g.*, Gary Glancy & Lee G. Healy, *Spartanburg School Districts 4 and 5 to Furlough Teachers*, Spartanburg Herald-Journal (June 29, 2010) ("the district made up a large portion of its shortfall by using... federal stimulus dollars to fund personnel").

This is not the first time in recent history when school districts' revenues have decreased, and according to Stanford economist Erik Hanushek, districts "have found the 'crying wolf' strategy always effective and thus have never really thought much about how to adjust to a leaner budget." Hanushek, *supra* note 67, at 40.

[73] Coe, *supra* note 61, at 763 (citing Mackey).

[74] Honadle, *supra* note 61, at 1434.

[75] *Id.*

[76] Alex P. Kellogg, *Detroit Schools on the Brink*, Wall St. J., (July 21, 2009) (in 2009, forensic accountants discovered 257 "ghost" employees receiving paychecks from DPS. A former payroll manager and another individual were indicted in May, 2009 on charges of embezzling roughly $400,000 since 2005.); Bowman, *Rebuilding Schools, Rebuilding Communities*, *supra* note 35.

The systemic factors identified above operate across decades and districts. The following three situational factors are more time-, region- or district- specific factors that also will exert increasingly substantial financial pressure on various states and school districts, if they have not done so already. The proposal presented later in this Article is aimed mainly at addressing systemic factors. But, awareness of future substantial situational factors still can help states and districts engage in useful long-term fiscal planning and thus have a better chance of maintaining long-term fiscal stability, which is a central goal of this Article.

#### a. Pensions, the Third Rail

Some districts already can tell tales of pension-related woe: in 2008, the Denver Public Schools entered into a creative financing deal to cover a $400 million shortfall in their pension obligations; because of the long arm of the recession, the deal has already cost the cash-strapped district at least $25 million more than it anticipated (the district may, however, come out ahead in this deal over the course of the 30-year term to which it agreed).[77]

Denver is not alone. A January 2010 article in the professional journal *District Administration* states:

> The financial state of the nation's public pension funds—which provide the retirement incomes for all state employees but in most states are dominated by teachers, administrators and other school employees—has gone from bad to worse, and for most it is only projected to worsen in coming decades.[78]

[77] Morgerson, *supra* note 66; David Milstead, *Analysis: Both Sides Right in the Pension Debate,* Apr. 12, 2010, www.ednewscolorado.org/2010/04/12/4295-analysis-both-sides.

[78] Kurt Eisele-Dyrli, *Will Pensions Bankrupt Your District? State retirement funds are in crisis, and school systems will likely pay more of the bill,* District Admin. (Jan. 2010).

The pension crisis has been exacerbated by the recent recession, but even before then, pension funds had become more dependent on investment returns than they had ever been in the past.[79] Thus, the stock market drops over the past decade, and in 2008 especially, affected pension funds substantially. [80] During 2008, Iowa's state pension fund declined by more than $3 billion and California's public employee and teachers' pension funds lost more than $100 billion.[81] States now are carrying hundreds of billions of dollars of unfunded pension obligations: estimates of the total unfunded liability for teachers' pensions across the country range from $330 billion to $900 billion.[82] The shortfall is scary, as is one major reason why the amount of the shortfall is so uncertain: few states or districts have done an actuarial study so that they can plan for the real future costs of retirees' health care and pensions, which remain largely unknown.[83]

Much like social security reform, pension reform appears to be a third rail, the sort of political issue so charged that engaging it directly is likely to inflict severe, if not fatal, damage to individual politicians' careers.[84] Reform is, of course, constrained by most states' very limited ability to alter previously accrued pension benefits, and by some states' slightly greater ability to change future pension accruals—although lawsuits in at least two states are testing the strength of these agreements.[85]

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[79] *Id.*
[80] *Id.*
[81] *Id.*
[82] Matt Miller, *Buyouts, not Bailouts, for Teachers*, Wash. Post (May 13, 2010); Eisele-Dyrli, *supra* note 78; Natalie Cohen, *San Diego City's Financial Crisis: The Past, Present, and Future*, June 10, 2010, *available at* http://www.bondsquawk.com/tag/municipal-bankruptcy/; *Review & Outlook*, Wall St. J., Mar. 20, 2010, at A14 (noting that New Jersey has $90 billion in unfunded pension and health care obligations).
[83] California Governor's Committee on Education Excellence, Students First: Renewing Hope for California's Future (2007). available at http://www.everychildprepared.org/docs/5finance.pdf 5, pp. 29-30
[84] The city of Vallejo, California recently neared bankruptcy and chose to lay off employees, cut back on services, and reduce retirees' health care benefits—but it would increased pensions. Steven Greenhut, *Vallejo's Painful Lessons in Municipal Bankruptcy*, Wall St. J., Mar. 26, 2010.
[85] Amy B. Monahan, *Public Pension Plan Reform: The Legal Framework*, 1-2 (2010 working paper), available at: http://ssrn.com/abstract=1573864; *Id.* at 3 ("State plans, however, are specifically exempted from the [federal] anti-cutback rule."); *Id.* at 27-30 (providing a chart summarizing a number of states' legal restrictions on limiting pension benefits; 7 of the states only limit the ability to alter already-accrued benefits; 12 of the states limit the ability to alter

A few states have begun to grapple with the problem of a growing pension fund shortfall, but even in those cases, their reforms rarely address teachers' pension funds.[86]

b. Recession-Related Litigation

Since 2009, a number of lawsuits involving various legal claims have grown out of school districts' recession-driven budget cuts. For example, in 2009, multiple lawsuits brought on behalf of students challenged Hawaii's decision to furlough teachers and close schools for 17 Fridays during the school year.[87] In February 2010, the ACLU and the Public Counsel Law Center sued the Los Angeles Unified School District, contesting the district's layoff of a disproportionate number of teachers at three inner-city, high-minority middle schools as a violation of students' rights.[88] Also in February 2010, New Jersey Governor Chris Christie ordered school districts to cover a portion of the per capita funding promised by the state by dipping into their own reserves at a total of $475 million statewide; not surprisingly, school districts sued the state.[89] In mid-May 2010, the board of a major suburban school district, Montgomery County, Maryland, unanimously decided that it would sue its parent municipality, the county, if the county allocated less money for public schools than the minimum level

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past or future accrued benefits; 3 of the states are unclear; 1 state is fact-specific; and 1 state has no restrictions). Jeannette Newman, *Pension Cuts Face Test in Colorado, Minnesota*, Wall St. J., June 12, 2010.

[86] A notable exception: starting in fall 2010, Louisiana's two major teacher pension funds will raise the employer pension contribution, one by nearly 5% and the other by nearly 7% of an employee's salary. Eisele-Dyrli, *supra* note 78; For an overview of states' approaches to the pension shortfall problem, see Katharine Barrett & Richard Greene, *Promises With a Price: Public Sector Retirement Benefits*, The Pew Center on the States (2007).

[87] Herbert A. Sample, *Hawaii Teacher Furlough Talks May Occur this Week*, ABC News, Nov. 4, 2009, available at: http://abcnews.go.com/Business/wireStory?id=8994832.

[88] *Judge Blocks Teacher Layoffs At 3 Inner-City LA Schools*, Educ. Week, May 19, 2010, at 4.

[89] Joan Gralla, *NJ Court Orders Schools to use $475 million of reserves*, June 14, 2010, *available at http://www.reuters.com/article/idUSTRE65D62920100614*

required by the state, which seemed likely.[90] A school finance lawsuit filed during May 2010 in California appears to have been triggered by state cuts resulting from the recession, as does a similar lawsuit filed in Indiana a few months earlier.[91] In June 2010, Kansas City residents sued the Governor, contending state funding for education had been cut below the amount required by the state funding formula.[92] In early August 2010, the Chicago Teachers Union sued the Chicago Public Schools, contesting the layoff of 240 teachers and instructional coaches, and the Detroit Public Schools' decision to outsource school security also was challenged in court.[93] Also in August 2010, the ACLU sued California school districts because they were imposing fees for materials for required courses, and also for elective courses.[94]

It is unclear whether these lawsuits are isolated occurrences or anecdotal examples of a larger trend, but because they arise from such different school districts and include a wide range of legal claims, I am inclined to think that, unfortunately, it may be the latter. And at a time when school districts are trying to save money by asking parents to buy rolls of paper towels for their children's classroom, large attorney bills hardly make districts' fiscal problems any easier.[95]

#### c. Changing Student Demographics

[90] *Maryland School Board May Sue Over Budget*, Educ. Week, May 19, 2010, at 4.
[91] Terence Chea, *Coalition Files Suit*, Bloomberg Businessweek, May 20, 2010; NSBA Legal Clips, May 27, 2010; AP, *Schools Decry Funding Disparity in Lawsuit*, Feb. 24, 2010.
[92] Scott Lauck, *Kansas City Residents Challenge School Funding Cut*, Missouri Lawyers Media, June 24, 2010.
[93] Stephen Sawchuck, *Chicago Union Sues to Prevent Layoffs; 'Effectiveness' a Theme*, Educ. Week, Aug. 4, 2010; Chastity Pratt Dawsey, *DPS is Ordered to Rehire Officers*, Detroit Free Press A3, Aug. 25, 2010.
[94] Sam Dillon, *Public Schools Face Lawsuit Over Fees*, N.Y. Times, Sept. 10, 2010.
[95] Some districts have litigation insurance. This presents two additional complications, though: first, if the insurer does decide to cover the cost of litigation, the insurer gains a say in what litigation strategy and maneuvers are covered, and what type of settlement is acceptable. Second, of course, these policies are written so that not all litigation is covered. *See, e.g.*, AP, *Philadelphia-area School District's Insurance Company Says it Won't Cover Laptop Spying Litigation* (Apr. 22, 1010); Association of American Educators, *Professional Liability Insurance*, *available at* http://www.aaeteachers.org/index.php/member-benefits/liability-insurance.

The population of school-aged children is growing across the U.S., and the vast majority of the increase comes from non-White students, many in poverty, and some not fluent in English.[96] A 2010 Brookings Institute report describes this population change as "the most significant socio-demographic change since the huge wave of immigrants in the early 20th century"[97]; the same report forecasts that White children will comprise less than half of the school-age population by 2023, and by 2042, the entire country will be "majority minority."[98] Over the next 40 years, Latinos/as and African-Americans are projected to account for 90% of the growth in the working adult-age population, yet because their college graduation rates are less than half of Whites' and Asians', and because disadvantaged groups are most affected by the recession-driven cuts in education and other human services, they likely will continue to be concentrated in lower-paying jobs and/or have higher rates of unemployment, both of which mean their children are more likely to grow up in or near poverty.[99] All of this must be understood in light of changing residential migration patterns: although three-fourths of people of color live in the 100 largest metro areas in the United States today, more people of color and more people in poverty live in the suburbs than in urban centers; and, *non*-African-American minorities (Latinos/as, Asian-Americans, etc.) are moving away from major immigrant gateway cities with increasing speed.[100] Thus, the demographic changes described above will affect many

[96] Erik W. Robelen, *Education Attainment Rises for Americans Across Race, Ethnicity*, Educ. Week, May 19, 2010, at 6.
[97] Bruce Katz & Judith Rodin, *An Impending National Transformation*, Brookings Blog, May 9, 2010.
[98] William H. Frey, *The State of Metropolitan America: Chapters, Race and Ethnicity*, Brookings Blog.
[99] Brookings Metro America at 160; Michael Greenstone, *Evidence From May's Employment Numbers on the Benefits of Education*, Brookings Blog, June 4, 2010; Bob Herbert, *A Ruinous Meltdown*, N.Y. Times, Mar. 19, 2010 ("In New Jersey, the newly elected governor, Chris Christie, has proposed a series of budget cuts that, among other things, would result in public schools receiving $820 million less in state aid than they had received in the prior school year. Some well-off districts would have their direct school aid cut-off altogether. Poorer districts that rely almost entirely on state aid would absorb the biggest losses in terms of dollars. They're bracing for a terrible hit.... For all the happy talk about "no child left behind," the truth is that in Arizona and New Jersey and dozens of other states trying to cope with the fiscal disaster brought on by the Great Recession, millions of children are being left far behind, and many millions of adults as well.").

different types of communities and districts all across the country: major urban districts, smaller urban districts, suburban districts, and some rural districts.

These demographic changes increasingly will have a financial impact on school districts. In the words of recent a Brookings Institution report, students of color, students in poverty, and English Language Learner ("ELL") students "require the most resources and the most focus . . . to achieve."[101] How much more they require is not clear, but according to the Education Trust, the National Center on Education Statistics, the U.S. Department of Education, the U.S. General Accounting Office, and Standard & Poor's, school districts should allocate 35-40% more resources to educate students in poverty than for non-poor students.[102] Educating ELLs appears to require a similar supplemental infusion of resources.[103]

Additionally, education research emphasizes not only the importance of investing in the education of at-risk children, but especially doing so when they are still quite young. For example, Latino/a children begin kindergarten with social and emotional skills comparable to middle-class White children.[104] Yet, Latinos/as have the highest dropout rates of any racial/ethnic group (22%, double that of African-Americans and almost four times that of Whites); on standards-based tests they perform worse than Whites but not quite as poorly as African-Americans; an estimated 18-45% of them are ELLs; and nearly half of Latino/a students

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[100] Frey, *supra* note 98; Elizabeth Kneebone & Emily Garr, *The State of Metropolitan America: Chapters, Income and Poverty*, Brookings Blog. Kristi L. Bowman, *Pursuing Educational Opportunities for Latino/a Students*, 88 N.C. L. Rev. 911, 935-36 (2010).

[101] Robelen, *Education Attainment Rises*, *supra* note 96.

[102] California Governor's Committee on Education Excellence, Students First: Renewing Hope for California's Future (2007). *available at* http://www.everychildprepared.org/docs/5finance.pdf 5 p. 12; *See also* Black, *supra* note 38 (noting that "research on the issue uniformly indicates that as the concentration of poverty increases, the negative educational effects of poverty are compounded."); *See also* Susan B. Neuman, *Public Media's Impact On Young Readers*, Educ. Week, Aug. 11, 2010, at 44.

[103] California Governor's Committee on Education Excellence, Students First: Renewing Hope for California's Future (2007). available at http://www.everychildprepared.org/docs/5finance.pdf 5 p. 21 ("Oregon provides 50 percent more funding for its English learners, while Florida provides 27.5 percent higher funding for them.")

[104] Mary Ann Zehr, *Social Skills of Latino and White Kindergartners Found to be on Par*, Educ. Week, May 12, 2010, at 16; Claudia Galdino & Bruce Fuller, *The Social Competence of Latino Kindergartners and Growth in Mathematical Understanding*, 46 Devel. Psych. 579 (2010).

attend schools that are both high-poverty and high-minority.[105] Thus, Sociologist Robert Crosnoe says "we need to make the investment at the start of school, when [Latino/a children] are eager and enthusiastic and motivated but before the many disadvantages they face (e.g. lower-quality schools, watered-down curricula) start to chip away at the socioemotional advantages they bring into school."[106]

The need for targeting additional resources for at-risk students will be higher than ever before, and this heightened need will occur at a time when there is a growing demographic disconnect between these children and the growing population of older adults without children who pay most of the local property taxes. In general, the members of the latter group are and will continue to be wealthier and White.[107] At best this creates a puzzling "cultural generation gap"[108] and at worst we will see more of what has already happened even in some relatively racially/ethnically homogenous communities: older property owners without children in the schools ban together to limit funding for public education.[109]

This challenge is the focus of race/ethnicity-conscious school finance litigation, which addresses fundamental inter-group inequities that are outside the scope of this Article. As I argued in another piece, since 1996, an increasing number of school finance cases have been "explicitly race/ethnicity-conscious. . . . in contrast with the long history of school finance

[105] Bowman, *Pursuing Educational Opportunities*, *supra* note 100, at 942.
[106] Mary Ann Zehr, *Social Skills of Latino and White Kindergartners Found to be on Par*, Educ. Week, May 12, 2010, at 16.
[107] Robelen, *Education Attainment Rises*, *supra* note 96, at 6.
[108] William H. Frey, *The State of Metropolitan America, Chapters, Age*, Brookings Blog.
[109] For a review of the literature in this area, see David N. Figlio & Deborah Fletcher, *Suburbanization, Demographic Change and the Consequences for School Finance*, NBER Working Paper 16137, 4-8 (June 2010), available at: http://www.nber.org/papers/w16137. Figlio and Fletcher conclude: "We find strong evidence that the development dates of the suburbs and the resulting modern age distributions influence the level of school spending in these districts. School districts encompassing suburbs that developed earlier and with consequently older populations tended to cut back on school spending sooner, all else equal, once the Baby Boomer generation was out of school, than did those with later-developing suburbs. These estimated effects are particularly strong in the metropolitan areas where minorities comprise a relatively large share of the school-aged population. . . . Our analyses go a long way toward cementing the conclusion that as a suburb ages, its support for schooling falls."

litigation in which race/ethnicity was the proverbial elephant in the room, but the legal harms and remedies were technically colorblind."[110] Thus, the districts facing substantial demographic change, and with it substantial financial need, are not destined necessarily to shoulder these costs by themselves.

### C. Summary

Undeniably, the recession has been a major cause of school districts' falling revenues over the past few years and it has triggered fiscal crises for an increasing number of school districts. However, the crisis would not be so acute without the governance problems embedded in the existing system, which can be divided generally into two categories: mismanagement and politics. In addition to understanding the ways in which these systemic factors have contributed to school districts' current fiscal crisis, it is important to anticipate and understand the situational factors that pose increasingly significant fiscal challenges for school districts. Not all school districts are able, or will be able to, balance their books. Hence, the need for legal mechanisms.

