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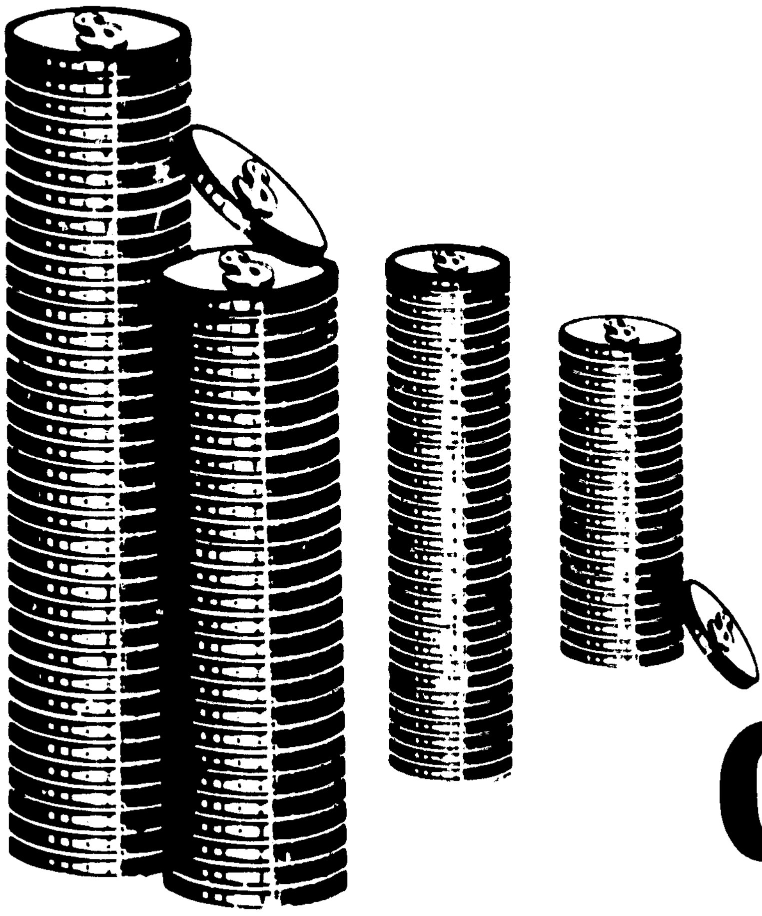
ABSTRACT

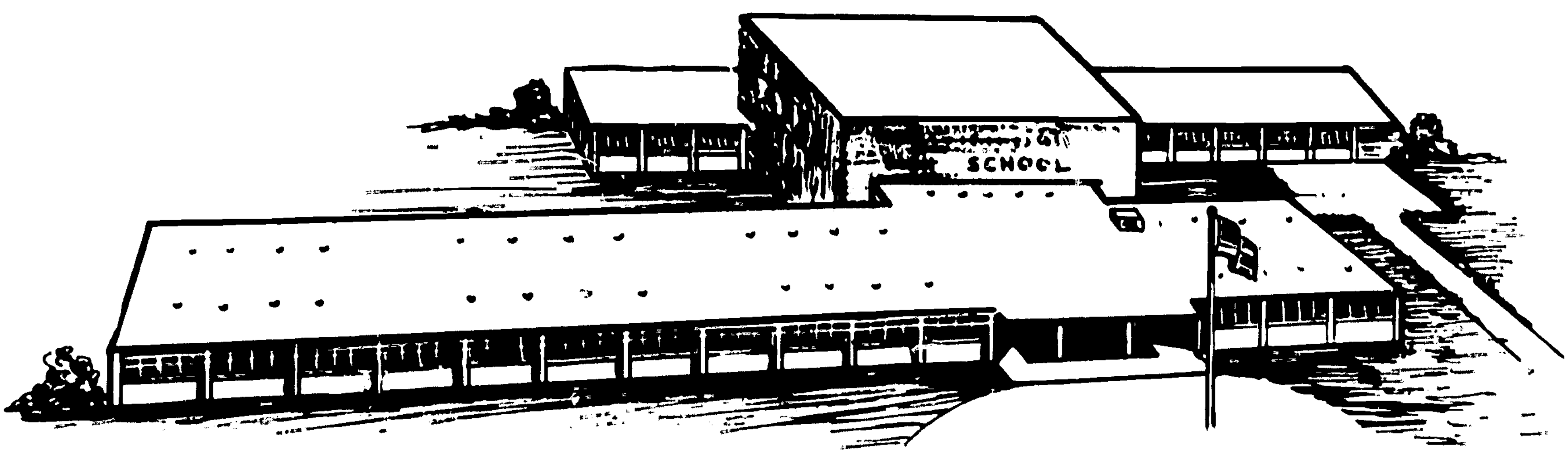
Information is presented regarding the various methods that may be employed by Pennsylvania school districts to finance building construction. Consideration is given to the following methods--(1) pay-as-you-go, (2) temporary loans, (3) general obligation bonds, (4) employment of municipality authorities, (5) employment of the State Public School Building Authority, and (6) state reimbursement. (FS)



