[J-67-2006]
IN THE SUPREME COURT OF PENNSYLVANIA
MIDDLE DISTRICT

CAPPY, C.J., CASTILLE, SAYLOR, EAKIN, BAER, BALDWIN, FITZGERALD, JJ.

PROGRAM ADMINISTRATION SERVICES, INC., F/K/A R.D. FOWLER & ASSOC., INC.,	:	No. 136 MAP 2005
Appellee	:	Appeal from the Order of the Commonwealth Court entered on May 19, 2005 at No. 2535 CD 2003, reversing the Order of the Court of Common Pleas of
v.	:	Dauphin County, Civil Division, entered on November 13, 2003 at No. 2992 S 2001
DAUPHIN COUNTY GENERAL AUTHORITY,	:	
Appellant	:	RE-SUBMITTED: May 18, 2006

OPINION

MR. JUSTICE SAYLOR[1] **DECIDED: August 20, 2007**

This appeal by allowance involves the issue of whether the board of directors of the Dauphin County General Authority may terminate, without cause, contracts executed by its predecessor board relating to the administration of certain school-related financing activities.

Appellant, the Dauphin County General Authority (the "Authority"), is a corporate agency of the Commonwealth created by Dauphin County pursuant to the Municipality

[1] This appeal was reassigned to this author.

Authorities Act.[2] The act authorizes the creation of municipality authorities for a wide range of purposes, one of which is to secure long term financing for public projects or uses, including public schools, by issuing revenue bonds for a term not exceeding forty years. Included among its powers under the act, the Authority may "make agreements with the purchasers or holders of the bonds or with others in connection with any bonds, whether issued or to be issued, as the authority shall deem advisable." 53 Pa.C.S. §5607(d)(12).

Pursuant to these powers, in 1986 the Authority launched a program to provide financial assistance to Pennsylvania school districts seeking to borrow money to finance new capital improvements or refinance existing debt. This program, known as "School Pool I," was funded by $200 million in proceeds from the public sale of 40-year tax-exempt bonds set to mature in 2026. The governing agreement for this project made Dauphin Deposit Bank (later Allfirst Bank) the trustee of the funds, and Appellee, Program Administration Services, Inc., the program administrator. The Authority began a similar program in 1997, known as "School Pool II," with $250 million from the public sale of tax-exempt 35-five year bonds set to mature in 2032. A similar agreement made Commerce Bank the trustee and, again, made Appellee the program administrator.[3]

Under both of these arrangements (the "Program Administration Agreements"), the bonds were purchased by private investors and the proceeds were used to create a

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[2] Act of May 2, 1945, P.L. 382, No. 164, §§1-19 (as amended, 53 P.S. §§301-322). The act was recodified and replaced by the Act of June 19, 2001, P.L. 287, No. 22, § 1 (as amended, 53 Pa.C.S. §§5601-5623). With regard to the issues involved in this case, the current statute is substantively identical to the former one. See 53 P.S. §306(B)(i) (repealed and recodified as amended at 53 Pa.C.S. §5607(d)(12)).

[3] At the time the 1986 agreement was executed, Appellee was conducting business as R.D. Fowler & Associates. It later changed its name to Program Administration Services, Inc., and is listed as such in the 1997 agreement.

"pool" of money that was available for the Authority to lend to qualifying school districts. The Authority lends money from these pools to school districts for dedicated purposes such as construction or reconstruction of school facilities, or debt refinancing. As school districts repay the principal and interest on their loans, interest is paid to the bondholders and principal is returned to the pool, from which it is available to be re-loaned. The Authority thus provides "conduit" financing, as it is positioned between school-district borrowers and the private-investor lenders. As program administrator, Appellee is responsible, inter alia, to market the programs to prospective school districts, assist school districts with their applications, calculate note payments, bill the school districts, and assist the Authority in securing investment of funds with the trustee banks. The Program Administration Agreements provide that they shall continue in force until one of the following three conditions occurs: (1) no portion of the bonds remains outstanding and unpaid; (2) continuing failure of Appellee to perform in any material respect; or (3) mutual consent of the parties to terminate.

