

**SEVENTH ANNUAL PRE-CONVENTION SCHOOL LAW SEMINAR**

**New York State School Boards  
Association AND New York State  
Association of School Attorneys**

**rochester, New York  
October 23, 2003**

**GROWING A MONEY TREE  
New Sources of Revenue for School Districts  
In Tough Fiscal Times**

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**I. Introduction and Overview:**

Just weeks after the 2003 budget battle in which the State Legislature overrode the Governor's veto, the Court of Appeals decided the Citizens for Fiscal Equity case, Campaign for Fiscal Equity, Inv. v. The State of New York, 2003 WL 21468502 (N.Y.), 2003 N.Y. Slip Op. 15615, declaring unconstitutional the State's system of funding New York City schools. Still reeling from double-digit budget increases, many districts now face the daunting task of formulating budgets for 2004-2005 school year. Given the uncertainty of the amount of State aid they will receive, districts are not only looking to contain costs, but to increase revenues. Although New York has traditionally (compared to many other states) been quite restrictive in allowing commercial funds to assist school districts, recent rulings from the Commissioner and Counsel's office may signal a new era which will give greater freedom to districts to obtain alternate sources of income.

**II. New York Law Through 1998:**

N.Y Constitution

Article VIII, §1 of the New York Constitution:

“No county, city, town, village or school district shall give or loan any money or property to or in aid of any individual, or private corporation or association, or private undertaking...”

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## B. Commissioner's Regulations

8 New York Codes, Rules and Regulations §23.2- “Boards of Education or their agents shall not enter into written or oral contracts, agreements or arrangements for which the consideration, in whole or part, consists of a promise to permit commercial promotional activity on school premises, provided that nothing in this Part shall be construed as prohibiting commercial sponsorship of school activities.

## C. Commissioner's Cases

Over four decades, the Commissioner had occasion to apply the prohibition of the State Constitution to various factual situations arising in school buildings. Generally, these cases involve whether an entity should be permitted to use school facilities in furtherance of a commercial activity and whether the activity served “a school purpose”.

### (i). Board Cannot Act as “Middleman”

For example, in Matter of Countryman, 1 Ed. Dept. Rep. 538 (1960), the Commissioner condemned the use of teachers to solicit and collect premiums for accident insurance from students participating in the athletic program.

In Matter of Shapnek, 3 Ed. Dept. Rep. 99 (1963), the Commissioner again condemned the solicitation of accident insurance through staff members.

In Matter of Kalsmith, 6 Ed. Dept. Rep. 20 (1966), the Commissioner stated:

...the board was “acting as a middleman and offering the product of a private corporation to the parents of school children, and in so doing is utilizing the time and services of school personnel in making such offer and collecting premiums. . .”

Likewise, in Matter of Hupert, 6 Ed. Dept. Rep. 91(1967):

“Boards of education may not act as *middlemen* in offering the product of a private corporation to the school children and in doing so utilize the services of school personnel in offering and collecting premiums and making out claim forms.”

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The Commissioner found improper the use of students themselves as middlemen for private undertakings in Matter of Darrall and Mort, 5 Ed. Dept. Rep. 197 (1996):

Where student council held and candy sale, at which candy was sold by pupils,

- a. there would be no legal objection if the students purchased the candy and resold it for a profit to finance student activities.
- b. it would be illegal if the students were using the school facilities and acting as agents or employees of the manufacturer for the purposes of selling the candies. “Public school facilities may not be used in aid of private business.”

(ii). School Photographs

Moving from insurance and candy, the Commissioner also developed a body of jurisprudence involving photographs. In Matter of Albert, 7 Ed. Dept. Rep. 7 (1967), the Commissioner held that photographs taken on school grounds for sale by a private enterprise were illegal:

“School children who are in attendance by reason of the compulsory attendance law should not be permitted to be exploited through the sale of products... The fact that a percentage of the sale price was turned over to a scholarship fund does not serve to meet the objection that the pupils are being exploited through the sale of a product to them under the auspices of school authorities.”

However, in Matter of King, 8 Ed. Dept. Rep. 86 (1968), the Commissioner found a way around the photograph issue. He stated that where photographs were taken for I.D. cards on school premises, the subsequent solicitation of additional prints through the PTA did not involve the use of school district facilities or personnel for private profit.

