

# EDUCATION FUNDING COMMITTEE

The Education Funding Committee was assigned the following responsibilities:

1. House Bill No. 1318 (2017) provided the Legislative Management appoint a committee consisting of five members of the Senate and six members of the House of Representatives to:
  - a. Examine how state aid for elementary and secondary education is determined and distributed under the state aid funding formula, analyze the impact of the state aid provided through the funding formula, and consider potential necessary changes to the funding formula to ensure equity, adequacy, and sustainability; and
  - b. Examine the delivery and administration of elementary and secondary education in the state and the short- and long-term policy and statutory changes that may result from or be necessitated by 21<sup>st</sup> century technological advances and global economics.
2. House Bill No. 1423 (2017) provided for a study of the portion of the elementary and secondary education funding formula which relates to the utilization of in lieu of property tax funds for the purpose of identifying and addressing any inequities in the application of the formula.
3. The Legislative Management also assigned the committee the responsibility to receive the following reports from the Superintendent of Public Instruction (SPI) regarding:
  - a. The financial condition of school districts (North Dakota Century Code Section 15.1-02-09);
  - b. Annual school district employee compensation reports (Section 15.1-02-13); and
  - c. The use of teacher loan forgiveness funds received under Senate Bill No. 2037 (2017), including the amount distributed, the number of eligible individuals receiving funds, the recruitment and retention of individuals participating in the program, the average starting salaries of individuals participating in the program, and the effectiveness of the program as determined under criteria developed by the SPI (Section 4 of Senate Bill No. 2037).

Committee members were Senators Donald Schaible (Chairman), Kyle Davison, Ralph Kilzer, Erin Oban, and David S. Rust and Representatives Pat D. Heinert, Richard G. Holman, Dennis Johnson, David Monson, Mark S. Owens, Mark Sanford, and Cynthia Schreiber-Beck.

The committee submitted this report to the Legislative Management at the biennial meeting of the Legislative Management in November 2018. The Legislative Management accepted the report for submission to the 66<sup>th</sup> Legislative Assembly.

## ELEMENTARY AND SECONDARY EDUCATION STATE AID AND FUNDING FORMULA STUDY

House Bill No. 1318 directed a study of how state aid for elementary and secondary education is determined and distributed under the state aid funding formula, the impact of the state aid provided through the funding formula, and potential changes to the funding formula to ensure equity, adequacy, and sustainability. The bill also directed an examination of the delivery and administration of elementary and secondary education in the state and the short- and long-term policy and statutory changes that may result from or be necessitated by 21<sup>st</sup> century technological advances and global economics. In addition House Bill No. 1423 provided for a study of the portion of the elementary and secondary education funding formula which relates to the utilization of in lieu of property tax funds for the purpose of identifying and addressing any inequities in the application of the formula. These directives were combined into one study.

### Background

#### North Dakota Constitutional Directives

Section 1 of Article VIII of the Constitution of North Dakota provides:

A high degree of intelligence, patriotism, integrity and morality on the part of every voter in a government by the people being necessary in order to insure the continuance of that government and the prosperity and happiness of the people, the legislative assembly shall make provision for the establishment and maintenance of a system of public schools which shall be open to all children of the state of North Dakota and free from sectarian control. This legislative requirement shall be irrevocable without the consent of the United States and the people of North Dakota.

Section 1 has been unchanged since its enactment in 1889.

Section 2 of Article VIII of the Constitution of North Dakota follows with the directive that:

The legislative assembly shall provide for a uniform system of free public schools throughout the state, beginning with the primary and extending through all grades up to and including schools of higher education, except that the legislative assembly may authorize tuition, fees and service charges to assist in the financing of public schools of higher education.

Section 3 of Article VIII of the Constitution of North Dakota requires that "instruction shall be given as far as practicable in those branches of knowledge that tend to impress upon the mind the vital importance of truthfulness, temperance, purity, public spirit, and respect for honest labor of every kind."

