

**A Heuristic Examination of Education Finance Formulas,  
Revenue Components, and Flexible Expenditure Possibilities:  
An Initial Report to the Texas Joint Committee to Study the Public School Finance System  
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The scope of research defined for this presentation is bounded the statement: *Provide an informative, comparative investigative report on the structure of education finance systems, their education revenue components, and their influences on educational quality.* As such, this presentation is designed to answer the following questions:

1. How is education revenue distributed to school districts through state funding formulas?
2. What types of educational services and personnel revenue components exist within state funding mechanisms?
3. How are different types of educational revenue structures related to service quality?

Although the main purpose of this presentation is to address the research questions above, a concomitant purpose is to generate thematic content areas where individual states can begin building research capacities that would improve the effectiveness of education finance and service delivery at the district and school level. In lieu of examining all 50 states, this presentation examines nine Western states (i.e., Arizona, Colorado, Kansas, Nebraska, New Mexico, Oklahoma, Texas, Utah, and Wyoming).

### **EDUCATION FINANCE FORMULAS IN THE WESTERN REGION**

Making changes – and evaluating the effects of changes – in education funding mechanisms was an issue for all states throughout the decade. Some states had laws that prohibited increases in property taxes (e.g., Nebraska and Colorado), while other states limited other forms of taxation for education. Funding issues led to conflicts over large versus small school districts, resulting in lawsuits. Indeed, at one point, secession was threatened in Kansas. As a result, finding similarities between the nine states of the Western was a daunting task, given the wide variation in the types of state-run public school system present in the nine states themselves. Consider, for a moment, some key markers of school finance in the Western states that illustrate this variation:

- State percentages of education spending ranged from a low of approximately 40% in Nebraska to New Mexico's 75%.
- Similarly, the number of local education agencies (LEAs) under state jurisdiction ranges from Utah's low of 40 (which has held constant over the last decade) to Texas' approximately 1100.
- There was wide variation in per pupil expenditures: Utah has relatively low expenditures per pupil while Wyoming has relatively high spending.

Overall, these figures present a picture of the nine Western states as a diverse aggregation of finance structures and statewide public school system. Closer scrutiny, however, yields some key commonalities in challenges, finance structures and school finance trends among nine states in the West. Take Arizona for example. Arizona's structure is both equity-based – in that it attempts to equalize spending among districts – and adequacy-based in that it attempts to adjust per pupil spending based on individual student categories and needs. Additionally, Arizona's plan is equity-based in that it provides a fiscal foundation for all districts, but adequacy-based in its attempts to equalize that foundation based upon district characteristics. It is clear from the Arizona example that many Western states have simply layered school finance policies over each other over time, resulting in a finance system that draws from many strategies.

The nine states examined are caught between a focus on equalization among districts (in order to lower the disparity between wealthy and poor districts) and a movement towards

student-based school funding mechanisms. Some have argued that district level equalization schemes have greater impact on taxpayer equity than on school equality. However, equalizing expenditures across districts remains an important political issue. The shared challenges, structures and trends described below all take place within the context of these conflicting priorities within each state's school finance structure itself.

*Shared Challenges:* Key challenges – articulated by finance experts and upheld by our analysis – for school finance in Western states include the following: a) School funding in Western states is lower than in other regions; b) Soaring enrollments in Western states; and, c) Growing student diversity in Western states.

*Shared Structures:* Despite the variation described above, many Western states share commonalities within the structure of their school finance systems.

- **Foundation.** All nine states claim their school finance structure to be either partly or wholly “foundational” in that they provide a firm floor of funding to prevent school districts from falling into poverty. Many states now supplement this foundation with equalization formulas or strengthen them with guaranteed tax bases (See *Table A* next page).
- **Weighting.** In addition to providing a foundation, all nine states use some sort of weighting factor in order to equalize spending within districts and/or between districts. The three categories most commonly used in weighting formulas are pupil based, teacher based and district based. Pupil based weights are applied at the per-pupil level and include special education status, at risk status and language status among others. Teacher weights are based on factors such as education and experience. District weighting factors are most often concerned with a districts size or isolation.
- **Equity not Adequacy.** Although some of the nine states are on the cutting edge with their school finance structures, most formulas function more with an eye towards equitable spending than towards anticipated outcomes. This equity focus is present in all states save Wyoming; which instead focuses on resources being applied towards student outcomes.