FINANCING SCHOOL BUILDING CONSTRUCTION

AN INVESTMENT IN EDUCATION

SCHOOL EXECUTIVE SERIES
NO. 5



Commonwealth of Pennsylvania
DEPARTMENT OF PUBLIC INSTRUCTION
Harrisburg
1964

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MESSAGE FROM THE SUPERINTENDENT

The school laws of Pennsylvania delegate to the board of school directors of each district the responsibility of providing the necessary grounds and suitable school buildings to accommodate all the children in the district between the ages of six and twenty-one years who attend school. In discharging this highly important responsibility, the decisions made by the members of the board affect the educational program in the district for the life of the buildings, conceivably for more than fifty years.

When it comes to capital expenditures, it is natural to want the best possible facilities, but a school board must be realistic. Quite frequently school building construction is a compromise between what is educationally desirable and that which is financially possible. This publication outlines the various methods that may be employed by a school district to finance building construction. The selection must be made by local school board members.

Charles H. Boehm

Commonwealth of Pennsylvania
DEPARTMENT OF PUBLIC INSTRUCTION
Bureau of Building
Construction and Transportation
Harrisburg - 17126

FINANCING SCHOOL BUILDING CONSTRUCTION

Methods of Financing School Building Construction

The General Assembly has delegated extremely broad powers to local school boards with respect to ways and means of financing the cost of constructing or reconstructing school plant facilities. The School Laws authorize local school boards to finance such construction in any of the following ways:

1. Out of current tax receipts on a pay-as-you-go basis
2. By floating a temporary loan
3. By issuing general obligation bonds
4. By lease agreement on a rental basis for approved facilities constructed by --

    a. A Municipality Authority
    b. The State Public School Building Authority
    c. A profit or non-profit corporation
    d. A partnership
    e. An association
    f. Individual persons

Districts are free to choose the method of financing to be used. However, such choice is often limited by such variable factors as credit rating, type of administrative organization, urgency of need for the facilities, constitutional and statutory limitations on borrowing and taxing powers, and the current status of the bond market. No hard and fast rule can be given as to which method is best for districts to use. A comparative study of costs should be made of all methods before selecting one.

The Pay-As-You-Go Method

This is no doubt the most economical method. However, most school districts usually need all their current tax receipts and State aid for operation and maintenance. Consequently this method is not generally used except by districts having a large tax base or by districts having little capital outlay needs.

Temporary Loans

It would appear that the next most economical method is to finance the cost of the project by floating a temporary loan. Since the interest and principal sum must be repaid within a period of five years, this method of financing is usually confined to projects involving relatively small capital outlay.

Most school districts are unable to finance school building construction either on the pay-as-you-go plan or by temporary loans. Thus it is necessary either to issue general obligation bonds or to resort to some type of authority financing.

