

Chapter 1

OVERVIEW OF APPROACHES TO STATE SCHOOL FUNDING

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Although each state relies on the same basic principles and types of funding, each state's funding system is idiosyncratic. Some of these differences are based on the state's history of funding public schools. Other differences occur as a result of litigation or changing demographics within the state. Other differences occur as political power shifts within the executive and legislative branches of the states. The result is that some states have relatively simple financing structures while others have highly complex structures. The variability and complexity make the task of providing an overview and placing data within tables a challenging endeavor.

This chapter provides the reader with some very basic introductory school finance concepts. This material is intended to help readers, who may not have a background in school finance, understand the descriptions and tables in this book. Readers will find comprehensive discussions of school finance concepts in the suggested readings at the end of this chapter. This chapter discusses how the basic approaches operate and some funding concepts associated with those approaches. In addition, Table 1.4 indicates the state and local funding provided in each state. Chapter 2 presents highlights of state funding programs. Of course, greater detail is provided in the individual state and provincial chapters. The individual state chapters are available on the National Center for Education Statistics website and on a cd which may also be obtained through NCES.

States provide two different types of school aid — basic support and categorical aid. These intergovernmental transfer payments serve three main purposes (Swanson & King, 1997). First, these payments help to fulfill state responsibility for providing and maintaining public education systems. Second, states can insure, through these payments, that minimal or adequate educational programs exist in local districts. Third, states have the advantage of a broader tax base from which to generate revenue that can then be more equitably re-distributed.

Basic support aid is the major component in state funding for schools. Basic state aid is sent to local school districts based on some state-specific formula. These dollars, when combined with local funding, provide for the general programs and

services for students. Often these formulas are designed to address disparities that exist among districts so that all students within the state have equitable educational opportunities. Basic support aid formulas often are designed to address the relationship between need and local ability to pay with those districts with the highest need and least ability to pay receiving the most state funding. Basic support aid tends to address the issue of horizontal equity.

Five basic support aid programs exist; however, some states use a combination of approaches. The basic approaches are flat grants, foundation programs, percentage equalizing, guaranteed tax base or guaranteed yield programs, and full state funding programs. Table 1.1 indicates the major approach used in each state. A second type of state funding is categorical aid. Categorical aid is provided to address a particular need or a particular policy goal. While basic support aid tends to operate as a general grant, categorical aid must be used in very specific ways. Often categorical aid reimburses the costs of particular services that schools provide such as transportation, special education, or vocational education. Other categorical aid may be targeted for compensatory education or programs for limited English speaking students, for example. Generally categorical aid is not based on a district's ability to pay (i.e., linked to local fiscal capacity) but rather on additional costs associated with special needs (vertical equity) and programs the state deems worthy of funding. Categorical funding is discussed in Chapter 3, and many tables provide information on the types and amounts of categorical funding each state provides. Again, the reader is directed to the individual state and provincial chapters for in-depth discussion.

Two states, Alaska and Mississippi, were unable to provide complete 1998-1999 data. We have chosen to include the descriptions of their programs in these overview chapters, but have not included pre-1998-1999 financial data because of issues of data comparability. However, the reader may find these financial data by reviewing the individual state chapters.

Funding Concepts

Educational need and the ability to pay are the two funding concepts on which education finance systems are based. This section will discuss these concepts.

Educational Need

Educational need is defined as the demand placed on a district's resources to fund education. Generally this demand is related to the number of pupils. Pupils are often weighted according to grade levels or specific needs in recognition of the

differing costs in educating differing populations. Other costs that are beyond the control of the district are also factored into determining educational need. With the exception of Hawaii and South Dakota, basic support aid is allocated based on a relationship between numbers of pupils and educational costs.

Pupil Count, Teacher Units, Instructional Units

Pupil count is the most common method of measuring educational need due to the obvious relationship between numbers of pupils to be educated and the resulting costs. States use three methods of determining pupil count: enrollment (ENR), average daily membership (ADM), and average daily attendance (ADA). ENR is based on a district's total enrollment on a given day; however, some states use a blended count of two or three specific days. Table 1.1 indicates that 14 states use enrollment as the basis for allocating funds. ADM is based on enrollment over a given time period. Table 1.1 indicates that 22 states use ADM. ADA is based on pupils who actually are in attendance over a given number of days; the number of students in attendance each day is summed and then averaged. Eight states indicated the use of ADA as the basis for allocation.