In November 2000, under a newly-appointed board of directors, the Authority notified Appellee that it intended to terminate the contracts without cause. Appellee initiated a declaratory judgment action in the trial court seeking a judicial determination that the contracts may not be terminated outside the terms specified by the agreements. The trial court ultimately entered a declaratory judgment in favor of the Authority, however, concluding that any agreements entered into by the parties or their predecessors were unenforceable as against the current Dauphin County General Authority. See Program Admin. Services, Inc. v. Dauphin County Gen. Auth., No. 2992 S 2001 (C.P. Dauphin 2003).

On appeal, a divided, en banc panel of the Commonwealth Court reversed in a published decision. Program Admin. Services, Inc. v. Dauphin County Gen. Auth., 874

A.2d 722 (Pa. Cmwlth. 2005) (en banc). The majority reasoned that the central question was whether the Program Administration Agreements involved a governmental function or a proprietary function, because contracts involving governmental services may be terminated by a successor governing body, without cause, irrespective of the termination date or other procedures for termination set forth in the contract. Id. at 725 (citing Lobolito, Inc. v. North Pocono Sch. Dist., 562 Pa. 380, 755 A.2d 1287 (2000)). The majority then stated that, in deciding whether the activity at issue was governmental or proprietary in nature, it should employ the test set forth in County of Butler v. Local 585, Service Employees Int'l Union, AFL-CIO, 631 A.2d 1389 (Pa. Cmwlth. 1993). Under this test, a court considers whether the activity: 1) is one that government is not statutorily required to perform; 2) also may be carried on by private enterprise; or 3) is used as a means of raising revenue.

Applying this test to the present case, the majority held that the Authority's activity of lending money to school districts was proprietary in nature since the Authority was not statutorily required to perform the activity and it is one that is carried on by many private lenders. The majority explained that the "mere fact that the Authority lends money to a school district for school construction does not make the act of lending governmental in character any more than it would be if the loan was made by a private bank." Program Admin. Services, 874 A.2d at 728. Furthermore, the majority distinguished this Court's decision in Lobolito, on the basis that Lobolito involved the decision of whether to build a school building -- a clear governmental function. In this case, however, the Authority is not involved in any decision to build schools, but only in financing such projects once the decision is made by another body. Likewise, the majority distinguished another Commonwealth Court case, State Street Bank & Trust Co. v. Commonwealth, 712 A.2d 811 (Pa. Cmwlth. 1998), on the basis that the funds

being lent in that case were assets of the state, whereas here they are assets of the bondholders, akin to the holdings of private depositors. Thus, the majority reasoned:

> Although the School Pool programs unquestionably facilitate school construction projects and so serve a valuable public purpose, it is incontrovertible that financing of school construction does take place through private channels and would do so if the School Pool programs cease to exist.

Id. at 729.

Finally, the majority also agreed with Appellee's alternative argument that Section 5607(d)(12) represents a "statutory exception" to the general rule that current governing bodies may not bind successors with regard to governmental functions. Program Admin. Services, 874 A.2d at 729. Thus, by noting that, under Section 5607(d)(12) of the Municipality Authorities Act, administration agreements are statutorily permitted to be coextensive with the full maturity period of the bonds, the court deemed the Program Administration Agreements fully enforceable.

Judge Cohn Jubelirer authored a dissenting opinion, joined by Judge Pellegrini, in which she used the same test from County of Butler, but concluded that the conduit financing employed by the Authority is distinct from ordinary borrowing, since the funds were raised by the sale of bonds and the bondholders have no recourse against the Authority. Further, the ultimate borrowers are the school districts, the ultimate lenders are the bondholders, and unlike a private bank, the Authority earns no profit. She further noted that, in Lobolito, this court considered the "crux" of the agreement in resolving the governmental versus proprietary question, and Lobolito concluded that the "crux" of the agreement was the construction of a new school, and that the "services aspect of the agreement [i.e., that portion pertaining to water and sewage treatment] would be devoid of meaning without the school board's predicate promise to build the school." Program Admin. Services, 874 A.2d at 733 (Cohn Jubelirer, J., dissenting).

Similarly, Judge Cohn Jubelirer opined that the "crux" of the Program Administration Agreements is the financing of new capital improvements for the public school system, which is ancillary to the capital improvement projects themselves; therefore, in her view, they involve governmental functions.