Section 4 of Article VIII of the Constitution of North Dakota directs the Legislative Assembly to "take such other steps as may be necessary to prevent illiteracy, secure a reasonable degree of uniformity in course of study, and to promote industrial, scientific, and agricultural improvements."

### **History of Education Funding**

Since the 1930s the Legislative Assembly has attempted to meet its constitutional directives by providing some level of financial assistance to school districts. In the late 1950s the Legislative Assembly initiated a foundation aid program that was based on a uniform 21-mill county levy and a supplemental state appropriation to ensure school districts would receive 60 percent of the cost of education from nonlocal sources.

For several years, the foundation aid program remained essentially unchanged. However, federal and state courts were beginning to address issues of spending levels for elementary and secondary education and whether those levels should be dependent upon the wealth of the school district in which a student resides. The Legislative Assembly, in an attempt to preempt such issues in North Dakota, responded by amending the foundation aid program in a way that evidenced a higher level of sophistication. Per student payments were more than doubled and weighting factors that recognized four classes of high schools were made part of the education formula. By the late 1970s a new funding category encompassing seventh and eighth grade students had been created and fiscal protections were instituted for school districts that experienced declining enrollment. In 1979 the Legislative Assembly appropriated \$208.4 million for the foundation aid program and added an additional \$1 million to pay for free public kindergartens.

The next major development affecting education finance occurred with the approval of Initiated Measure No. 6 at the general election in November 1980. This measure imposed a 6.5 percent oil extraction tax and provided 45 percent of the funds derived from the tax must be used to make possible state funding of elementary and secondary education at the 70 percent level. To meet this goal, the 1981 Legislative Assembly allocated 60 percent of the oil extraction tax revenues to the school aid program. Initiated Measure No. 6 also provided for a tax credit that made the 21-mill county levy inapplicable to all but the owners of extremely high-value properties. The Legislative Assembly eliminated the 21-mill county levy and increased state aid to compensate for the revenues that otherwise would have been derived from the levy.

Discussions continued on issues of funding inequities among school districts. Districts spending similar amounts per student and having similarly assessed valuations were not levying similar amounts in property taxes to raise the local portion of education dollars. It was alleged the system encouraged some districts to levy much smaller amounts than their spending levels and assessed valuations would seem to justify. Both the Legislative Assembly and legislative interim committees continued to evaluate the impact of weighting factors, considered the effects of increasing the mill levy equalization factor, and explored the excess mill levy grant concept. While individuals and organizations articulated the need to alter the state's education funding system, little agreement was reached beyond recommending increases in the level of per student aid.

### **Litigation**

In 1989 several school districts and parents joined in suing the state to have North Dakota's system of public school financing declared unconstitutional. The complaint in *Bismarck Public School District No. 1 v. State of North Dakota* charged that disparities in revenue among the school districts had caused corresponding disparities in educational uniformity and opportunity and those disparities were directly and unconstitutionally based upon property wealth. Four years later a district court declared the state's system of education financing to be in violation of Sections 1 and 2 of Article VIII and Sections 21 and 22 of Article I of the Constitution of North Dakota. The decision was appealed and in January 1994, by a one-vote margin, the North Dakota Supreme Court did not uphold the lower court's ruling. The Supreme Court indicated areas that were in need of legislative attention but, unlike courts in other states, it did not mandate specific legislative action.

Within a decade after the court decision, the Legislative Assembly's commitment to education funding had exceeded \$665 million. In 2003 the state was providing educational services to 99,174 public school students--50 percent of whom were being educated in the state's eight largest school districts. The remaining students were distributed across

205 other districts. Best estimates indicated that by 2013, the number of enrolled students could fall below 90,000. Against a backdrop of declining student numbers, rising expectations for services, and a belief the available resources were both insufficient and inequitably distributed, another lawsuit was brought against the state by the school districts of Williston, Devils Lake, Grafton, Hatton, Larimore, Surrey, Thompson, United, and Valley City.

