

SHORT-TERM FINANCING OF SCHOOL DISTRICT NEEDS

By: T. Daniel Goodwin

Arkansas law obligates school boards to maintain schools in a good state of repair. To meet this obligation, school districts must usually finance the cost of new construction, renovation or system upgrades. However, Arkansas school districts cannot borrow money for more than one year unless they issue bonds to the public, borrow money from the State's Revolving Loan Fund or issue qualified 10 or 30-year lease-purchase agreements, installment sales contracts or post-dated warrants to the creditor. Issuing bonds or using the Revolving Loan Fund can be time consuming and complicated, especially if the school district must hold an election to raise its millage for the bonds. Depending on the school district's needs, lease-purchase agreements, installment sales contracts or post-dated warrants ("Short-Term Finance Instruments") may offer the most hassle-free and flexible approach. Recent changes in Arkansas law and Arkansas Department of Education ("ADE") regulations make it more important than ever that school district boards understand this method of finance.

Short-Term Finance Instruments allow school districts to finance the purchase of school buses; the payment of certain insurance premiums; the purchase of equipment; the repair and renovation of school facilities; the purchase of school sites; the payment on loans relating to litigation against a school district; the payment of the district's pro rata share the cost of real estate appraisers for ad valorem tax purposes; the purchase of energy conservation measures; and the training of teachers or other programs under the federally recognized Qualified Zone Academy Bond program.

Other key elements of short-term finance include: (1) a maximum 10-year term (30 years on certain public-private projects); (2) registration of the debt with the ADE, the treasurer of the district and the board; (3) annual payments under Short-Term Finance Instruments must not exceed revenue receipts of the district for that particular year; (4) an optional authorization to withhold state aid from the district in the event of a default; (5) a rate of interest that can not exceed the maximum rate for school bonds; and (6) joint liability of the district and the school fiscal officer for any payment charged against the revenues of a school year if it exceeds the revenue receipts of the district for that school year.

In its 2003 regular session, the General Assembly passed Act 1738 which imposed additional restrictions on most school district contracts, including Short-Term Financing Instruments.

Article 1738 prohibits a school board from approving any service agreement with a term exceeding 1 year or any obligation relating to the sale, acquisition or repair of school facilities or equipment exceeding \$75,000, without ADE approval. This prohibition does not extend to "regularly scheduled maintenance" projects. Unfortunately, the ADE has given conflicting guidance regarding what constitutes "regularly scheduled maintenance." Some ADE agents have stated that total HVAC replacement and re-roofing might qualify while other agents have stated that such activities constitutes long-term capital improvements. The good news is that the ADE approval process is relatively benign and an expedited emergency approval can sometimes be obtained in as little as 1 or 2 days. In general, the board should always consult with its finance attorney before entering into a contract exceeding 1 year or \$75,000 and when in doubt should seek ADE approval.

Many school districts concerned about indoor air quality and reducing utility costs use Short-Term Finance Instruments to acquire energy conservation measures ("ECM") such as HVAC equipment, energy control systems, energy-efficient lighting, etc. A common misconception exists that the financing of an ECM can extend to 15 or 20 years. This is not true. Although an installation, service or maintenance contract could potentially have a 20-year term, the Short-Term Finance Instrument funding that contract is still limited to a 10-year term.

In conclusion, Short-Term Finance Instruments provide a useful and relatively easy tool for school boards to fulfill their obligation to maintain schools. However, with the multiple short-term finance requirements and the recent changes in Arkansas law, school boards are well advised to consult with their finance attorney before issuing a Short-Term Finance Instrument.

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