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School Finance Reform and the Fiscal Year 2010 Budget

This brief examines Fiscal Year (FY) 2010 school funding proposals and their relationship to the school funding reforms of the past two decades. By looking at the basic framework for how schools are funded, criticisms of that framework and attempts at reform, it is easier to understand the proposed distribution of federal stimulus to help school districts and to consider alternatives.

SCHOOL FINANCE IN MASSACHUSETTS: 1993 – 2006

The existing distribution system for state aid to public schools, described in Chapter 70 of the Massachusetts General Laws, was created in 1993 as part of the Education Reform Act. That same year, the Supreme Judicial Court ruled that Massachusetts had an obligation under the state's Constitution to provide all public school students with the opportunity to receive an adequate education.

While the Education Reform Act's formula for funding public schools was complicated, the basic components were straightforward:

1. Based on total enrollment by grade, regional cost differences, and the number of low-income and English language learners, the state determines the cost of providing an adequate education in every school district. This cost is called a district's Foundation Budget and is adjusted for inflation each year.

2. Measures of local ability to pay based on income, property wealth and revenue growth are used to determine how much the communities in a school district can fairly contribute towards the Foundation Budget. This amount is called a district's Required Contribution.

3. The state then provides funds to meet any gap between the Foundation Budget and the Required Contribution.

Under the Education Reform Act, state aid would increase annually until all school districts met their Foundation Budget. Through the 1990s, the state steadily increased its support of public education and, by FY 2000, all school districts in the state were spending at least their Foundation Budget amount.

The implementation of the Education Reform Act led to significant increases in state aid to public education, particularly in lower-income districts. By 2007, the Massachusetts education funding system was among the most progressive in the nation.[1] Massachusetts students are scoring at the top of the nation in the National

[1] For more information on school funding progressivity around the country see the Ed Trust 2006 Funding Gap report, available online at http://www2.edtrust.org/EdTrust/Product+Catalog/main.htm#ff.

Assessment of Education Progress rankings and near the top of the world in the 2007 Trends in International Mathematics and Science Study.[2]

CALLS FOR REFORM

While the Chapter 70 funding formula led to significant funding improvements, particularly in lower-income districts, there was dissatisfaction from a number of school districts. Some communities felt that their Required Contribution was unfair, while neighboring communities often questioned why seemingly similar towns received different levels of state support. Many education advocates also questioned whether the Foundation Budget truly captured the costs of a quality education.

In general, the criticisms revolved around three major issues:

- Adequacy – whether the Foundation Budget was actually sufficient to meet the educational needs of students as defined by the state's Curriculum Frameworks;
- Fairness – whether Chapter 70 aid and the Required Contribution were calculated in a way that fairly represented a district's ability to pay and its need for state aid; and,
- Clarity and predictability – whether changes in state aid and local contribution levels from year to year were easy to explain.

Specifically, several aspects of the implementation of Chapter 70 formula were cited as problematic:

- The amount districts contributed to education prior to the enactment of the Education Reform Act heavily influenced what these districts were required to spend in future years. The intent of the act was to ensure that over time each district would contribute an amount determined solely by its ability to pay. In reality, many districts were never required to increase their contribution to the levels indicated by the formula, while a few were required to contribute far above the levels dictated by the formula;
- Political pressure to ensure that no district received a reduction in state aid resulted in state aid levels out of line with the original formula;
- Because the formula was perceived as difficult to understand, districts had trouble projecting how much state aid they would receive in a given year, making the budget process more difficult;
- Communities with high property values, but average incomes, felt unfairly treated;
- Aside from annual inflation adjustments, the formula used to determine each district's Foundation Budget was not updated to reflect new estimates for the costs of educating different types of students or for meeting new standards; and,
- Some wealthy communities argued that they were paying for a large percentage of state aid through their state taxes, while receiving too little Chapter 70 aid in return.