In a separate dissent joined by Judge Cohn Jubelirer, Judge Pellegrini expressed discomfort with the idea that a public entity such as the Authority could be locked into a 40-year contract with a private party notwithstanding changes in the Authority's governing board and the concomitant new policies that the successor boards may wish to implement. He noted, in this regard, that the purpose of the rule allowing government entities to be free from long-term contracts entered into by their predecessor boards is to avoid such "capture" by private interests at the potential expense of public interests as ultimately expressed by the electorate through the ballot box. See id. at 730-31 (Pellegrini, J., dissenting).

Both the trial court and the Commonwealth Court panel concentrated their analysis primarily on the distinction between contracts relating to governmental functions and those pertaining to proprietary or business functions. Indeed, as noted by the Commonwealth Court majority and by this Court in Lobolito, Inc. v. North Pocono Sch. Dist., 562 Pa. 380, 755 A.2d 1287 (2000), such a distinction has been recognized in Pennsylvania since the mid-Nineteenth Century. See id. at 384, 755 A.2d at 1289 (citing Western Saving-Fund Soc'y of Phila. v. City of Phila., 31 Pa. 175, 183 (1858) (distinguishing governmental contracts, or contracts encompassing "things public," from proprietary contracts, or contracts encompassing "things of commerce")). Likewise, the parties presently open their arguments to this Court by reference to this consideration and differ chiefly in whether the functions performed by Appellee should be deemed

governmental or proprietary in nature. See Brief for Appellant at 15-27; Brief for Appellee at 19-29.

The policy basis for the governmental-proprietary distinction, as developed in the common law of this Commonwealth, was discussed at length in Lobolito, in which the Court there undertook a historical survey, see Lobolito, 562 Pa. at 384-87, 755 A.2d at 1289-91, and recognized the underlying rationale as it had previously been expressed:

> The obvious purpose of the rule is to permit a newly appointed governmental body to function freely on behalf of the public and in response to the governmental power or body politic by which it was appointed or elected, unhampered by the policies of the predecessors who have since been replaced by the appointing or electing power. To permit the outgoing body to 'hamstring' its successors by imposing upon them a policy[-]implementing and to some extent, policy[-]making machinery, which is not attuned to the new body or its policies, would be to most effectively circumvent the rule.

Id. at 385, 755 A.2d at 1289-90 (quoting Mitchell v. Chester Housing Auth., 389 Pa. 314, 324-25, 132 A.2d 873, 878 (1957)). Lobolito also noted that the rule's only exception recognized at common law pertains to situations in which "considerations of urgency and necessity, especially when coupled with the stipulated public interest and absence of bad faith or ulterior motivation," militated in favor of upholding the contract at issue. Id. at 386, 755 A.2d at 1290 (quoting MacCalman v. County of Bucks, 411 Pa. 316, 321, 191 A.2d 265, 267 (1963)).

Thus, the precept that governmental contracts are voidable in some range of circumstances is a common-law rule premised upon considerations of public policy. In applying this principle, however, courts should not lose sight of the respective roles of the General Assembly and the courts in terms of establishing public policy. In particular, it is the Legislature's chief function to set public policy and the courts' role to

enforce that policy, subject to constitutional limitations. See generally Parker v. Children's Hosp. of Philadelphia, 483 Pa. 106, 116, 394 A.2d 932, 937 (1978) (explaining that "the power of judicial review must not be used as a means by which the courts might substitute [their] judgment as to the public policy for that of the legislature"). Accordingly, with the common-law framework as a backdrop, and absent constitutional infirmity, the Legislature may nonetheless modify the approach in particular sets of circumstances. See generally Hilkmann v. Hilkmann, 579 Pa. 563, 578-799, 858 A.2d 58, 68 (2004); Scheipe v. Orlando, 559 Pa. 112, 116, 739 A.2d 475, 477 (1999); Gingold v. Audi-NSU-Auto Union, A.G., 389 Pa. Super. 328, 348, 567 A.2d 312, 323 (1989) ("The function of the common law is to fill the interstices left by the legislatures." (quotation marks omitted)). This is undoubtedly what the Commonwealth Court panel meant by the term, "statutory exception."