## II. AVAILABLE LEGAL MECHANISMS

For a variety of reasons, many school districts across the country are in fiscal crisis or will be facing a financial crisis very soon. Perhaps because school districts and other municipalities have been so financially stable historically, the law is not anywhere near as well-developed when the debtor is a municipality as it is when the debtor is a corporation or individual. There are three legal mechanisms available to school districts in fiscal crisis and in

[110] Bowman, *A New Strategy*, *supra* note 24, at 58.

this section I analyze them in turn, discussing each option along with its utility for school districts in fiscal crisis.

## A. Federal Municipal Bankruptcy

### 1. A Brief History of Federal Municipal Bankruptcy and School Districts' Experiences

The availability of federal municipal bankruptcy was not at first intended to be permanent. Congress adopted the first such provision as a temporary measure in 1934, during the middle of the Great Depression.[111] The Supreme Court invalidated the provision in 1936 and Congress adopted a modified (though still temporary) municipal bankruptcy provision in 1937.[112] The provision eventually became a permanent part of the Bankruptcy Code in 1946, was made more accessible to municipalities when amended in 1976, and exists in substantially similar form today.[113] Importantly, the definition of "municipality" is broad—unlike state constitutions which generally define "municipality" to include only counties, cities, and towns,[114] the Bankruptcy Code defines municipalities to include any "political subdivision or public agency or instrumentality of the state," including school districts.[115]

[111] Spiotto, *Introduction to Municipal Bankruptcy*, *supra* note 4, at 613-615; Malito, *supra* note 4, at text accomp. notes 12-66.
[112] *Id.*
[113] Kimhi, *Chapter 9*, *supra* note 4, at 367; Spiotto, *Introduction to Municipal Bankruptcy*, *supra* note 4, at 613-615; Malito, *Municipal Bankruptcy*, *supra* note 4, at text accomp. notes 12-66.
[114] Alaska Const. art. X; Ark. Const. art XII, § 3; Ariz. Const. art. XII, § 1; Cal. Const. art. XIIIB, § 8d; Colo. Const. art. XIV § 13; Colo. Const. art. XX, §§ 6, 9; Colo. Const. art. IX, § 15; Conn. Const. art. X, § 1; Fla. Const. art. IX, § 4; Ga. Const. art. IX, §§ 1, 2, 3; Idaho Const. art. XII, § 1; Ill. Const. art VII, § 1; Ky. Const. § 156a; La. Const. art. VI, §§ 1-3; Md. Const. arts. 11A, 11E, 11f; Mich. Const. of 1963, art. VII, § 21; Mont. Const. art. XI, § 1; N.D. Const. art. VII; Nev. Const. art. VIII, § 8; N.C. Const. art. VIII, § 1; N.M. Const. art. IX, § 11 to N.M. Const. art. IX, § 12; Ohio Const. art 10, §§ 10.01, 10.03; Okla. Const. art. XVIII, § 1; Or. Const. art. XI, § 2; Pa. Const. art. III, §

Municipal bankruptcy is different from individual and corporate bankruptcy proceedings in several substantial ways. For example, to be eligible to file for bankruptcy, municipalities must meet a more strict definition of "insolvency" than applies to private entities—they must be almost literally unable to pay their bills.[116] Additionally, in bankruptcy proceedings, municipalities are not permitted to liquidate assets.[117] This is because the goal of the proceedings is not to eliminate a municipality's debt or wind up business, but rather to restructure a municipality's debt and major expenditures.[118] Perhaps most different from individual and corporate bankruptcy proceedings, because the federal Constitution's Tenth Amendment limits the reach of the federal government,[119] states must explicitly authorize municipalities to file for bankruptcy in federal court.[120] To one degree or another, 24 states do so.[121]

Municipal bankruptcy is very rarely used, though, despite its availability. Less than 600 municipalities have filed for bankruptcy since 1936 and this includes so few school districts that we probably can count them on one hand.[122] Even after filing for bankruptcy, not all municipalities complete the process—some school districts in particular have been able to

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20; S.C. Const. art. VIII, § 13d; S.D. Const. art. IX, § 1; Tex. Const. art. XI; Utah Const. art. XI, §§ 4,5,7; Wash. Const. art. XI, § 3, 4; W.Va. Const. art. XII, § 6; Wis. Const. art. IX, § 3; Wyo. Const. art. XVI, § 5.

[115] Malito, *Municipal Bankruptcy*, *supra* note 4, at text accompanying note 78.

[116] Tung, *supra* note 4, at 901-02; Kimhi, *Reviving Cities*, *supra* note 57, at 650-51; Malito, *Municipal Bankruptcy*, *supra* note 4, at passim; McConnell & Picker, *supra* note 4, at 456.

[117] Spiotto, *Introduction to Municipal Bankruptcy*, *supra* note 4, at 616; McConnell & Picker, *supra* note 4, at 427.

[118] *Id.*

[119] Bankruptcy courts are not permitted "to intervene directly in municipal management or operations, a sphere that falls squarely within the province of the respective states." Tung, *supra* note 4, at 890.

[120] In 1994, an amendment to the Bankruptcy Code required specific authorization from states, prior to that time, only general authorization was required. Tung, *supra* note 4, at 890.

[121] 17 states specifically authorize municipal bankruptcy; 7 states conditionally authorize municipal bankruptcy. Sylvan G. Feldstein & Frank Fabozzi, The Handbook of Municipal Bonds 157 (2008).

[122] Nicholas McGrath & Ji Hun Kim, *The Next Chapter for Municipal Bankruptcy*, Am.. Bankr. Inst. J. 14, 14 (June 2010); Texas school district, small oil-boom town, 1947. UPI, *San Jose Schools Can Cut Pay, U.S. Bankruptcy Court Rules*, Aug. 29, 1983; Copper River, Alaska school district in bankruptcy proceedings 1986-1988; 500-student district covering huge land mass of 25,000 square miles. Fossey & Sedor, *In Re Copper River School District*, *supra* note 50, at 134; James Spiotto, *Municipal Bankruptcy Remains "Last Resort" Despite Troubled Economy*, June 8, 2010 ("Traditional U.S. state and local government bonds enjoy a proud history of a low number of defaults and, when they rarely occur, higher recoveries compared to corporate debt, both investment grade and speculative. The default rate for municipal securities dramatically lags the default rate for corporate counterparts.").

renegotiate bargaining agreements out of court while their bankruptcy petitions were pending[123] or receive an emergency loan from the state[124] and thus negate the necessity of bankruptcy. Other times, public consideration of filing for bankruptcy (without actually filing) has been enough for some stakeholders to devise an alternative and change the contours of the district's fiscal crisis. This is true in three major urban school districts in recent memory. The Chicago Public School system in 1980,[125] the Baltimore Public School District in 2004,[126] and the Detroit Public School district in 2009[127] all were precipitously near insolvency. In Chicago, the governor negotiated funding assistance from local banks.[128] In Baltimore, a $42 million emergency loan from the local city council provided the needed relief.[129] In Detroit, the situation was and is more complicated. The Detroit Public Schools emergency financial manager, Robert Bobb publicly stated after a few months on the job that given the district's $259 million deficit which resulted from 7 years of deficit spending, bankruptcy might be the best way to turn around the financially failing system.[130] DPS has avoided bankruptcy for now, but the district's deficit rose to $363 million by late 2010, even after massive cuts and restructuring were implemented.[131] DPS is not out of the woods yet.[132]

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[123] San Jose, California school district filed for bankruptcy in 1983 but then negotiated a new CBA w/teachers union out of court and was not declared insolvent; 30,000 students at the time. Fossey & Sedor, *supra* note 50, at 142.

[124] Richmond Unified School District, 1991, 30,000 students, 70% minority AP, *Northern California School District Files for Bankruptcy Protection*, Apr. 19, 1991 (eventually bailed out by a loan from the state); William Celis, *California Has Agreed on Bailing Out Schools*, N.Y. Times, May 1, 1992, A23 (in 2008, renamed school district was near bankruptcy). Local News, *Local School District Out of Money*, Mar. 6, 2008, *available at* http://abclocal.go.com/kgo/story?section=news/local&id6004296

[125] News Services and Staff Reports, *Illinois Governor Announces a Plan for Near-Bankrupt Chicago Schools*, Wash. Post, Jan. 6, 1980.

[126] Tim Craig & Nancy Trejos, *Baltimore Schools Solvency Plan Rejected; Erlich Will Announce Own Bankruptcy-Prevention Step Today, Officials Say*, Wash. Post, Feb. 24, 2004, at B5.

[127] Dakarai I. Aarons, *Decline and Fall*, Educ. Week, Aug. 12, 2009, at 24.

[128] News Services and Staff Reports, *Illinois Governor Announces a Plan for Near-Bankrupt Chicago Schools*, Wash. Post, Jan. 6, 1980.

[129] Lori Montgomery & Craig Whitlock, *Baltimore Rejects State Bailout of Schools*, Wash. Post, Mar. 9, 2004, at B08.

[130] Aarons, *supra* note127, at 24, 26.

[131] Alex P. Kellogg, *Schools Learn to Survive*, Wall St. J., Aug. 9, 2010.

[132] Alex P. Kellogg, *Detroit Schools on the Brink*, Wall St. J., July 21, 2009.

### 2. Benefits and Disadvantages of Municipal Bankruptcy

The basic benefits of bankruptcy for a municipality are that creditors' collection efforts are hampered by a stay when a bankruptcy petition is filed,[133] and the municipality's largest expenditures—usually collective bargaining agreements (CBAs)[134] and debt service[135]—are modified. In the short term, the stay enables the municipality to continue to provide public services—education, in the case of a school district—and to pay its employees while its fiscal situation is sorted out.[136] In the long term, the adjustments to CBAs and debt obligations often, but not always, place the district on more advantageous fiscal footing.[137] Although bankruptcy courts have the authority to unilaterally modify CBAs and to oversee the renegotiation of municipal debt, they are especially reluctant to do the former. Thus, sometimes unions and creditors attempt to renegotiate their contracts without the involvement of the court in an attempt to secure more advantageous terms.[138] The basic benefits of bankruptcy to the creditors are a right to be heard, a formal, transparent process, and an adjudicated decision.[139]

Like the benefits, the disadvantages of bankruptcy for a municipality are both short- and long-term. First, the stigma of filing for bankruptcy fits into both of these categories, and indeed the hit to a municipality's reputation when it files for bankruptcy, especially if the municipality is

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[133] Tung, *supra* note 4, at *893*; Kimhi, *Reviving Cities*, *supra* note 57, at 650-51.
[134] McConnell & Picker, *supra* note 4, at 467; Tung, *supra* note 4, at 897.
[135] Extend term of debt, reduce principal/interest, refinance debt. Tung, *supra* note 4, at 897; Malito, *Municipal Bankruptcy*, *supra* note 4, at text accomp. note 67.
[136] Tung, *supra* note 4, at 893; Kimhi, *Reviving Cities*, *supra* note 57, at 651-51.
[137] Henderson, *supra* note 4; Kimhi, *Chapter 9*, *supra* note 4, at 381-82.
[138] Ronald D. Wenkart, *Unilateral Modification of Collective Bargaining Agreements in Times of Fiscal Crisis and Bankruptcy: An Unconstitutional Impairment of Contract?*, 225 West Ed. L. Rep. 1, 19-20 (2007); Henderson, *supra* note 4.
[139] Kunibert Raffer, *Internationalizing U.S. Municipal Insolvency: A Fair, Equitable, and Efficient Way to Overcome a Debt Overhang*, 6 Chi. J. Int'l L. 361, 364, 368 (2005).

a school district, can be significant.[140] Second, the costs of renegotiating CBAs fall squarely on teachers, clerical and custodial staff, bus drivers, and other modestly-paid individuals. Especially if a school district is a major employer in a community, the effects of modifying a CBA can be felt widely. Third, especially in small school districts, bankruptcy proceedings may literally cost more than they save: these costs come both through attorneys' fees and district employees' diverted time and attention.[141] Fourth, as with individual bankruptcy, municipal bankruptcy will affect a municipality's credit rating and decrease its ability for future borrowing at competitive rates, thus decreasing its likelihood of long-term solvency.[142] It may also affect other municipalities in the state in the same way.[143] Given these substantial disadvantages, it is not surprising that both the California and Rhode Island legislatures are currently entertaining proposals to make it more difficult for municipalities to file for bankruptcy.[144]

But fifth and perhaps most importantly, bankruptcy is an ill fit to address school districts' fiscal crises because bankruptcy courts' powers are so limited due to federalism concerns.[145] As Michael McConnell and Randal Picker described in their seminal work on municipal bankruptcy, "In most cases, chronic financial difficulty is a sign that ordinary political processes are not functioning properly."[146] Bankruptcy courts cannot influence these "ordinary political processes" or the problems of mismanagement—they cannot affect a school district's choices about its

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[140] Spiotto, *Introduction to Municipal Bankruptcy*, *supra* note 4, at 641; Kimhi, *Chapter 9*, *supra* note 4, at 382.
[141] Tung, *supra* note , at 911 (in the Orange County bankruptcy proceeding, the cost to the county was $50 million in attorney fees and related expenses).
[142] Tung, *supra* note 4, at 903-904; Kimhi, *Chapter 9*, *supra* note 4, at 382-83.
[143] Tung, *supra* note 4, at 903-904, 911.
[144] Capitol Alert Blog, http://blogs.sacbee.com/capitolalertlatest/2010/05/cox-asks-to-sen.html (May 25, 2010) (California); *R.I. Assembly Digest: Rules Change on Municipal Bankruptcy*, (June 11, 2010), http://www.projo.com/generalassembly/ASSEMBLY_DIGEST_11_06-11-10_FJIR3P2_v29.191a9d6.html.
[145] Specifically, the administration of local government is typically left to the states. Kimhi, *Reviving Cities*, *supra* note 57, at 633; Kimhi, *Chapter 9*, *supra* note 4, at 351; *See also* "Chapter 9 does not give courts the power to address the policy matters of municipalities that may have led to bankruptcy in the first place" Malito, *Municipal Bankruptcy*, *supra* note 4, at text accomp. note 144; *see also* Jonathan J. Spitz, Comment, *Federalism, States, and the Power to Regulate Municipal Bankruptcies: Who May Be a Debtor Under Section 109(c)?*, Comment, 9 Bankr. Dev. J. 621, passim (1993).
[146] McConnell & Picker, *supra* note 4, at 472.

operating budget, consolidate school districts with one another, require the reorganization of a school district's administrative or operational structure, or order that a school district raise taxes, issue bonds, or replace key decision makers.[147] Yet it is these sorts of changes that would address the systemic causes of a school district's fiscal difficulties, the causes which, when amplified by a recession, can lead to fiscal crisis.

Thus, while municipal bankruptcy does offer some advantages to cash-strapped school districts, those benefits almost always will be outweighed by the substantial costs—including the fundamentally poor fit between the aims of federal municipal bankruptcy and the problems of school districts' fiscal crisis. And because of the limitations imposed by the 10th Amendment, there is no way to transform federal municipal bankruptcy so that it is a better fit for school districts' needs. Accordingly, we turn to an examination of legal options available at the state level to assist school districts in fiscal crisis.

## B. Receivership

### 1. A Brief History of Receivership and School Districts' Experiences

In receivership, a fiduciary agent is appointed by a state court to manage a financially troubled legal entity. In a corporate receivership, a receiver typically manages a company with the goal of "maximizing [the] returns from [the corporation's] assets, thus stabilizing the company financially."[148] Traditionally, corporate receivership is more like Chapter 11 bankruptcy in that it usually is focused on reorganization, although sometimes the receiver

[147] McConnell & Picker, *supra* note 4, at 435*;* Malito, *Municipal Bankruptcy*, *supra* note 4, at text accomp. note 105-06.
[148] Ken Philip & Kerin Kaminski, *Receivership: A Value-Adding Tool*, The Secured Lender, 30 (Jan./Feb. 2007).

decides that the best course of action is to liquidate assets and wind up the business.[149] Of course, for a municipality such as a school district, winding up business is not an option (unless a school district is consolidated with one or more contiguous districts, of course) and thus a receiver must pursue the same reorganization-type goals as in a municipal bankruptcy proceeding.

Municipal receivership has existed since the 1870s, when Missouri became the first state to enact a statute permitting municipal receivership.[150] A few other states adopted municipal receivership legislation during the last few decades of the 19th Century, but most adopted such legislation, like federal municipal bankruptcy legislation, during the Great Depression.[151] Although 48 states now authorize some municipalities to be put into receivership, the eligible municipalities usually are public utilities—only two states specifically authorize public school districts to be put into receivership.[152]

### 2. Benefits and Disadvantages of Municipal Receivership

The main difference between municipal bankruptcy and municipal receivership is that a receiver's authority to change a municipality's internal practices is much more far-reaching than

[149] *Id.*
[150] Tennessee was the first state to impose municipal receivership, disincorporating the city of Memphis in 1879. McConnell & Picker, *supra* note 4, at 436.
[151] *Id.*
[152] M. David Gelfand, *State and Local Government Debt Financing Database*, James E. Spiotto, Chapter 13: Municipal Insolvency: Bankruptcy, Receivership, Workouts, and Alternative Remedies, II. Chapter 9 of the Bankruptcy Code, 13:39 fn.1 (Dec. 2009) (Kentucky and Pennsylvania).

