



STATE OF ARIZONA

OFFICE OF THE ATTORNEY GENERAL

1275 WEST WASHINGTON, PHOENIX 85007-2926

MAIN PHONE : 542-5025

TELECOPIER : 542-4085

GRANT WOODS
ATTORNEY GENERAL

February 24, 1998

The Honorable Ruth Solomon
Arizona State Senate
State Capitol Complex
Phoenix, Arizona 85007-2890

Re: I98-003 (R97-014)

Dear Senator Solomon:

You have asked a number of questions regarding the disposition of property by charter schools that close. We conclude that, in the abstract, Arizona Revised Statutes Annotated ("A.R.S.") § 15-183(U), which allows a charter school to retain all property it accumulates, is constitutional. Thus, a charter school that closes may keep the property it accumulates, including property purchased with State funds.¹ The specific disposition of the proceeds from the liquidation of the assets of a charter school would be determined by the school's contractual and legal obligations to the State and others. Finally, we caution that receipt of State aid and stimulus funds by individual charter schools may violate the Arizona Constitution if the funds are not used for a public purpose or if the public value provided by the school is far less than the consideration paid by the State.

Background

Your opinion request raises the constitutional issue of when payment of State funds to a private entity becomes a gift that violates the Arizona Constitution. In 1910, the Arizona constitutional convention adopted article IX, section 7 of the Arizona Constitution ("the gift clause") as one of several measures meant to ensure that individuals and businesses operate on a level field, without government favoritism. See John D. Leshy, *The Making of the Arizona Constitution*, 20 ARIZ. ST. L. J. 1, 96 (1988).

Arizona's gift clause was taken from a Montana constitutional provision, *State v. Northwestern Mutual Insurance Company*, 86 Ariz. 50, 52-53, 340 P.2d 200, 201 (1959),

¹ Our conclusion and analysis do not address a charter school's use of federal funds or the ownership of goods or property purchased with federal funds. Those issues would be controlled by federal law and the terms of the federal grant or contract.

that was enacted in response to significant government spending in the 1800s for rail and industrial growth that yielded no public benefit because projects went unfinished. Scott Meyer, Note, *Wistuber v. Paradise Valley Unified School District: Arizona Adopts an "Equitable and Reasonable Consideration" Test to Identify Gifts of Public Funds to Private Entities*, 27 ARIZ. L. REV. 579, 580 (1985). Like Montana's gift prohibition, the gift clause in Arizona's Constitution was meant to prevent government entities from depleting the public treasury by giving advantages to special interests, *Industrial Development Authority of Pinal County v. Nelson*, 109 Ariz. 368, 372, 509 P.2d 705, 709 (1973), or by engaging in non-public enterprises. *State v. Northwestern Mut. Ins. Co.*, 86 Ariz. at 53, 340 P.2d at 201.

In 1994, the Legislature created a hybrid public school in Arizona known as a charter school. 1994 Ariz. Sess. Laws, Ninth Sp. Sess., ch. 2, § 2. Although financed with public funds, A.R.S. § 15-181(B), charter schools may be operated by public bodies, private persons, or private organizations, A.R.S. § 15-183(B), and are exempt from many of the restrictions imposed on school district governing boards and school districts. A.R.S. § 15-183(E)(5).²

The Legislature has authorized charter schools to receive two types of State funds: State aid and stimulus funds. State aid is paid to every charter school according to its student count. A.R.S. § 15-185. This aid is similar to the aid paid to other public schools. Stimulus funds are awarded to selected charter schools applicants and existing charter schools for start-up costs and costs associated with renovating or remodeling school buildings. A.R.S. § 15-188.