The Commonwealth Court previously recognized this principle in Chichester Sch. Dist. v. Chichester Educ. Ass'n, 750 A.2d 400, 403 (Pa. Cmwlth. 2000), where it upheld certain holdover collective bargaining agreements entered into by a predecessor school board as against its successor board by relying upon the statutory authority for such agreements contained in the Public Employee Relations Act. The court acknowledged that the previous board's actions were governmental in character, but continued:

> Here, the contracts executed between the Board and the [employee organizations] were actually ratified by the Board at public hearings approximately two years prior to the election and seating of the successor Board members. Sections 701 through 904 of the Public Employee Relations Act (PERA) provide the Board members with the statutory authority to engage in negotiations and execute such contracts with employee organizations.

Id. at 404 (footnotes omitted); see also Falls Township v. Scally, 115 Pa. Cmwlth. 56, 59, 539 A.2d 912, 914 (1988) ("If Scally was performing a governmental function, then,

absent a statute to the contrary, the outgoing Board of Supervisors had no authority to tie the hands of its successors." (emphasis added)); Altoona Hous. Auth. v. City of Altoona, 785 A.2d 1047, 1053 (Pa. Cmwlth. 2001) ("The Court agrees with the Housing Authority as to the vitality of the general principle that a board exercising legislative authority lacks the power to bind its successors as to governmental functions. Nevertheless, specific statutory provisions may affect the analysis in particular situations." (citations omitted)).

As applied here -- and as noted above -- the General Assembly has expressly authorized municipality authorities "to make agreements with the purchasers or holders of [authority] bonds or with others in connection with any bonds . . . as the authority shall deem advisable," 53 Pa.C.S. §5607(d)(12); see also id., §5607(d)(6) (enabling municipality authorities to "finance projects by making loans, which may be evidenced by and secured as may be provided in loan agreements, mortgages, security agreements or any other contracts, instruments or agreements, which contracts, instruments or agreements may contain such provisions as the authority shall deem necessary or desirable for the security or protection of the authority or its bondholders" (emphasis added)). These provisions embody a legislative policy decision favoring predictability, stability, and certainty with regard to some range of matters connected with public bond issues by municipality authorities. Because bond terms may be as long as forty years, these provisions authorize the execution of contracts that outlast the terms of the individual board members who approve the contracts, which are generally limited to five years. See 53 Pa.C.S. §5508(b). To the extent this legislative policy is in tension with the competing common-law concern relating to the freedom of a new board to respond to popular pressures, the latter must yield to the former. For purposes of this inquiry, then, we must determine whether the Program Administration Agreements

constitute agreements "in connection with" the Authority's 1986 and 1997 bond issues for purposes of Section 5607(d)(12).[4]

We find that they do. Although the Authority extensively develops that the agreements are not directly intertwined with, or validated by, the 40-year bond issues authorized by Section 5607(d)(12), see Brief for Appellant at 28, the statutory language does not contemplate such specific intertwining with, or validation by, particular documents. Rather, the same passage that enables bond issues, Section 5607(d)(12), also authorizes contracts "with others in connection with" such bonds, as set forth above. The most reasonable conclusion is that a contract under which an entity, such as Appellee, is to provide support for the administration of a bond program -- including marketing the bonds to school districts and investing the funds on deposit with a trustee -- is an agreement "with [another] in connection with" the bond issue.[5],[6]

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[4] The issue is preserved for our consideration because Appellee highlighted the statutory authorization in its underlying action, see First Amended Complaint at ¶4, RR. 2a-3a, raised the issue before the Commonwealth Court, see Program Admin. Services, 874 A.2d at 729, and repeats its argument to this Court. See Brief for Appellee at 30-33.

[5] The dissent indicates that our understanding of the word "others" within the statutory phrase, "to make agreements . . . with others in connection with any bonds," is overly broad, and would apparently constrain its meaning to the trustee banks. See Dissenting Opinion, slip op. at 2. We may assume, however, that if the Legislature had intended so specific a limitation, it would have said so. Moreover, unlike the dissent, we do not view the promotion of predictability, stability, and regularity as to such agreements as "vitiating the Authority's ability to carry out its governmental functions." Id. at 3 n.1.

[6] This conclusion is not intended to imply any predicate finding by this Court that the Program Administration Agreements embody governmental functions. Rather, the point here is that the existence of statutory authorization for the contracts eliminates the need to distinguish between governmental and proprietary functions.