Arizona calls its takeover mechanism "receivership," but this mechanism is overseen by the state education bureaucracy, not the courts. Thus, it is not "receivership" in the traditional sense discussed in this section. A.R.S. 15-103 & 15-107; Pat Kossan, *Colorado City School District Faces Bankruptcy*, Az. Repub., Aug. 12, 2005.

a bankruptcy court's.[153] Thus, a receiver can interrupt the "ordinary political processes" and incidents of mismanagement which often contribute substantially to municipal fiscal crisis.[154] Because receivership has its genesis in state law and thus is not constrained by the Tenth Amendment, in numerous ways, it is more flexible than bankruptcy.[155] Also, it brings the benefit of expertise—in the corporate context, a receiver "should be a skilled turnaround consultant,"[156] and fortunately for school districts this concept of a turnaround consultant is familiar to education as well.[157] Thus, states could select receivers who have in-depth knowledge about public education, educational policy, and best fiscal practices in school districts.

However, while receivership is theoretically a better fit than bankruptcy for most school districts in fiscal crisis, it also has major drawbacks for districts. First, receivership may not be as expensive as bankruptcy, but it still is not without some financial cost (as in bankruptcy, this consists of the cost of outside counsel as well as the diverted attention of district administrators).[158] Second, receivership involves the more stringent and extensive procedures of court oversight when the looser procedures of administrative agency oversight may well be sufficient. Third, receivership is a procedure rarely used in the U.S., and thus while receivers may bring subject matter expertise, courts "often do not have extensive experience or precedent relating to receiverships"[159]— this seems especially likely in the rare and unusual context of municipal receivership.

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[153] Ted Hampton, *Receivership an Alternative to Filing Chapter 9 for Troubled Cities, But It's Not Without Costs*, The Bond Buyer, 1 (June 24, 1991).
[154] McConnell & Picker, *supra* note 4, at 472.
[155] Philip & Kaminski, *supra* note 148, at 30.
[156] *Id.*
[157] See, e.g., EdVenture, http://www.theedventuregroup.org/consulting.html?gclid=CN_Iy-DhrKACFQOfnAodx0z1Zg. Not all turnaround firms may be what they seem, though. As of August 2010, the U.S. House of Representatives planned to hold hearings to review turnaround firms. Dakarai I Aarons, *House Panel to Examine Turnaround Firms*, Educ. Week, 5, Aug. 25, 2010.
[158] Philip & Kaminski, *supra* note 148, at 30.
[159] *Id.*

Thus, similar to federal municipal bankruptcy, state receivership could be advantageous to school districts in fiscal crisis, but at best it is not a widely tested legal mechanism and at worst it may cause new problems even while it solves others. In part, it is not surprising that neither federal municipal bankruptcy nor state receivership present a good mechanism for addressing school districts' fiscal crises—they were not designed to address these problems or these contexts. Accordingly, the next section turns to a procedure that was specifically designed to address school districts needs.

C. State Fiscal Takeover of School Districts

1. A Brief History of State Fiscal Takeover and School Districts' Experiences

State statutes and regulations authorizing the "takeover" of major school district administrative functions have emerged over the past thirty years. Today, 33 states authorize a state or mayoral takeover of a local school district for academic and/or fiscal reasons.[160] Seventeen of those 33 states authorize a takeover due to a school district's fiscal crisis, while 16 limit a takeover to situations of academic crisis alone.[161] School district takeovers are more common than school district bankruptcy filings, but they are still quite rare: only 73 takeovers have occurred over the past 30 years.[162] In 43% (31) of these instances, the takeover was

[160] *See* Appendix. In 1989, only six states authorized state takeover of school districts. Patricia Cahape Hammer, *Corrective Action: A Look at State Takeovers of Urban and Rural Districts*, AEL Policy Briefs 2 (July 2005).
[161] *See* Appendix.
[162] Joseph O. Oluwole & Preston C. Green, III, *State Takeovers of School Districts: Race and the Equal Protection Clause*, 42 Ind. L. Rev. 343, 363-394 (2009).

triggered primarily because of the district's fiscal distress; in 30% (22) of the instances, the takeover was comprehensive (focusing on academic, management, and fiscal problems); in 4% (3) of the instances, the takeover began as fiscal-only but became comprehensive; and in 23% (17) of the instances, the takeover did not directly address the district's fiscal health but focused on academic or management problems.[163] Prior to the mid-1990s, most takeovers focused solely on reforming school districts' finances; since then, more takeovers have been comprehensive.[164] However, we likely are entering another period during which an increasing number of takeovers will be triggered in substantial part by fiscal crises.

There is great variation among statutes and regulations in the 17 states which authorize state takeover for fiscal reasons, but the most comprehensive takeover statutes and/or regulations share the following six elements: First, they list specific factors which can trigger state investigation or involvement, such as a school district running a deficit and not having a plan to remedy the situation; failing to pay employees' wages or retirement benefits; failing to pay bond debt service; or declaring a fiscal emergency.[165] Second, they try, at the start, to solve the district's fiscal problems at the district level with the state involved only in an advisory capacity. For example, a financially troubled district could be required to work with a state-approved expert to generate a fiscal plan and submit it to the state board of education; if the state board accepts the plan and the school district is able to implement it, the state does not become

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Takeovers are more likely to occur in major cities and rural areas than in suburban areas. Thirteen of the nation's largest urban districts have been taken over by the mayor or the state in the past twenty years. Black, *The Takeover Threat*, *supra* note at 34.

[163] The calculations presented above the line in this article are summaries of the data discussed by Oluwole and Green. Oluwole & Green, III, *supra* note 162, at 363-394 (2009).

Takeovers are more likely to occur in major cities and rural areas than in suburban areas. Thirteen of the nation's largest urban districts have been taken over by the mayor or the state in the past twenty years. Black, *The Takeover Threat*, *supra* note 162, at 34. The scope of a takeover influences its duration: takeovers focused on districts' fiscal problems are shorter than those with a more comprehensive focus. Hammer, *supra* note 160, at 3.

[164] Kenneth K. Wong & Francis X. Shen, *City and State Takeover As a School Reform Strategy*, ERIC Clearinghouse on Urban Education, No. 174, July 2002.

[165] *See, e.g.*, M.C.L.A. 141.1231-1244 (Michigan); West's F.S.A. § 218.503 (Florida); A.C.A. 6-20-1900-11 (Arkansas).

involved any further.[166] Third, the relevant statutes and regulations contain a framework in which the state's involvement will escalate if the district's fiscal condition continues to be poor, or worsens.[167] Fourth, they make clear who will have authority to intervene in a school district's affairs at a certain point, and/or how that agent will be selected—is it an emergency financial manager selected by the legislature and the governor, a fiscal oversight board selected by the state board of education, a multi-member group selected in part by a local court, or something else entirely?[168] Fifth, the relevant statutes and regulations describe the extent of the agent's authority and set forth an illustrative list of actions the agent may take. The agent may have the authority of a superintendent, a new CFO, or even a school board; it may create a new budget, borrow money, negotiate or renegotiate contracts including collective bargaining agreements, recommend that the state dissolve the school district and consolidate it with adjacent districts, and many more things.[169] And sixth, although these plans may expect the state to subsidize the cost of additional human resources they supply to a district, they do *not* necessarily involve education "bailout" funds supplied by the state.

### 2. Benefits and Disadvantages of Takeovers

The main proven benefit of takeovers is that they fairly consistently have been able to achieve the goal of increased fiscal stability at the district level, which is no small thing for a

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[166] *See, e.g.*, Cal. Ed. Code 1630, 41320, 41326 (California); 105 ILCS 5/1A-8, 1B1-22 (Illinois); Miss. Code Ann. § 37-17-6.

[167] *See, e.g.*, Ala. Code 16-6B-4 (Alabama); KRS 158.785, 158.780(1) (Kentucky); R.C. 3316.03-05 (Ohio); Tex. Educ. Code 39.102 (Texas); W.Va. Code 18-2E-5 (West Virginia).

[168] *See, e.g.*, M.C.L.A. 141.1231-1244 (Michigan); 105 ILCS 5/1A-8, 1B1-22 (Illinois); 24 P.S. 6-692 (Pennsylvania)

[169] *See, e.g.*, West's F.S.A. 218.503 (Florida); W.Va. Code 18-2E-5 (West Virginia); Preston C. Green, III, Joseph O. Oluwole & Bruce D. Baker, *No School Left Behind: Providing Equal Educational Opportunities*, 12 J. Gender Race & Just. 285, 297 (2009); Todd Ziebarth, *State Takeovers and Reconstitutions: Policy Brief*, 1 (2002, updated March 2004); Oluwole & Green, III, *State Takeovers of School Districts*, *supra* note 162, at 396.

school district in fiscal crisis.[170] In fact, the consensus in the limited literature is that fiscal stability is much easier to achieve than academic improvement.[171] In a way, this is not surprising—the former is much more straightforward than addressing the countless factors which influence the latter.[172]

However, takeovers, too, have substantial drawbacks. But before reaching those, it is important to note that unlike bankruptcy, which a district voluntarily, if regretfully, selects, state intervention and takeover are involuntary for a district. As this article will discuss, this is both the greatest strength and the most complicating drawback of the takeover mechanism. More specific drawbacks are as follows: First, depending on the statutory/regulatory structure providing for a takeover, the decision about whether to initiate a takeover either can be ad hoc or phrased in the most general of terms so that state involvement is viewed as a politically-motivated decision.[173] More specifically, if the district is racially isolated, as so many districts are, members of the community may question whether the state intervention is racially-motivated.[174] Second, the impact of takeovers on student achievement is inconclusive at best, thus comprehensive takeovers are much more likely to generate fiscal stability than academic success, and challenges in the latter could prolong state involvement.[175] Third and probably most

[170] Eugene Judson, Phyllis Schwartz, Kimberly Allen & Tommie Miel, *Rescuing Distressed Schools*, Am. Sch. Bd. J. 42 (April 2008); Del Stover, *Take It To The Limit*, Am Sch. Bd. J. 33 (Nov. 2007) (discussing the fiscal success of mayoral takeover in Chicago); David R. Berman, *Takeovers of Local Governments: An Overview and Evaluation of State Policies*,25 Publius 55, 66 (1995) (discussing two districts in New Jersey); Ziebarth, *supra* note 169.

[171] Patricia Cahape Hammer, *Corrective Action: A Look at State Takeovers of Urban and Rural Districts*, AEL Policy Briefs 2 (July 2005); Ziebarth, *supra* note 169.

[172] Stover, *supra* note 170, at 33 ("limited financial resources, coupled with the effects of poverty and high populations of limited English-proficient students, make significant academic gains challenging to any school leadership, regardless of its composition or governance structure."); Fahim, *supra* note 170.

[173] Kimhi, *Reviving Cities*, *supra* note 57, at 654.

[174] Oluwole & Green, III, *supra* note 162, at 405 (investigating this claim of racially-motivated state takeovers, and finding it overwhelmingly not to be the case).

[175] Judson et al., *supra* note , at 42; Stover, *supra* note 170, at 33; Glenn Cook, *Taking Charge*, Am. Sch. Bd. J. (Dec. 2002); Berman, *supra* note 170, at 66; Ziebarth, supra note 169. There is little research on the impact of takeovers beyond an assessment of student performance on standardized or standards-based tests, and that research shows little or no improvement resulting from takeovers. Black, *The Takeover Threat*, *supra* note 162, at 34.

important is the incredible level of local resistance that can face an agent in charge of overseeing the takeover.[176]

The Detroit Public Schools demonstrate both the advantages and especially this last disadvantage of the takeover approach.[177] However, it is important to keep in mind that the dynamics at work in the DPS takeover are amplified by a long history of what some would describe as racially-tinged acrimony between the city of Detroit and the rest of the state.[178] In spring 2009, Michigan Governor Jennifer Granholm appointed veteran public administrator Robert Bobb as the DPS emergency financial manager. Bobb had not only a background as the city administrator and deputy mayor of Washington, D.C., but he also had been president of the D.C. school board and was a graduate of an urban superintendents academy.[179] In short, Bobb brought municipal financial management experience to the table as well as a nuanced understanding of challenges facing urban public schools—a unique combination and one which prepared him well to take on the fiscal leadership of DPS. Since his appointment, Bobb has instituted many changes, beginning with an intensive audit of the district in which forensic accountants discovered 257 "ghost" employees receiving paychecks from DPS.[180] He also has

[176] Philip Kloha, Carol S. Weissert & Robert Kleine, *Someone to Watch Over Me: State Monitoring of Local Fiscal Conditions*, 35 Am. Rev. of Pub. Admin. 236, 237 (2005); Berman, *supra* note 170, at 67.
[177] Although most state-authorized takeovers arise out of statutes or regulations designed specifically for states and enacted in the past few decades, some arise out of more general municipal fiscal distress procedures, as in Michigan. Hampton, *supra* note153, at 1; Daniel J. Freyberg, Comment, *Municipal Bankruptcy and Express State Authorization to be a Chapter 9 Debtor: Current State Approaches to Municipal Insolvency—And What Will States Do Now?*, 23 Ohio N.U. L. Rev. 1001, 736-37 (1997); Kimhi, *Reviving Cities, supra* note 57, at 654. In Michigan, the governor can appoint a financial review board or manager to assume financial control of a municipality—including a school district—in fiscal crisis. The governor's use of this procedure in 2009 commenced the second state takeover of the Detroit Public Schools in recent memory.
[178] Dante Chinni, *Along Detroit's Eight Mile Road, Stark Racial Split*, Christian Science Monitor (Nov. 15, 2002).
[179] Aarons, *Decline and Fall*, *supra* note 127, at 24, 26, 27.
[180] Kellogg, *Detroit Schools on the Brink*, *supra* note (a former payroll manager and another individual were indicted in May, 2009 on charges of embezzling roughly $400,000 since 2005).

made many programmatic and capital changes in a district whose student enrollment was roughly 77,000 students in fall 2010—less than half what it was in 2001.[181]

The district still faces epic fiscal challenges, though, including running a deficit of $363 million dollars as of late 2010—$140 million more than in mid-2009, when Bobb took the helm.[182] This deficit keeps growing at a time when the population of the school district and the community are plummeting and district revenues are expected to keep falling.[183] That particular challenge is more unique to DPS, but this one is not: Bobb's tenure at DPS also indicates how resistant the local government can be to state involvement in education. Over the course of one year, the school board has sued him twice, first claiming in August 2009 that Bobb's academic reforms exceeded his authority as emergency financial manager, and more recently in March 2010 alleging that Bobb violated state ethics rules by accepting part of his salary from a foundation.[184] The strength of the local resistance may be in part because Bobb actually has the authority to disrupt the processes of politics and mismanagement which helped drive DPS to the brink of disaster even before the recession hit.

Thus, while state takeovers hold much more promise for assisting school districts in fiscal crisis than bankruptcy or receivership, they, too, are not without drawbacks.

### D. Summary

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[181] Aarons, *Decline and Fall*, *supra* note 127, at 24, 26; Candice Williams, *College Scholarship Program Expands to All DPS Students*, The Detroit News, Oct. 5, 2010.
[182] Alex P. Kellogg, *Schools Learn to Survive*, Wall St. J., Aug. 9, 2010.
[183] Alex P. Kellogg, *Detroit Schools in Financial Rut Despite Cuts*, Wall St. J., July 1, 2010, at A2; Diane Bukowski, *DPS Debt Balloons*, Michigan Citizen, July 18, 2010, at A1.
[184] Aarons, *School Transformation*, *supra* note 45, at 1, 12; Corey Williams, *Manager to Move Ahead With Detroit Closings*, Bloomberg Businessweek, Apr. 21, 2010. In the most recent chapter in the showdown between Bobb and the Board, the Board contested (in court, of course) Bobb's authority to terminate the superintendent's contract. Hours after the local trial court determined that Bobb did have that authority, he sent a letter to the superintendent terminating her. Chastity Pratt Dawsey, *DPS's Bobb Terminates Superintendent Guyser*, Detroit Free Press, June 30, 2010.

In sum, federal and state law contain three means of assisting school districts in fiscal crisis, none of which are an ideal solution to school districts' problems. First, although municipal bankruptcy has the advantages of restructuring a district's debt and unilaterally renegotiating its CBAs, ultimately bankruptcy proceedings cannot reach far enough to fundamentally restructure a school district in ways necessary to interrupt problems driven by politics or mismanagement. As a result, in the 24 states where bankruptcy is an option for school districts, it is a bad option. Second, state receivership has more flexibility and the potential to create greater systemic change than the bankruptcy process, but is only available to school districts in 2 states; almost entirely untested in the case of school districts' fiscal crises; and even when available likely triggers more court involvement than necessary. Third, fiscal takeover mechanisms, like receivership, can address root causes of fiscal crisis better than bankruptcy; they are much more common than receivership and have had respectable success in stabilizing districts financially. But, they are available in quite varied forms in 17 states, and when employed they can face high levels of local resistance. Furthermore, 19 states school districts do not have access to even one of these three imperfect options. Taken together, states as a whole do not provide anywhere near sufficient support for the increasing number of school districts facing or nearing fiscal crisis across the country.

## III. THE PROPOSAL: STATE FISCAL ACCOUNTABILITY IN EDUCATION

The recent recession's impact on school districts has illuminated a number of systemic defects and situational challenges in school finance. It also has cast light on many school districts' inability to adjust and weather difficult financial times, and the inadequacy of legal mechanisms in most states to assist school districts in fiscal crisis. Because school districts are experiencing many of the same types of problems all across the country, a long-term, nation-wide solution is needed.