Four states indicated the use of teacher or instructional units in allocating state funds. These units are determined using formulas that are tied to pupil counts; i.e. a certain number of pupils earn a teacher or instructional unit.

Weighting Procedures

Weighting procedures are used to recognize the varying costs associated with educational programs and services. Varying costs may occur because of differences in providing programs for elementary, middle school and high school students. Other variations in cost may be due to differences in students caused by physical or mental disabling conditions. Whatever the circumstances, weighting procedures are ways to fund the education of students with differing needs and abilities.

There is no agreement or standardization of weights among the states. For example, some states recognize the education of a regular elementary school pupil as the basic cost and weight this student as 1.0. A high school student may be weighted at 1.5, specifying that it costs 50% more to educate a high school student as an elementary school student. Or a particular state may decide that the regular high school student is valued at 1.0 and the early elementary student is weighted at 1.5. Further weighting is given to special education students, usually based on the severity of the disabling condition, to recognize the additional costs

of educating this special population. Weighting may be used for recognizing additional costs associated with at-risk students or gifted students or students with limited English speaking ability. There are as many weighting schemes as there are states that use them in their funding systems. Their purpose is to recognize costs based on educational needs.

Table 1.1 indicates that at 32 states use some form of weighting in the calculation of pupil or teacher/instructional units.

Other Educational Costs

Many states include within their basic funding formula adjustments that recognize other special needs that impact the costs of delivering educational programs and services. Some factors which may be considered requiring adjustments include the sparsity of isolated districts, district size, teacher training and experience, enrollment growth, enrollment decline, municipal overburden, cost of living differentials, etc. These adjustment factors are included in the tables in Chapter 2 and are described in detail in the individual state chapters.

Ability to Pay

Because the property tax has been the primary basis for local funding of schools, the ability to pay for educational programs and services is determined by the local property assessed valuation. Property values are assessed at differing levels across the states. All utilize some percentage of market value. These percentages range from 100% to 12% of true market value. In addition, property values are equalized within states to adjust for differences in assessment practices.

While assessed property values are still the primary measure of local fiscal capacity (ability to pay), other measures are being used as states work toward developing more equitable school finance systems. Other measures include personal income taxes, local sales tax, motor vehicle taxes, and other measures.

Table 1.2 indicates that 24 states rely on assessed property valuation alone as a measure of fiscal capacity. Ten states use assessed property valuation in combination with personal income as their measure of local fiscal capacity. Four states rely on assessed property valuation, personal income, and other measures, and eight states use assessed valuation and other revenue sources not including income. Four states, Hawaii, North Carolina, Rhode Island, and Washington, indicated that they did not use local fiscal capacity in the distribution of the basic support aid. The reliance on assessed property valuation has been the issue in

school finance litigation, so it is logical that this measure of local fiscal capacity would be at the heart of equalization efforts in the distribution of basic support aid.

Basic Support Funding Mechanisms

Basic support funding mechanisms provide general aid to local school districts. Generally, these funds operate as block grants with unrestricted use of the dollars. While some states may require that certain percentages be used in certain areas (for example, there may be a requirement that part of this grant must be used for facilities or teacher salaries) for the most part, the dollars are discretionary at the district level. As mentioned above, there are five basic funding mechanisms used by states to transfer dollars for basic support aid: flat grants, foundation programs, percentage equalizing, guaranteed tax base or guaranteed equal yield programs, and full state funding. States sometimes use a combination of these mechanisms to transfer payments from the state to the local district level. Each mechanism or program has its own philosophical basis; within the political context of legislative decision making, basic support aid mechanisms are reflect not only philosophical or policy beliefs but also reflect the political realities that exist within states. This section discusses the theoretical models for funding. Table 1.1 indicates the model which was reported in the individual state chapters by the authors or in some cases, the editors interpretation of the author s description. Chapter 2 presents highlights from each of the state descriptions. Readers will find abbreviated descriptions of the basic support program in each state, and of course, the individual state chapters present detailed information. Again, readers are provided with basic information regarding these funding mechanisms. Readers are encouraged to consult the readings listed at the end of this chapter for in depth discussion and analysis.