In August of 1974, then counsel to the Commissioner, Robert D. Stone, issued his exegesis on the law of school photographs (Exhibit A). Notwithstanding the memo, appeals continued to proliferate regarding school photographs:

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Matter of Jones, 16 Ed. Dept. Rep. 156 (1976). Where there was no school purpose, the use of school facilities by the PTA to sell photographs violates the State Constitution.

Matter of Fusare (Elmira Heights C.S.D.), 19 Ed. Dept. Rep. 543 (1980). The use of school facilities by private photographer held impermissible.

Matter of Fusare (Elmira City S.D.), 20 Ed. Dept. Rep. 14 (1980). Since there was no school purpose, use of school office contrary to the State Constitution.

Matter of Hoyt (Fulton City S.D.), 20 Ed. Dept. Rep. 316 (1980). Class photographs are a school purpose, however, solicitation of the private sale of photos impermissible.

(iii) School Rings

Having exhausted the law of school photographs, the Commissioner and Counsel Stone then had occasion to develop a jurisprudence involving school rings:

In Matter of Puls, 17 Ed. Dept. Rep. 430, 431 (1978), the Commissioner held:

“The practice of allowing representatives of a private firm to use school premises to solicit orders for graduation announcements and class rings is clearly illegal.. No valid school purpose is served...”

Likewise, in Matter of Toftegaard, 23 Ed. Dept. Rep. 405 (1984), the Commissioner held that the benefits of fundraising and class unity “can be readily achieved through the use of a systems which does not violate the clear dictates of the State Constitution.”

In Appeal of Gary Credit Corp., 25 Ed. Dept. Rep. 385 (1986), the Commissioner held:

“Permitting the use of school personnel and premises for the conduct of private business, including the practice of allowing representatives of private firms to solicit orders for class rings on public school property, clearly contravenes the constitutional prohibition.”

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Perhaps reacting to outcry from parents, students and jewelry manufacturers throughout the State, Counsel Stone issued a memo (Exhibit B) on December 8, 1986, which established the ten commandments of school rings. Basically:

“Sale of class rings would be a “school purpose” where:

- a) the board of education has authorized in-school promotion and sale of class rings.
- b) all prospective vendors are given full and equal opportunity to compete.
- c) students are fully involved in the process.”

Bob Stone’s memo was officially adopted by the Commissioner in a sequel to Appeal of Gary Credit Corp., 26 Ed. Dept. Rep. 414 (1987). In a significant erosion of his holdings on constitutional prohibitions, Commissioner Ambach stated:

“Rather, where the primary purpose of such an arrangement is a public benefit, i.e., where it serves a school purpose and any benefit accruing to the private entity is merely incidental to such public purpose, the constitution is not violated.”

Most recently in Appeal of Tarolli, 38 Ed. Dept. Rep. 60 (1998), Acting Commissioner Cate held:

“...the participation of school personnel and the use of school property in the taking of yearbook photographs is permissible only if the three conditions specified for a “school purpose”...are met...

- a) the board of education has approved the practice.
- b) all prospective vendors are given full and equal opportunity to compete.
- c) students are fully involved in the process.”

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### **III. Traditional Sources of Revenue:**

#### **A. Taxes and State & Federal Aid**

##### **i. Real Property Taxes:**

Districts provide approximately 56% of public school funding statewide.

Of course, the ratio of funding from State Aid vis-a-vis local property taxes varies significantly:

**ii. State Aid:** The State provides approximately 40% of public school funding statewide.

Almost half of the State aid component consists of operating aid, which is allocated using a complex statutory formula that apportions various categories of aid based on a district's Combined Wealth Ratio – which measures its ability to generate revenue – and student attendance (see Education Law §3602). The statute contains extensive prescriptions regarding how districts may use funds, and it is perhaps the proliferation of highly specific aid categories that most differentiates the current section 3602 from its shorter, simpler predecessors (see e.g. L 1962, ch 657). Campaign for Fiscal Equity, Inc., et al. v. The State of New York, et al., 2003 WL 214685 (N.Y.), 2003 N.Y. Slip Op. 15615.

**iii. Federal Aid:** The Federal Government provides approximately 4% of the total funding statewide.

##### **Specialized Federal Aid & Grants**

- a. Universal Service Discount Rate
- b. Department of Education Technology Innovation
- c. Challenge Grants
- d. Library Services & Technology Activity Grant
- e. Department of Commerce Technology Opportunitie Program

Grants are competitive, have strings attached and may be very political

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B. Income from District's Own Assets

i. Income from Use of Buildings:

Education Law §414 provides:

“§414. Use of schoolhouse and grounds

1. Schoolhouses and the grounds connected therewith and all property belonging to the district shall be in the custody and under the control and supervision of the trustees or board of education of the district. The trustees or board of education may adopt reasonable regulations for the use of such schoolhouses, grounds or other property, all portions thereof, when not in use for school purposes or when the school is in use for school purposes if in the opinion of the trustees or board of education use will not be disruptive of normal school operations...

(a) For the purpose of instruction in any branch of education, learning or the arts.

(b) For public library purposes...

(c) For holding social, civic and recreational meetings and entertainments, and other uses pertaining to the welfare of the community; but such meetings, entertainment and uses shall be non-exclusive and shall be open to the general public.

(d) For meetings, entertainments and occasions where admission fees are charged, when the proceeds thereof are to be expended for an educational or charitable purposes; but such use shall not be permitted if such meetings, entertainments and occasions are under the exclusive control, and the said proceeds are to be applied for the benefit of a society, association or organization of a religious sect or denomination, or of a fraternal, secret or exclusive society or organization other than organizations of veterans of the military, naval and marine service of the United States and organizations of volunteer firefighters or volunteer ambulance workers.

(e) For polling places...

(f) For civic forums and community centers...

(g) For classes of instruction for mental retarded minors...

(h) For recreation, physical training and athletics, including competitive athletic contests of children attending a private, nonprofit school...

(j) For graduation exercises held by not-for-profit elementary and secondary schools, provided that no religious service is performed.”

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It is well established that a district may charge entities using its building “an amount sufficient to cover all resulting expenses.” Although many districts have in the past been extremely generous in allowing outside groups to use its buildings with minimal fees, in these tough fiscal times, districts are now tightening their belts and looking to increase the revenue stream from the use of buildings. In Appeal of Emilio, 33 Ed. Dept. Rep. 75 (1993), Commissioner Sobol made two important holdings. First, he interpreted the reference in Education Law §414 to the general public as meaning the general public of the community, “that is of the school district.” Therefore, he held “I can discern no evidence of legislative intent that a school district should be precluded from denying or limiting access to school property by non-residents.” Furthermore, and more importantly, he held that the fee which a school district charges may exceed actual expenses. It would seem logical therefore that if a school district wishes to increase its income from the use of buildings, it could charge higher fees for non-resident groups, thus increasing its revenue.

ii. Lease of School Buildings:

Education Law §403-a provides that by resolution of the board of education, a school district may lease real property of the district that is currently not needed for school district purposes. The terms of the lease are subject to the following statutory guidelines:

The rental payment shall not be less than the fair market rental value as determined by the board of education.

The term of the lease shall not exceed ten years.

Upon termination, the lessee shall be obligated to restore the real property to its original condition less ordinary depreciation, provided that the school district may waive such requirement if the tenant has made improvements to such real property which may not be removed without causing substantial damage to such real property.

Education Law §403-a(1):

With respect to the ten-year lease term limitation, the statute further provides that: “Upon the consent of the commissioner, renewal of a lease may be made for a period of up to ten years”. Education Law §403-a(2). The precise meaning of “up to

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ten years” is unclear. In addition, the board of education may enter into a lease for a term in excess of ten years upon voter approval by referendum. Education Law §403-a(4). However, a recent letter (Exhibit C) from the State Education Department provided some clarification. It stated that the Commissioner cannot consent to any lease renewal that would bring the entire term of the lease past ten years. The letter also states that the board would have to either seek voter approval for a renewal of a lease beyond the initial ten year term or the board could let the lease expire at the ten-year mark and prepare a new lease. The implication is if the new lease itself is not more than ten years, voter approval or Commissioner’s consent would not be necessary.

The statute also permits the lease to provide for cancellation by the board upon the following events:

- (a) a substantial increase or decrease in pupil enrollment; or
- (b) a substantial change in the needs and requirements of a school district with respect to facilities; or
- (c) any other change which substantially affects the needs or requirements of a school district or the community in which it is located. Education Law §403-a(6).

iii. Selling School Property:

The board of education has the power, to sell, when authorized by voter approval, any former school site or lot or any real estate and the buildings thereon, at such price and upon such terms as the voters shall prescribe. Education Law §1709(11).

School boards have a fiduciary responsibility to obtain the best price possible when selling school district property. Matter of Ross v. Wilson 308 N.Y. 605 (1955).

The definition of highest or best price can include good faith considerations of such factors as to exact the highest rate of return. Matter of New City Jewish Center v. Flagg, 111 A.D.2d 814 (2d Dept. 1985); aff’d., 66 NY2D 980 (1985). In the New City case, the Court of Appeals affirmed the lower court’s decision that the school

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board may properly consider the future tax consequences of a proposed sale of school property in determining which of two nearly identical offers will result in the best possible price. The Court held that the board validly chose the \$2000 lower offer from a buyer that would restore the property to the tax rolls.

The Board may exercise its judgment and discretion in good faith concerning the method of sale that will bring the best price. Matter of Baker, 14 Ed. Dept. Rep. 5 (1974).

### C. Outside Sources of Revenue

#### i. Gifts of Personal Property.

Education Law §1709(12)- School Board may “take and hold for the use of the schools or any department of the same, ... any gift, legacy or annuity, of whatever kind, given or bequeathed to the ... board, and apply the same, or the interest and proceeds there of according to the instructions of the donor or testator”.

A school board may accept a gift of money to be used for a specific program, provided that the board does not delegate to a third party the decision of whether or not to offer the program in the first place and does not delegate any control over the matter in which the program is offered. Appeal of DeMasi et al, 18 Ed. Dept. Rep. 320 (1978).

All gifts must be free of restrictions or requirements which are contrary to law or district policy. For example, Title IX of the Federal Educational Amendments of 1972 prohibits school districts from discriminating based on sex. Therefore, a district should not accept and/or administer a trust which has terms that provide scholarships only to male or female students.

However, a trust established to provide scholarships for students of a particular gender does not necessarily violate the law. In the Matter of Wilson, 59 N.Y.2d 461 (1983), the Court of Appeals ruled “gender restrictions in private trusts do not necessarily violate public policy.”

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ii. Gifts of Real Property

According to Education Law §1709(12) the School Board may “take and hold for the use of schools or any department of the same, any real estate transferred to it by gift, grant, bequest or devise.” Real property may be acquired in any school district for school purposes and for any other purpose by gift, grant or devise. Voter approval is not necessary to acquire real property by gift, grant or devise. Education Law §1709(12-a).

iii. Private Foundations:

Private foundations are entities that are established as a nonprofit corporation or a charitable trust, with the principal purpose of making grants to unrelated organizations or institutions, or to individuals for scientific, educational, cultural or other charitable purposes.

Section 501(c)(3) of the Internal Revenue Code covers tax exempt organizations that are organized and operated exclusively for ..charitable, .... or educational purposes.

All Private Foundations must file Form 990-PF, an annual information return, about their finances, board members, and grants.

In New York, 18% of school districts currently have foundations and 15% are considering forming one. Brian O. Brentor & John C. Pijanowsk, *Shaking the Tree: The Benefits (and Costs) of District Education Foundations*, SCHOOL BUSINESS AFFAIRS, May 2003, at 6.

Reasons Districts Establish Foundations:

- Improve School-Community relationships
- Improve the quality of the educational program
- Supplement local revenues
- Facilitate tax-exempt donations
- Identify large donors
- Fund a specific project

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How Foundations Raise Money:

Special events  
Telephone solicitations  
Mail solicitations  
Door to Door solicitations  
Grants  
Planned giving

Types of Projects Funded:

Special teacher-developed projects  
Instructional materials  
Instructional equipment  
Extracurricular activities (i.e. sports, trips, and special events)  
Facilities and grounds (i.e. construction and renovation)  
Professional development for teachers and administrators  
Salaries for additional personnel  
Salary enrichment or stipends for existing personnel  
Awards for exceptional teachers and other staff  
Scholarships for college-bound students

Examples of Private Foundations:

Harrison Educational Foundation:

Established in 1994  
Operates independently from the Board of Education  
Run by parent volunteers  
Money raised pays for academic extras:  
    New piano for high school music room  
    Lesson with Shakespearean actors  
    Renovation of the library  
Raised money by sponsoring a \$600 per head golf outing

San Francisco Education Fund ([www.sfedfund.org](http://www.sfedfund.org)):

Established in 1979  
Over the past 24 years has channeled \$16 million into San Francisco public schools

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Programs encourage teacher innovation and creativity in the schools, increase the range of educational opportunities available to students, and promote support for public education by informing and involving parents and the community.

Leadership & Professional Development Grants Program- financial support to teachers to implement innovative projects in classroom

Golden Apple Fellowships/Josephine Miles Fellowship- gives teachers the opportunity to enhance teaching skills by attending classes at Berkeley without cost.

Teacher Incentive Program- recruit and retain quality teachers in the school district.

#### Benefits of Foundations:

Improved school-community relationships

Improved quality of the educational program

Allow the district to provide programs that would otherwise be impossible

Improve teacher attitudes and morale

#### Downside to Foundations:

District can become vulnerable if it relies too heavily on grants

Fundraising inequality between districts with foundations and those without

State government will take ancillary funds into account in the aid distribution formulas

#### How to Form an Educational Foundation

School Districts, which are considering establishing a private foundation, should seek assistance from their school attorney. If your school attorney does not have an expertise in the non-profit tax area, special counsel may be necessary or a foundation consultant. It is also helpful to have an accountant familiar with these matters. If your school auditor is not versed in this field, another accounting firm may be necessary.

Most Educational Foundations are set up as a Not-For-Profit Corporation. A Not-For-Profit Corporation may be formed by filing a Certificate of Incorporation with the Department of State. According to §404(d) of the Not-For-Profit Corporation Law,

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an Educational Foundation would also need to get the approval of the Commissioner of Education, as well as permission from the school district.

Once the Not-For-Profit Corporation has been established it is necessary to qualify as a tax-exempt organization. In order to become tax-exempt Form 1023 must be completed and sent to the Internal Revenue Service. Once the Foundation becomes tax-exempt, donors will be able to enjoy tax deductions for all donations given to the Foundation.

#### **IV. Emerging Sources of Revenue**

##### **A. Licensing District Property- Pouring Rights**

In 1998, Kathy A. Ahearn, Esq. issued a memorandum (Exhibit D) regarding contracts for exclusive “pouring rights.” The memo acknowledged that throughout the state, growing numbers of districts were being solicited to enter into contracts giving a specific beverage manufacturer the exclusive right to sell its beverages on campus in exchange for a fee and other consideration. Interestingly, the memo and model contract sought to balance the commercial exploitation of children and the use of school facilities for private commercial gain against “the search for new revenue streams.” As with Counsel Stone’s prior memoranda, the 1998 memo broke new ground and opened the door for many districts throughout the state to enter into contracts with Coke, Pepsi or Snapple and to receive scoreboards, lights on the football field, and other compensation in exchange. Although counsel’s memo does not carry with it the opinion that such agreements are legal, subsequent Commissioner’s opinions have established its basic validity. Interestingly, unlike the previous case law involving rings, yearbooks and photographs, the pouring rights agreement does not identify the school purpose which the contracts promote. Is the generation of revenue in and of itself a sufficient “school purpose”?

##### **(i). Prohibition on Multi-Year Contracts:**

The courts have applied the principle that a contract whose duration exceeds the one-year term of each board of education violates the public policy that one board may not bind a successor board in areas relating to governmental matters unless a longer term is expressly

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provided for in statute. Morin v. Foster, 45 N.Y.2d 286(1987); Matter of Lake v. Binghamton Housing Authority, 130 A.D.2d 913 (3d Dept. 1987). However in the Matter of Ramapo Carting Corp. v. Reisman, 192 A.D.2d 922 (3d Dept 1993), the Court held that when there is a adequate provision in a contract for a successor board to terminate a multi-year contract at will, the contracting board will not be illegally binding the successor board and the multi-year contract is not void as against public policy. Although the Commissioner has cautioned in Appeal of Citizens for Responsible Fiscal & Educ. Policy, 40 Ed. Dept. Rep. 315 (2000), that “front-loaded multi-year contracts may make it difficult for future Boards to terminate”, he has not invalidated pouring rights contracts on this ground.

(ii). Advertising in Connection with Pouring Rights Contracts:

In the Appeal of American Quality Beverages LLC I, 42 Ed. Dept. Rep. \_\_\_ Decision No. 14804 (Sept. 4, 2002), the Commissioner concluded that the use of a lighted product panel on a vending machine containing only a photograph of an actual bottle of Pepsi soda with the name Pepsi written on it did not violate the Constitution because the vending machines are the mechanism by which the vendor provides the service contracted for by the Board. Any advertising effect of the panels would be incidental to the services and products provided pursuant to the contract and such incidental benefit to the vendor would not violate the Constitution.

In the Appeal of American Quality Beverages LLC II, 42 Ed. Dept. Rep. \_\_\_ Decision No 14805 (Sept. 4, 2002), the Commissioner reached the same conclusion regarding lighted panels for PowerAde which contained not only a picture of the product and its name, but also printed information on the bottle label that the product is “the official sports drink of the Olympic Games.” The Commissioner stated with great conviction, “districts should consider whether such apparently promotional statements are appropriate to be placed in its school at all or whether the district should require that only plain, generic panels should be used in schools.”

(iii). Prohibiting the sale of certain sweetened foods

Education Law §915 prohibits the sale of certain sweetened foods. The statute states, “from the beginning of the school day until the end of the last scheduled meal period, no sweetened soda water, no chewing gum, no candy including hard candy, jellies, gums, marshmallow candies, fondant, licorice, spun candy and candy coated popcorn, and no water ices except those which contain fruit or fruit juices, shall be sold in any public school within the state.”

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## B. Commercial Activities

Definition of Commercial Activities- the sale of products, direct advertising, indirect advertising and market research

Since 1990 commercial activity in schools has risen 473%.

Only 19 states have adopted laws to regulate commercial activities in the classroom.

### Categories:

Sponsorship of Programs and Activities - paying or subsidizing school events)

Thompson Middle School in Newport, Rhode Island- auctioned off to corporations for as much as \$250,000 the right to put business names and logos on anything from individual books to entire school buildings.

Exclusive Agreements - i.e. Pouring Rights

Incentive Programs - providing goods, awards, or services to a district when students engage in a specific activity

Pizza Hut's "Book It" promotion awards individual size pizzas to students who complete an allotted amount of reading.

Appropriation of Space – allowing the corporation to place a corporate logo on school space.

International School Licensing Corporation- corporations donate a percentage of sales to be distributed to schools in return for the right to display a star shaped America's Schools logo on their products.

Sponsored Educational Materials – materials supplied by the corporation with instructional content

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Verizon Wireless distributed a drivers education curriculum called Vehicle Intelligence Quest which teaches new drivers about wireless safety behind the wheel.

Jelly Belly distributed science, math and social studies lessons which includes product tie ins as well as sample packets of jelly bellys.

Electronic Marketing- giving school electronic programming or equipment in return for the right to advertise in the school

Privatization – management of schools by private for-profit corporations or non-public entity

Edison Schools is one of the largest for-profit schools in the United States

Fundraising – activity conducted to raise money for school operations or extra-curricular activities.

General Mills donates money to schools based on the number of General Mills box top coupons the students turn in

Current Projects:

Channel One ( a broadcast of news features and commercials) is shown in about 25% of the nations middle schools

Zap Me offers schools free computers with screens that include continuously flashing ads

Textbook covers distributed by Clairol, Ralph Lauren, Reebok and Philip Morris with company names and logos

In NYC the Board of Education is considering a plan that would provide computers for all of its students which might carry ads and encourage shopping on a particular Web Site.

AOL@School is a free online service that would provide schools with access to AOL's library of educational content.

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Sell to corporations the right to put their names and logos on school buildings, gymnasiums, libraries and instructional material (i.e. School in Brooklawn New Jersey named a new gym after the supermarket ShopRite for \$100,000.)

Advertising on school buses – illegal in New York. N.Y. Veh & Traf. Law §375(21-h).

#### **V. The Brave New World: Utopia or Dystopia?**

School/business relationships based on sound principles can contribute to high quality education. However, the compulsory attendance law confers on educators an obligation to protect the welfare of students and the integrity of the learning environment. Therefore, when working together, schools and businesses must ensure that educational values are not distorted in the process.

Corporate involvement in schools must support the goals and objectives of the schools. Programs of corporate involvement must be structured to meet an identified education need, not a commercial motive.