Accordingly, in this section I first analyze the federal government's strong interest in the fiscal stability of school districts in all 50 states. Second, I make the case for a federal requirement for individualized state plans which demonstrate states' fiscal accountability for federal education dollars. Third, I propose model federal legislation so that these plans are imposed as a condition of funding under the Elementary and Secondary Education Act (ESEA), which is expected to be amended and reauthorized in 2011, and again roughly every five years after that.[185] The state plans should have three aspects: (1) help school districts create cost savings immediately, (2) monitor school districts' fiscal health and intervene when districts approach and enter fiscal crisis, and (3) attempt to stabilize state-level education funding long-term. Importantly, these options are not intended to facilitate a further education "bailout"—none of the options are intended to allow or require a state to buoy a district with an infusion of cash. This becomes clear as, in the final part of this section, I briefly discuss a variety of policies that states could use to satisfy the obligations I propose.

### A. Why a Federal Requirement for a State Plan?

[185] No Child Left Behind Act, 20 U.S.C. §§ 1041–1044, 3427, 6052, 6053e, 6054b, 6055h, 6056a (2006) (amending the Elementary and Secondary Education Act of 1965, 20 U.S.C. §§ 6301–6578); Donald M. Payne, *Reauthorization of the Elementary and Secondary Education Act: Challenges Throughout the Legislative Process*, 26 Seton Hall Legis. J. 315, 316 (2002).

Education may be the quintessential local issue, but the federal interest in fiscally stable school districts is strong as well. In short, much like a family must know that it can pay its rent or mortgage before considering whether a child should play soccer or learn the violin, school districts must be fiscally stable before they can implement meaningful educational reforms that improve educational quality and thus help create local, state, and nationwide economic and civic benefits.[186] In 2009, "relatively few" school districts reported to the Government Accountability Office that they were "making significant progress" in achieving federal education reform goals.[187] That same year, 3% of districts reported that they had decreased Title I-related reform efforts compared to the previous year; before the 2010 stimulus funding passed, 11% of districts reported that they planned to decrease Title I-related education reform efforts during FY 2011.[188]

The economic and civic effects of stagnant and declining educational quality are a substantial federal concern in part because 63% of all adult Americans have moved away from the community where they were born and 43% of adult Americans have left the state where they were born.[189] Thus, local communities are less and less often the direct, long-term beneficiaries of the education they give to the children in their community, especially because the more educated an individual is, the more likely he or she is to move out of town or out of state.[190] Additionally, whether or not individuals move, their ability to contribute to the United States' global competitiveness and to meaningfully enjoy the rights of federal citizenship is the same. Accordingly, as I discuss in this section, the federal interest in financially stable schools is an interest in maintaining improving educational quality through reform, which is driven by two

[186] Jacob E. Adams, Jr., *Where's the Smart Money in a Great Recession?*, Educ. Week 36, Sept. 15, 2010.
[187] GAO, *Recovery Act, supra* note 15, at 39 (As Adams notes, "states are unlikely to accomplish ambitious learning goals until they fix the finance systems that support the nation's schools.").
[188] *Id.* .
[189] D'Vera Cohn & Rich Morin, *American Mobility: Who Moves? Who Stays? Where's Home?*, 1, Pew Research Center, Dec. 29, 2008.
[190] *Id.* at 2.

main concerns: one economic, the other civic. In pursuit of the federal interest, there are many reasons for imposing a general federal requirement which allows states some policy-making leeway.

### 1. The National Economic Benefits of Strong Public Schools

In 1983, the U.S. Department of Education report "A Nation at Risk" called for a major investment in public education, arguing that the United States was being overtaken by global competitors and the eroding quality of our education system was a major factor in this shift.[191] Twenty-five years later in 2008, the U.S. Department of Education issued a follow-up report, contending that "if we were 'at risk' in 1983, we are at even greater risk now"[192] and acknowledging that U.S. students have been "at best[] running in place, while other nations are passing us by."[193] The report noted that only roughly 70% of U.S. students complete high school within four years.[194] Graduating from high school has a dramatic impact on an individual's earnings[195] as well as a larger economic impact which Goodwin Liu has summarized:

> Increases in schooling have long been associated with reduced crime, incarceration, and related costs, and with greater political participation and likelihood of voting. Educational attainment is also positively associated with lower utilization of public health insurance, cash assistance, food stamps, and

[191] U.S. Department of Education, National Commission on Excellence in Education, *A Nation at Risk: The Imperative for Educational Reform*, (1983), *available at* http://www2.ed.gov/pubs/NatAtRisk/index.html.
[192] U.S. Department of Education, *A Nation Accountable: Twenty-five Years After A Nation at Risk*, 1 (2008), *available at* http://www2.ed.gov/rschstat/research/pubs/accountable/accountable.pdf.
[193] *Id. See also* Superfine, *supra* note 27, at 656.
[194] This statistic varies widely by racial/ethnic group, with four-year completion rates for African-Americans and especially Latinos/as being much lower than for Whites still today. U.S. Department of Education, *supra* note 9; Kristi L. Bowman, *Pursuing Educational Opportunities for Latino/a Students*, 88 N.C. L. Rev. 912, 938-940, 942 (2010).
[195] *Id.*

public assistance. . . . [A]nnual losses in federal and state income taxes due to high-school noncompletion, aggregated over all working age adults 'likely exceed $50 billion'—enough to cover the annual discretionary expenditures of the U.S. Department of Education.[196]

Not surprisingly, improving public education has been, in the words of a 2010 Brookings Institute report, "no less than a public policy obsession for many public- and private-sector leaders, at all levels of the system."[197] The report continues:

> [This focus is] with good reason—the rising human capital levels of our population explained much of America's economic success in the 20th century, and will probably be an even more important contributor to our standards of living into the future.[198]

Similarly, when the *Wall Street Journal* asked a group of CEOs in late 2009 about their ideas for rebuilding global prosperity, the CEOs ranked education second only to sustainable job creation.[199] U.S. Secretary of Education Arne Duncan wrote in 2010 that "to maintain our competitive advantage in knowledge-based industries and fields, the United States must implement an education policy that produces a 'more flexible labor force that can cope more readily with non-routine tasks and occupational change.'"[200] Federal Reserve Chairman Ben Bernake stated, when speaking to the U.S. Chamber of Commerce in 2007, that:

> Economists have long recognized that the skills of the workforce are an important source of economic growth. Education fundamentally supports increases in

[196] Goodwin Liu, *Interstate Inequality in Educational Opportunity*, 81 N.Y.U. L. Rev. 2044, 2113, 2125-26 (2006); *see also* Arne Duncan, *Through the Schoolhouse Gate: The Changing Role of Education in the 21st Century*, 24 Notre Dame J. L. Ethics & Pub Pol'y 293 (2010).
[197] Brookings Metro America, at 160.
[198] *Id.*
[199] William Cibes, *Your View*, Hartford Courant, Dec. 1, 2009, at A11.
[200] Arne Duncan, *Through the Schoolhouse Gate: The Changing Role of Education in the 21st Century*, 24 Notre Dame J. L. Ethics & Pub Pol'y 293 (2010).

productivity, upon which our ability to generate continued improvement in our standard of living depends.[201]

For all of these reasons, the Brookings Institute advises: "Over the longer run, educational policies that prepare a larger segment of the workforce to serve in higher-paying industries and occupations are [a] wise investment."[202] Yet, the percentage of younger adults who have completed college has been falling, and this has led to a situation where national averages show that more middle-aged workers are better educated than younger ones.[203] This varies by region and in part is a result of where college-educated adults choose to live.[204] Not coincidentally, the regions with less-educated workers have many of the highest rates of unemployment—and the education and employment disparities between the "haves" and "have nots" of metro areas and regions are expected to grow, unless deliberate public policy initiatives counteract these trends.[205] These regional trends could dovetail in dangerous ways with the earlier-discussed demographic changes anticipated to occur in public schools—the increasing population of disadvantaged students, especially in disadvantaged communities—producing an even larger gap in educational equity and economic achievement than currently exists.[206] The federal government's goal of ensuring the United States' continued global competiveness and prosperity is also linked to an interest in deterring these regional disparities. For education to affect regional, national, or global prosperity, school districts must implement substantial reform. And before they can focus on reform, districts must have a foundation of fiscal stability.

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[201] Ben S. Bernake, *Education and Economic Competitiveness*, Speech to the U.S. Chamber of Commerce on September 24, 2007, *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20070924a.htm; Duncan, *supra* note 196, at ("the correlation between education and economic success is strong").
[202] Brookings Metro America, *supra* note 197, at 161.
[203] *Id.* at 107.
[204] *Id.* at 109-110.
[205] *Id.* at 115-16; Michael Greenstone, *Evidence From May's Employment Numbers on the Benefits of Education*, Brookings Blog, June 4, 2010 ("job opportunities are increasingly concentrated in relatively high-skill, high wage jobs and low-skill, low wage jobs.").
[206] *See supra* Section I.B.2.c.

### 2. Federal Constitutional Citizenship

In 1979, the Supreme Court wrote: "The importance of public schools in the preparation of individuals for participation as citizens . . . has long been recognized by our decisions." [207] To be sure, there is no presently-recognized fundamental federal right to education,[208] but taken together, the Court's jurisprudence demonstrates a strong federal interest in the public good of an educated citizenry—people who can contribute constructively to public debate, meaningfully exercise their own federal constitutional rights, and participate in and ultimately sustain a democratic government.[209] Like economic benefits, civic benefits inure to the federal

[207] Ambach v. Norwalk, 441 U.S. 68, 76-77 (1979).

[208] Professor Goodwin Liu has written about the Fourteenth Amendment's citizenship clause giving rise to a Congressional obligation to "ensure a meaningful floor of educational opportunity throughout the nation." Liu, *Education, Equality, and National Citizenship*, *supra* note 38, at 334.

[209] The long line of cases discussing the relationship between education and citizenship has three primary parts. The first part addresses the creation or nurturing of nationalism. *See, e.g.*, Pierce v. Society of Sisters, 268 U.S. 510, 534 (1925); Minersville v. Gobitis, 310 U.S. 586, 598 (1940); West Virginia v. Barnette, 319 U.S. 624, 637 (1943).

The following excerpt from *Brown* is not the decision's most famous language, but it was a necessary premise for *Brown*'s ultimate conclusion because it explained why denying some children a quality education mattered:

> Compulsory school attendance laws and the great expenditures for education both demonstrate our recognition of the importance of education to our democratic society. It is required in the performance of our most basic public responsibilities, even service in the armed forces. It is the very foundation of good citizenship. Today it is a principal instrument in awakening the child to cultural values, in preparing him for later professional training, and in helping him to adjust normally to his environment. In these days, it is doubtful that any child may reasonably be expected to succeed in life if he is denied the opportunity of an education.

Brown v. Board of Education, 347 U.S. 483 (1954). See discussion of the same in Wisconsin v. Yoder, 406 U.S. 205, 221 (1972); Ambach v. Norwalk 441 U.S. 68, 76-77 (1979). This language was quoted in Board of Education v. Pico, 457 U.S. 853, 864 (1982), quoted in Board of Education v. Mergens, 496 U.S. 226, 265 (1990) (Marshall, J., concurring); Board of Education v. Pico, 457 U.S. 853, 876 (1982) (Blackmun, J., concurring); Plyler v. Doe, 457 U.S. 202, 221 (1982).

Additionally, some of the Court's First Amendment cases specifically focus on the idea that students are citizens-in-training, practicing the exercise of their rights in public schools. The above-cited language from *Barnette* has appeared in the majority opinion in the seminal 1969 student free speech case, *Tinker v. Des Moines,* Tinker v. Des Moines, 393 U.S. 503, 507 (1969), the majority opinion in a 1982 case permitting [insert Pico holding], *Board of Education v. Pico,* Board of Education v. Pico, 457 U.S. 853, 864 (1982), Justice Stevens' 1990 dissent in Board of Education v. Mergens, Board of Education v. Mergens, 496 U.S. 226, 290 (1990) (Stevens, J., dissenting), and Justice Ginsburg's 2002 dissenting opinion in a student search and seizure case, *Board of Education v. Earls,* Board of Education v. Earls, 536 U.S. 822, 855 (2002) (Ginsburg, J., dissenting).

government as well as state and local governments, which are the entities primarily responsible for funding and providing education.[210] They also apply to all citizens, whether or not they move out of the state in which they were born.

Admittedly, school districts' fiscal crises will not result in the federal government receiving no economic or civic benefits—students enrolled in school districts that are in fiscal crisis will still receive some sort of education. But, districts' fiscal crises will inevitably weaken districts' ability to maintain their preexisting level of educational quality, let alone fulfill education reform priorities identified by the federal government. In a district in fiscal crisis, the extent to which schools are able to prepare students for a global workforce and federal citizenship by providing a high-quality education will decrease, and although the drop will be difficult if not impossible to measure, that does not mean the effects are insignificant.

#### 3. Individualized State Plans

Even though the federal government has a strong interest in the existence of fiscally strong schools that can implement reform, this does not mean that a uniform federal solution to the problem of school districts' fiscal crises should follow from that interest. In this section, I discuss four reasons why the legislation proposed below requires each state to develop its own plan to assist school districts in current and future fiscal crises.

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The civic lessons learned while participating in school were also at issue in *Hazelwood v. Kuhlmeier*, but in a less overt way. The Court held that a school principal's decision to censor portions of the school newspaper before publishing did not violate students' free speech rights. Justice Brennan, disputing this holding, wrote in dissent: ""Public education serves vital national interests in preparing the Nation's youth for life in our increasingly complex society and for the duties of citizenship in our democratic Republic." Hazelwood School District v. Kuhlmeier, 484 U.S. 260, 278 (1988) (Brennan, J., dissenting). Bethel School District v. Fraser, 478 U.S. 675, 681, 683 (1986), quoted in Board of Education v. Earls, 536 U.S. 822, 840 (2002) (Breyer, J., concurring); Lee v. Weisman, 505 U.S. 577, 590 (1992).

[210] Brown v. Board of Education, 347 U.S. 483 (1954); U.S. v. Lopez (both describing education as a traditional state function).

First, some sort of a federal requirement is necessary because the federal interests discussed above should not be satisfied in some states but not others. Right now, 33 states do not authorize state involvement in school districts' fiscal crises at all.[211] That number includes the 19 states in which school districts in fiscal crisis are not able to take advantage of *any* legal mechanisms to help them cope with fiscal crisis.[212] The solution need not be the same in every state, but the problem must be addressed in all states. To achieve this goal, I propose legislation that is written to be part of Title I of NCLB/ESEA, which provides $15 billion to public schools annually.[213] Although the conditions in NCLB are onerous, no state has yet opted out of NCLB/ESEA and refused these funds.[214] Especially in the current economic climate, it seems highly unlikely that a state would start to opt out of NCLB/ESEA at this point.

Second, this approach of a federal requirement for a state policy is consistent with federal education policy more generally. Ultimately, my proposed legislation is about accountability, which on the academic front has been a growing focus of federal education policy since the 1980s.[215] And, the accountability is accomplished through spending conditions, which are common in federal legislation in general and have become increasingly common in federal education legislation over the past few decades.[216]

Third, like many of the NCLB conditions, my proposed legislation also involves significant deference to states and thus allows states to satisfy the purpose of the conditions in a

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[211] *See* Appendix.
[212] *See* Appendix.
[213] U.S. Dept. of Education, Budget Summary and Background Information, Fiscal Year 2011, Summary of Discretionary Funds, Appendix 1, *available at* http://www2.ed.gov/about/overview/budget/budget11/summary/appendix1.pdf
[214] Jane Gordon, *Towns are Rejecting No Child Left Behind*, N.Y. Times (Dec. 21, 2003); Lei Zhou & Frank Johnson, *Revenues and Expenditures for Public Elementary and Secondary Education: School Year 2007-2008*, 6 (May 2010), available at http://nces.ed.gov/pubs2010/2010326.pdf.
[215] *See, e.g.*, Superfine, *supra* note 27, at 673-74; Black, *The Congressional Failure to Enforce Equal Protection Through the Elementary and Secondary Education Act, supra* note 38, at 371-72.
[216] David Engdhal, *The Contract Thesis of the Federal Spending Power*, 52 S.D. L. Rev. 486, 535 (2007).

way that makes sense given their unique demographics and dynamics.[217] As Michael McConnell, Randall Picker, and Omer Kimhi have convincingly argued, compared to federal law, state law is much better suited to the task of addressing municipal fiscal crisis.[218] Therefore, in the proposed legislation I set out statutory language which, for two of the three requirements, includes not only several options for compliance but also a provision which permits the U.S. Department of Education to approve alternatives proposed by the states, as it does with some aspects of NCLB.[219] And even for the third requirement, states are expected to develop their own way of complying with the terms.[220]

Fourth, a general federal requirement also gives states political cover to enact controversial policies during difficult economic times. States, too, have a strong interest in the fiscal health of school districts—not only can a bankrupt school district affect the credit rating of the rest of the state, but all states' constitutions also contain provisions establishing some right to an education, however limited.[221] States also have an interest in helping communities maintain schools that are good enough to retain their population, if not even attract new residents.[222] And

[217] Brookings Metro America, *supra* note 197, at 162 ("National policy responses must recognize the diverse starting points of metropolitan areas and, where necessary, ensure that interventions are tailored to those differing on-the-ground realities.... Because [the 100 largest metro areas] pulled even farther apart from one another on several dimensions of the new realities in the 2000s, federal policy alone cannot provide a solution tailored to each metropolitan area's individual situation. Therefore, leaders at the state, regional, and local levels must now more than ever understand and respond purposefully to the demographic, social, and economic changes most affecting their places.").

[218] Kimhi, *Reviving Cities*, *supra* note 57; Kimhi, *Chapter 9, supra* note 4.

[219] *See infra* Section III.B.1.

[220] *Id.*

[221] Baker, *What Do We Expect?*, *supra* note 27, at 318 n.5 (listing all such provisions).