Analysis

A. The Statute That Allows a Charter School to Retain All Property That It Accumulates Is Constitutional.

We presume that all legislative enactments are constitutional. *State v. Cook*, 139 Ariz. 406, 408, 678 P.2d 987, 989 (App. 1984). Consequently, we must construe A.R.S. § 15-183(U), if possible, to have a reasonable and constitutional meaning. *Stewart v.*

² For example, A.R.S. § 15-183(E)(5) exempts charter schools from many fiscal controls such as A.R.S. §§ 15-905(L) (State Board of Education authority to penalize school districts for exceeding their budget limits), 15-905(M) (mandated reduction in school district budgets), 15-944 (base revenue control limit), 15-946 (transportation revenue control limit), 15-947 (revenue control limit), 15-951 (revenue control limit, capital outlay revenue limit, capital levy revenue limit), and 15-961 through -963 (limits on capital outlay and capital levy). However, charter schools still must comply with federal and Arizona health, safety, civil rights, and insurance standards; instructional and educational performance goals; and financial record-keeping requirements. A.R.S. § 15-183(E), (F), (G), and (I).

Robertson, 45 Ariz. 143, 150-51, 40 P.2d 979, 983 (1935); *see also Selective Life Ins. Co. v. Equitable Life Assurance Soc'y*, 101 Ariz. 594, 598, 422 P.2d 710, 714 (1967).

The gift clause of the Arizona Constitution establishes the standard against which A.R.S. § 15-183(U) is measured. The gift clause provides as follows:

Neither the State, nor any county, city, town, municipality, or other subdivision of the State shall ever give or loan its credit in the aid of, or *make any donation or grant, by subsidy or otherwise, to any individual, association, or corporation*

Ariz. Const. art. IX, § 7 (emphasis added).

In *Wistuber v. Paradise Valley Unified School District*, the Arizona Supreme Court established a two-part test to determine when agreements between public entities and private parties violate the gift clause. 141 Ariz. 346, 349, 687 P.2d 354, 357 (1984). The court held that the agreement must serve a recognized public purpose and the public benefit to be obtained from the private entity must constitute "valuable consideration" -- that is, the value received by the public must not be far exceeded by the consideration paid by the public. *Id.* In making these two determinations with respect to the two types of State funds provided to charter schools -- State aid and stimulus funds -- we take a broad view of the facts, evaluate the reality of the transaction in terms of its purpose and the consideration given, and give appropriate deference to any legislative determinations. *Id.*

1. Allowing a charter school to retain, as its property, the State aid that it receives does not automatically violate the gift clause.

Applying the two elements of the *Wistuber* test -- public purpose and valuable consideration -- to A.R.S. § 15-183(U) leads us to conclude that the statute does not violate the gift clause of the Arizona Constitution. The provision of public education to Arizona's youth is a constitutionally recognized public purpose. Ariz. Const. art. XI, § 1 (directing the Legislature to enact laws to establish and maintain a general and uniform public school system). The State receives a public education benefit from the State funds that it pays to charter schools to educate approximately 30,000 students at over 220 locations throughout Arizona. Arizona Department of Education, FEDERAL GRANT PERFORMANCE REPORT 4 (1997). Furthermore, because the State aid paid to charter schools for their educational services is substantially similar to the State aid paid to other public schools and the core requirements imposed on charter schools are also imposed on public schools (all must comply with educational goals established by the State Board, as well as health, safety, civil rights, and special education requirements), the consideration exchanged is theoretically proportional.

In this case, we defer to the Legislature's election to expand educational choices and to provide learning environments that will improve pupil achievement. A.R.S. § 15-181(A). We defer as well to the legislative determination of the value of such services. In considering these factors, we find that A.R.S. § 15-183(U), which allows charter schools to retain, as their property, the State aid (and the goods and property purchased with that aid), theoretically satisfies the *Wistuber* test and is therefore constitutional.