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*Table A.*  
Descriptions of State School Finance Structures  
In the Western Region

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Arizona	“Equalized foundation”
Colorado	“Foundation with mandatory local participation”
Kansas	“High-level foundation”
Nebraska	“Foundation and equalization components”
New Mexico	“Foundation program”
Oklahoma	“Two-tiered equalization program”
Texas	“Combined foundation and guaranteed tax base plan”
Utah	“Foundation program”
Wyoming	“Resource block grant model”

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*Shared Trends:* In addition to shared structures, many of the nine Western states are concerned with ensuring that all districts have an equal opportunity to provide a quality education for their students. The following trends highlight efforts across all nine states:

- Equity. By focusing their school finance efforts on equity, all nine states indicate a commitment to equalize educational opportunities for all students. Missing is an explicit link between spending and outcomes.
- Isolated or small district aid. Finally many of the reviewed districts have developed a focus on small/sparse or isolated school districts with an understanding that the operating costs of these districts will be higher than average. This strikes on a particularly Western adaptation within the various school funding formulas.
- Land Use. Many of the nine states also rely upon monies generated by state natural resources to fund public education. Current movements in Arizona illustrate some of the advantages and controversies in such as finance strategy. Although Arizona plans to use land trust funds to supplement their funding for public education, many are concerned if this is an appropriate use of these funds.

Court cases in Western states illustrate a growing legal concern with special education students, English language learners and school facilities. As more of these cases and decisions coalesce into a coherent case law, states will eventually have to take greater responsibility for local funding and decisions. Time will tell if this responsibility will result in greater state level control of funds and finance.

#### **A SUMMARY OF EDUCATION FINANCE REVENUE COMPONENTS WITHIN WESTERN STATE FUNDING MECHANISMS**

*Arizona Basic Support Program:* Arizona uses a foundation program, including state funding for maintenance and operation, school transportation, capital outlay, and “soft capital.” For maintenance and operation, the state limits expenditures in all districts except for a group of low-enrollment districts. With the exception of the soft capital funds, state funds are considered to be block grants. School districts are not required to spend specific amounts on specific programs, and the monies allocated for capital outlay may be budgeted for maintenance and operations. The foundation formula is weighted to account for special needs and other higher needs students groups. The state equalization formula provides a base revenue amount per weighted student for maintenance and operation – plus additional funding for school transportation, capital outlay, high school textbooks, and soft capital – from a combination of state, county, and local funds. The state payment is the difference between the district's formula entitlement and the amount raised by the qualifying tax rate from local and county tax sources. There are revenue weights for special need students in preschool programs through grade 12 for children with cognitive, emotional, or physical disabilities (e.g., including but not limited to hearing handicapped; multiple disabilities, autism, and severe mental; retardation resource and self-contained programs; and, orthopedic impairment resource and self contained programs).

*Colorado Basic Support Program:* Colorado's school funding structure includes a foundation program with mandatory local participation created by the Public School Finance Act of 1994 (Colo. Rev. Stat. § 22-54). Local funding in Colorado comes from property and local vehicle taxes. If a local district's taxes exceed formula amounts without increasing the levy rate, the district must “buy out” the state provisions and fund them on their own. The funding formula allocates all revenue on a per-pupil basis. Each district's per pupil funding level is determined

individually with adjustments to the statewide base to account for size, cost of living, and the proportion of at-risk pupils. The categorical buy out provisions of the School Finance Act requires that certain districts offset or "buy out" state categorical aid with local property tax revenue. Any district that has funded its program cost, less minimum state aid and specific ownership taxes, with a levy less than the prior year's levy or a property tax change less than the sum of inflation plus the percentage change in enrollment must levy additional mills to offset all or part of state categorical support. The categorical programs that are subject to the local buy out provisions include special education, the English Language Proficiency Act, transportation, and vocational education. Three and four-year-old special education students and at-risk pre-school students are also weighted at 0.5 FTE.