SCHOOL FINANCE IN MASSSACHUSETTS: 2006 - 2008

In 2006, changes were made to the Chapter 70 formula primarily to address concerns about perceived fairness and predictability. The changes, to be phased in between FY 2007 and FY 2011, altered how the state

[2] NAEP scores can be found at http://nces.ed.gov/nationsreportcard/nde/statecomp/; Massachusetts TIMMS performance can be found at http://www.doe.mass.edu/news/news.asp?id=4457.

determined local contributions and state aid. These changes were made through the state budget process and were never adopted in the Massachusetts General Laws, meaning that the original Chapter 70 formula still remains in law. New provisions included the following:

Target Contribution and Target Share

Under the changes, a new measure of ability to pay, called Target Contribution, was determined for each community based equally on local property values and incomes in the community. Each community's initial target contribution is equal to the sum of what it would raise with a 1.5 percent local income tax on all income earned by residents and a property tax rate of $3 dollars per thousand on all property in the town.

If a town's initial target contribution exceeds 82.5 percent of its Foundation Budget, the target contribution is capped at 82.5 (when this provision is fully-phased in). This cap helps those districts with the highest incomes and property values where the basic formula would indicate there is enough local capacity to pay for more than 82.5 percent of the full costs of educating their children. It requires that regardless of how little need is indicated by the basic formula, the state will still provide enough aid to pay for the remaining 17.5 percent of any town's Foundation Budget.

The difference between each community's target contribution and their Foundation Budget is their Target Share – the amount of Chapter 70 aid a community should receive to reach its Foundation Budget.
While target contributions vary greatly by community because of different levels of income and property wealth in different communities, in FY 2010 the formula requires that statewide, local communities contribute 59 percent of the Foundation Budget level and the state contributes the remaining 41 percent.

What happens if a community is contributing above its Target Contribution?

When Chapter 70 reforms were made in FY 2007, 232 of the state's 351 cities and towns were required to contribute above their target contribution (due to higher historic contributions). Each of these communities was allowed to reduce its required contribution toward its target contribution by an increasing percentage each year.[3]

What happens if a community is contributing below its Target Contribution?

Communities whose required contribution level falls below their Target Contribution must move toward their target contribution. Each year, these communities have their Required Contribution increased based on their Municipal Revenue Growth Factor (MRGF).[4] Communities whose Required Contribution falls more than 5 percent below their target contribution have an additional percentage point added to their MRGF. Communities whose Required Contribution is more than 10 percent below Target Contribution have two percentage points added to their MRGF.

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[3] From FY 2007 to FY 2009, the reduction percentage increased from 20 percent to 33 percent of the gap. As discussed later, both FY 2010 proposals reversed the trend of increasing the reduction percentage.

[4] Municipal Revenue Growth Factor is used to approximate revenue growth in a municipality. Contributors to MRGF include property tax levy limit, state aid, and other local revenue sources.

How is state aid distributed?

The 2007 reforms calculate four different types of state aid for every community, with the community receiving whichever type is largest. The types of aid are:[5]

Foundation aid

Foundation aid is the difference between a district's Required Contribution and its Foundation Budget. Foundation aid is the simplest type of Chapter 70 aid and has existed since the 1993 Education Reform Act. Under the 2006 reforms, a portion of the foundation aid many communities receive is aid to make up for the reductions in local contributions for communities that have historically spent at above their new target contribution. This includes communities that have the local capacity to pay for the full Foundation Budget amount, but are not required to do so because of the 82.5 percent cap.

Growth aid

Growth aid is a form of aid designed to help districts experiencing enrollment growth (because of how it is calculated it can also help districts whose Foundation Budget is increasing because of inflation). A district's growth aid is equal to the target share percentage of their Foundation Budget increase. For example, if a district has a target share of 50 percent and its Foundation Budget increases by $2 million, then its growth aid is equal to $1 million.

Down-payment aid

Down-payment aid is designed to help school districts who are spending above their target contribution and are therefore allowed to reduce local spending, but who would not otherwise be getting new foundation aid in that year. These are districts that would eventually get foundation aid as their local contribution decreases, but not until it has been allowed to decrease enough that such aid would be needed for the district to be able to spend at the Foundation Budget amount.

Minimum aid

Minimum aid is simply $50 for each student in a school district. This form of aid was used to ensure that each district received an aid increase each year.

Did the reforms address the adequacy of the Foundation Budget?