We caution, however, that although we view A.R.S. § 15-183(U) as constitutional when theoretically applied to the general issue of State aid, payments to individual charter schools may violate the gift clause if the funds are not used for a public purpose or if the consideration paid by the State far exceeds the public value that the school provides. In other words, while the statute may be constitutional, its application to a given set of facts may be unconstitutional. Compare *Tennessee v. Garner*, 471 U.S. 1, 11 (1985) (holding that a state statute authorizing a police officer to use all necessary means to arrest a fleeing suspect was constitutional on its face but unconstitutional insofar as it authorized the use of deadly force to seize an unarmed, nondangerous suspect); *United States v. Grace*, 461 U.S. 171, 183 (1983) (holding that a statute prohibiting demonstrations on the grounds of the Supreme Court was constitutional on its face but unconstitutional when applied to prohibit picketing on public sidewalks around the building). As the Arizona Supreme Court noted in *Wistuber*, one must take a "panoptic view" of the facts of each transaction and must make the determination of constitutionality based on actual, rather than abstract, facts. 141 Ariz. at 349, 687 P.2d at 357. Thus, the analysis in this opinion should serve as a guide and be applied to the unique facts of each case to determine whether the payment of State aid to an individual charter school violates the gift clause of the Arizona Constitution. Attention should be given to whether the charter school actually spent State aid for educational purposes and whether the State received the quality and quantity of services for which it paid.

2. Allowing a charter school to retain, as its property, the stimulus funds awarded by the State Board does not automatically violate the gift clause.

The *Wistuber* test also applies to stimulus funds. The public purpose supporting the award of stimulus funds is the facilitation of a public education for Arizona's children by assisting charter schools and those applying to become charter schools with money for start-up and renovation costs, A.R.S. § 15-188(A), because charter schools, unlike other public schools, lack power to issue bonds or tax. A.R.S. § 15-185(B)(8). The legislatively required consideration is the charter school's assurance of opening a school and providing an education to Arizona's children within eighteen months of the award. A.R.S. § 15-

188(B)(1), (2) (requiring a stimulus fund recipient to return the funds, with interest, if the charter school does not begin operating within eighteen months).

With stimulus funds, it is difficult to compare the proportionality of the value received by the State with the consideration paid by the State because each award differs in purpose and amount. Thus, we defer to the Legislature to determine the relative value of the consideration received for each stimulus grant. We trust that the Legislature has considered that charter schools will offer educational choice and improve pupil achievement, the significance of the need, and the public interest to be served in making the award. *See* A.A.C. R7-2-316(F) (establishing the factors to be considered in making the stimulus fund award); *cf. Wistuber*, 141 Ariz. at 349-50, 687 P.2d at 357-58 (noting that courts will give appropriate deference to the findings of the governmental body and will not assume disproportionality of consideration). Consequently, as long as the charter school uses the funds for the public purpose mandated by the State Board in making the award and provides the legislatively required consideration, we cannot find that the statutory provision allowing a charter school to retain stimulus funds, as its property, theoretically violates the gift clause.

As we previously observed, one must take a "panoptic view" of the facts of each transaction and must make the determination of constitutionality based on actual, rather than abstract, facts. *Id.* For example, if a charter school receives stimulus funds but uses them for noneducational purposes, it would violate the gift clause and expose the recipient to a broad range of sanctions. The public purpose and adequacy of consideration factors should be applied to the specific facts of each case to determine whether individual schools may have violated the gift clause in the receipt and use of stimulus funds.

B. Pursuant to A.R.S. § 15-183(U), Charter Schools Retain Ownership of All Property That They Accumulate, Including Cash, Realty, Capital Equipment, and Other Assets, Subject to Certain Conditions.

You also inquired (i) whether a charter school may retain ownership of property purchased with State funds when it closes, and (ii) who is entitled to proceeds if a charter school were to liquidate its assets. The answer to those questions depends on a number of factors. Therefore, we are only able to answer your questions generically because we are without specific facts on which to base an analysis.