*Kansas Basic Support Program:* Kansas has a foundation program with a high level of state control. This foundation level is high level, with weighting scheme for programs, low enrollments, and other selected features. Some categorical funds also are described later. In 1992, Kansas passed new legislation which increased state-level control. The resulting spending equalization plan resulted in a large increase in state percentage of funding for its 304 school districts. Kansas uses a uniform local tax rate that is set by legislature. Districts can add up to 25% of base budget with public approval through a local referendum. General State Aid (GSA) is the main funding program for districts' entitlement to state revenue and is based on an enrollment driven formula. A district's spending power, called State Financial Aid (SFA), is determined by multiplying its adjusted (weighted) full-time equivalent (FTE) enrollment by Base State Aid Per Pupil (BSAPP). Adjusted enrollment includes the full-time regular enrollment of pupils in the district after taking into account a declining enrollment feature and seven other adjustments (weights) that have been added to reflect higher costs associated with serving certain pupil populations, transporting pupils, operating low or high enrollment districts, and adding new facilities. Specific weights are for: 1) low enrollment, 2) small schools, 3) transportation, 4) vocational education, 5) bilingual education, 6) at-risk pupils, and, 7) operation of new facilities. Despite their weighted foundation approach, Kansas still uses a well-defined categorical fund approach for special education funding.

*The Nebraska Basic Support Program:* Nebraska uses a foundation and equalization components in its school finance structure, outlined in the Tax Equity and Educational Opportunities Support Act. The state computes both a "needs" estimate and a "resources" estimate for each school district, and equalizes the difference between these two numbers. Nebraska categorizes districts by census data as very sparse, sparse, or standard, and has a set per-pupil amount for each category. For districts within an affiliated school system, the "formula needs" and "formula resources" are aggregated to determine "system needs" and "system resources." Equalization aid is calculated for the system based on the difference between "system needs" and "system resources." School districts are grouped into very sparse, sparse, and standard cost groupings according to census students per square mile in the county where the high school is located, formula students per square mile in the high school system, and distance between high school attendance centers. Estimated general fund operating expenditures per adjusted formula student for each of these groups is calculated. The local system's cost grouping cost per student is then multiplied times the "adjusted formula students" in the system, plus transportation allowance and special education allowance to arrive at "formula need." "Adjusted Formula Students" include the Average Daily Membership (ADM) of the system, resident students the system is contracting out to other systems or service providers, as well as adjustments for demographic factors for poverty, limited English proficiency and students

residing on Indian land. Special need students are not treated consistently within the funding mechanism.

*The New Mexico Basic Support Program:* The basic structure of New Mexico's innovative 1974 Public School Finance Act still is in place. New Mexico finances public education through a foundation program, which relies on program units. These units are adjusted by special education student count, added together and multiplied by each district's "training-and-experience index" to produce adjusted program units. These units are further modified based on special categories (e.g., students served in non-profit special education programs; small and rural district status; growing district status; new district status; or, at-risk factors status) and save harmless clauses that apply to very small districts. This final figure is used to compute New Mexico's state equalization guarantee. In general, the public school funding formula uses cost differentials to reflect the costs associated with providing educational service to students. The program cost for each school district is determined by multiplying the student full-time equivalency in a particular grade or a program full-time equivalency by the respective cost differential to generate units. Those student full-time equivalencies and program full-time equivalencies are determined by district membership on the 40th day of school and adjusted by the count of special education students on December 1. All of the program units are then added together and multiplied by the district's training and experience index to produce the adjusted program units.

*Oklahoma Basic Support Program:* Oklahoma uses what is termed a two-tiered equalization program. This funding program is based on a foundation formula with transportation supplement and a modified guaranteed yield formula. Oklahoma earmarks school land earnings, motor vehicle collections, gross production taxes, and Rural Electrification Association Cooperative Tax revenues for support of public education. The foundation program for a given local district includes a legislatively determined statewide base support factor multiplied by the district's weighted ADM. The local foundation program income for the district is subtracted from this product. ADM are adjusted for four categories of weights. The first two categories are grade level and special education. For districts that qualify, ADM are additionally provided a small school or isolation weight.