Relatedly, the Authority also urges that the trust indenture documents that secure the bonds make no commitment to the duration of Appellee's services as program administrator, but rather, define that term to include "any other person appointed by the Authority, from time to time, to administer the Program . . .." Trust Indenture, dated July 1, 1986, at 15; see RR. 280a. The Authority suggests that this and other provisions of these documents clearly refrain from granting any rights to Appellee to continue as administrator indefinitely, and correspondingly, give the Authority the discretion to replace Appellee at will. In this respect, the Authority also notes that nothing in Section 5607(d)(12) requires the term of a program administrator to be coextensive with the maturity date of the issued bonds.

While we agree that the statute does not require such coextensiveness, the Legislature would not need to require long-term contracts in order to authorize municipality authorities to enter into legally-binding, long-term contracts; it needed only to authorize them. Additionally, we have no present occasion to consider whether a proper interpretation of the specific provisions of the indenture agreements and/or the Program Administration Agreements would affirm that Appellee was intended to be replaceable at the Authority's sole discretion. Based on the questions framed in the Authority's Petition for Allowance of Appeal, review in this case is limited to whether conduit financing services constitute a governmental activity; whether the mere existence of statutory authority for long-term contracts ancillary to financing by a municipality authority make administrative service contracts enforceable against the Authority's subsequent governing boards; and whether the agreements should be deemed unenforceable as against public policy. See Petition for Allowance of Appeal at 6. In answering the second question affirmatively, the first was rendered moot. See

supra note 6. As to the third, we have already observed that the General Assembly's policy choices as reflected in the statute are controlling.[7]

This is not to say that there can never be circumstances under which a successor board of directors may avoid a contract held over from its predecessor, even where such a long-term contract is statutorily authorized. In this respect, it is relevant that the governmental-functions test was originally directed to bad faith efforts on the part of "lame duck" governing bodies to "handcuff" their successors. Fraternal Order of Police, E.B. Jermyn Lodge No. 2, by Tolan v. Hickey, 499 Pa. 194, 200, 452 A.2d 1005, 1008 (1982). See generally Chichester, 750 A.2d at 403 ("An outgoing board that attempts to create these types of long-term obligations . . . is commonly referred to as a 'lame duck' board."). In Mitchell, for example, the Housing Authorities Act provided for gubernatorial appointment of a majority of the Chester Housing Authority. When a new governor was elected, the prospect of a change in control of the board prompted the existing board to enter into a five-year employment contract with the secretary of the authority, a contract that this Court allowed the incoming board to avoid. Compare Falls Township v. McManamon, 113 Pa. Cmwlth. 504, 508-09, 537 A.2d 946, 947 (1988) (invalidating a holdover police-chief employment contract entered into by a lame-duck board of supervisors), and Moore v. Luzerne County, 262 Pa. 216, 220, 105 A. 94, 95

[7] In forwarding its policy argument, the Authority asserts that Appellee's faulty business judgment has caused it to lose confidence in Appellee as administrator. Whether Appellee's alleged deficiencies in this regard would supply the Authority with cause under the terms of the Program Administration Agreements to terminate Appellee's role as administrator is a question that is not before us in view of the limited scope of this appeal. As discussed, we here determine only that the Program Administration Agreements constitute agreements "in connection with" the Authority's 1986 and 1997 bond issues for purposes of Section 5607(d)(12), and thus, assuming that their effective period extends beyond the term of the governing board that approved them, they are enforceable against successor boards.

(1918) (denying recovery on a contract between a board of county commissioners and an engineer, where the contract was executed in bad faith just before the expiration of the commissioners' terms), with Horvat v. Jenkins Township Sch. Dist., 337 Pa. 193, 10 A.2d 390 (1940) (upholding a supervising principal's employment agreement extending beyond the school board's term where the parties entered into the agreement in good faith well before the expiration of that term). Thus, nothing in this Opinion should be understood to foreclose the possibility that the avoidance of a holdover contract entered into in bad faith by an outgoing board may ultimately be upheld, notwithstanding the presence of legislation authorizing the making of the contract in the first instance. However, that situation is not presently before us.

For the foregoing reasons, the judgment of the Commonwealth Court is affirmed.

Mr. Chief Justice Cappy and Messrs. Justice Castille, Baer and Fitzgerald join the opinion.

Mr. Justice Eakin files a concurring opinion.

Madame Justice Baldwin files a dissenting opinion.