The 2006 reforms made three minor changes to address the adequacy of the Foundation Budget:

- The statutory cap on inflation, of 4.5 percent, was eliminated to ensure that Foundation Budgets increased at the actual rate of inflation;
- The Foundation Budget amount for English language learners was increased by $50 per pupil; and
- The Foundation Budget amount for low-income children was increased by $25 per pupil.

[5] For a more in depth look at the Chapter 70 reforms undertaken in FY 2007, see MassBudget's *Public School Funding in Massachusetts*, available online at http://www.massbudget.org/doc/507

Aside from these three small changes, nothing was done in 2006, or since, to comprehensively examine whether or not the Foundation Budget is an adequate approximation for the costs of educating children in Massachusetts.

FY 2010 EDUCTION FINANCE PLANS

The Governor's House 1 Budget

In light of the ongoing fiscal crisis, the Governors' FY 2010 budget funded Chapter 70 at the FY 2009 level and using the FY2009 distribution formula.

While the Governor level-funded the state aid portion of the Chapter 70 formula, he continued to implement (in some form) aspects of the FY 2007 reforms, including:

- Calculating Target Contributions using the method described above; and,
- Reducing FY10 contributions for high-contribution communities by 25 percent of the gap between their initial required spending and their target contribution, in the manner described above.[6]

- At the same time the Governor's proposal suspends or eliminates other features of the reforms, such as:

- Growth aid, which guarantees state aid to all districts with growing Foundation Budgets;
- Down-payment aid, which provides aid to districts who are above their target contribution, but not yet eligible for foundation aid;
- Minimum aid, which guarantees every district at least $50 dollars per pupil in new aid;
- Sets the inflation rate on Foundation Budgets at the statutory maximum of 4.5 percent, despite the actual inflation rate of 6.75 percent.[7]

The Governor also introduced a new component to the formula:

As in the past three years of the Chapter 70 reforms, communities with preliminary local contributions below their Target Contributions had their required contributions increased. In the past, these low-effort communities were required to increase their contribution based on local revenue growth.[8] Under Governor Patrick's proposal, low-effort communities are required to contribute the lesser of 95 percent of their FY 2008 target contribution or their target share. This change is designed to get low contributing districts much closer to their target contribution in one year. This means that many communities – including several lower-income

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[6] This includes communities whose Required Contribution is capped at 82.5 percent through the Chapter 70 floor.

[7] The 6.75 percent rate is calculated as defined in statute, Mass. General Laws Chapter 70, section 2.

[8] In FY 2008, a new element of the plan was introduced to increase the contributions of low-effort communities: communities contributing below their target level by more than 5 percent had their Municipal Revenue Growth Factor adjustment to their Required Contribution increased by either 1 or 2 percentage points. This was done to bring these communities closer to the level dictated by the formula. The Governor's change, which captures up to 95 percent of low-effort communities' FY 2008 actual contribution as required contribution will not actually force increased local spending on education, but it does reduce increase the local share of the Foundation Budget, meaning that less state aid will be needed for the community to reach its Foundation Budget in the future.

communities – receive significantly less aid than they would have received if this new reform had not been implemented this year.

Result of the Governor's Proposal

Because Chapter 70 aid was kept at last year's level, the Governor's original plan meant that in 153 operating school districts the combination of Required Contribution and Chapter 70 aid would not meet that district's Foundation Budget previously determined to be the minimum amount needed to meet the constitutional obligation to provide an adequate education to students in those districts.

Together these districts would have received $168 million less than the amount they would need to meet the minimum requirements of the Foundation Budget formula. This would likely constitute a violation of the state's constitutional obligation to ensure that every school district has the resources needed to provide access to an adequate education. While the state could adjust local and state contributions in several different ways to ensure that every district will spend the Foundation Budget amount, it can not, constitutionally, fail to ensure that every district can spend at the Foundation Budget level that is the minimum needed to provide an adequate education to the students in that district.

The House Ways and Means Proposal

One April 15, the House Committee on Ways and Means (HWM) released its FY 2010 budget recommendations. The HWM budget approached Chapter 70 in the same way as Governor Patrick, level funding all districts at their FY 2009 level for a total of $3.948 billion.