*Texas Basic Support Program:* Texas relies on a combination foundation and guaranteed tax base plan. The Texas public school funding system is a shared arrangement between the state and local school districts. In order to offset variation in local capacity to fund schools through the property tax, the state provides funding to school districts in inverse relation to district wealth. State and local funds for public education in Texas are allocated through a system of formulas known collectively as the Foundation School Program (FSP). The system consists of two tiers: a) Tier 1 is a foundation program that includes adjustments and weights designed to distribute funding according to the characteristics of the school district and its students; and, b) Tier 2 is a guaranteed yield program that guarantees school districts equivalent taxable property wealth per weighted student. Tier 1 is the base or "foundation" funding level in the Texas FSP. Calculation of Tier 1 funding begins with the Basic Allotment, which is the base level of funding for each student in average daily attendance (ADA). The formula calls for the Basic Allotment to be multiplied by district adjustments that include the Cost of Education Index (CEI), the Small and Mid-Size District Allotments, and the Sparsity Adjustment. Adjusting the Basic Allotment by all the district adjustments results in the Adjusted Allotment. Instructional program weights are applied to the adjusted allotment, based on the numbers of students enrolled in or served by various special programs. The program weights are applied for special education, compensatory

education, bilingual education, career and technology education (i.e., vocational programs), and gifted education. Specifically, For special education and vocational education programs, weights are calculated on a full-time equivalent (FTE) student basis. For other programs, weights are applied to ADA served in the program (or to the school lunch count for compensatory education) on an add-on basis.

*Utah Basic Support Program:* Utah provides a basic levy amount per pupil foundation program – called the Minimum School Program – for instruction, maintenance and operations. These funds are distributed on a per pupil basis. Special education is weighted in the pupil counts, and districts that experience negative growth are held harmless for one year. Although Utah has implemented a state mandated tax rate, local districts can tax above it. Funding for Utah's basic support programs is identified in Utah's Minimum School Program as Regular Basic School Programs, which is composed of four sets of services: 1) K-12 Instruction; 2) Necessarily Existent Small Schools; 3) Professional Staff; and 4) Administrative Costs. These services provide for general maintenance and operation functions, which support basic classroom instruction. Funding for these services is based on the Minimum Basic Levy (against local property values) and the State's income tax.

*Wyoming Basic Support Program:* Wyoming's guaranteed tax base program (with a required minimum levy) is a resource block grant model, based on student attendance and a model school cost out. The state makes adjustments for smaller districts and regional cost of living. School finance in Wyoming has been driven by the driven by 1995 ruling in *Campbell County v. State*. The Education Resource Block Grant Model (commonly referred to as the MAP Model) provides the Legislature a mechanism to ensure each Wyoming student receives an equal opportunity to receive a proper education (i.e., a legislatively determined basket of education goods and services) by specifying the instructional and operational resources necessary to provide this basket. The model accomplishes this by systematically determining the competitive market costs of educational operating resources and aggregating these costs within each school district. A total revenue amount in the form of a "block grant" is provided to each school district to facilitate provision of the basket. The actual dollar amount of the block grant is a function of an interaction between the model components necessary for implementation of the basket and the characteristics of the schools and students within a particular district. Twenty-five specific cost components necessary to deliver the basket are contained within the prototype for each grade-level grouping. These cost components can be grouped into five major categories, as follows: 1) Personnel; 2) Supplies, Materials, Equipment; 3) Special Services; 4) Special Student Characteristics; and, 5) Special School/District/Regional Characteristics. Specifically, the model attempts to avoid segregation of students with special needs by assuming resources for small schools, small class sizes, teaching specialists and professional development sufficient to enable teachers to deal more effectively with special needs students within the general education classroom setting. The model identifies four categories of special students: Special Education; Gifted Students; Limited English Proficient Students; Economically Disadvantaged Youth. Importantly, Wyoming replaces 100% of special education costs - this is accounted for in Wyoming's block grant model.

