

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** PCB EAC 12-01 Financial Emergencies

**SPONSOR(S):** Economic Affairs Committee

**TIED BILLS:**                   **IDEN./SIM. BILLS:**

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
Orig. Comm.: Economic Affairs Committee	13 Y, 3 N	Rojas	Tinker

### SUMMARY ANALYSIS

The bill makes several changes in ch. 218, F.S., which in part controls determination and treatment of financial emergencies in local governments and district school boards.

The bill deletes one of the statutory triggers for financial emergency specified in s.218.503(1)(e), F.S., relating to a deficit fund balance or net assets balance, and amends s. 218.39(5), F.S., to require auditors to consider that same condition in determining whether deteriorating financial conditions exist that are required to be discussed with the entity's governing body.

The bill amends s. 218.503(3), F.S., to create a timeframe of 45 days after the date of a request for information which entities must respond to requests for information by the Executive Office of the Governor or the Commissioner of Education. If the entity does not comply with the request, the Governor, or the Commissioner of Education, or their respective designee then notifies the Legislative Auditing Committee who may take action pursuant to s. 11.40, F.S.

The bill further amends s. 218.503(3), F.S., regarding measures to resolve financial emergencies. This section authorizes financial emergency boards appointed by the Governor or Commissioner of Education to consult with other governmental entities for the consolidation of administrative direction and support services. Such services include, but are not limited to, services for:

- asset sales,
- economic and community development,
- building inspections,
- parks and recreation,
- facilities management,
- engineering and construction,
- insurance coverage,
- risk management,
- planning and zoning,
- information systems,
- fleet management, and
- purchasing.

There is no fiscal impact associated with this bill.

The bill has an effective date of July 1, 2012.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. EFFECT OF PROPOSED CHANGES:

##### **Current Situation**

##### ***Local Government Entity and District School Board Financial Emergencies***

Part V of Ch. 218, F.S., comprises the Local Governmental Entity, Charter School, Charter Technical Career Center, and District School Board Financial Emergency Act (Act). The purpose of the Act is to preserve the fiscal solvency of local government entities,<sup>1</sup> charter schools, charter technical career centers, and district school boards that are in a state of financial emergency. Under the Act's provisions, those bodies that meet one of the statutory indicators of financial distress are required to notify the Governor or Commissioner of Education and the Legislative Auditing Committee.<sup>2</sup>

##### ***Conditions Indicating Financial Distress***

Subsections (a)-(e) of s. 218.503(1), F.S., provide indicators of financial distress which include any one of the following conditions based on lack of funds:

- Failure to pay short-term loans or failure to make bond debt service or other long-term debt payments within the same fiscal year in which due.
- Failure to pay uncontested claims from creditors within 90 days after the claim is presented.
- Failure to transfer taxes withheld on the income of employees, failure to transfer employer and employee contributions for Federal social security, or failure to transfer any pension, retirement, or benefit plan of an employee at the appropriate time.
- Failure to pay wages and salaries owed to employees or retirement benefits owed to former employees for one pay period.
- An unreserved or total fund balance or retained earnings deficit, or unrestricted or total net assets deficit, for which sufficient resources of the entity are not available to cover the deficit.<sup>3</sup>

The Auditor General recently recommended in a report<sup>4</sup> on the Local Government Financial Reporting System, that the condition specified in s.218.503(1)(e), F.S., regarding a deficit fund balance or net assets balance has not been an effective indicator of a state of financial emergency. The report recommended eliminating that provision of law and revising s. 218.39(5), F.S., to require auditors to consider that same provision in determining whether deteriorating financial conditions exist that are required to be discussed with the governing body.

##### ***Determination of Financial Emergency***

Upon notification that one or more of these conditions is met, the Governor or Commissioner of Education, as appropriate, must determine whether state assistance is needed to resolve or prevent the

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<sup>1</sup> s. 218.502, F.S., defines local government entity to mean "a county, municipality, or special district".

<sup>2</sup> s. 218.503(1)-(2), F.S. Note: a charter school must notify the charter school sponsor, the Commissioner of Education, and the Legislative Auditing Committee; a charter technical career center must notify the charter technical career center sponsor, the Commissioner of Education, and the Legislative Auditing Committee; and the district school board shall notify the Commissioner of Education and the Legislative Auditing Committee.

