

School Funding Facts and Principles

Preamble

The Ohio Supreme Court opined in *DeRolph I* that Ohio's elementary and secondary schools are neither thorough nor efficient, thus unconstitutional. The Court ordered that the system of school finance must undergo a complete systematic overhaul in order to remedy the unconstitutional education system. As recent as May 16, 2003, the Court in *DeRolph V* reiterated the *DeRolph IV* order, which directed the General Assembly "to enact a school-financing scheme that is thorough and efficient, as explained in *DeRolph I*, *DeRolph II*, and the accompanying concurrences." The "complete systematic overhaul" ordered in *DeRolph I* and *II* involves but is not limited to:

- a determination of a per-pupil base level that is predicated on the learning resources required and the outcomes expected of a constitutional thorough and efficient system of public education
- fund an adequate education in every school district
- reduction in reliance on property tax
- elimination of forced borrowing to meet ordinary school district expenses
- provision for adequate funding for school facilities
- elimination of unfunded mandates
- elimination of phantom revenue
- provision for a statewide school facilities assessment
- provision for strict statewide academic standards including input and output standards

The *Blue Ribbon Commission on Financing Student Success* must address all components of the complete systematic overhaul referenced in the Court decisions. These major issues must be fully addressed; otherwise the Commission will bog down in merely tweaking the old failed unconstitutional system.

Governor Taft's charge to the Commission is to "make recommendations for reforming the funding system for Ohio's schools." It must be assumed that this charge is consistent with the state's responsibility to give the school funding system a complete systematic overhaul in accordance with the *DeRolph I*, *DeRolph II* and *DeRolph IV* decisions.

The first order of business for the Commission is to determine what educational opportunities must be available in the classrooms and school buildings of Ohio and what is expected of students upon graduation. Both inputs and outcomes are germane to this necessary first step.

The cost of an adequate education, of course, depends on the definition of adequacy. Any definition of an adequate education that does not include the identification of learning resources required for students to meet the outcome standards will result in a fabricated per pupil support level.

DeRolph Triggered Additional Funds to Public K-12 Education

- A. The Ohio School Facilities Commission (OSFC) was established in response to the DeRolph litigation. Governor Taft's \$23 billion school rebuilding program was announced in September 1999. A comparison of the district-by-district cost estimates in the Governor's 1999 plan with the actual cost of projects approved by OSFC shows that the plan will actually cost about \$33 billion.
- B. The state budget priority for public K-12 education increased during the DeRolph litigation era. In the late 1970s over 40% of the state's budget was allotted to public K-12 education. By FY 1992, the year DeRolph was filed, that percentage had dwindled to 34.5. With the pressure from the DeRolph case, the state budget priority for public K-12 education increased to 39.3% in FY 2003. Hence, the DeRolph litigation merely restored the state budget priority for public K-12 education that was in place in the 1970s.

Release of Court Jurisdiction Precipitated Lower State Budget Priority for Education

The Court reiterated in December 2002 and May 2003 that the school funding system is still unconstitutional but released jurisdiction of the DeRolph case. Without pressure from the Court, the legislature backed away from the trend in the state budget priority for public K-12 education that began subsequent to the DeRolph Case filing. In FY 2004, the percentage of the state budget assigned to public K-12 education declined to 38.6%. This percentage went down to 38.5 in FY 2005.

According to the Legislative Service Commission, Ohio's General Revenue Budget will increase by 6.69% in FY 2004 and 3.5% in FY 2005. Public K-12 education will increase by 2.25% in FY 2004 and 2.36% in FY 2005.

It is not being suggested that the 1973 era percentage of the state budget assigned to public K-12 education is the standard that should be met. Since 1973 numerous additional programs are being funded by the public K-12 education state appropriations. Included among these additional programs are auxiliary services and administrative cost reimbursement for non public schools; charter schools; mandatory preschool for children with disabilities; Headstart; preschool; expanded special education, vocational, gifted and disadvantaged programs; programs for MR/DD and proficiency testing.