Section 15-183(U), A.R.S., states that "[a]ll property accumulated by a charter school shall remain the property of the charter school." The primary rule of statutory construction is to give effect to the Legislature's intent. *State v. Korzep*, 165 Ariz. 490, 493, 799 P.2d 831, 834 (1990). To determine intent, we look first to the statute's language. *Kriz v. Buckeye Petroleum Co., Inc.*, 145 Ariz. 374, 377, 701 P.2d 1182, 1185 (1985). When the statutory language is unambiguous, it is usually conclusive, absent a clearly expressed

legislative intent to the contrary. *State ex rel. Corbin v. Pickrell*, 136 Ariz. 589, 592, 667 P.2d 1304, 1307 (1983).

The Legislature authorized charter schools to retain "all" property that they accumulate. A.R.S. § 15-183(U). We interpret this unambiguous authorization to include all funds charter schools receive from the State and property purchased with those funds.

If facts demonstrate that a charter school has violated the gift clause of the Arizona Constitution or the State determines that the school breached the charter contract, the State would have a cause of action against the charter school.³ See *Young v. Border Broad. Co., Inc.*, 75 Ariz. 298, 302, 255 P.2d 888, 890 (1953). If the State were successful with its action, it would obtain a judgment against the school (and perhaps others) for the amount of State money that was overpaid.⁴ This process is time consuming, and the State's attempts to collect the debt or to secure its claim would be delayed until after it received a judgment from the court. Additionally, in their first year of operation, charter schools are paid one-third of their yearly apportionment (based on an estimated student count) before opening their doors, they may have few assets, and staff members may be unskilled in the business of operating a school, thus increasing the financial risk to the State and making successful collection difficult.⁵

To protect the taxpayers' financial interests, the Legislature may wish to consider several actions such as establishing a statutory lien on the school's property immediately on the transfer of State funds, requiring a performance bond, or clarifying that a charter school operator is a trustee or fiduciary of State funds. Without financial assurances, State

³ Of course, the State would have criminal and other remedies if State funds were obtained fraudulently or misused. See, e.g., A.R.S. §§ 13-1802 (theft), 35-212(A) (civil remedy to recover State money illegally paid plus 20%, interest, costs, and attorney fees); 13-2202 (deceptive business practices). A court may also impose a constructive trust to prevent unjust enrichment of a charter school that holds property to the detriment of the State. See *Burch & Cracchiolo, P.A. v. Pugliani*, 144 Ariz. 281, 285, 697 P.2d 674, 678 (1985).

⁴ We note that other creditors may also have a claim against the assets including those with secured interests (A.R.S. §§ 47-9101 through -9507), statutory liens (A.R.S. §§ 33-931 through -1015 (including health care provider liens, judgment liens on real property, mechanics' and materialmen's liens, and personal property liens)), judgments, or tax liens.

⁵ A charter school that files for bankruptcy would pose even more onerous collection problems for the State and successful collection in those cases would depend on whether the bankruptcy was filed as a chapter 7, 11, or 13, whether any exceptions to discharge of the debt applied, the amount of funds in the estate, and the number and amount of the claims of secured and non-secured creditors. See, e.g., 11 U.S.C. §§ 523, 701, 1101, and 1301.

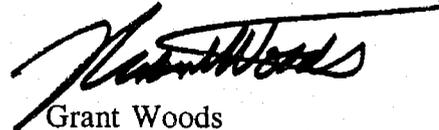
The Honorable Ruth Solomon
February 24, 1998
Page 7

funds could be at substantial risk should a charter school fail to perform or inadequately perform the duties required by State law and its charter contract.

Conclusion

We conclude that, in the abstract and absent specific facts to the contrary in a particular situation, A.R.S. § 15-183(U), which allows a charter school to retain all property it accumulates, is constitutional. Under current law, upon closing, a charter school would be allowed to keep the property accumulated by the school, including property purchased with funds received from the State, assuming that the charter school used the funds for a public purpose and provided adequate consideration for the funds it received. The disposition of the proceeds from the liquidation of the assets of a charter school would be determined by its legal and contractual obligations to the State and others.

Sincerely,



Grant Woods
Attorney General