[222]Otherwise, if poor-quality schools are one factor that helps drive away existing or potential residents, as in Detroit, the affected city or town will become hampered by a dwindling tax base, furthered limiting its ability to improve the government services which were already so bad they helped drive away residents. Kimhi, *Reviving Cities*, *supra* note 57, at 640. And, the city or town in effect will be shifting the burden of its residents to surrounding communities and thus potentially creating financial difficulties for those receiving municipalities as they struggle under the weight of an increased population. Kloha et al., *Someone to Watch Over Me, supra* note 176, at 237; Bowman, *Rebuilding Schools, Rebuilding Communities*, *supra* note 35.

states are in a much better position than local districts to grapple with the systemic problems of mismanagement and politics.[223]

## B. Proposed Legislation

States should have substantial flexibility in fashioning the plans that will structure their involvement with school districts' fiscal difficulties. As the legislation proposed below will make clear, the plans must contain three crucial parts: (1) measures to assist districts in generating additional immediate cost savings; (2) plans to monitor when school districts are nearing fiscal crisis and to intervene when school districts approach or enter fiscal crisis; and (3) practices intended to stabilize education funding. This section sets forth proposed legislation and analyzes the validity of the legislation pursuant to the Spending Clause. The final section will briefly discuss the policies presented immediately below.

### 1. Proposed Legislative Text

The proposed legislation contained below would add a subsection to the text of Title I, Part A, Subpart 1 of the No Child Left Behind Act, which was signed into law in January 2002 as the most recent iteration of the 1965 Elementary and Secondary Education Act.[224] Subpart 1 contains the basic requirements for the compliance plans each state must submit to the U.S.

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[223] This may be especially true for urban districts, which are already financially burdened by having greater concentrations of disadvantaged students, and where problems of corruption often accompany the more common systemic deficiencies. Kimhi, *Reviving Cities*, *supra* note 57, at 636 (States have "both the legal authority and the political power to deal with the causes of urban crisis").

[224] No Child Left Behind Act, 20 U.S.C. §§ 1041–1044, 3427, 6052, 6053e, 6054b, 6055h, 6056a (2006) (amending the Elementary and Secondary Education Act of 1965, 20 U.S.C. §§ 6301–6578).

Department of Education as a condition of receiving its share of the $15 billion in annual Title I funding.[225] The proposed legislation is included below in bold text:

TITLE I—IMPROVING THE ACADEMIC ACHIEVEMENT OF THE DISADVANTAGED

PART A—IMPROVING BASIC PROGRAMS OPERATED BY LOCAL EDUCATIONAL AGENCIES

Subpart 1—Basic Program Requirements

SEC. 1111. STATE PLANS.

(a) PLANS REQUIRED

(b) ACADEMIC STANDARDS, ACADEMIC ASSESSMENTS, AND ACCOUNTABILITY

(c) OTHER PROVISIONS TO SUPPORT TEACHING AND LEARNING.

(d) PARENTAL INVOLVEMENT

**(e) FISCAL ACCOUNTABILITY.—Each State plan shall demonstrate that the State is a responsible steward of the funding allocated pursuant to this Act. Such a demonstration shall—**

**(1) Through legislation or regulation, enable school districts to create additional cost savings during FY 2012. Such cost savings shall be created by—**

**(A) Expanding the fiscal expertise available to school districts by—**

[225] Goodwin Liu, *Improving Title I Funding*, *supra* note 38, at 976.

i. **Entering into a long-term contract with an outside consulting agency with expertise in education policy and municipal finance, and partially subsidizing such consultants' interactions with school districts; or**

ii. **Approving partnerships between school districts and universities with education and municipal finance expertise for the purpose of studying the effect of cost-saving measures on student learning;**

**(B) Requiring the administrative or comprehensive consolidation of school districts with 1000 students or fewer;**

**(C) Permitting school districts to more easily outsource contracts for non-instructional services;**

**(D) Providing incentives for the reduction of school districts' salary expenses. Such reductions shall occur through the layoff of low-performing teachers regardless of seniority; or**

**(E) Satisfying the purposes of this part, (e)(1), as determined by the Secretary of Education and in accordance with such criteria as the Secretary establishes.**[226]

**(2) Through legislation or regulation, provide structural assistance to anticipate and assist school districts in fiscal crisis. Such assistance shall—**

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[226] The language for parts (e)(1)(E) and (e)(3)(D) is modified from No Child Left Behind, PUBLIC LAW 107–110, 115 STAT. 1425, (I)(A)(1)(113)(a)(7)(B).

**(A) Assess school districts' fiscal health on an annual basis. This assessment shall—**

**i. Be based on pre-determined criteria; and,**

**ii. Make public the names of the districts approaching and in fiscal crisis; and**

**(B) Determine a plan of escalating state intervention to assist a school district approaching and in a fiscal crisis.**

**(3) Through legislation or regulation, seek to stabilize education funding over the long term. Such stabilization shall—**

**(A) Set in place guaranteed state funding allocations, tied to the previous fiscal year;**

**(B) Create an adequately-funded state reserve fund for education which may not be used for other purposes;**

**(C) Create a system which allows school districts to insure against idiosyncratic risk of fiscal crisis;**

**(D) Authorize school districts to engage in private contracts to stabilize funding and regulate such financing arrangements; or**

**(E) Satisfy the purposes of this part, (e)(3), as determined by the Secretary of Education and in accordance with such criteria as the Secretary establishes.**

(f) PEER REVIEW AND SECRETARIAL APPROVAL

(g) DURATION OF THE PLAN

(h) PENALTIES

### 2. A Legitimate Exercise of Congressional Spending Power

Conditions on federal funding, like the ones proposed above, are incredibly common.[227] However, to be a valid exercise of Congress's spending power, legislation containing conditions must satisfy the four-part test laid out by the Supreme Court in 1987 in *South Dakota v. Dole*.[228] For the following reasons, this proposed legislation does so.

First, *Dole* requires that spending power legislation must "be in pursuit of 'the general welfare.'" [229] The term "general welfare" is expansive and easily includes public education. Second, the legislation must be "unambiguous" about the conditions it contains and the consequences of not complying with the conditions.[230] (The second prong of *Dole* has been given the most teeth, precedentially speaking, by the Supreme Court.[231]) Like some aspects of NCLB, the proposed legislation is specific about what is required of states yet for two of the three parts also permits the Department of Education to approve other types of compliance plans if they satisfy the same main goals of the proposal.[232] And, the consequences of non-compliance are present in the already-enacted legislation: the Department of Education has the authority to withhold funding from a state until it is satisfied that the state has provided a plan that complies with the requirements.[233] Third, the legislation must contain conditions that are related "to the

[227] Engdhal, *supra* note 216, at 535.
[228] Craig Eichstadt, *Twenty-Year Legacy of* South Dakota v. Dole, 52 S.D. L. Rev. 458, 458-59, 463-64 (2007). Eichstadt was counsel to the state of South Dakota in this legendary case.
[229] South Dakota v. Dole, 483 U.S. 203, 207-08 (1987).
[230] *Id.*
[231] Eichstadt, *supra* note 228, at 458-59; Black, *The Congressional Failure to Enforce Equal Protection*, *supra* note 38, at 332-33.
[232] The language for parts (e)(1)(E) and (e)(3)(D) is modified from No Child Left Behind, PUBLIC LAW 107–110, 115 STAT. 1425, (I)(A)(1)(113)(a)(7)(B).
[233] No Child Left Behind, PUBLIC LAW 107–110, 115 STAT. 1425, I.A.1.(g).

federal interest in particular national projects or programs." [234] The nexus between the condition and the federal interest in this situation is easily sufficient: the conditions require that states enact policies to ensure the current and future fiscal health of school districts. As discussed above, the federal government has a demonstrated interest in the fiscal stability of local districts across the country so that districts can implement reform in pursuit of federal economic and civic benefits.[235] Fourth, the legislation must not conflict with an "independent constitutional provision"[236] such as the First Amendment's Free Speech Clause or the Fourteenth Amendment's Equal Protection Clause. The proposed legislation has no such conflict. For these reasons, the proposed legislation is fully compliant with the requirements of *Dole*.

### C. Policy Proposals

This Section briefly discusses each of the policies included in the proposed legislation set forth above.[237] Importantly, because the proposed legislation permits states to satisfy the first and third conditions (creating additional immediate cost savings for districts, and seeking to stabilize educational funding) in ways not stated in the legislation, states should not be limited to the policy options discussed here. Similarly, although the proposed legislation requires states to have mechanisms for monitoring school districts' fiscal health and for intervening in school districts' fiscal crises, states retain substantial flexibility about the substance of those measures. To be sure, each of these policies is complex and this section is designed merely to introduce each topic and summarize its possible benefits and shortcomings. Many of the policy proposals contained

[234] South Dakota v. Dole, 483 U.S. 203, 207-08 (1987).
[235] *See supra* Section III.A.
[236] 483 U.S. at 207-08 ; *Dole* also contained a discussion focusing on coercion, but did not elaborate this or include it as part of the four-part test. *Id.* at 211.
[237] *See supra* Section III.C.1.

here are likely to be highly controversial, but as one commentator has noted, "it takes a crisis [like a recession] to shake up the equilibrium of policy decisions, budgetary commitments, and interest-group politics that supports education's business as usual" and to create substantial, lasting education finance reform.[238]

### 1. Ameliorating the Immediate Crisis

As is obvious, the recession has not spared school districts.[239] Because the effects of the recession are layered on top of the systemic problems of politics and mismanagement as well as the situational factors of pension fund shortfalls, litigation growing out of recession-driven cuts, and changing demographics, an increasing number of school districts are or will be nearing a point of fiscal crisis—and even those not in crisis are not doing all that well.[240] Accordingly, to address the problem of falling revenues, this first part of the proposed legislation calls for states to amend or adopt legislation or regulation which will enable school districts to create additional cost savings in FY 2012, which in most states will begin in July 2011.

The four short-term policy solutions discussed below are examples of policy approaches that may do this, depending on the unique environment of the state. As mentioned above and noted throughout this section, different approaches will be better suited to different states and the suitability may depend on factors such as the traditional relationship between the state and local governments; the demographics of the state—for example, whether it has a large urban and/or rural population; and the traditional strength of unions in a given state.

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238 Jacob E. Adams, Jr., *Where's the Smart Money in a Great Recession?*, Educ. Week 36, Sept. 15, 2010.
239 *See supra* Section I.A.1-2.
240 *Id.*

### a. Expand Available Human Resources

As the past few years have shown, many school districts lack fiscal sophistication.[241] This is not a problem most of the time, but the need for fiscal expertise has been especially acute during the past couple of years. Thus, states should endeavor to connect school districts in fiscal crisis with individuals who do have this unique sort of expertise.

As proposed above, a state could take at least two approaches in pursuit of this goal.[242] First, the state could enter into a long-term contract with an entity which would be able to provide well-trained consultants who could effectively assess a school district's fiscal state and make specific recommendations for meaningful fiscal and programmatic changes. Several existing entities are already well-positioned to fill this need: a regional educational laboratory which already serves multiple states,[243] a regional office of education which serves many counties within a given state,[244] or a national non-profit such as the RAND Corporation,[245] all could fill this role. Although it may seem that states should be able to provide this assistance directly, unfortunately they simply do not have the capacity or knowledge to do so on a large scale. To finance this long-term contract, Title I could allocate funding specifically to cover the state's additional cost of seeking and maintaining a contract, and help the state to partially subsidize districts' use of these services. Districts still would bear a good portion of the costs, however. Additionally, states and/or the federal government should make efforts to attract the

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241 Morgerson, *supra* note 66.
242 *See supra* text accompanying notes.
243 http://www.learningpt.org/rel/.
244 http://www.k12.wa.us/maps/ESDmap.aspx (Washington); http://www.isbe.state.il.us/regionaloffices/Default.htm (Illinois).
245 http://rand.org.

attention of major foundations which support educational reform and seek to engage many of those foundations in funding this effort.[246]

Second, another approach a state could take is to encourage formal partnerships between school districts and colleges or universities with the goal of studying the educational impact of certain cost-saving measures which are not believed or known to reduce academic quality.[247] One such notable partnership has grown out of a district takeover: Boston University managed the Chelsea Public School District for nearly a decade; the partnership was not without problems, but at the same time it was advantageous enough to both parties that they agreed to extend it for several years beyond the initial period. [248] A state could serve a clearinghouse function, gathering names of interested researchers and proposed research questions and making that information available to school districts. Or, it could let the partnerships happen organically. Regardless, if researchers are able to secure grant funding to study the effect of cost-saving education reforms, particular school districts would benefit in the short term by having strong connections to education researchers and possibly receiving additional funding related to the research. In the long term, school districts across the state and also the country would benefit from having more current, quality education research that is designed to study the relationship between certain cost-saving measures and student achievement.[249]

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[246] Before talking with Dr. Raegen Miller, I had proposed that states merely create ad hoc lists of people who were potentially able to perform these functions, such as former superintendents and university faculty, and make that information available to school districts. Our conversation convinced me not only that something more formal was needed, but also that identifying existing, outside organizations would be a good idea. Dr. Miller also helped me understand the necessity of funding such a program, and the potential for foundation support of this policy approach, as well. Interview with Raegen Miller, Sept. 27, 2010.

[247] Superfine, *supra* note 27, at 657-58, 690-92, 695-96 (noting the limited literature on the topic of the relationship between specific reforms and easily quantifiable results and discussing the limitations the educational context imposes on various types of research design, and calling for more research in this area).

[248] The calculations presented above the line in this article are summaries of the data discussed by Oluwole and Green. Oluwole & Green, III, *supra* note 162, at 405-06.

[249] Especially in emergency situations, it seems necessary to incentivize research. Six years after Hurricane Katrina hit the Gulf Coast, researchers bemoan the lack of research analyzing the innovative educational responses to the

b. Consolidate Districts with Fewer than 1000 Students

District consolidation is such an unpopular policy in small districts that it seems highly unlikely any districts would voluntarily enter into it. But, when exceptionally small districts are consolidated, the consolidation has been shown to produce substantial cost savings, expand curricular offerings, and increase specialized services such as education for students with disabilities.[250] Specifically, economists William Duncombe and John Yinger concluded in a study conducted in New York from the mid-1980s through the late-1990s that "consolidation is likely to lower the costs of two 300-pupil districts by over 20 percent, to lower the costs of two 900-pupil districts by 7 to 9 percent, and to have little, if any, impact on the costs of two 1,500-pupil districts."[251]

Thus, district consolidation may be especially beneficial in states such as Illinois, which has 868 districts,[252] of which more than half (447) enroll 1000 students or less. [253] Illinois is not the only state with numerous small districts, though—out of the 13,234 school districts across the

crisis. Sarah D. Sparks, *Missed Opportunities: Research Scarce on Post-Katrina Reforms*, Educ. Week, 13, Aug. 25, 2010.

250 Joe Bard, Clark E. Gardener & Dr. Regi L. Wieland, *Rural School District Consolidation*, 4:2 Academic Leadership, Feb. 12, 2007; Melissa Maynard, *Still too many schools?*, Stateline.org, Mar. 22, 2010, http://www.stateline.org/live/details/story?contentId=470554.

251 William Duncombe & John Yinger, *Does School District Consolidation Cut Costs?* Center for Policy Research Working Paper No. 33, 3-4 (Jan. 2001, updated in 2005). Interestingly, consolidation is similar to an idea Omer Kimhi advocates: creating special districts which have access to both the city and suburban tax base, for example. However, Kimhi discusses this as a way of assisting a particular distressed municipality; for political reasons at the very least (which relatively financially sound school district wants to be consolidated with an economically failing school district?), this issue is not discussed in the context of school district consolidation. However, it is one a state should be aware of, and for which it should provide adequate support, if mandating or strongly incentivizing district consolidation. *See* Kimhi, *Reviving Cities*, supra note 57, at 667-68.

252 http://nces.ed.gov/ccd/districtsearch/

253 *Id.* (Illinois' total number of districts (868) is not too far behind Texas (1031) even though Texas' public schools enroll more than twice as many students as Illinois'.). http://nces.ed.gov/ccd/districtsearch/; http://nces.ed.gov/programs/stateprofiles/sresult.asp?mode=short&s1=17.

country, 6067 enroll 1000 or fewer students.[254] As one would expect, the cost savings from district consolidation result mainly from economies of scale—a mid-sized, consolidated district will have fewer administrative and infrastructure-type costs than two smaller, separate districts.[255] Yet, these savings may be offset to a degree by increased costs of transportation, additional capital expenditures, and salary increases (salaries often rise to the highest level paid by any of the affected districts prior to consolidation).[256] Still, Maine reported $36 million in savings as a result of moving from 290 school districts to 215.[257] A recent report suggests that Michigan could stand to save hundreds of millions of dollars by aggressively consolidating districts.[258] Arkansas and Iowa also have consolidated dozens of smaller districts in recent years, anticipating substantial cost savings.[259] And during the past ten years, district consolidation has been on the table in Arizona, Indiana, Kansas, Maine, Mississippi, Montana, Nevada, New York, Pennsylvania, South Carolina, Vermont, Washington, Wyoming, and West Virginia.[260]

The disadvantages of consolidation are that students' academic achievement sometimes suffers and often the smaller districts subjected to consolidation are major employers and social anchors for the rural communities in which they are located.[261] For these reasons, the National

[254] *Id.*
[255] Brookings Metro America, *supra* note 197, at 165; Vermont Legislative Research Shop, *School District Consolidation*, (Mar. 2007).
[256] Education Northwest, *What the Research Says (or Doesn't Say): Consolidation of School Districts;* Vermont Legislative Research Shop, *School District Consolidation*, (Mar. 2007).
[257] Brookings Metro America, *supra* note 197, at 165; but see Marvin E. Dodson, III & Thomas A. Garrett, *Inefficient Education Spending in Public School Districts: A Case for Consolidation?* Contemp. Econ. Pol'y (Apr. 2004) (finding that transportation costs decrease after consolidation).
[258] Mary Schulken, *Consolidation Could Save Mich. Millions, Study Says*, Educ. Week, 4, Aug. 25, 2010; Sharif Shakrani, *School District Consolidation Study in 10 Michigan Counties*, Sept. 3, 2010, available at: http://www.epc.msu.edu/documents/School-District-Consolidation-Study-Sharif-Shakrani-Sept-2010.pdf.
[259] Bard, et. al., *supra* note 250; Maynard, *supra* note 250; Dodson, III & Garrett, *supra* note 257.
[260] Brookings Metro America, *supra* note 197, at 165; Bard, et. al., *supra* note 250; Maynard, *supra* note 250; Education Northwest, *What the Research Says (or Doesn't Say): Consolidation of School Districts;* Dodson & Garrett, *supra* note 257.
[261] Vermont Legislative Research Shop, *School District Consolidation*, (Mar. 2007).