While the House Ways and Means school funding proposal is identical to the Governor's proposal in terms of state aid distribution, there are two major differences in how the House determined required contribution. These differences affect the amount of additional funding necessary for all districts to reach their Foundation Budget.

The Governor's budget proposal and that of House Ways and Means make different choices in terms of non-Chapter 70 revenue for cities and towns. The Governor proposes smaller non-Chapter 70 cuts, new revenue sources at the local level, and assumes cities and towns will have more revenue in FY 2010 than does the House Ways and Means budget. Because of the different assumption about local revenue, the Governor's Chapter 70 plan uses larger MRGF's to calculate required local spending for each city and town. In short, the Governor's budget assumes that cities and towns will be able to contribute more toward their Foundation Budget than does the House Ways and Means budget. Because the House Ways and Means budget is more conservative in its calculation of MRGF, the gap between the Foundation Budget and Required Contribution is greater in the House Ways and Means budget.

In order to partially offset the effects of using smaller MRGF's, the House Ways and Means budget allows high-effort communities to reduce their required contribution by only 15 percent of the gap between their initial required spending and their target contribution, as opposed to 25 percent proposed by the Governor. Reducing the amount high-effort communities can reduce their contributions limits the statewide gap between Required Contribution and the Foundation Budget, and therefore the amount of aid needed to fill this gap.

Result of the House Ways and Means Proposal

Like the Governor's plan, by level-funding Chapter 70 aid, the House Ways and Means proposal creates a gap in some districts between the combination of Required Contribution and state aid, and the Foundation Budget. Due to the differences between the two plans described above, the House Ways and Means plan falls $184 million below the amount of state aid necessary to ensure that all districts reach Foundation Budget.

FEDERAL STIMULUS AND CHAPTER 70

On March 19, Governor Patrick announced plans to use federal stimulus funds, appropriated in the American Recovery and Reinvestment Act (ARRA), to provide the $168 million necessary to ensure that required school spending met the Foundation Budget in the 153 districts for which that was not the case in the Governor's proposal. The House Ways and Means budget proposal, released on April 15, authorizes the Governor to use $184 million to ensure that required school spending in all districts meet the Foundation Budget.

What types of districts receive money and why?[9]

1. Districts with low incomes and low property values[10]

While much attention has been focused on districts that would receive money and do not seem to need it, a large share of federal stimulus funds went to communities that have clear need. These are districts that the state formula allocates additional resources to because these districts do not have the local resources to provide the minimum spending required to ensure an adequate education for projected enrollment in FY 2010. For example, $13.2 million was allocated to Springfield, $3.1 million to New Bedford, and $5.6 million to Brockton. In total, $89.7 million of the ARRA funds were distributed to these types of communities.

2. Districts that have been contributing more of their local resources than the formula requires[11]

In 2007, reforms to the state education funding formula reduced local contributions and increased state aid for those communities that were spending more of their own resources than other towns with the same capacity. Because the Governor's distribution continues to phase in this reform, some communities receive aid increases when other very similar communities do not – but this is because these communities receiving the new ARRA funds have historically received less aid, proportionately, than comparison communities. For example, Framingham contributes much more than the target set by the formula. Therefore, Framingham is allowed to reduce its contribution towards the target and gets $3.5 million in new aid. Altogether, $50.1 million of the ARRA funds went to these types of communities. It is important to note that some of these communities are

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[9] Analysis of ARRA distribution and the options ahead for school finance in FY 2010 are based on the Governor's House 1 proposal due to the availability of the underlying data for the Governor's plan on the Department of Elementary and Secondary Education's website. The categories described are not mutually exclusive. For communities that could belong to more than one group, this analysis assigns that district to the category it best fits. Districts that are contributing at too high a level, and are experiencing rapid enrollment growth, were assigned to group #2.

[10] For the purpose of this analysis, communities were included in this category if their Target Share is greater than 50 percent.

[11] Districts are considered to be contributing more of their local resources than required by the formula if their state aid level falls below their Target Share.

also experiencing rapid enrollment growth, and would have been eligible for ARRA funds even if the effort reduction provision had been suspended.