*Williston Public School District No. 1 v. State of North Dakota* did not go to trial. Instead, the plaintiffs and the defendants entered a settlement agreement in which it was stated:

[I]t is desirable and beneficial for them and for the citizens of the State of North Dakota to stay this Act and provide the North Dakota Legislative Assembly the opportunity to settle, compromise, and resolve this Action in the manner and on the terms and conditions set forth in this Agreement. The terms and conditions required that the Governor, by executive order, create the North Dakota Commission on Education Improvement and submit to the Legislative Assembly in 2007 an executive budget that includes at least \$60 million more in funding for elementary and secondary education than the amount appropriated by the Legislative Assembly in 2005.

### **North Dakota Commission on Education Improvement**

The North Dakota Commission on Education Improvement, as initially configured, consisted of the Lieutenant Governor--in his capacity as the Governor's designee, the SPI, four members of the Legislative Assembly, four school district administrators, and three nonvoting members representing education interest groups. The commission was instructed to recommend ways in which the state's system of delivering and financing public elementary and secondary education could be improved, and to specifically address the adequacy of education, the equitable distribution of funding, and the allocation of funding.

The recommendations of the North Dakota Commission on Education Improvement became the basis for Senate Bill No. 2200 (2007), which provided a new education funding formula. The bill consolidated education funding that had been assigned to a variety of existing funding categories and established new weighting factors that reflected the added costs of providing education to certain categories of students and the added costs of providing various statutorily mandated services. In addition, the new formula factored in the variable cost of providing services and programs in small, medium, and large school districts. The Legislative Assembly increased the availability of capital improvement loans for needy school districts, provided increased funding for new career and technical education centers and programs, and provided funding for full-day kindergarten programs. The Legislative Assembly reauthorized the North Dakota Commission on Education Improvement and directed that it focus its attention on developing recommendations regarding educational adequacy.

### **2007-08 Interim**

After the 2007 legislative session, the North Dakota Commission on Education Improvement contracted with Lawrence O. Picus and Associates (Picus) to identify the resources needed to ensure an adequate education for all students. Picus began with the premise that adequacy requires all students to be taught the state's curriculum and strategies must be deployed to use resources in ways that would double student performance on state tests over 4 to 6 years. Picus determined very early in its efforts that while North Dakota students performed reasonably well on state tests, only 30 to 40 percent of North Dakota students performed at or above the proficiency standard measured by the National Assessment of Educational Progress. It was Picus' determination that North Dakota students would need to achieve at much higher levels if they were to be deemed fully prepared, upon high school graduation, for either college or the workplace. Picus concluded existing state per student payments, coupled with the yield of 185 mills on 88.5 percent of the state average imputed valuation per student, amounted to approximately \$7,024 per student, and to achieve adequacy, the expenditure per student would need to be \$7,293.

Picus also insisted expending a specific dollar amount per student would not achieve the desired results unless the expenditures were linked to certain programmatic strategies that guaranteed the desired results. Without such linkages, the final effect would be nothing other than the existing education system at a much higher cost to taxpayers. Picus' recommendations were centered around prototypical schools having 432 students in the elementary grades, 450 students in the middle grades, and 600 students at the high school level.

### **2009 Legislative Session**

In 2009, after reviewing the Picus report, the North Dakota Commission on Education Improvement made its own recommendations to the Legislative Assembly, many of which were enacted in House Bill No. 1400. At the conclusion of the 2009 legislative session, the North Dakota Commission on Education Improvement began its third and final interim effort and provided its recommendations to the 2011 Legislative Assembly.

### **2011 Legislative Session**

As had its predecessors, the 2011 Legislative Assembly incorporated the recommendations put forth by the North Dakota Commission on Education Improvement through the enactment of Senate Bill No. 2150 and Senate Bill No. 2013.

The amount appropriated for the grants - state school aid line item was \$918,459,478. In addition, the Legislative Assembly provided \$16 million for special education contracts and \$48.5 million for transportation.