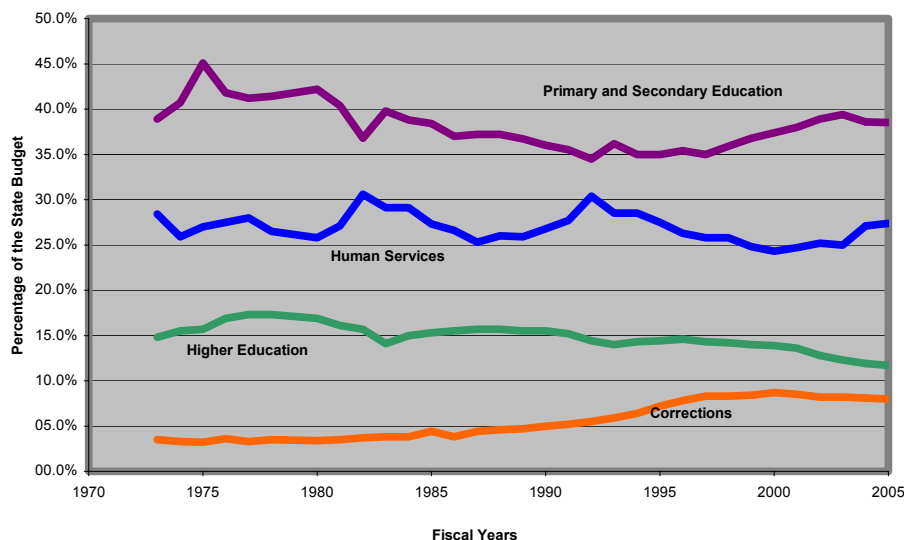
The total state revenue and demand for other services are important considerations in the distribution of state money. The Court found fault with the state's practice of "residual budgeting" i.e., predetermining the total amount of money to be assigned to public education and then "backing in" to the per pupil base cost amount. The process must be reversed—a formula based on pupil needs must be developed.

Trends In State Budget Priority For Certain State Services 1973-2005

Public K-12 Education and Human Services have about the same state budget priority in FY 2005 as in FY 1973. During that same period, Higher Education lost ground while Corrections gained in percentage of the state budget. The graphic below shows the trends over time.

**Percentage of State Budget by Agency
FY1973 - 2005**

Source: LSC at www.lsc.state.oh.us



Five Year Fiscal Forecast Data Underscore The Inadequacy Of The School Funding System

School districts are required to project five-year fiscal forecasts and to file such forecasts with the Ohio Department of Education. Even though these forecasts are estimates, the trends are instructive. In FY 2003, seven districts projected an aggregate deficit of \$3,001,465. The number of districts and aggregate deficits projected by year follows:

| Fiscal Year | Number of Districts | Aggregate Deficit |
|--------------------|----------------------------|--------------------------|
| 2004 | 58 | \$62,604,146 |
| 2005 | 164 | \$485,866,039 |
| 2006 | 261 | \$1,382,316,204 |
| 2007 | 364 | \$2,933,927,297 |

Many districts that projected deficits will pass levies and/or reduce programs and personnel in order to balance their respective budgets. The addition of local millage runs counter to the Ohio Supreme Court's admonition to reduce reliance on property tax. Reductions in programs and personnel diminish educational opportunities for students. This diminishes the potential of accomplishing a thorough and efficient system of public common schools.

No Child Left Behind Act (NCLBA) Will Cost States And School Districts

According to a note from the Office of General Counsel of the National School Boards Association (NSBA), the U.S. Secretary of Education, in a recent meeting with the NSBA Board of Directors, expressed frustration that school leaders are not giving enough recognition to the \$11 billion increase in federal funds to education since the current administration took office. NSBA General Counsel noted in the June 12, 2003 Legal Clips:

The context in which this increase has occurred is important: 1) school costs are increasing from greater enrollment, higher special education expenses, and, not least, the full range of looming NCLBA mandates, including for testing, for highly qualified teachers and paraprofessionals, for supplemental services, for technical assistance, for transportation, etc.; 2) 28 years after Congress enacted IDEA and committed to fund 40% of special education costs, the federal contribution is at 18%, and it remains to be seen whether Congress will make adequate yearly progress toward providing its "full" 40%; and 3) similarly, actual NCLBA appropriations have been billions less than the amounts authorized with great fanfare when the act was passed.

The U.S. General Accounting Office (GAO) has released a study by Congress on the costs of implementing the testing requirements under the No Child Left Behind Act. The study describes states' Title I tests, estimates what states may spend to implement the required tests, and identifies factors that explain variations in expenses. In summary: 1) if all states use tests with machine-scored multiple-choice questions, total state expenditures will be about \$1.9 billion; 2) if all states use tests with a mixture of multiple-choice questions and a limited number of essay or other open-ended questions that require written responses and hand scoring, total spending would be about \$5.3 billion; 3) if states stick to the mix of question types they reported to GAO, the cost will be about \$3.9 billion; and 4) several states are exploring ways to reduce assessment expenses, but information on their experiences is not broadly shared.

Full GAO report at <http://www/gao/gov/new.items/d03389.pdf>

The GAO report should not be construed to be the whole story. The NCLBA mandate will require massive new fiscal resources. Will the feds provide these new resources? U.S. Secretary of Education Richard Riley, in a letter of January 19, 2001, indicated that the states have the responsibility of providing educational resources to meet new standards. Riley wrote: "Indeed, raising standards without closing resource gaps may have the perverse effect of exacerbating achievement gaps and setting up many children for failure."

In the May issue of Phi Delta Kappan, Dr. William J. Mathis, a Vermont school superintendent and education finance professor at the University of Vermont, reviews the projected cost of implementing NCLBA in 10 states. Mathis projects the additional cost to implement NCLBA nationwide to be between \$84.5 billion and \$148 billion. The current federal Title I appropriation is \$11.3 billion and the administration's budget request is \$12.3 billion. NCLBA may be the most burdensome unfunded mandate in U. S. history.