3. Districts where enrollments are growing rapidly

In many of the cases described above, the formula factors combined with enrollment growth determine how much aid particular communities receive. Increases in a district's Foundation Budget are the result of both inflation and enrollment changes. Thus any element of the formula that relates to the Foundation Budget is sensitive to changes in enrollment. Altogether, $17 million of the ARRA funds went to communities whose gap between the combination of state aid and required contribution and the Foundation Budget was due to growing enrollments.

4. Districts with high incomes and high property values

The maximum target contribution (or ceiling) of 82.5 percent of district's Foundation Budget means that many wealthy communities are considered high-effort and have had their minimum required contributions reduced over the past three years. Most of the districts that received ARRA money, and appear to have limited need, are receiving money because of this provision. It is a provision of the law which was specifically designed to increase funding for those who have the least need as measured by the needs-based formula. This includes $1.4 million for Belmont, $1.2 million for Wellesley and $1.2 million for North Andover. Altogether, $14 million of the total amount distributed was due to this provision.

What types of districts are not receiving any of the $168 million?

1. Many districts with declining enrollments

Districts with declining enrollment are less likely to receive aid because the Foundation Budget formula is based on the number of students in a district. Many of the lower income districts that are not receiving additional aid have declining enrollments and the formula therefore treats them as not less need.

2. Districts with high local capacity that have been contributing relatively less of their resources

The current education formula seeks to require every community to contribute the same proportion of local resources towards their schools. Therefore, those communities whose local spending is a smaller share of local incomes and property values than average are expected to increase local spending rather than receive new state aid.

WHAT'S NEXT?

As the state budget process progresses, the Legislature can examine overall education funding levels. It could decide that some of the elements of the formula should be changed, either permanently or for this fiscal year.[12]

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[12] ARRA calls for the education portion of the State Fiscal Stabilization Fund to be distributed using existing formulas. In Massachusetts, however, this language probably leaves significant flexibility as the reforms to the formula adopted in FY2007 were never put into the general laws and have been altered since their adoption. In addition, the Legislature could adjust state chapter 70 funding to offset elements of the distribution of the ARRA funding that would not be consistent with a revised distribution plan.

For example, the Legislature could decide that some of the FY 2007 reforms, such as local effort reduction or the minimum aid floor, should be suspended to allow more of the available resources to go to districts with the greatest need. One requirement that the Legislature does have to meet, however, is to make sure each district has the resources, from a combination of state aid and local contributions, to spend the Foundation Budget amount for every child. Providing at least that minimum funding level is required by the state Constitution.

What could be added to the Governor's proposal?

1. *Uncap inflation*

The Governor capped the Chapter 70 inflation rate at 4.5 percent instead of using the actual rate of 6.75 percent. While statute does cap inflation at 4.5 percent, in previous years when inflation has exceeded the cap, the actual rate has been used. The inflation rate is applied to the individual components of the Foundation Budget, meaning that if the inflation rate were uncapped, each district's Foundation Budget increase would be 2.25 percent higher. Uncapping the rate, with no other changes, would increase the gap between each district's Required Contribution and their Foundation Budget by $108 million, meaning that $276 million in federal funds (as opposed to $168) would be needed to ensure each district met its Foundation Budget. However, if both the 82.5 percent ceiling and the 25 percent effort reduction components were suspended, uncapping inflation would increase the foundation gap by $76 million – and far fewer dollars would go to wealthy communities. Alternatively, increasing the inflation factor by one percentage point, to 5.5 percent, would better reflect increasing costs at the local level, while limiting the increased gap between Required Contributions and Foundation Budget to $46.7 million. This would mean that $214.6 million in federal funds would be required to ensure that all districts meet their Foundation Budgets.

Who would this help?

Uncapping inflation would provide additional aid to each of the 166 districts receiving federal aid under the current plan. In addition, another 44 districts would be in need of Foundation Aid if the actual inflation rate were used.