Rural Education Association is categorically opposed to mandatory consolidation.[262] However, the local social and economic impact of school closings which result from district consolidation has been somewhat mitigated when the consolidated district maintains, for example, an elementary school in one community and a high school in the other.[263] Furthermore, even if geographic constraints make traditional district consolidation impractical (where schools are consolidated as well as administrative functions), states should still consider consolidating districts administratively, even if all or most students continue to attend the same school they attended prior to consolidation.[264] Recent studies in Michigan show that this alternative of administrative consolidation without school closures is substantially more palatable to voters.[265] Because local resistance can be so strong, it is especially important that the state provide major incentives for district consolidation, or require consolidation outright in particular cases.

Finally, there may be limited circumstances in which smaller districts should not be consolidated, either because financial savings will not result or because public policy dictates otherwise. For example, especially isolated rural districts and districts on Native American Reservations should be exempt from consolidation.

c. Permit More Outsourcing of Non-Instructional Services

All states regulate the procedures by which local governments award contracts to private vendors.[266] Judging by the frequency of outsourcing in school districts, in some states the

[262] Bard, et. al., *supra* note 250.
[263] *Id.*
[264] Dodson & Garrett, *supra* note 257.
[265] Shakrani, *supra* note 258, at 8.
[266] Jennifer Maciejewski, *Ins and Outs of Outsourcing*, District Admin. (Aug. 2007).

regulation is fairly permissive.[267] In others, such as California, state law restricts local governments from contracting out services unless the local government can prove "a guaranteed cost savings."[268] Not surprisingly, because "it is often difficult to verify efficiencies and prove them in court," California municipalities—including school districts—are much more hesitant to outsource contracts for services than they were prior to the enactment of the restrictive statute.[269] Furthermore, in Illinois, 2008 changes to state law included, in the words of one Illinois attorney, "requirements [] so prohibitive that subcontracting no longer remains a viable or cost-effective alternative for school boards."[270]

Outsourcing non-instructional services is not a panacea for districts' fiscal woes, and it can have disadvantages that affect many stakeholders. Vendors generate some cost savings because of economies of scale, but often this is dwarfed by the savings generated because the

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[267] Mary McCain, *Serving Students: A Survey of Contracted Food Service Work in New Jersey's K-12 Public Schools* 1 (2009), *available at* http://www.cww.rutgers.edu/Docs/NJschoolcafeteriaworkers.pdf.

[268] California Governor's Committee on Education Excellence, Students First: Renewing Hope for California's Future (2007). *available at* http://www.everychildprepared.org/docs/5finance.pdf 5 p. 31

[269] *Id.* (the California Governor's Committee on Education Excellence advocates repealing the statute because "[c]ontracting for non-teacher services generally results in lower costs, which can free up funds for other education purposes."); So does Lisa Snell of the Reason Foundation. Lisa Snell, *Lift Restrictions on School Outsourcing in California*, June 30, 2009, *available at* http://reason.org/news/show/lift-restrictions-on-school-ou.

[270] Matt Roeschley, *New Legislation Deters Outsourcing by School Districts*, (Spring 2008), *available at* http://www.obkcg.com/article.asp?a=309. A vendor must submit a bid, plus:

A. Evidence of liability insurance that is greater than or equal in scope and amount to the liability insurance provided by the school board;
B. Employee benefits comparable to those provided to employees of the school board;
C. A complete list of the number of employees who will provide the non-instructional services, their job classifications, and the wages they are paid by the third party;
D. A minimum three (3)-year cost projection for each and every expenditure category and account for the performance of non-instructional services; such projection may not be increased if the third party's bid is accepted;
E. Upon the request of the school board, composite information including: criminal and disciplinary records, DCFS complaints and investigations, traffic violations, license revocations and other license problems; and
F. A notarized affidavit from the president or CEO of the third party attesting that, within the three (3) months immediately preceding the submission of its bid, each of its employees has completed a criminal background check that complies with the requirements of the School Code. (105 ILCS 5/10-22.34c(a)(3)

*Id.* Additionally, "Third party contracts must now require that a contractor offer any available positions to qualified school personnel who have lost their jobs because of the contract and must contain provisions that require the employer to ensure non-discrimination and equal employment opportunity for all persons. (105 ILCS 5/10-22.34c(a)(7) and (8))." *Id.*

vendors pay their employees less and give them fewer benefits than the school district did.[271] Sometimes vendors are attuned to working in a business environment but not a school environment.[272] At other times, the savings are not what the school district thought they would be, especially if a district is trying to bid out a contract for which there is not much competition, which often occurs when districts try to outsource transportation.[273] Finally, any school district that seeks to outsource non-instructional services should consult an attorney to ensure that the district complies with relevant statutory and regulatory requirements—attorney fees, plus administrative time spent conducting the process, are disadvantages of this option, as well.[274] The importance of complying with relevant regulations and thus avoiding litigation cannot be overstated, though: in August 2010, the Detroit Public School District was in court, defending their outsourcing of security services.[275]

But if done well and carefully, outsourcing some non-instructional services may generate enough cost savings for a district that, despite the disadvantages, outsourcing is worthwhile.[276] In school districts across the country, three non-instructional services are outsourced more frequently than any others: transportation, custodial services, and food service.[277] In fact, 13% of school districts across the country outsource food service, and this number continues to grow.[278]

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[271]McCain, *supra* note 267.
[272] Mike Dano, *When Outsourcing Didn't Work, This School Cancelled its Contract*, *available at* http://www.sourcingmag.com/content/c051110a.asp.
[273] Sheryl S. Lazarus & Gerard J. McCullough, *The Impact of Outsourcing on Efficiency in Rural and Nonrural Districts: The Case of Pupil Transportation in Minnesota*, 35 J. of Regional Analysis & Pol'y 55 (2005); Maciejewski, *supra* note 266.
[274] William J. Mathis & Lorna Jimerson, *Weighing Outsourcing*, The School Administrator 10-15 (Oct. 2009).
[275] Chastity Pratt Dawsey, *DPS is Ordered to Rehire Officers*, Detroit Free Press A3, Aug. 25, 2010.
**[276]** Office of Program Policy Analysis and Government Accountability, *Information Brief: With Effective Planning, Accountability, and Oversight, School Districts can Successfully Outsource Services*, Mar. 24, 2004, *available at* http://www.oppaga.state.fl.us/MonitorDocs/Reports/pdf/0426rpt.pdf.
[277] Michael D. LaFave & Daniel J. Smith, *Survey: School Outsourcing Grows*, Aug. 1, 2005, *available at* http://www.mackinac.org/7212.
[278] McCain, *supra* note 267.

Other school districts also have outsourced maintenance,[279] school security,[280] IT services,[281] school nurses,[282] substitute teachers,[283] special education aides,[284] and drivers' education.[285] And depending on the service, some school districts have been able to solicit bids from vendors across the country, thus increasing competition for the contract even more.[286]

#### d. Incentivize Layoff of Low-Performing Teachers

In 15 states, state law requires that seniority is the controlling factor when school districts lay off employees; in countless individual school districts across the country, this same approach also is memorialized in countless collective bargaining agreements.[287] Thus, this is the proposal likely to face the most political opposition, especially in states with a strong union tradition.[288] Yet, like pension reform, it must be part of the current discussion, and increasingly over the past year it has been.[289] During late 2009, Arizona amended state law to require that layoffs be

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[279] LaFave & Smith, *supra* note 277.
[280] AP, *School Chief: Outsourcing Security Saves Millions*, Educ. Week, Aug. 11, 2010.
[281] Mike Dano, *When Outsourcing Didn't Work, This School Cancelled its Contract*, *available at* http://www.sourcingmag.com/content/c051110a.asp.
[282] Keith Paradise, *Franklin County's School Districts Outsource jobs to Save More Money*, Public Opinion, Aug. 1, 2010.
[283] Maciejewski, *supra* note 266.
[284] Mary Mann, *School District to Outsource Special Education Paraprofessionals*, Mar. 23, 2010, *available at* http://southorange.patch.com/articles/school-district-to-outsource-special-ed-paraprofessionals-2
[285] Paradise, *supra* note 282.
[286] Victor Rivero, *Tightening the Purchasing Process: Superintendents Get More Involved in Buying Policies* (Nov. 2009) (this is the practice in Troy, Michigan's school district).
[287] Larry Abramson, *In Teacher Layoffs, Seniority Rules. But Should It?*, NPR, June 2, 2010.
[288] Ruben Navarette, *Why Let Senior Teachers Get a Free Pass During Layoffs?*, CNN.com, April 29, 2010, *available at* http://cnn.staging.perfectmarket.com/2010-04-29/opinion/navarrette.teachers.unions_1_teachers-unions-senior-teachers-younger-teachers; Stephen Sawchuck, *L.A. Times Stirs Controversy With Teacher-Effectiveness Scoring*, Educ. Week, 4, Aug. 25, 2010; Stephen Sawchuck, *NEA, AFT Chose Divergent Paths on Obama Goals*, Educ. Week 1, 18-19, Aug. 25, 2010.
[289] *See*, *e.g.*, Hanushek, *supra* note 9; Abramson, *supra* note 287; Pat Wingert & Evan Thomas, *Chicago's Lesson in Layoffs*, Newsweek, July 17, 2010 (Increasingly and in response to Race to the Top, states "have changed their laws to make teacher performance matter in tenure and firing decisions, but very few can use it to make layoff decisions.").

conducted without regard to teachers' seniority or tenure.[290] In 2010, California, Colorado and New York all considered legislative proposals to let districts make layoff decisions based on performance and need rather than seniority alone—but all of those proposals failed.[291]

Despite deep-seated political opposition, especially in union states such as California, Colorado, and New York,[292] this policy approach merits consideration because of the incredible cost-savings a district can generate without sacrificing educational quality—recall that school districts spend more money on salaries than any other category of expenditures.[293] In 2009, Marguerite Roza published a paper modeling the number of layoffs needed to reduce a hypothetical district budget by 1-10% under both a seniority-neutral and seniority-based system, documenting what is intuitive: under a seniority-based system, more layoffs were needed because the teachers being laid off were the most junior, who were paid the least.[294] In May 2010, Stanford economist Erik Hanushek wrote:

> [O]ne of the most consistent education research findings [over the past several decades] has been that there is no systematic impact of teacher experience past the first two or three years. [Thus, schools should] lay off ineffective teachers selectively while letting class sizes drift up a little. . . . An increase of two students per class typically amounts to

[290] Alex Bloom, *Arizona Law Changes Way Teachers Contract With Districts*, The Arizona Republic, Nov. 23, 2009. Because Arizona has been a "right to work" state, legislators faced comparatively little opposition to this change.

[291] Jennifer Medina, *Bill Would Allow Layoffs of Teachers With Seniority*, N.Y. Times, Apr. 12, 2010; Navarette, *supra* note 288; For the status of the New York bill, see http://assembly.state.ny.us/leg/?default_fld=%0D%0A&bn=S7346&Summary=Y&Actions=Y&Votes=Y&Memo=Y&Text=Y; for the status of the California bill, see http://www.legislature.ca.gov/cgi-bin/port-postquery?bill_number=sb_955&sess=CUR&house=B&author=huff.

[292] *See, e.g.*, Jennifer Medina, *Last in, First out? City has Another Idea*, N.Y. Times, Apr. 24, 2010; Jennifer Medina, *Bill Would Allow Layoffs of Teachers With Seniority*, N.Y. Times, Apr. 12, 2010.

[293] *See supra* Section I.A.2.

[294] Marguerite Roza, *Seniority-Based Layoffs will Exacerbate Job Loss in Public Education*, Center for Reinventing Public Education (2009).

> a savings of some 10 percent in per-pupil spending, more than most estimates of the current fiscal shortfalls.[295]

And, as numerous media articles document, laying off the most junior teachers often hurts the lowest-performing schools, which are more likely to be schools with high concentrations of students in poverty and/or students of color.[296] In fact, this effect on students was the subject of one of the many lawsuits that have been filed as a result of recession-driven cuts.[297]

Nonetheless, it is important that school districts and education advocates continue to work on ways to measure a teacher's performance and thus use fair evaluations of teachers' performance when making employment decisions (in other words, not merely relying on one factor such as students' performance on standards-based tests or principal evaluation of the classroom).[298] Understandably, unions' central objection to seniority-blind evaluation systems is that, in one advocate's words, "Without an objective criterion for judging teachers . . . the game would be rigged in favor of younger, less expensive teachers."[299]

Performance evaluation systems are becoming more commonplace; major public school districts in Denver, Detroit, and Washington, D.C. have recently implemented evaluation systems.[300] One interesting initiative has demonstrated that teachers may not be as resistant to increasing performance evaluations as might be assumed: in a spring 2009 survey of 9000

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[295] Hanushek, *supra* note 9. *See also* Rivkin, Steven G., Eric A. Hanushek, and John F. Kain (2005). "Teachers, Schools, and Academic Achievement." Econometrica 73(2): 417–458.

[296] Abramson, *supra* note 287; Medina, *supra* note 291; Wingert & Thomas, *supra* note 289; Larry Abramson, *In Teacher Layoffs, Seniority Rules. But Should It?*, NPR, June 2, 2010, available at: http://www.npr.org/templates/story/story.php?storyID=127373157 (quoting Marguerite Roza) (Layoffs of junior teachers "disproportionately hurt students attending the lowest-performing schools, because they tend to have the highest proportion of new teachers. In some Los Angeles schools last year, such cuts wiped out 50 to 70 percent of the faculty.").

[297] *Judge Blocks Teacher Layoffs At 3 Inner-City LA Schools*, Educ. Week, May 19, 2010, at 4.

[298] The D.C. Public School District employed a new evaluation process for the first time in 2009. *See* Stephen Sawchuck, *New D.C. Evaluation Process Targets Hundreds for Firing*, Educ. Week, Aug. 11, 2010, at 4.

[299] Larry Abramson, *In Teacher Layoffs, Seniority Rules. But Should It?*, NPR, June 2, 2010, available at: http://www.npr.org/templates/story/story.php?storyID=127373157

[300] Peggy Walsh-Sarnecki, *DPS' Bobb: 'Good Things are Happening in Detroit'*, Detroit Free Press, Sept. 26, 2010.

teachers, 74% of teachers in one district, 77% in another district, and more than half of the most senior teachers in both districts thought factors in addition to seniority should be considered when a district is making layoffs.[301] The teachers also were asked about the most important factors to be considered when evaluating teaching effectiveness: they selected "classroom management," "teacher attendance," "specific licensure," and "instructional performance based on evaluation rating" as the most important. [302] From a practical perspective, it would seem that involving teachers in the development of seniority-neutral determinations of performance is essential.

### 2. Remedying the Lack of an Adequate Legal Mechanism

As Part II of this Article demonstrated, most states do not have adequate legal mechanisms on which schools in fiscal crisis can rely.[303] First, federal municipal bankruptcy is only available in 24 states and even then has many disadvantages, including that it is a very poor fit for school districts in fiscal crisis.[304] Second, state receivership is only available in 2 states and while more flexible and far-reaching than bankruptcy, it is untested in the realm of school districts' fiscal crises and requires more extensive court oversight when administrative agency oversight is likely sufficient.[305] Third, state fiscal takeover, like receivership, has the ability to affect the systemic factors which contributed to fiscal crisis, but it is plagued by local resistance and available in various forms in only 17 states.[306] Furthermore, in 19 states, not one of these

[301] Policy Brief, *A Smarter Teacher Layoff System*, The New Teacher Project, Mar. 2010, at 3.
[302] *Id.* at 4.
[303] *See supra* Section II.
[304] *See supra* Section II.A.
[305] *See supra* Section II.B.
[306] *See supra* Section II.C.

imperfect legal mechanisms is available.[307] The proposal in this section aims to fill that substantial gap.