Education Opportunities And Educational Attainment

It has been well documented by national reports of state-by-state comparisons, state reports and the DeRolph litigation that Ohio does not provide high quality educational opportunities for all school children. Education Week recently graded Ohio D- in school funding equity. The Morgan Quitno Press ranked Ohio 41st (tied with Alabama) in State and City Rankings Publications-2002 Smartest State Award.

A 1996 U. S. General Account Office study reported that Ohio has the worst public school buildings in the nation.

Ohio's school funding system has been unconstitutional since March 24, 1997.

Ohio is 41st in the nation in per full time student support of higher education. Tuition at state supported higher education institutions is high and escalating. The percentage of the state budget allotted to public higher education has declined significantly from FY 1992 to FY 2003.

High levels of educational attainment are predicated on the availability of high quality educational opportunities. Ohio's educational attainment is low compared to other states according to U.S. Census data.

A report prepared by **Education Trust, Inc.-Education Watch Ohio, Winter 2002-2003**, provides the following comparison regarding enrollment in college and completion.

Participation and Persistence in Postsecondary

| | <u>Ohio</u> | <u>Top States*</u> |
|--|-------------|--------------------|
| H.S. freshman enrolling in any U.S. college within 4 years | 40% | 54% |
| 1 st year community college students returning their 2 nd year | 56% | 63% |
| Freshman at 4 year college returning their sophomore year | 75% | 83% |
| First-time full-time freshman completing a BA within 6 years | 50% | 61% |

*Top States = median of top 5 performing states (Measuring Up 2002)

You may access this report at www.edtrust.org

Shifting Of The Tax Burden

A Multistate Tax Commission report released July 15, 2003 helps explain part of Ohio's budget problem.

According to the report, Corporate Tax Sheltering and the Impact on State Corporate Income Tax Revenue, state corporate income taxes as a proportion of corporate profits, declined by 34%, from approximately 9.6 % during the 1980s to 5.9 % in 2001. Tax sheltering and state policy changes have contributed to the reduction.

Corporate tax sheltering reduced state corporate income tax revenues by more than one-third in 2001.

The report indicates that the lost revenue attributable to corporate income tax sheltering is adding to the size of state budget deficits while at the same time undermining the equity and integrity of state tax systems.

The vast majority of U.S. businesses are not a part of the state corporate income tax sheltering problem, according to the Multistate Tax Commission report.

The typical state suffered a corporate tax collection loss of 31.1%. The range was from 10.3% to 57.8%. Ohio was at 56.9%, second only to West Virginia with 57.8%.

The percentage of the state budget revenue provided by corporate franchise tax has decreased from over 16% to less than 5% over the last quarter century. Many major corporations in Ohio currently pay only \$50 per year in corporate franchise tax.

A national report, *"Who Pays? A Distributional Analysis of the Tax Systems in All 50 States"*, produced by the Institute on Taxation and Economic Policy (ITEP) released earlier this year, shows that low-income and middle-income Ohio families pay a greater share of their income in state and local taxes than the state's most affluent. The top 1% pays 9.7% while the families in the lowest-income quintile of taxpayers pay 11%.

A study by the Education Tax Policy Institute shows that the property tax burden has recently shifted dramatically from business to individuals. In the period from 1990 to 2000, residential and agricultural real property valuation has grown from 53% to 61% of total taxable valuation. Annual taxes on residential and agricultural property increased by \$1.7 billion in the 10 year period between 1990 and 2000 while taxes on all other classes of property increased \$1.1 billion. This trend will be exacerbated by acceleration of the phase out inventory valuation and other downward adjustments in tangible property in HB 95. The continuing tax abatements by local political jurisdictions compound the problem for individual property taxpayers.

The June 2003 newsletter of the Ohio Public Expenditure Council (OPEC) references the ITEP report mentioned above with a focus on sales tax. The OPEC Newsletter shows that Ohio sales tax is regressive. Ohioans with an average income of \$8800 pay 6.3% of their income to sales and excise taxes while those in the top 1% in income pay 1% of their income in sales and excise taxes.

Charter School Payments Deducted From School Districts

According to the August payment schedule posted on the Department of Education website, the Department will deduct \$237,148,578.59 in FY 2004 from Ohio school districts to pay charter schools. This deduction will increase as the 2003-2004 school year unfolds.

State officials claim charter schools are paid from state money even though the funds are deducted from school district payments. Others view the payments as a combination of state and local funds. Regardless, public schools will have \$237 million less to spend in FY 2004 due to deductions for charter schools.

Charter schools were paid \$205 million FY 2003 and \$138 million in FY 2002. Unless the trend levels out or is reversed, public school districts losses to charter schools will exceed a billion dollars within a few years.