#### **EDUCATIONAL REVENUE STRUCTURES AND STUDENT SERVICE QUALITY**

In examining the relationship between the structure of education school finance systems and educational service quality, the usefulness of any economic or financial analysis rests upon the strength and validity of the assumptions used to define the context of the analysis. This

presentation, therefore, examines the influence of each state's cultural, demographic, and economic contexts on their individual – and regional – educational experiences. Within these refined research objectives, two primary themes form the regional context within which analyses took place:

- There was shift in the political landscape away from vertically equitable spending on student needs (i.e., students with different characteristics receiving different amounts of funding in order to create similar in educational opportunities) toward a greater demand for more efficient and measurable student, teacher, and school accountability; and,
- There was a shift in education finance policies – and the philosophies that support them – away from ideas of increasing levels of educational expenditure equity among special need students and toward the investigation – in some cases the development of – educational finance systems based on concepts of educational adequacy (i.e., determining a “base cost” for the provision of educational services that should enable students to attain a prescribed minimum standard).

Given these larger political ideas a background, four themes emerged from this review of the Western states that affected – and will continue to affect – school quality:

- Changes in Funding Mechanisms. Across the Western states, court-ordered or legislatively mandated changes to education finance mechanisms marked the beginnings of political change from equity to adequacy in school funding. These changes begin to investigate how much revenue levels, tax rates, access to assessed valuation, and usage of categorical supplements directly influence educational attainment.
- Major Demographic Changes. Three significant changes in demographics are notables: a) General increases in the special need student population; b) Increases in the number of special need students from predominately low-wealth schools and districts; and c) Increases in the number of ethnic and language minority special need students.
- Erosion of Local Control. At a fundamental level, due to efforts to link educational outcomes to funding, Western states were forced to consider what equitable educational opportunities actually are for their special need students. In the midst of these considerations, individual states struggled to maintain local control of schools while developing state-mandated educational standards, assessment instruments, and defend the fairness of its school finance mechanisms for special needs students. Interestingly, this erosion of local control occurred while the dominant political climate in these states were becoming more conservative. A reversion toward locally should be expected to continue over the next few years.
- Pressure to give local districts and schools revenue flexibility. In tight budget times that characterize the last four years in state capitols, as well as the history of inclusive practices suggested by Sailor and Burrello in Chapter Two, school districts and schools want discretions over appropriate administrative, instructional, and policy practices in order to serve all students with special learning needs well. Policy effectiveness should be the driving value here; that is, educational leaders need to ensure resources are utilized in manners that lead to



improved educational attainment and post-schooling outcomes that are aligned with the goals of federal enabling legislation.

After nearly years of favorable economic conditions – and the consequent growth in state revenues – most Western states ended 2008 struggling over the various ways to reduce expenditures while grappling simultaneously with sharply reduced revenue projections. Given this fact, remember that two specific state actions taken during the “Booming 2000s” may exacerbate the fiscal challenges of the next few (or more) years:

- 1) States legislatures reduced tax rates. In order to increase rates again, lawmakers will have to take unpopular political action.
- 2) State legislatures funded new programs. During these austere economic times, new programs such as charters now will compete with long-standing public school services for funding.

With many state budgets being reduced by the current economic slowdown and long-term structural deficits, legislatures are considering a variety of short-term revenue options (e.g., drawing revenues from “rainy day funds”), spending reductions, and tax cuts. The use of certain short-term measures may be appropriate in some cases; however, if the state’s budget imbalance primarily reflects structural problems, these measures will only make it harder for states to balance their future budgets. Maintaining funding for wide number of existing state services places enormous pressure on state legislatures to continue the proactive strategy of sharply reining in – if not reducing – their appropriations to public education. Being cognizant of these changing economic influences will directly affect the pursuit any of the recommendations proposed in this research.

### **RECOMMENDATIONS**

It is important to remember that states practice the science of education inside of political, economic, and social arenas. Educators are asked to perform the difficult tasks of special education finance policy interpretation, implementation, and evaluation. Yet, only recently have these experienced education professionals been asked to *develop* policies that can improve the system of education and educational outcomes. Ironically, state and federal legislators -- some with expertise in education, most with none -- do develop special education finance policies and organizational goals. Further, even though the responsibility for implementing -- and the accountability for achieving -- special education finance policy goals are placed on educational professionals, little of their expertise was put to use during the policy development and legislative phases. Therefore, while political influences and mechanisms of legislatures generate education policies -- many with conflicting purposes and goals -- education professionals are held accountable for attaining positive results from all policies regardless of their original intent.

### **References:**

Available Upon Request