In particular, this section champions the state monitoring and fiscal takeover mechanism, attempting to reduce the pitfalls of that approach which have become clear in some states, and also to ensure some consistency in mechanisms across states. Of course, this requirement, too, is phrased generally, leaving states much discretion in determining its particulars. In my view, the ideal role of the state in any of these plans is limited, temporary, and narrow;[308] however, states should be able to decide this for themselves. Several states—including Alabama, California, Florida, Illinois, Kentucky, Michigan, Ohio, Texas, and West Virginia—already satisfy some if not all of the requirements imposed by the relevant portion of the proposed legislation, and, accordingly, provide a variety of models for the many other states which lack such legislation or regulation.[309]

#### a. Monitoring School Districts' Fiscal Health, and Making the Diagnosis Public

Although most states do not monitor municipalities' fiscal health in any systematic way,[310] it has become relatively common for states to engage in a very basic level of such monitoring: requiring school districts to submit an annual budget or audit to the state.[311]

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[307] *See infra* Appendix.
[308] Berman, *Takeovers of Local Governments, supra* note 170, at 68.
[309] [insert IL School Code citation]; Kimhi, *Chapter 9, supra* note 4, at 392-95.
[310] Kimhi, *Reviving Cities, supra* note 57, at n.236, *citing* Kloha, at 252-53; McQuillin, *The Law of Municipal Corporations*, Ch. 39, Financial Powers in General, IV. Collection and Distribution of Funds (Mar. 2010) ("The largest group of states have no enabling statutes or other provision within their law for dealing with municipal financial distress.").
[311] *See, e.g.*, 14 Del. C. 155 (Delaware); Ind. Code ann. 20-25-9-4 (Indiana); RS 17:88 - 17:99 (Louisiana); 13A.02.07.01 - 13A.02.07.10 (Maryland); 123B.77; 127A.19 (Minnesota); Miss. Code. Ann. 31-67-9 (Mississippi);

However, there are many factors outside a district's budget which can serve as an indication of a district's fiscal health, and few states gather that information. Furthermore, only four states' statutes and regulations indicate how a state evaluates a district's submission of its budget or audit; what action a state takes if the submission raises red flags; and establish procedures for creating and publicly releasing of a list of school districts approaching or in fiscal crisis.[312] Thus, most states' ability to assess when school districts are nearing fiscal crisis is severely limited.

Both this type of monitoring and the public distribution of a financial early warning or watch list are critically important for several reasons, though. As discussed earlier, school districts often do not have long-term fiscal plans or fiscal expertise.[313] But, even if a district has one or both of these things, district officials in many different roles have incentives for making the district's fiscal situation seem better than it actually is.[314] This is unfortunate, because the earlier a district's fiscal crisis is discovered by a person or agency with the authority to intervene, the easier it is to assist the district and bring it back to a point of fiscal health.[315] Relatedly, this lack of state monitoring and public disclosure inevitably has exacerbated some school districts' fiscal crises. And, it also may have increased local resistance to state intervention and takeover because the parents and other community members in a taken-over district have had very little time to process an unfortunate fact: if a school district is approaching or in fiscal crisis, local control has failed.

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Mo. Rev. Stat 160.720 (Missouri); 20-9-211 (Montana); 79-528(3)(a)(b) (Nebraska); Section 198:4-d (New Hampshire); 22-8-6; 22-9-41 (New Mexico); N.Y. Educ. Law 2590-h & 8 (New York); 5-134.1 (Oklahoma); 59-69-240; 59-69-250 (South Carolina); Tex. Educ. Code 44.008 (Texas); Title 53A, Chapter 19 (Utah); 21.1.90; 21.1.97 (Virginia); RCW 28A.330.090; 28A.505.070 (Washington).

312 ACA 6-20-1900 (Arkansas); California (California Education Code 1630); 105 ILCS 5/1A‑8 (Illinois); Section 3316.03 (A) of Revised Code (Ohio).

313 *See supra* section.

314 *Id*.

315 R.I. Assembly Digest: Rules change on municipal bankruptcy, June 11, 2010, *available at* http://www.projo.com/generalassembly/ASSEMBLY_DIGEST_11_06-11-10_FJIR3P2_v29.191a9d6.html; Kimhi, *Chapter 9*, *supra* note 4, at 385.

Fortunately, establishing a monitoring and public reporting structure is fairly straightforward, and the four states where these procedures exist—Arkansas, California, Illinois, and Ohio—provide solid examples of a variety of approaches.[316] The relevant statutes or regulations usually set forth a procedure first for evaluating a school district's fiscal health based on pre-determined criteria, and then for assigning school districts to one of two or three categories delineating various degrees of fiscal crisis.[317] Additionally, public policy literature contains multiple approaches for evaluating municipalities' fiscal health; approaches applicable to towns or small cities are likely also largely applicable to many school districts.[318]

#### b. Authorizing and Structuring State Fiscal Takeover of School Districts

[316] Ark Code Ann. § 6-20-1904; ACA 6-20-1900 (Arkansas); California Education Code 1630 (California); 105 ILCS 5/1A‑8 (Illinois); Section 3316.03 (A) of Revised Code (Ohio).

[317] The factors include "the previous [pre-2002] Fund Balance to Revenue Ratio plus four additional measures, including Expenditures to Revenue Ratio, Days Cash on Hand, Percent of Short-Term Borrowing Ability Remaining, and Percent of Long-Term Debt Margin Remaining. These five indicators are individually scored on a scale from one to four (four being the highest or best), weighted, and added together to produce a financial profile score for each district." Illinois Comptroller's Office, *School Performance Under Scrutiny, available at* http://www.ioc.state.il.us/FiscalFocus/article.cfm?ID=101.

On July 1, 2010, the Arkansas Department of Education announced that 8 school districts were on the state's financial distress list, down from 12 the year before. Arkansas Department of Education, *Fiscal Distress Districts os of July 1, 2010*, available at http://arkansased.org/about/reports.html; Arkansas Department of Education, *2009-2010 Fiscal Distress Districts*, http://www.arkansased.org/about/pdf/fiscal_distress_09-10_050809.pdf. In spring 2010, the California Superintendent of Public Instruction announced that 126 school districts were on the state's fiscal watch list; 114 of these districts had qualified certification, and 12 had a negative certification. Corey G. Johnson, *Facing Deep Cuts, More Schools Make "Watch List,"* California Watch, April 2, 2010, *available at* http://californiawatch.org/watchblog/facing-deep-cuts-more-schools-make-fiscal-watch-list. Also in spring 2010, the Illinois State Board announced that 66 school districts were on the state's Financial Early Warning List and 29 were on the state's Financial Watch list. Chris Fusco & Art Golab, *Cash Crunch Hits More Schools*, Chicago Sun-Times, Mar. 25, 2010, *available at* http://www.suntimes.com/news/watchdogs/2122099,CST-NWS-watchdogs25.article. As of spring 2010, 18 Ohio school districts were on the state's fiscal caution list, 5 on the fiscal watch list, and 9 on the fiscal emergency list. *Fiscal Caution School Districts*, Apr. 22, 2010, *available at* http://www.ode.state.oh.us/GD/Templates/Pages/ODE/ODEDetail.aspx?page=3&TopicRelationID=1012&ContentID=7646&Content=76157; *School Districts in Fiscal Watch* and *School Districts in Fiscal Emergency*, June 30, 2010, *available at* http://www.auditor.state.oh.us/services/lgs/fiscalwatch/Schools.pdf.

[318] Ken W. Brown, *The 10-Point Test of Financial Condition: Toward an Easy-to-Use Assessment Tool for Smaller Cities*, Gov't Fin. Rev. 21 (Dec. 1993); R.I. Assembly Digest: Rules change on municipal bankruptcy (June 11, 2010), http://www.projo.com/generalassembly/ASSEMBLY_DIGEST_11_06-11-10_FJIR3P2_v29.191a9d6.html; Kimhi, *Reviving Cities*, *supra* note 57, at 680, n.241.

Only 17 states have any statutory or regulatory authority to intervene if a school district is approaching or in fiscal crisis,[319] and in those states, state takeovers of financially troubled school districts have produced remarkable financial stability.[320] But in the remaining 33 states, school districts in fiscal crisis are either dealt with by the state in an ill-advised ad hoc manner, or receive no guidance from the state. This is not acceptable. All states should have a plan for escalating involvement in a school district approaching or in fiscal crisis, and school districts should have notice of the contours of that plan.

The type and degree of state intervention could vary from one state to another, but ideally each state's plan would have all six of the characteristics of comprehensive plans discussed earlier in this Article.[321] First, in the interest of fairness, consistency, and transparency, a plan should contain specific triggers for various levels of state involvement, rather than responding to individual districts' fiscal crises on a case-by-case basis.[322] Second, to reduce local resistance, minimize the necessity of state involvement, and also encourage early action by the state, the plan should require an initial attempt to solve the problem at the district level with minimal state involvement. For example, the state could provide a consultant to assist the district in budgeting or reviewing its fiscal practices; require the district to produce a budget which the State Board of Education would need to approve; or set an expenditure cap within which the school district must operate.[323] Third (and this is the only element explicitly required in the proposed legislation because it is the most essential), also for reasons of consistency and deference to districts when

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[319] *See* Appendix.
[320] *See supra* Section II.C.
[321] *See supra* Section II.B.1.
[322] Kimhi *Reviving Cities*, *supra* note 57, at 655-56, 678; Kimhi, *Chapter 9*, *supra* note 4, at 390-91.
[323] Illinois Comptroller's Office, *School Performance Under Scrutiny, available at* http://www.ioc.state.il.us/FiscalFocus/article.cfm?ID=101; Kimhi *Reviving Cities*, *supra* note 57, at 670.

possible, the plan should establish a framework for escalating state involvement in a district's fiscal matters. For example, the state involvement could move from the consultation described above, to information gathering (conducting financial inquiries, including internal audits), to debt management (securing more funds for the financially troubled school district), to fiscal management (implementing a recovery plan).[324] Fourth, the plan should contain a clear statement about who will have the authority to take these actions and how that agent will be selected: will the state create a fiscal oversight board, appoint a fiscal manager/advisor, or follow another approach?[325] Fifth, the plan should include a clear statement about the extent of the agent's authority, establishing whether the state agent may, for example, terminate senior administrators' contracts or dissolve the elected school board.[326] And sixth, the plan should not function as a financial bailout for fiscally troubled school districts.

As discussed in Section II.C.2, the state takeover approach can have incredible benefits: it can bring additional fiscal expertise to a financially floundering district; correct poor management practices that have contributed to the fiscal crisis; and interrupt municipalities' entrenched political dysfunction which prevents a district from functionally dealing with an approaching or existing fiscal crisis.[327] And unlike bankruptcy, submitting to a state takeover is not voluntary. For these reasons and others, state takeovers have demonstrated success in financially stabilizing districts in fiscal crisis.[328] Because the legal mechanism of state fiscal takeover can be such a good fit for the problem of school districts' fiscal crises, it is important to try to minimize the pitfalls of this mechanism—first among them, local resistance. The policy

[324] Kimhi, *Chapter 9, supra* note 4.
[325] *Id.*
[326] Illinois Comptroller's Office, *School Performance Under Scrutiny, available at* http://www.ioc.state.il.us/FiscalFocus/article.cfm?ID=101.
[327] *See supra* Section II.C.2.
[328] Recall the specific example of Detroit public schools emergency financial manager Robert Bobb who has enabled DPS to face the next chapter of its existence, which is no small feat. *See supra* text accompanying notes 166-170.

advocated here seeks to minimize that resistance in two main ways: First, the relevant state statute and regulations must be transparent about the entire process and use clear, predetermined criteria as much as possible, to minimizing resistance from within the district. Second, the state must communicate with the public about school districts that are approaching or entering fiscal crises and the reason for state intervention so that the local community understands the unfortunate degree to which local control has failed.

#### 3. Stabilizing Education Funding

In August 2010, Federal Reserve Chairman Ben Bernake gave a speech in which he noted that "many government programs . . . such as education . . . are likely to be most effective when funding sources are stable and predictable, allowing for long-term planning."[329] The funding cuts to education during FY 2010, FY 2011, and those forecasted for FY 2012 have illuminated the instability of education funding at both the state and local levels.[330] And districts' desperate responses to these revenue drops have demonstrated precisely why this instability must be reduced in the future.[331] The good news is that the extent of instability with which many school districts across the country are grappling can be reduced, but that bad news is that doing so will be politically and pragmatically difficult. Accordingly, in this section I discuss four measures included in the proposed legislation with the goal of moving toward greater long-term fiscal stability for school districts.

##### a. Guarantee a Floor of State Funding

[329] Bernake, *supra* note 15.
[330] *See supra* Section I.A.1.
[331] *See supra* Section I.A.2.

In an average school district, 48% of revenues come from state coffers.[332] Thus, even if a school district can estimate its local and federal revenues for the next fiscal year, if its state funding is unstable. that instability can affect short- and long-term budgeting and financial planning substantially. In fact, because some states' budgets are not finalized until mid-year, school districts in those states often are not able to finalize their own annual budgets until after the fiscal year has begun, and sometimes after the school year has started.[333] School districts' budgeting process is further complicated when the education funding proposed in an early version of the state budget is dramatically different from that eventually finalized by the state.[334]

This problem could be reduced to a degree if the federal government required that states provide a certain level of funding based on the previous year's per capita educational expenditures (for example, at least 98%); or, if states statutorily or constitutionally required themselves to do this. While this would not eliminate other causes of uncertainty such as reductions in special program funds or falling local tax revenues, school districts could create various budget options if they knew that a floor of state funding was guaranteed. This proposal is similar in function to the "maintenance of effort" requirement in the 2010 education stimulus bill, which requires:

> [F]or State fiscal year 2011, the State will maintain State support for elementary and secondary education (in the aggregate or on the basis of expenditures per

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[332] Zhou & Johnson, *supra* note 25.

[333] California Governor's Committee on Education Excellence, Students First: Renewing Hope for California's Future (2007), *available at* http://www.everychildprepared.org/docs/5finance.pdf 5 p. 5-5.

[334] *Id.*:

> The timing of the annual adoption of the state budget leaves schools little time to develop their budgets, making it difficult for districts to make long-term plans. [Education] budgets often change significantly from the January 10 version to that proposed in the May Revision. These changes may produce billions of additional revenues to schools... or billions less. Then, state budgets are often so late that districts, especially those with year-round schools, have already started their school year before the state adopts its budget for that school year.

pupil) . . . at not less than the level of such support . . . for State fiscal year 2009.[335]

Importantly, the "maintenance of effort" approach in the 2010 stimulus bill is different from ESEA's long-standing "maintenance of effort" approach in a few ways: it focuses on state expenditures for education rather than district-level expenditures for education, and although it permits a reduction to 2009 (or potentially 2006) levels, it does not easily allow a 10% drop in education expenditures from the previous year, as the ESEA approach did.[336] However, both of those "maintenance of effort" provisions were implemented for a substantially different reason than stabilizing districts' budgets: they were intended to help ensure that federal funds supplement, and do not supplant, state or local funds for education.[337]

Of course, a state's ability to commit to providing a certain level of per capita education funding may in part depend on the availability of reserve funds, which is what the next subsection suggests.

b. Create an Untouchable, Adequately-Funded State Reserve Fund for Education

Between 2008 and 2010, 33 states and the District of Columbia have cut funding for K-12 public education.[338] As state revenues have shrunk, there has been somewhat of a buffer at

[335] 2010 Education Stimulus Bill, pp. 7-8. The 2010 education stimulus bill also included the following exception: if state tax collections were less in 2009 than in 2006, the fund at least at 2006 levels. Education Stimulus Bill p. 7-9.
[336] Government Accounting Office, *Disadvantaged Students: Fiscal Oversight of Title I Could Be Improved*, 1 (Feb. 2003).
[337] Black, *The Congressional Failure to Enforce Equal Protection, supra* note 38, at 319-20.
[338] Johnson, Oliff & Williams, *supra* note 30 (funding has fallen in Alabama, Arizona, California, Colorado, Connecticut, Delaware, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Maine, Maryland, Massachusetts, Michigan, Mississippi, Missouri, Nebraska, Nevada, New Jersey, North Carolina, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, Utah, Virginia, Washington, and the District of Columbia).

the state level—in 47 states and the District of Columbia, state budget stabilization funds (otherwise known as "rainy day funds") exist.[339] However, only two states—Alabama and Oregon—have state reserve funds that are limited to funding public education.[340] As Federal Reserve Chairman Ben Bernake and others have noted, there are few political incentives for governors and state legislators to set aside funds in reserves.[341] In fact, because the rainy day funds represent, in one scholar's words, "a political gift from one legislature to another across time . . . [which] cannot be repaid," reserves have fallen far short of what has been needed to stabilize state finances over the long-term.[342]

However, because 49 of the 50 states must balance their budgets each year, maintaining reserves is essential to future stability of state budgets—including stable state allocations for education. Adequately funded state rainy day funds help extend the amount of time over which a state's revenue and expenditure flow exists; instead of focusing on an annual budget, a rainy day fund can allow a state to stabilize its finances over a longer term business cycle.[343] Federal education legislation has not yet given states an incentive to create or adequately fund education reserves, though; in fact, the 2010 education stimulus bill, focused on job recovery, explicitly prohibited states from using stimulus funds to directly or indirectly rebuild their reserves,

[339] Daniel G. Thatcher, *State Budget Stabilization Funds*, National Conference of State Legislatures 1 (2008); *see also* Kimhi, *Chapter 9*, *supra* note 4, at 387 (discussing the wisdom of budget stabilization funds); California Governor's Committee on Education Excellence, Students First: Renewing Hope for California's Future (2007). available at http://www.everychildprepared.org/docs/5finance.pdf 5 p. 5-26 (recommending the establishment of such a fund in California).
[340] Thatcher, *supra* note 339.
[341] Bernake, supra note.
[342] David A. Super, *Rethinking Fiscal Federalism*, 118 Harv. L. Rev. 2544, 2611 (2005); *see also* Andrew Reschovsky, *Proceedings of a Colloquium at Marquette University Law School*, 88 Marq. L. Rev. 135 (2004); Robert Ward Shaw, *The States, Balanced Budgets, and Fundamental Shifts in Federalism*, 82 N.C. L. Rev. 1195, 1231 (2004); William F. Fox, *The Ongoing Evolution of State Revenue Systems*, 88 Marq. L. Rev. 19 (2004).
[343] *Id.*

although it did allow some of the stimulus funds to be used during FY 2012.[344] But, a federal requirement could compensate for the political will that state legislators lack. Finally, to be clear: this proposal is not intended to create education bailout funds at the state level, but rather to create reserves which allow the state to maintain a more stable amount of funding for education from one year to the next.