<sup>3</sup> Section 1011.051, F.S., provides additional insufficient resource conditions for school districts. If the unreserved general fund balance in a district's approved operating budget is projected to drop below 3 percent and 2 percent of projected general fund revenues, the school board superintendent is required to provide written notice to the district school board and the Commissioner of Education. Florida Auditor General Report No. 2012-023 cited three school districts in the state that met this condition in the 2009-10 fiscal year.

<sup>4</sup> Florida Auditor General Report No. 2011-196

financial deterioration. The entity is determined to be in a state of financial emergency if state assistance is needed.<sup>5</sup>

Once a determination is made, the Governor or Commissioner of Education has the power to implement certain remedial measures to resolve the financial emergency. Pursuant to s. 218.503(3), F.S., the Governor or Commissioner of Education may:

- require the local governmental entity or district school board's budget to be approved by the Governor or Commissioner of Education, respectively;
- authorize and provide for repayment of a state loan to the local governmental entity;
- prohibit issuance of bonds, notes, certificates of indebtedness, or any other form of debt while in a state of financial emergency;
- inspect and review the entity's records, information, reports, and assets;
- consult with local governmental entity and district school board officials and auditors to discuss necessary procedures to bring accounting books, systems, financial procedures, and reports into state compliance;
- provide technical assistance;
- establish a financial emergency board to oversee local government or district school board activities, appointed by the Governor or State Board of Education as appropriate; and
- require and approve a plan to be prepared by the local governmental entity or district school board that prescribes necessary actions to adjust the entity's debt.

Subsection (5) of s. 218.503, F.S., prohibits a local government entity or district school board from applying for bankruptcy under the United States Constitution without prior approval from the Governor for local governmental entities or the Commissioner of Education for district school boards.

Current law does not provide time frames within which entities must respond to requests for information by the Executive Office of the Governor or the Commissioner of Education, or provide consequences for failure to respond.

### ***Financial Emergency Board***

One of the measures available to the Governor or the Commissioner of Education to assist in resolving a financial emergency is the establishment of a financial emergency board.<sup>6</sup> This board is charged with overseeing activities of the targeted entity. The Governor or the State Board of Education shall appoint members and select a chair. Once established, the board may:

- review the entity's records, reports, and assets;
- consult with local entity officials and auditors and with state officials regarding the necessary steps to bring the entity's accounting books, systems, financial procedures, and reports into compliance with state requirements; and
- review the entity's operations, management, efficiency, productivity, and financing of functions and operations.<sup>7</sup>

All recommendations and reports made by the financial emergency board must be provided to the Governor for local governmental entities or to the Commissioner of Education and the State Board of Education for district school boards.<sup>8</sup>

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<sup>5</sup> s. 218.503(3), F.S.

<sup>6</sup> s. 218.503 (3)(g)1., F.S.

<sup>7</sup> s. 218.503 (3)(g)1.a.-c., F.S.

<sup>8</sup> s. 218.503 (3)(g)2., F.S.

## ***Financial Emergency Plan***

Another measure the Governor or Commissioner of Education may require of entities when resolving a financial emergency is the development of a plan prescribing remedial actions.<sup>9</sup> Subject to Governor or Commissioner approval, the adopted plan must include but is not limited to:

- provision for full payment of obligations outlined in s. 218.503(1), F.S., designated as priority items, that are currently due or will become due;
- establishment of priority budgeting or zero-based budgeting to eliminate items that are not affordable; and
- the prohibition of a level of operations which can be sustained only with nonrecurring revenues.<sup>10</sup>

### ***Article IV, Section 7 of the Florida Constitution: Suspensions***

Article IV, section 7 of the Florida Constitution provides the following:

*By executive order stating the grounds and filed with the custodian of state records, the governor may suspend from office any state officer not subject to impeachment, any officer of the militia not in the active service of the United States, or any county officer, for malfeasance, misfeasance, neglect of duty, drunkenness, incompetence, permanent inability to perform official duties, or commission of a felony, and may fill the office by appointment for the period of suspension.*

### **Effect of Proposed Changes**

The bill deletes the condition specified in s.218.503(1)(e), F.S., regarding a deficit fund balance or net assets balance and amends s. 218.39(5), F.S., to require auditors to consider that same condition in determining whether deteriorating financial conditions exist that are required to be discussed with the governing body. The effect is to require auditors to consider fund balances as a potential indicator of financial distress rather than a statutory indicator. The independent auditor then reports it as one potential sign of deteriorating financial conditions to the governing body.