### **Property Tax Relief Legislation**

While educational equity and adequacy continued to be dominant legislative concerns, additional time and attention was now being given to the desire for property tax relief. In the 2007 session the Legislative Assembly enacted property tax relief through the use of income tax credits and transferred \$115 million from the permanent oil tax trust fund to the state general fund to offset anticipated revenue losses resulting from the credits. Due to inherent administrative difficulties resulting from the use of income tax credits for property tax relief the 2009 Legislative Assembly instituted a statewide system of property tax relief through state-funded school district mill levy reductions. The biennial cost of the program was \$299 million. By 2011 the program's price tag had risen to \$341.8 million and there existed concerns regarding the overall effectiveness of the mill levy reduction grant program as a mechanism for property tax relief, the program's potential to result in the rededication of locally generated revenues to other purposes, and long-term sustainability.

## **State School Aid and Integrated Property Tax Relief**

### **2013 Legislative Session**

When the Legislative Assembly convened in January 2013, the principal education funding package contained a new proposal for funding elementary and secondary education, which included property tax relief provided through an integrated formula. Introduced as House Bill No. 1319, the new proposal was defeated on the morning of the 80<sup>th</sup> day of the legislative session, but the content was attached later as an amendment to House Bill No. 1013 and enacted. The legislative appropriation for the state school aid program followed substantially the executive budget recommendation to integrate property tax relief in the K-12 state school aid funding formula. The formula change discontinued the mill levy reduction grant program and provided the state will determine an adequate base level of support necessary to educate students by applying an integrated payment rate to the weighted student units. This base level of support will be provided through a combination of local tax sources, local revenue, and state integrated formula payments. The local funding requirement is set at 60 mills and a percentage of identified local in lieu of property tax sources and local revenues. Base level support not provided by local sources is provided by the state through the integrated formula payment. In addition, school districts are allowed an additional 10-mill levy for general fund purposes, an additional 12-mill levy for miscellaneous purposes, and a 3-mill levy for a special reserve fund. The legislation provided for a district's weighted student units to be multiplied by integrated formula payment rates of \$8,810 during the 1<sup>st</sup> year of the 2013-15 biennium and \$9,092 during the 2<sup>nd</sup> year, an inflationary increase based on total expenditures per student suggested by Picus during the 2008 study conducted for the North Dakota Commission on Education Improvement.

Minimum and maximum payment levels were established using a statutorily defined baseline funding level that includes:

- All state aid received by the district in accordance with Chapter 15.1-27 during the 2012-13 school year;
- The district's 2012-13 mill levy reduction grant, as determined in accordance with Chapter 57-64, as it existed on June 30, 2013;
- An amount equal to that raised by the district's 2012 general fund levy or that raised by 110 mills of the district's 2012 general fund levy, whichever is less;
- An amount equal to that raised by the district's 2012 long-distance learning and educational technology levy;
- An amount equal to that raised by the district's 2012 alternative education program levy; and
- An amount equal to:

75 percent of all revenue received by the school district and reported under code 2000 of the *North Dakota School District Financial Accounting and Reporting Manual*, as developed by the SPI in accordance with Section 15.1-02-08;

75 percent of all mineral revenue received by the school district through direct allocation from the State Treasurer and not reported under code 2000 of the *North Dakota School District Financial Accounting and Reporting Manual*, as developed by the SPI in accordance with Section 15.1-02-08;

75 percent of all tuition received by the school district and reported under code 1300 of the *North Dakota School District Financial Accounting and Reporting Manual*, as developed by the SPI in accordance with Section 15.1-02-08, with the exception of revenue received specifically for the operation of an educational program provided at a residential treatment facility and tuition received for the provision of an adult farm management program;

75 percent of all revenue received by the school district from payments in lieu of taxes on the distribution and transmission of electric power;

75 percent of all revenue received by the school district from payments in lieu of taxes on electricity generated from sources other than coal;

All revenue received by the school district from mobile home taxes;

75 percent of all revenue received by the school district from the leasing of land acquired by the United States for which compensation is allocated to the state under 33 U.S.C. 701(c)(3);

All telecommunications tax revenue received by the school district; and

All revenue received by the school district from payments in lieu of taxes and state reimbursement of the homestead credit and disabled veterans' credit.