### c. Allow Districts to Insure Against Idiosyncratic Risk

A different approach to the goal of stabilizing districts' budgets is inspired by workers compensation systems, which require businesses ("firms") to pay into an insurance pool and allow those firms to make claims when the unexpected happens and a workplace injury or death results.[345] While these systems provide a safety net for workers, they also give firms an incentive to prioritize workplace safety because making a claim means that, as with most insurance systems, a firm's workers compensation contributions must increase in the future.[346] The larger the claim, the greater the increase in the firm's contribution.[347] While the systems are not perfect, many economists seem to agree that these systems balance the various parties' incentives in a fair and efficient manner.[348]

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[344] Because the 2010 Education Stimulus Bill was intended to help with job retention and creation, it explicitly prohibited stimulus funds for being used to directly or indirectly pay down a state's or district's debt, or to create or supplement any existing "rainy day funds." Education Stimulus Bill, pp. 4-5.

[345] Richard A. Epstein, The Historical Origins and Economic Structure of Workers' Compensation Law, 16 Ga. L. Rev. 775 (1982) ; P. Blake Keating, *Historical Origins of Workmen's Compensation Laws in the United States: Implementing the European Social Insurance Idea*, 11 Kan. J.L. & Pub. Pol'y 279 (2002). See, for example, the California system which allows firms to self-insure, privately-insure, or state-insure. Division of Workers Compensation, *The California Workers' Compensation System* (Sept. 2007), available at: http://www.dir.ca.gov/dwc/basics.htm.

[346] Keating, *supra* note 345.

[347] *Id.*

[348] Christopher F. McLaren, Robert T. Reville & Seth A Seabury, *How Effective are Employer Return to Work Programs?*, S-1 (Mar. 2010) (working paper); Darius N. Laksawalla, Robert T. Reville & Seth A. Seabury, *How Does Health Insurance Affect Workers' Compensation Filing?*, 2-7 (Apr. 2005) (working paper).

This same general type of pooled-risk system could be adapted to education funding. In short, a few years down the road when most state and local education funding increases, states could implement a system in which eligible districts would be required to pay in to an insurance program at a particular rate. (To be eligible, a district might have to meet criteria demonstrating that it is a moderately good risk—for example, 3% of its annual expenditures are in unrestricted reserves.) In return, districts would receive specific benefits—notably, the ability to make a claim for additional revenue in a future year when they face a shortfall in a given year. The system might also provide a dividend or reduced rate to districts with especially good records.[349]

School districts will not all face fiscal challenges in the same way—for example, demographic changes, pension shortfalls, and litigation will have a substantial effect on some districts' budgets but not on others[350]—thus creating a system in which the insured entities are a blend of fiscally more and less "healthy" districts. And if this system supplants local school districts' larger "rainy day funds," then presumably many districts will be able to save less and yet have at least the same amount of emergency cushion because instead of bearing all the risk themselves, the risk will be pooled and also at the highest practical level: the state.

#### d. Authorize and Regulate Private Contracts to Stabilize Funding[351]

As discussed in Section I.A.1., both state and local funding for education have been incredibly unstable over the past few years.[352] Also over the past twenty years, an increasing number of municipalities (including school districts) have begun to manage their revenue

[349] For example, an Arizona insurance carrier does this. *See* ASBA, *ASBA Offers a Special Cost-Saving Workers' Compensation Insurance Program Through SCF Arizona*, available at: http://www.asba.com/?page=workerscomp.
[350] *See supra* Section I.A.2.
[351] Many thanks to my colleague Ben Walther for helpful conversations about these issues.
[352] *See supra* Section I.A.1.

streams in creative ways, most often through derivative instruments.[353] These schemes have in many cases lowered districts' borrowing costs, provided needed cash infusions, and stabilized the revenue stream.[354] However, they are systems much more complex than school districts or other municipalities are used to working with, and as a result of several factors, a derivative-financing scheme has become an albatross for more than one school district. Consider what recently happened in the Denver Public Schools:[355] In 2008, Denver needed $400 million to cover underfunded pension obligations.[356] It entered into a financing scheme which had the potential to save the district $129 in pension costs over the next three decades.[357] However, because the scheme was dependent on a variable interest rate, and a credit crisis hit unexpectedly later that year, the district has paid at least $25 million more than it expected to during the past two years and can only get out of the 30-year contract by paying $81 million in termination fees.[358] The school district may come out ahead in the long run, but for right now, it is bearing costs it did not expect to shoulder.[359]

Denver and other school districts often get stung by this sort of financing scheme for several of the same reasons. Most significantly, the complexity of the deal means that a district is likely out of its league and, among other things, is not told or does not understand its level of risk, the fees the bank stands to gain, and the cost of terminating the contract before the end of

[353] Walter A. Robbins, *GASB 53: New Standards for Derivative and Hedging Activities in the Public Sector*, CBS MoneyLine (Apr. 2009); Gretchen Morgenson, *Exotic Debt Deals Put Denver Schools Deeper in Debt*, N.Y. Times (Aug. 5, 2010).
[354] Walter A. Robbins, *GASB 53: New Standards for Derivative and Hedging Activities in the Public Sector*, CBS MoneyLine (Apr. 2009).
[355] Morgenson, *supra* note 353.
[356] *Id.*
[357] *Id.*
[358] *Id.* (public sector entities regularly have been entering into contracts with a term such as 30 years—this term would be "highly unusual among private sector issuers like corporations" which generally only commit to such contracts for five years, especially because the termination rates are often so high).
[359] David Milstead, *Analysis: Both Sides Right in the Pension Debate*, Apr. 12, 2010, www.ednewscolorado.org/2010/04/12/4295-analysis-both-sides.

the term.[360] Even the most common form of outside expertise is not helpful: the "independent" advisors districts usually employ have a vested interest in the deal happening because that is the only circumstance under which they will get paid.[361] Additionally, the deals are usually made outside of the traditional public bidding system, thus competition does not lower price or even given the district a sense of the market and districts have little or no comparative data about what they should be paying in these situations.[362] Finally, as with any transaction, a bank may engage in tortuous activity, as some allegedly have.[363]

However, because local government entities must be authorized by the state to enter into contracts involving derivatives,[364] there is the potential for the state to regulate school districts' involvement with derivative contracts, and/or to publish a list of approved investment advisors, and thus preserve the benefits of this financing structure while managing districts' risk. A number of commentators have called for increasing state oversight of these sort of transactions, arguing that the increasingly complicated municipal finance market has "outgrown" state regulation,[365] that the existing regulation "fails to account for new instruments and risk,"[366] and that state regulation should grant more independence to the more financially sophisticated

[360] Martin Z. Braun & William Selway, *Hidden Swap Fees by JPMorgan, Morgan Stanley Hit School Boards*, Bloomberg, Feb. 1, 2008, *available at* www.bloomberg.com/apps/news?pid=21070001; Hamilton, *supra* note 33, at 1018-19; Money magazine survey in 1995 documented the lack of sophisticiated municipal finance knowledge among municipal finance officers. Ruth Simon, *Why Your Town Could Get Stung Like Orange County*, Money, Feb. 1995, at 20. Among school districts at least, the situation seems to have changed little since then. *See, e.g.*, Braun & Selway, *supra* note 360.
[361] Braun & Selway, *supra* note 360.
[362] *Id.*
[363] After Orange County, California emerged from the largest municipal bankruptcy in history, it sued Merrill Lynch, alleging that the firm had sold derivatives to the county that were not well suited to municipal investment. Thirteen other municipalities joined Orange County as plaintiffs and the lawsuit settled out of court, with Merrill Lynch agreeing to pay the municipalities $32.5 million. Andrews Chapter 11 update, *City of Atascadero v. Merrill Lynch*, (May 2000). Current litigation alleging that financial services firms rigged bids for municipal bond derivatives. Daniel W. Hawthorne, *Recent Trends in Federal Antitrust Class Action Cases*, Antitrust 58, 60 (Summer 2010).
[364] Jeanette Redmond, *State and Local Government Entities: In Search of... Statutory Authority to Enter Into Interest Rate Swap Agreements*, 63 Fordham L. Rev. 2177, 2180 (1995).
[365] Hamilton, *supra* note 33, at 1019.
[366] Charles D. Thompson, III, *Money for Nothing—Or Dire Straits? Public Funds and the Derivatives Market*, 1997 U. Ill. L. Rev. 611, 637 (2007).

municipal investors but much less deference to others.[367] Some states have responded to these concerns, but most have not.[368] Thus, because sufficient regulation can minimize many of the substantial risks of the use of derivatives, states should consider whether they want to implement or amend state law to permit creative financing with the goal of stabilizing districts' long-term revenue.

### E. Summary

This section has made the case for a federal interest in fiscally stable school districts, set forth proposed federal fiscal accountability legislation in pursuit of that interest, and presented brief descriptions of ten specific policy proposals included as alternative ways of satisfying the three main requirements in the proposed legislation. Changing fiscal education policy is not easy, and the goal of this legislation is to require many of the most difficult decisions to be made at the state level.

## CONCLUSION

School districts' shrunken budgets are one aspect of the recession expected to lag behind the country's economic recovery generally; when FY 2012 begins in July 2011, many school districts across the country will be looking over the edge of a funding cliff. That is a complex problem, and accordingly in this article I have argued for a complex solution. Specifically, I have argued for a three-part fiscal accountability amendment to the ESEA because, first, prudent state

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367 *Id.* at 632-37.

368 *See, e.g.*, Michigan Department of Treasury, Bureau of Bond Finance, *Bond Structures With Variable Rate and Derivative Transactions* (Jan. 5, 2009), available at: http://www.michigan.gov/documents/treasury/SBQLP_261702_7.pdf.

policy can help districts generate immediate cost savings. Second, both now and in the future, state plans to publicly monitor districts' fiscal health and intervene when a district approaches or enters fiscal crisis can help districts head off a fiscal crisis, or reduce its duration and long-term effect. And third, looking down the road even further, states can help stabilize districts' revenues for years to come, which will enable districts to engage in better long-term fiscal planning and reduce the need for future state intervention.

In *Brown v. Board of Education*, Chief Justice Earl Warren famously wrote for a unanimous Court that education is "perhaps the most important function of state and local governments."[369] The unprecedented drop in school districts' revenues, the uneven impact of systemic and situational factors, and the desperate, sometimes haphazard ways in which districts have tried to reduce their expenditures over the past few years do not reflect the importance of education to the Court, to the country's future economic prosperity and civic health, or to the 49 million children who are enrolled in public schools in the United States today.[370] It is not too late to change this, and another education "bailout" is not the answer.

## APPENDIX

Table 1. Legal mechanisms available for school districts in fiscal crisis.

| State | Federal bankruptcy available to municipalities, including school districts | State receivership available to school districts | State takeover of a school district for fiscal reasons (for academic reasons) | No mechanism available |
|---|---|---|---|---|
| Alabama | AL ST § 11- | | Ala. Code § 16-6B-4 | |

[369] Brown v. Board of Education, 347 U.S. 483 (1954).
[370] Amber M. Noel & Jennifer Sable, *Public Elementary and Secondary School Student Enrollment and Staff Counts from the Common Core of Data: School Year 2007-2008*, 4-5 (Nov. 2009), *available at* http://nces.ed.gov/pubs2010/2010309.pdf.

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|---|---|---|---|---|
| | 81-3; (amendment 2001) | | Ala. Code § 16-6B-3 | |
| Alaska | | | 4 AAC 06.840 | X |
| Arizona | A.R.S. § 35-603 | | A.R.S. §15-103 & §15-107 | |
| Arkansas | A.C.A. § 14-74-103 | | A.C.A. § 6-20-1900-11<br>A.C.A. § 6-15-403, §6-15-430 & ADE 162 – see http://www.arkansased.org/pdf/sarg_resource_guide_060909.pdf (refer to section on state directed schools) | |
| California | West's Ann. Cal. Gov. Code § 53760 | | Cal. Ed. Code § 1630, 41320, 41326<br>Cal. Ed. Code § 52055.5 (f)<br>http://www.leginfo.ca.gov/cgi-bin/displaycode?section=edc&group=52001-53000&file=52053-52055.55 | |
| Colorado | C.R.S.A. § 32-1-1402 | | | |
| Connecticut | C.G.S.A. § 7-566 | | | |
| Delaware | | | 14 Del.C. § 155 & DE ADC 103 6.0 | |
| Florida | West's F.S.A. § 218.01 | | West's F.S.A. § 218.503 | |
| Georgia | | | | X |
| Hawaii | | | | X |
| Idaho | I.C. § 67-3903 | | IDAPA 08.02.03.112 & 08.02.03.114 http://adm.idaho.gov/adminrules/rules/idapa08/08index.htm. | |
| Illinois | | | 105 ILCS 5/1A-8, 1B-1—1B-22<br>105 ILCS 5/2-3.25f & 105 ILCS 5/34-1 – 34-1.1 (Chicago Public Schools) – Section on Chicago Public Schools doesn't seem to have any specific sections re: takeovers | |
| Indiana | | | Ind. Code Ann. 20-25-9-4, 20-25-15-1, 20-25-15-2, 20-25-15-3 (applies to Indianapolis Public Schools) | |
| Iowa | | | I.C.A. § 256.11<br>Amendment: 2010 Ia. Legis. Serv. S.F. 2289 (West) | X |
| Kansas | | | | X |
| Kentucky | KRS § 66.400 | KRS §162.220 | KRS § 158.785, 158/.780(1)<br>KRS § 158.6455, 158.780, 158.785 & 703 KAR 3:205, 5:130 | |
| Louisiana | LSA-R.S. | | | |

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| | 39:619 | | | |
| Maine | | | Maine Department of Education Regulation 125, Section 14 | X |
| Maryland | | | 13A.02.07.01 - 13A.02.07.10<br>SB 795 (1997)<br>http://mlis.state.md.us/1997rs/billfile/sb0795.htm<br>HB 949 (2002)<br>http://mlis.state.md.us/2002rs/billfile/hb0949.htm & COMAR 13A.01.04.08 | |
| Massachu-setts | | | M.G.L.A. 69 § 1J, 1K & 603 CMR §2.01 – 2.06, 2.03 | |
| Michigan | M.C.L.A. 141.1222 | | M.C.L.A. § 141.1231 – 1244<br>M.C.L.A. 380.372 & 380.371 | |
| Minnesota | M.S.A. § 471.831 | | | |
| Mississippi | | | Miss. Code Ann. § 37-17-6, 37-18-7 Amendment: 2010 Miss. Laws Ch. 420 (H.B. 625). & CMSR § 36-000-069 | |
| Missouri | V.A.M.S. 427.100 | | Mo. Rev. Stat § 160.720<br>162.081, 163.023 | |
| Montana | MCA 7-7-132 | | | |
| Nebraska | Neb.Rev.St. § 13-402 | | | |
| Nevada | | | N.R.S. 385.3772; 385.3773 | X |
| New Hampshire | | | | X |
| New Jersey | N.J.S.A. 52:27-40 | | N.J.S.A. § 18A: 7A-10, 11; N.J.S.A. § 18A:7A-14, 15, 15.1 | |
| New Mexico | | | N.M.S.A. § 22-2-2, 22-2-14, 22-2C-7 | X |
| New York | McKinney's Local Finance Law § 85.80 (amended, 2009 Sess. Law News of N.Y. Ch 494 (S. 66002)). | | N.Y. Educ. Law § 2590-h & 8 NYCRR §100.2 | |
| North Carolina | N.C.G.S.A. § 23-48 | | N.C.G.S.A. § 115C-447, 4514; N.C.G.S.A. § 115C-105.39, § 115C-325, §115C-105.37 | |



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| North Dakota | | | | X |
| Ohio | R.C. § 133.36 | | R.C. § 3316.03-.05 R.C. § 3302.04, § 3302.03, § 3302.041, § 3302.10 | |
| Oklahoma | 62 Okl.St.Ann § 281 | | 70 Okl.St.Ann. § 1210.541 | |
| Oregon | | | | X |
| Pennsylvania | 53 P.S. § 11701.261 | 24 P.S. § 791.7 | 24 P.S. § 6-691 -- 697 24 P.S. § 17-1701-B -- § 17-1716-B | |
| Rhode Island | | | R.I. Gen. Laws § 16-7.1-5 | X |
| South Carolina | Code 1976 § 6-1-10 | | Code 1976 § 59-1A8-1570 | |
| South Dakota | | | | X |
| Tennessee | | | T.C.A. § 49-1-601 - § 49-1-602. | X |
| Texas | V.T.C.A., Local Government Code § 140.001 | | Tex. Educ. Code § 39.102 | |
| Utah | | | | X |
| Vermont | | | 16 V.S.A. § 165 | X |
| Virginia | | | | X |
| Washington | West's RWCA 39.64.040 | | | |
| West Virginia | | | W. Va. Code, § 18-2E-5 & W. Va. Code State R. 126-13-1 thru 126-13-12 | |
| Wisconsin | | | Wis. Stat. Ann. 118.42 | X |
| Wyoming | | | | X |
| TOTAL | 24 | 2 | 17[371]/29 (only academic, not fiscal: 16) (total: 33) | 19 |

[371] This number does not include Connecticut, which passed special legislation declaring the Hartford school district to be in a state of emergency and authorizing a comprehensive takeover by the state. Special Act 97-4 (1997 Regular Session).