2. *Include Growth Aid*

The Governor suspended Growth Aid, which provides additional funding to districts whose Foundation Budget increases. Growth Aid is calculated irrespective of a community's target contribution, so even if a community does not meet its target contribution, as long as their Foundation Budget increased it would receive growth aid. For example, if Growth Aid were funded in FY 2010, Boston would receive an additional $6 million. Assuming no other changes, Growth Aid would provide an additional $54 million in state aid in FY 2010.

Who would this help?

Growth Aid would help 231 districts who would receive more in Growth Aid than they would through Foundation Aid. Growth Aid helps districts irrespective of whether or not a district meets its target contribution, so funding growth aid would help a number of communities with low contributions and increasing enrollment.

3. *Fund Minimum Aid*

Minimum Aid is the most direct way to assist communities with declining enrollment. Because Minimum Aid is determined by multiplying enrollment by $50, even those districts losing enrollment would receive additional money. Including a Minimum Aid provision would add $19.8 million to Governor Patrick's Proposal.

4. *Fund Down-payment Aid*

The Governor's proposal suspends Down-payment Aid, which provides funds to communities who have reduced their Required Contribution, but are not yet eligible for Foundation Aid.

What would be the effect?

Funding 33 percent of the gap between districts' Chapter 70 aid and their Target Share would provide $12.8 million to communities who are contributing above what the formula calculates they would fairly contribute. However, without also suspending the maximum local contribution, as described above, much of this increase would go to wealthy communities.

What could be eliminated from the Governor's proposal?

1. *Suspend the Maximum Target Contribution*

Suspending the maximum target contribution would mean that certain high-wealth school districts would be required to increase their Required Contributions above their FY 2009 levels. Because these districts contribute above their required levels, this suspension would not require substantial increases in what school districts actually spend.

What would be the effect of suspending the maximum target contribution?

Suspending the 82.5 percent ceiling would significantly reduce the amount of ARRA funds going to districts with the lowest levels of need. By not capping these districts' required contribution at 82.5 percent of foundation, these districts would no longer appear to be in need of additional state aid to reach their Foundation Budget. Suspending maximum local contributions would free up approximately $14 million in ARRA funds.

2. *Suspending local effort reduction*

The Governor's FY 2010 proposal allows communities contributing above their target share to reduce their local contributions by 25 percent of the difference between their initial required contribution and their target share. Suspending effort reduction in FY 2010, while making no other changes to the Governor's school finance proposal, would free up approximately $16 million in ARRA funds.

What would be the effect of suspending effort reduction?

While the effort reduction reforms serve the long-term goal of establishing a fairer method for determining local contributions, in the short term, ensuring that adequate funding is available for every district may be determined to be more important than providing extra aid to those districts that had historically been required to spend above the new target amounts.

3. Eliminate New Provisions to Increased Required Contribution

To help communities required to contribute below their target share, the state could eliminate the provision of Governor Patrick's plan that captures 95 percent of a district's actual FY 2008 contribution as required contribution. This change, proposed by Governor Patrick, accomplishes two things:

- It moved a number of low contributing districts much closer to their target contribution in one year, without requiring substantial increases in actual local contributions. One of the chief hurdles the 2006 reforms had to overcome was how to bring low contributing districts up to their target contribution. Initially, the required contributions for low contributors was increased by MRGF, however since the inflation factor for the Foundation Budget often outpaces MRGF this was ineffective. While a change was made in the last two years to increase the factor by which required contributions are increased, Governor Patrick's change will make sure that the majority of actual spending in these districts is included in their required contribution;
- It reduced the amount of Foundation Aid necessary to keep all districts at Foundation Budget. By substantially increasing the required contribution in districts affected by this provision, the gap in those districts between required contribution and the Foundation Budget is reduced or eliminated.

What would be the effect?

If the 95 percent provision were eliminated, an additional $48 million in Foundation Aid would be distributed to school districts around the state that would have received that aid under the existing formula if this new change had not been implemented this year.

CONCLUSION

The current economic crisis creates great challenges to the state's ability to provide adequate support for public education in a fair manner. Thus far, both the Governor and House Ways and Means have proposed plans that make important policy decisions regarding how the state's existing finance formula will be implemented. While these decisions are largely designed to reduce costs to the state in the short term, it is important to consider how these decisions affect principles of funding fairness and adequacy moving forward.