Flat Grants

The flat grant recognizes the state s responsibility in funding education at some minimal level. Flat grants guarantee that each unit (pupil, FTE, teacher, instructional unit, etc.) is funded at an equal dollar amount. The formula for a flat grant is:

$$S_i = FN_i$$

- Where: S_i = State flat grant to the i th district;
F = the flat grant amount;
 N_i = the number of units (pupils, etc.) in the i th district.

Because the flat grant is an allocation per unit, local fiscal capacity is not addressed. Districts with the greatest property wealth receive the same amount per unit as districts with the least property wealth. However, it is possible that a flat grant could provide some equalization across districts depending on the ratio of state to local funding. The greater the level of state funding the more equalizing the flat grant becomes as it approaches the point of full state funding.

Flat grants may also address the issue of educational need if the units have been weighted. The weighting process is designed to recognize the differences in costs of programs and services for differing students. Districts with students having greater educational need (special education, limited English speaking, etc.) would receive more aid.

Table 1.3 indicates that only one state, Delaware, uses the flat grant (with weighting) as its primary mechanism for allocating state aid.

Foundation Programs

Foundation programs establish a funding level that the state considers appropriate. Often that funding level is a minimum funding guarantee, which can then be supplemented by additional local dollars. However, a few states (such as Michigan) are moving to a foundation allowance that does not allow for additional local spending. The basic formula for a foundation grant is:

$$S_i = N_i F - r W_i$$

Where: S_i = State foundation grant to the i th district;
 N_i = the number of units (pupils, etc.) in the i th district;
 F_i = the foundation level;
 r = the required tax rate;
 W_i = the value of the tax base of the i th district.

The foundation grant, like the flat grant, may use weighted units in the calculation of a district's foundation allowance. This weighting addresses educational need. The foundation grant, however, addresses ability to pay also. Since most foundation programs require a local effort, the value of the tax base (local fiscal capacity) is an important component of this funding mechanism. Because the amount raised through the required local effort is subtracted from the foundation allowance, the state distributes state dollars in an inverse relationship to ability to pay. Thus, the foundation allowance provides a measure of equalization as

districts with higher tax bases are required to provide more local dollars to meet the foundation amount than districts with lower tax bases.

States that use foundation programs differ in whether the local contribution is mandatory or whether it is simply used to compute the state share and the local district has the option of lowering the tax rate. Since the foundation program is generally considered to be a minimum or adequate or basic program, most districts choose to tax themselves at rate higher than the required rate. A tax rate over the required rate may not be equalized, so funding disparities are likely to occur with the option of a local tax that exceeds the required rate.

The foundation program approach is the most widely used mechanism for allocating state dollars. Table 1.3 indicates that 44 states use the foundation program as their primary funding mechanism. Of these 44, authors of 7 states indicated that local effort was mandatory. The remaining 37 state authors indicated that local effort was either required or calculated and used as a computational device, so that districts might choose to tax themselves at a lower than required rate but would still receive the calculated state funding.

Percentage Equalization, Guaranteed Tax Base/Yield Programs

These grants are based on a philosophy of equal access to funding. Each local district determines its own level of spending or level of taxation. These programs stress local determination of finance decisions. These programs are considered fiscally neutral in that the funding is a function of the wealth of the state; these programs guarantee that local communities have the power to raise funds to support schools at their chosen spending levels (Swanson & King, 1997, p. 203). The basic difference between these programs is that percentage equalization focuses on expenditures per unit while guaranteed tax base/yield program focuses on units of tax effort. Percentage equalization and guaranteed tax base/yield both provide a level of state equalization aid in inverse relationship to fiscal capacity (Alexander & Salmon, 1995). While it may be possible that local districts exceed the state guaranteed level, states generally do not power-equalize or recapture excess funds.