General Obligation Bonds

Experience indicates that, in general, lower net cost can be realized if the facilities are constructed by the school district through the issuance of general obligation bonds. Moreover, this method of financing is more flexible than authority type of financing and gives the district a greater degree of local control over the project as it moves through various stages. However, a large majority of our school districts are unable to use this method because of the constitutional limitation on borrowing capacity. School districts may not issue general obligation bonds in an amount which would cause the total indebtedness of the district to exceed seven per cent of the last assessed valuation taxable for school purposes. Since assessments are extremely low in most districts, the seven per cent limitation imposed by the Constitution will not permit many districts to raise sufficient funds to defray the cost of the proposed construction.

Municipality Authorities

The most commonly used method of financing the cost of school plant construction has been to employ a municipality authority - a separate corporate entity usually created by the school districts to construct the facilities and rent them to the districts on a long-term lease. The Authority issues its own bonds and pays the interest and principal as the bonds mature from rentals paid by the school districts from current funds.

This method of financing is somewhat less flexible than the general obligation bond method but more flexible than financing through the State Public School Building Authority. If the project is constructed by a municipality authority, the bond issue may be amortized over such a term as may be agreed upon by the authority and the districts, whereas projects financed through the State Public School Building Authority have a lease hold term of 37-38 years. Thus, amortizing the bonds over a shorter period may result in a lower total interest cost even though the rate may be higher than it would be if financed through the State Public School Building Authority.

The State Public School Building Authority

The second most commonly used method of financing has been that of employing the State Public School Building Authority, an agency of the Commonwealth created by the General Assembly, to construct the facilities and rent them to the districts on a long-term lease. The Authority issues its own bonds which are amortized from rentals paid by the school districts from current funds.

While this method of financing does not permit as high a degree of flexibility as other methods, it usually offers a rate of interest lower than municipality authorities and, therefore, becomes attractive to districts with poor credit rating. In the past these Authority bonds have not been marketed directly to the public. They have been sold to the State Employes' Retirement Fund and the Teachers' Retirement Fund. The Authority now solicits public bids for the sale of its bonds, thereby entering the competitive money market.

A profit or non-profit corporation, Partnership, Association, Individual persons

These methods of financing school building projects are not used, but are provided for in the Public School Code of 1949, as amended.

It should be noted that a profit corporation, partnership, association or individual persons, will be subject to taxes which could have an effect upon the cost of the building project to the school district.

State Reimbursement

The Commonwealth reimburses local school districts for a portion of the cost of financing approved school building projects except when the work is done with current funds. Such reimbursement for any project is based upon an amount obtained by multiplying the rated pupil capacity of the building by either $1100 (in the case of elementary schools) or $1700 (in the case of secondary schools), or the actual cost of construction, whichever is the lesser amount, plus site acquisition costs, cost of rough grading to receive the building and sewage disposal costs.

State Reimbursement - Continued

Example:

Elementary school	180	pupils
	x $1100	per pupil
	$198,000	potential for State reimbursement based on approved construction cost, architect's fee not to exceed 6% of such cost, and essential fixtures and equipment.

Plus:

Site Cost	$10,000
Rough Grading	2,000
Sewage	3,000
Total	$213,000

The formula used in determining the State's share of annual rental payments made by the school district is as follows:

Annual rental x percentage of project reimbursable x the square of district's capital account reimbursement quotient equals State's share of rental.

Assuming in the example cited the total bond issue to be $250,000, an annual rental of $17,350 ($250,000 @ 4% for 30 years plus 20% reserve), a reimbursable percentage of 85.2% ($213,000 ÷ $250,000), a capital account reimbursement quotient of .70, the computation is as follows:

Rental x percentage reimbursable x reimbursement fraction

	$17,350	85.2		$.70^2$ (*)
=	$17,350 x	85.2	x	.49
=		$14,782.20	x	.49

= $7,243.27 = State's share of rental payment

$17,350.00 - $7,243.27 = $10,106.73 = District's share of rental payment.

(*) When the Capital Account Reimbursement Quotient is less than .50, the formula is:

$$.50 \times CARQ^2 + .25 \times CARQ$$

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