The bill amends s. 218.503(3), F.S., to create a timeframe of 45 days after the date of a request for information which entities must respond to requests for information by the Executive Office of the Governor or the Commissioner of Education. If the entity does not comply with the request, the Governor, or the Commissioner of Education, or their respective designee then notifies the Legislative Auditing Committee who may take action pursuant to s. 11.40, F.S.<sup>11</sup>

The bill further amends s. 218.503(3), F.S., regarding measures to resolve financial emergencies. This section authorizes financial emergency boards appointed by the Governor or Commissioner of Education to consult with other governmental entities for the consolidation of administrative direction and support services. Such services include, but are not limited to, services for:

- asset sales,
- economic and community development,
- building inspections,
- parks and recreation,
- facilities management,
- engineering and construction,

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<sup>9</sup> s. 218.503 (3)(h), F.S.

<sup>10</sup> Section 1011.051(2), F.S., provides additional emergency plan provisions for school districts. If a school district's unreserved general fund is projected to drop below 2 percent of general fund revenues and the Commissioner of Education determines that the district does not have a plan that is reasonably anticipated to avoid a financial emergency, the Commissioner shall appoint a financial emergency board to assist the district.

<sup>11</sup> The LAC has broad investigative powers and may exercise the powers of subpoena by law vested in a standing committee of the Legislature.

- insurance coverage,
- risk management,
- planning and zoning,
- information systems,
- fleet management, and
- purchasing.

The bill also provides that entities required by the Governor or Commissioner of Education to develop remedial financial emergency plans must include provisions, where applicable, for implementing the consolidation, sourcing, or discontinuance of administrative direction and support services as part of the entity's adopted plan. Such services include, but are not limited to, the services cited above.

Finally, the bill creates s. 218.503(6), F.S., to clarify the constitutional ability of the Governor to suspend and recommend removal of members of governing bodies who fail to resolve a state of financial emergency. This failure constitutes malfeasance, misfeasance, and neglect of duty for purposes of Article IV, s. 7 of the Florida Constitution. This is consistent with the Governor's existing authority in the constitution to remove elected officials for malfeasance, misfeasance and neglect of duty.

**B. SECTION DIRECTORY:**

**Section 1** amends s. 218.39(5), F.S., to , to require auditors to consider a deficit fund balance or net assets balance in determining whether deteriorating financial conditions exist that are required to be discussed with the governing body.

**Section 2** amends s. 218.503(3), F.S., relating to various measures necessary to resolve financial emergencies in local governments and district school boards.

**Section 3** provides that this act shall take effect July 1, 2012.

**II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT**

**A. FISCAL IMPACT ON STATE GOVERNMENT:**

1. Revenues:

None.

2. Expenditures:

None.

**B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

1. Revenues:

None.

2. Expenditures:

See Fiscal Comments

**C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

None.

**D. FISCAL COMMENTS:**

Financial emergency boards acting on behalf of an entity that has been declared to be in a state of financial emergency will be authorized to consult with other governmental entities for the consolidation of all administrative direction and support services.

Local government entities and district school boards in a state of financial emergency who are required to adopt financial emergency plans must include provisions, where applicable, for implementing the consolidation, sourcing or discontinuance of administrative direction and support services as part of the entity's adopted financial emergency plan.

### **III. COMMENTS**

#### **A. CONSTITUTIONAL ISSUES:**

##### **1. Applicability of Municipality/County Mandates Provision:**

Not Applicable. The bill does not appear to require counties or municipalities to spend funds or take action requiring the expenditures of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of state tax shared with counties or municipalities.

##### **2. Other:**

The bill creates s. 218.503(6), F.S., to clarify the constitutional ability of the Governor to suspend and recommend removal of members of governing bodies who fail to resolve a state of financial emergency. This failure constitutes malfeasance, misfeasance, and neglect of duty for purposes of Article IV, s. 7 of the Florida Constitution.

#### **B. RULE-MAKING AUTHORITY:**

None.

#### **C. DRAFTING ISSUES OR OTHER COMMENTS:**

None.

### **IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES**