STATE OF MICHIGAN

COURT OF APPEALS

GALIEN TOWNSHIP SCHOOL DISTRICT,

Plaintiff,

and

DELTON-KELLOGG SCHOOLS,

Plaintiff-Appellee,

v

DEPARTMENT OF EDUCATION and SUPERINTENDENT OF PUBLIC INSTRUCTION,

Defendants-Appellants.

FOR PUBLICATION
August 14, 2014
9:00 a.m.

No. 317734
Ingham Circuit Court
LC No. 13-000367-AA

GALIEN TOWNSHIP SCHOOL DISTRICT and DELTON-KELLOGG SCHOOLS,

Plaintiffs-Appellees,

v

DEPARTMENT OF EDUCATION and SUPERINTENDENT OF PUBLIC INSTRUCTION,

Defendants-Appellants,

No. 317739
Ingham Circuit Court
LC No. 13-000367-AA

Before: SAAD, P.J., and OWENS and K.F. KELLY, JJ.

PER CURIAM.

In this consolidated appeal, defendants Department of Education and Superintendent of Public Instruction appeal as of right, in Docket No. 317734, a circuit court order that granted plaintiff Delton-Kellogg Schools declaratory judgment, determining that defendants did not have

the authority to retroactively audit plaintiff. In Docket No. 317739, the same defendants appeal by leave granted[1] the same circuit court order, which also granted plaintiff Galien Township School District declaratory judgment for the same reasons. The circuit court order also granted plaintiffs' claim of appeal, overruled the superintendent's final decision that reduced plaintiffs' state aid because of the findings of the retroactive audits, and ordered that defendants reinstate all wrongfully deducted full-time equivalent students (FTEs) and return state aid. In Docket No. 317734, we conclude that the circuit court did not have subject-matter jurisdiction over Delton-Kellogg's claims and reverse the circuit court's order in its entirety. In Docket No. 317739, we reverse the circuit court's order in its entirety and remand for reinstatement of the superintendent's final decision.

I. BACKGROUND

After plaintiffs admitted teacher misconduct in reporting student attendance, defendants claimed authority under the State School Aid Act (SSAA), MCL 388.1601 *et seq.*, and audited prior years' attendance records. The audit could not verify 225.75 FTEs enrolled in Galien Township School District and 408.75 FTEs enrolled in Delton-Kellogg Schools. Based on these retroactive audits, defendants reduced approximately $750,000 in state aid from Galien and approximately $1,500,000 from Delton-Kellogg. Both school districts sought administrative review. Galien exhausted its administrative remedies, and in a first-level review, the Michigan Department of Education (MDE) reinstated 35.27 FTEs. Galien sought further administrative review requesting 190.38 additional FTEs be reinstated. Superintendent of Public Instruction, Michael Flanagan, conducted the final review and issued his report on March 14, 2013. The final administrative review resulted in 1.84 additional reinstated FTEs. Galien then filed the instant action, including a claim of appeal, in the circuit court.

Delton-Kellogg, on the other hand, did not exhaust its administrative remedies. In a first-level review, the MDE reinstated 162.4 FTEs. Delton-Kellogg appealed to the superintendent, and that appeal remains pending. In the meantime, Delton-Kellogg brought the instant action in the circuit court.

II. SUBJECT-MATTER JURISDICTION

A. DOCKET NO. 317734

Defendants argue that the circuit court erred by holding that it had subject-matter jurisdiction over all of Delton-Kellogg's claims because Delton-Kellogg failed to exhaust all the administrative remedies available. We agree. "Whether a court has subject-matter jurisdiction is a question of law that we review de novo." *Bruley Trust v Birmingham*, 259 Mich App 619, 623; 675 NW2d 910 (2003).

MCL 24.301 addresses judicial review in the context of administrative exhaustion:

[1] *Galien Twp Sch Dist v Superintendent of Pub Instruction*, unpublished order of the Court of Appeals, entered December 18, 2013 (Docket No 317739).

> When a person has exhausted all administrative remedies available within an agency, and is aggrieved by a final decision or order in a contested case, whether such decision or order is affirmative or negative in form, the decision or order is subject to direct review by the courts as provided by law. Exhaustion of administrative remedies does not require the filing of a motion or application for rehearing or reconsideration unless the agency rules require the filing before judicial review is sought. A preliminary, procedural or intermediate agency action or ruling is not immediately reviewable, except that the court may grant leave for review of such action if review of the agency's final decision or order would not provide an adequate remedy.

Delton-Kellogg does not dispute that it has not exhausted all administrative remedies, but it argues that exhaustion was not required here. As stated, exhaustion is not required "if review of the agency's final decision or order would not provide an adequate remedy," MCL 24.301, i.e., "if it would run counter to the policies which underlie the doctrine." *IBM v Dep't of Treasury*, 75 Mich App 604, 610; 255 NW2d 702 (1977); see also *Citizens for Common Sense in Gov't v Attorney General*, 243 Mich App 43, 53; 620 NW2d 546 (quoting *IBM*). These policies include,

> (1) an untimely resort to the courts may result in delay and disruption of an otherwise cohesive administrative scheme; (2) judicial review is best made upon a full factual record developed before the agency; (3) resolution of the issues may require the accumulated technical competence of the agency or may have been entrusted by the Legislature to the agency's discretion; and (4) a successful agency settlement of the dispute may render a judicial resolution unnecessary. [*IBM*, 75 Mich App at 610; see also *Citizens for Common Sense*, 243 Mich App at 53.]

Relying on *IBM*, Delton-Kellogg asserts that exhaustion was not required here because the question raised only challenged the MDE's legal authority to take the complained-of action, it was clearly framed for review, fact-finding was unnecessary, application of the MDE's expertise was not required, review by the circuit court promoted judicial economy, and the MDE did not have exclusive jurisdiction over questions of statutory authority. We disagree. The record shows that Delton-Kellogg submitted to the administrative procedure, but disrupted the progression of the otherwise cohesive process by seeking relief in the circuit court. Further, Delton-Kellogg was successful in the first level of review, regaining 162.4 FTEs. Not only will this Court not presume that administrative review is futile when the outcome has aided the party seeking review, see *Papas v Mich Gaming Control Bd*, 257 Mich App 647, 664-665; 669 NW2d 326 (2003), but also full review through the administrative process could very well result in the reinstatement of all contested FTEs, which would provide the relief requested, rendering judicial review unnecessary. As such, the interests of judicial economy are not served here by interrupting the administrative process. Given the pending appeal before the superintendent, the disruptive potential of pursuing judicial review is a circumstance to be avoided. See *Detroit Auto Inter-Ins Exch v Comm'r of Ins*, 125 Mich App 702, 709 336 NW2d 860 (1982); see also *Citizens for Common Sense*, 243 Mich App at 52, quoting *Judges of the 74th Judicial Dist v Bay Co*, 385 Mich 710, 727; 190 NW2d 219 (1971) ("Our Supreme Court has stated that 'administrative law dictates that courts move very cautiously when called upon to interfere with

the assumption of jurisdiction by an administrative agency.' "). Therefore, we conclude that because Delton-Kellogg failed to exhaust its administrative remedies, the circuit court lacked jurisdiction over all of Delton-Kellogg's claims.

B. DOCKET NO. 317739

Defendants next attack the circuit court's subject-matter jurisdiction to hear Galien's claims because its claim of appeal and claim for declaratory relief were comingled in a single pleading. Defendants also assert that the circuit court did not have jurisdiction over Galien's claim for declaratory relief because there was no claim or controversy. Again, we afford this issue de novo review. *Bruley Trust*, 259 Mich App at 623.

We reject defendants' argument that the circuit court lacked jurisdiction because Galien comingled claims. A circuit court has subject-matter jurisdiction over a claim of appeal from a final administrative order or decision. MCL 600.631; MCR 7.103(A)(4). To vest the circuit court with jurisdiction in an appeal of right, MCR 7.104(B), provides that

> an appellant must file with the clerk of the circuit court within the time for taking an appeal:
>
> (1) the claim of appeal, and
>
> (2) the circuit court's appeal fee, unless the appellant is indigent.

Likewise, a circuit court has jurisdiction over a claim for declaratory relief if "the court would have jurisdiction of an action on the same claim or claims in which the plaintiff sought relief other than declaratory judgment," MCR 2.605(A)(2), and this jurisdiction is invoked by filing a complaint with the court, MCR 2.101. Thus, given that the circuit court has jurisdiction to hear appeals regarding final orders or decisions of the MDE, MCR 7.103(A)(3), it follows that it would have jurisdiction over Galien's claim for declaratory relief. By the plain language of the court rule, the existence of an appeal does not void jurisdiction over the declaratory judgment, as such jurisdiction applies "whether or not other relief is or could be sought or granted." MCR 2.605(A)(1).

Further, Galien's act of combining the claims into one document did not divest the circuit court of jurisdiction, according to the plain language of the court rules. The record indicates, and defendants have not argued to the contrary, that Galien invoked the court's jurisdiction by filing its claim of appeal and complaint for declaratory relief, and paying the fees. This is sufficient to invoke the court's jurisdiction over both claims. While it would perhaps have been advisable to bring the appeal and declaratory relief actions under separate circuit court dockets and move for consolidation, the presentation of the claims together is insufficient to divest the court of subject-matter jurisdiction. This is particularly true where the record indicates that the circuit court addressed the two claims separately, as reflected in its opinion and order. See *Chen v Wayne State Univ*, 284 Mich App 172; 771 NW2d 820 (2009) (noting that cases consolidated for administrative convenience or judicial economy retain their separate identities).

Nevertheless, we do find that the circuit court did not have jurisdiction to grant declaratory relief because substantively the claim failed to address a future harm. MCR 2.605 governs declaratory judgments, reading in relevant part as follows:

> (A) Power To Enter Declaratory Judgment.
>
> (1) In a case of actual controversy within its jurisdiction, a Michigan court of record may declare the rights and other legal relations of an interested party seeking a declaratory judgment, whether or not other relief is or could be sought or granted.
>
> (2) For the purpose of this rule, an action is considered within the jurisdiction of a court if the court would have jurisdiction of an action on the same claim or claims in which the plaintiff sought relief other than a declaratory judgment.
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> * * *
>
> (C) Other Adequate Remedy. The existence of another adequate remedy does not preclude a judgment for declaratory relief in an appropriate case.
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> * * *
>
> (F) Other Relief. Further necessary or proper relief based on a declaratory judgment may be granted, after reasonable notice and hearing, against a party whose rights have been determined by the declaratory judgment.

A case of actual controversy is a "condition precedent to invocation of declaratory relief." *Citizens for Common Sense*, 243 Mich App at 55 (quotation marks and citation omitted). "Generally, an actual controversy exists where a declaratory judgment is necessary to guide a plaintiff's future conduct in order to preserve the plaintiff's legal rights." *Id.* It is essential that a plaintiff "pleads facts entitling him to the judgment he seeks and proves each fact alleged," and those facts "indicate an adverse interest necessitating the sharpening of the issues raised." *Shavers v Attorney General*, 402 Mich 554, 589; 267 NW2d 72 (1978).

Here, Galien styled the relief requested in circuit court as declaratory relief, asserting that future retroactive audits may compel the district to refund additional state-aid monies. It is undisputed that the audits were completed by the MDE, were decided against Galien, and that the MDE reduced current and future school aid over a number of years to make up the deficiency revealed by the audit. These facts establish a controversy between Galien and the MDE, but a *current* conflict based on a past controversy. That the MDE allowed the funding deficits to be repaid over several years is not dispositive because the determination of the legal rights of the parties was already settled. See *Lansing Schs Ed Ass'n v Lansing Bd of Educ (On Remand)*, 293 Mich App 506, 516; 810 NW2d 95 (2011) (holding that an actual controversy was lacking because plaintiffs did not allege imminent injury where the alleged physical injuries had already

occurred). Accordingly, the circuit court did not have jurisdiction over Galien's claim for declaratory relief.[2]

III. RETROACTIVE AUDITS

Defendants also argue that the circuit court improperly granted plaintiffs appellate relief based on the erroneous conclusion that the MDE lacked authority to retroactively audit and adjust state school aid.[3] This issue requires us to interpret and apply various sections of the SSAA. Interpretation and application of a statute is a question of law we review de novo. *McAuley v Gen Motors Corp*, 457 Mich 513, 518; 578 NW2d 282 (1998). The foremost rule of statutory construction "is to discern and give effect to the intent of the Legislature." *Whitman v City of Burton*, 493 Mich 303, 311; 831 NW2d 223 (2013). Interpretation strives to give effect to "every phrase, clause, and word in the statute and, whenever possible, no word should be treated as surplusage or rendered nugatory." *Id.* at 311-312. Each word or phrase of a statute is given its commonly accepted meaning, unless otherwise expressly defined. *McAuley*, 457 Mich at 518. "Statutes should be construed so as to prevent absurd results, injustice, or prejudice to the public interest." *Id.*

During the course of proceedings below, section 15 of the SSAA provided, in pertinent part,

> (1) Subject to subsections (2) and (3), if a district or intermediate district has received more than its proper apportionment, the department, upon satisfactory proof, shall deduct the excess in the next apportionment. Notwithstanding any other provision in this article, state aid overpayments to a district, other than overpayments in payments for special education or special education transportation, may be recovered from any payment made under this article . . . .
>
> (2) If the result of an audit conducted by or for the department affects the current fiscal year membership, affected payments shall be adjusted in the current fiscal year. A deduction due to an adjustment made as a result of an audit conducted by or for the department, or as a result of information obtained by the department from the district, an intermediate district, the department of treasury, or the office of auditor general, shall be deducted from the district's

[2] We note that although we conclude that the circuit court did not have jurisdiction over Delton-Kellogg's claims due to failure to exhaust its administrative remedies, for the same reasons provided here, even if it had exhausted its administrative remedies, we find that the circuit court would not have had jurisdiction to grant declaratory relief to Delton-Kellogg.

[3] In light of our conclusion that the circuit court did not have jurisdiction over any of Delton-Kellogg's claims, we need not consider this issue as it relates to Delton-Kellogg. However, because our analysis of this issue is the same for both plaintiffs, we will address the issue as it relates to both plaintiffs.

> apportionments when the adjustment is finalized. . . . [T]he department may grant up to an additional 4 years for the adjustment . . . .
>
> (3) If, because of the receipt of new or updated data, the department determines during a fiscal year that the amount paid to a district or intermediate district under this article for a prior fiscal year was incorrect under the law in effect for that year, the department may make the appropriate deduction or payment in the district's or intermediate district's allocation for the fiscal year in which the determination is made. . . . [MCL 388.1615[4].]

Further, section 18 provided, in pertinent part,

> (4) For the purpose of determining the reasonableness of expenditures and whether a violation of this article has occurred, all of the following apply:
>
> (a) The department shall require that each district and intermediate district have an audit of the district's or intermediate district's financial and pupil accounting records conducted at least annually at the expense of the district or intermediate district, as applicable, by a certified public accountant or by the intermediate district superintendent, as may be required by the department, or in the case of a district of the first class by a certified public accountant, the intermediate superintendent, or the auditor general of the city.
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> * * *
>
> (d) The pupil and financial accounting records and reports, audits, and management letters are subject to requirements established in the auditing and accounting manuals approved and published by the department.
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> * * *
>
> (8) The department shall review its pupil accounting and pupil auditing manuals at least annually and shall periodically update those manuals to reflect changes in this article. [MCL 388.1618[5].]

And section 168 provides,

> In order to receive funds under this act, a district . . . or other entity that directly or indirectly receives funds under this act shall allow access for the

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[4] 2014 PA 196 amended section 15, effective October 1, 2014, to add a new subsection (4): "The department may conduct audits, or may direct audits by designee of the department, for the current fiscal year and the immediately preceding 3 fiscal years of all records related to a program for which a district or intermediate district has received funds under this article."

[5] 2014 PA 196 also amended subsection 18(4)(a) to indicate that audits could be conducted "at such other times as determined by the department," and that districts "shall retain these records for the current fiscal year and from at least the 3 immediately preceding fiscal years."

> department or the department's designee to audit all records related to a program for which it receives such funds. The district . . . shall reimburse the state for all disallowances found in the audit. [MCL 388.1768.]

Section 168, which empowers the MDE "to audit all records related to a program," notes that it is applicable to "funds under this act," indicating that the section 168 power and definitions apply to the entire SSAA. Thus, the ability to access the records to conduct an audit applies to the other sections under consideration here, including sections 15 and 18. Although the MDE is clearly empowered to audit, the question is whether it may retroactively audit.

We conclude that when read in its entirety, the interplay of sections 15 and 168 authorize the MDE to conduct retroactive audits.

> If, because of the receipt of new or updated data, the department determines during a fiscal year that the amount paid to a district or intermediate district under this article for a prior fiscal year was incorrect under the law in effect for that year, the department may make the appropriate deduction . . . in the district's or intermediate district's allocation for the fiscal year in which the determination is made. . . . [MCL 388.1615(3).]

Subsection 15(3) clearly empowers the MDE to make deductions from a district's allocation for incorrect allocations of a prior fiscal year. Any deduction is driven by the "receipt of new or updated data." Further, section 168 requires districts to "allow access for the department or the department's designee to audit all records related to a program for which it receives funds." MCL 388.1768. "All records" necessarily includes past and present records and the right of access to complete an audit is placed with the MDE. Subsection 15(3), unlike subsection 15(2), does not use the term "audit," but that is the most likely avenue for the MDE to receive new or updated data, especially given the reference to audit in subsection 15(2). The MDE clearly has audit power and there is no indication in subsection 15(3) that this power cannot be used to gather "new or updated data." Therefore, the audit power can look retroactively to gather updated data on a prior fiscal year.[6] Accordingly, we hold that the circuit court erred by concluding that the MDE did not have the authority to retroactively audit.

IV. CONCLUSION

In Docket No. 317734, we reverse the circuit court's order in its entirety and direct Delton-Kellogg to exhaust its administrative remedies.

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[6] We reject Galien's argument that the amendments made by 2014 PA 196 indicate that the MDE previously lacked the authority to conduct retroactive audits. As we have concluded, before the amendments, the SSAA clearly granted the MDE the authority to conduct retroactive audits. The recently passed amendments simply clarify this authority by specifically limiting the scope of audits and record keeping requirements to three years, rather than an undefined standard.

In Docket No. 317739, we reverse the circuit court's order in its entirety and remand for reinstatement of the superintendent's March 14, 2013 final decision.

Reversed and remanded.

/s/ Henry William Saad
/s/ Donald S. Owens
/s/ Kirsten Frank Kelly