Percentage Equalization

In percentage equalization, the state establishes an aid ratio or the rate at which the state will match local funds. The formula for a percentage equalization grant is:

$$S_i = N_i E_i [1 - ((W_i/W)k)]$$

Where: S_i = State equalization aid to the i th district;
 N_i = the number of units (pupils, etc.) in the i th district;
 E_i = expenditure level for the i th district;
 W_i = local fiscal capacity for the i th district;
 W = state fiscal capacity per unit;
 k = constant (aid ratio) established by the state.

The percentage equalization approach does not mandate a minimum level of effort; instead it allows for a local decision of the expenditure level the district wishes to maintain and equalizes the level of fiscal effort. The state determines the level (k) at which it will match local funds. For example, if a local fiscal capacity of the i district is equal to the state fiscal capacity and the aid ratio (k) is 0.4, then the state equalization aid would be 60% ($1 - 0.4$) times the expenditure level times the number of units.

Theoretically, there is no limit on the amount of expenditures (E) that the state will match; however, in practice states have capped that amount. The capping of the amount is referred to as an expenditure ceiling. Table 1.3 indicates only one state, New York, uses percentage equalizing as the primary state funding mechanism.

Guaranteed Tax Base/Yield Programs

The guaranteed tax base (GTB) and guaranteed tax yield (GTY) programs are conceptually the same, but technically different. In both programs, equal tax efforts produce equal revenue per pupil. Both programs provide taxpayer equity since equal effort produces equal fundings. GTB programs guarantee a given level of assessed valuation per pupil.

The formula for the GTB is:

$$S_i = N_i r_i (W_s - W_i)$$

Where: S_i = State equalized aid to the i th district;
 N_i = number of units (pupils, etc) in the i th district;
 W_s = Value (wealth) of the state tax base;
 W_i = Value (wealth) of the tax base of the i th district;
 r_i = Tax rate (local effort) of the i th district.

In the GTB program, the state chooses the assessed valuation that it wishes to equalize to; that amount may be the state average assessed valuation but it can be any level. While the amount of equalization that occurs is dependent on the level of assessed valuation the state chooses, local fiscal control is maintained since the local district can determine its own tax rate (fiscal effort).

The formula for the GTY is:

$$S_i = N_i (Y - Y_i) r_i$$

Where: S_i = State equalized aid to the i th district;
 N_i = Number of units (pupils, etc.) in the i th district;
 Y = Guaranteed yield per unit value;
 Y_i = Yield per unit value of the i th district;
 r_i = Tax rate (local effort) of the i th district.

In the GTY program, the state chooses a constant yield per unit of tax effort. The GTY program provides the greatest taxpayer equity. In its uncapped or unrestrained form it provides for wealth neutrality. Most states, however, cap or limit the number of mills or local effort that will be equalized. Often percentiles are used for the ceilings of equalization. As with the GTB, the GTY program provides for local fiscal control in determining level of effort. Table 1.3 indicates that only two states, Indiana and Wisconsin, use the guaranteed yield approach as their primary funding mechanism.

Full State Funding

Two states, Hawaii and Washington, reported full state funding. However, Alexander and Salmon (1993) argue (as was argued in the last edition of this volume) that only Hawaii uses full state funding since the state is responsible for raising all of the revenues for schools and the local districts has no fiscal

autonomy in raising additional revenue. Washington, as the result of a court order, is required to assume full responsibility for funding the basic educational program; however, local districts may levy additional taxes to fund non-basic programs. Although Swanson and King (1997) make a distinction between Hawaii having a full state-financed and state controlled program and Washington having a court ordered fully funded basic educational program, they identify both states as full state funding in their book.

Suggested References

Alexander, K. & Salmon, R. G. (1995). *Public School Finance*. Needham Heights, MA: Allyn & Bacon.

Monk, D. H. (1990). *Educational Finance: An Economic Approach*. New York: McGraw — Hill Publishing Co.

Odden, Allan R. & Picus, L. O. (2000). *School Finance: A Policy Perspective*. 2nd Edition. Boston: McGraw- Hill Publishing Co.

Swanson, A. D. & King, R. A. (1997). *School Finance: Its Economics and Its Politics*. White Plains, NY: Longman Publishers.