From this baseline total, the legislation called for a subtraction of 60 mills multiplied by the district's taxable valuation, not to exceed the amount in dollars subtracted the prior year plus 12 percent, and a subtraction of the specified portion of the in lieu of taxes revenues listed in the preceding paragraph.

School district boards had been authorized to levy an amount sufficient to cover a multitude of expenses; however, the enactment of House Bill No. 1013 provided for the consolidation of these levies. The bill authorized the board of a school district to levy:

- A tax not exceeding the amount in dollars the school district levied for the prior year, plus 12 percent, up to a levy of 70 mills on the taxable valuation of the district, for any purpose related to the provision of educational services;
- No more than 12 mills on the taxable valuation of the district, for miscellaneous purposes and expenses;
- No more than 3 mills on the taxable valuation of the district for deposit into a special reserve fund; and
- No more than the number of mills necessary, on the taxable valuation of the district, for the payment of tuition.

### **2013-14 Interim**

During the 2013-14 interim, the Education Funding Committee was assigned a study, pursuant to Section 58 of House Bill No. 1013 (2013), of state-level and local-level responsibility for the equitable and adequate funding of elementary and secondary education in the state. The dollar amounts by which a district's weighted student units were multiplied, to arrive at a funding level for the 2013-15 biennium, were determined by applying an inflationary increase to the "adequate" funding level the Picus study recommended as part of its final report to the North Dakota Commission on Education Improvement in 2008. Given the passage of 5 years and changes in the state's economic and demographic circumstances, the Legislative Assembly determined it would be appropriate to review and clarify state-level and local-level responsibility for the equitable and adequate funding of elementary and secondary education. To meet its study directive, the interim Education Funding Committee asked Picus to review its 2008 recommendations and conduct a recalibration using an evidence-based model and the most recent data available. Based on available information and assumptions, Picus recommended recalibrated weighting factors and increased payment rates from the 2013-15 biennium levels of \$8,810 and \$9,092 to \$9,347 and \$9,442. The interim committee did not recommend the Picus funding model. The committee recommended Senate Bill No. 2031 (2015) relating to the funding of elementary and secondary education. The bill set per student funding rates of \$9,482 for the 1<sup>st</sup> year of the biennium and \$9,766 for the 2<sup>nd</sup> year. The rate of \$9,482 was determined by subtracting \$236, which represented the 8 days of professional development Picus had recommended, but which the committee did not require, from the Picus recommendation of \$9,442. The remainder was then increased by 3 percent to arrive at \$9,482. A 2<sup>nd</sup> year increase of 3 percent brought the 2<sup>nd</sup> year payment rate to \$9,766.

### **2015 Legislative Session**

In 2015 the Legislative Assembly approved Senate Bill No. 2031 which provided increases in the integrated payment rate of 3 percent per year during the 2015-17 biennium, based on the integrated formula payment rate during the 2<sup>nd</sup> year of the 2013-15 biennium. Integrated payment rates were set at \$9,365 during the 1<sup>st</sup> year and \$9,646 for the 2<sup>nd</sup> year of the 2015-17 biennium. In addition, the bill removed the sunset on the K-12 integrated formula for state school aid, adopted by the 2013 Legislative Assembly. The 2015 Legislative Assembly also approved Senate Concurrent Resolution No. 4003, which proposed a constitutional amendment to allow the Legislative Assembly to appropriate or transfer the principal balance of the foundation aid stabilization fund in excess of 15 percent of the general fund appropriation for state school aid for the most recently completed biennium for education-related purposes. The resolution was approved by voters in November 2016. In 2016, due to revenue shortfalls during the 2015-17 biennium, the Governor ordered two allotments totaling 6.55 percent and transfers from the foundation aid stabilization fund to offset foundation aid reductions made by executive action totaled \$116,053,293.

## 2017 Legislative Session

In 2017 the Legislative Assembly considered House Bill No. 1324. The bill included changes to the percentages of local "in lieu of" revenues deducted from the total formula payment when determining state funding. However, formula changes approved in House Bill No. 1324 did not include changes to local revenue deductions, but included an adjustment to set the integrated payment rate at \$9,646 for each year of the 2017-19 biennium, the same as the 2<sup>nd</sup> year of the 2015-17 biennium. The Legislative Assembly, in House Bill No. 1318, provided for a Legislative Management study of how state aid for elementary and secondary education is determined and distributed under the state aid funding formula; the impact of state aid; potential changes to the funding formula to ensure equity, adequacy, and sustainability; the delivery and administration of elementary and secondary education in the state; and the short- and long-term policy and statutory changes that may result from or be necessitated by 21<sup>st</sup> century technological advances and global economics. In addition, the Legislative Assembly approved House Bill No. 1423 to provide for a Legislative Management study of the in lieu of property tax portion of the elementary and secondary education funding formula for the purpose of identifying and addressing any inequities in the application of the formula.

In House Bill No. 1013 (2017) the Legislative Assembly provided an appropriation of \$1,935,204,163, of which \$1,334,657,258 was from the general fund, \$295,000,000 from the foundation aid stabilization fund, and \$305,546,905 from the state tuition fund for state school aid integrated formula payments. Of the \$295,000,000 provided from the foundation aid stabilization fund, \$185,000,000 was to be considered one-time funding. This level of funding represents an increase of \$18,564,163, including a decrease in funding of \$246,795,449 from the general fund and increases in funding of \$178,946,707 from the foundation aid stabilization fund and \$86,412,905 from the state tuition fund, from the 2015-17 biennium adjusted appropriation for integrated formula payments of \$1,916,640,000. Increases in state school aid integrated formula payments included the cost-to-continue the 2015-17 biennium 2<sup>nd</sup> year integrated formula payment increase (\$54 million), cost of projected student growth (\$57.7 million), and cost associated with an increase in the English language learner weighting factors approved by the 2015 Legislative Assembly and effective July 1, 2017 (\$900,000). These increased costs were partially offset by increases in the local cost-share, including local property tax sources and local revenue.

The Legislative Assembly provided \$55.4 million from the general fund for transportation aid during the 2017-19 biennium. This level of funding is \$1.6 million less than 2015-17 biennium funding of \$57 million from the general fund. Section 13 of House Bill No. 1013 requires the Department of Public Instruction (DPI) to distribute transportation aid for the 2017-19 biennium based on the state transportation formula as it existed on June 30, 2001, except that the department is to provide reimbursement at the rate of:

- \$1.11 per mile for schoolbuses having a capacity of 10 or more passengers.
- \$0.52 per mile for vehicles having a capacity of nine or fewer passengers.
- \$0.50 per mile round trip for family transportation of a student with a disability whose individualized education program plan requires that the student attend a school outside the student's school district of residence.
- \$0.50 per mile one way for family transportation if the student lives more than 2 miles from the public school the student attends.
- \$0.30 per student for each one-way trip.

The Legislative Assembly provided \$19.3 million from the general fund for special education contracts during the 2017-19 biennium. This level of funding is \$2 million more than 2015-17 biennium funding of \$17.3 million from the general fund. In addition, the Legislative Assembly, in Section 26 of House Bill No. 1013, repealed Section 6-09-45, relating to a required transfer from Bank of North Dakota undivided profits to provide funding for special education contract costs in excess of funds appropriated. In Section 11 of House Bill No. 1013, the Legislative Assembly provided if special education contract obligations exceed funds provided for the 2017-19 biennium, the SPI shall request a deficiency appropriation from the 66<sup>th</sup> Legislative Assembly.

The Legislative Assembly, in Senate Bill No. 2272, provided one-time funding of \$6,000,000 from the foundation aid stabilization fund to the SPI for rapid enrollment grants during the 2017-19 biennium. This level of funding is \$6,504,530 less than the adjusted one-time 2015-17 legislative appropriation of \$12,504,530 from the general fund. Grants are distributed to districts experiencing an increase of at least 4 percent, or 150 students, and no less than 20 students. The district's grant is determined by reducing the actual percentage increase in the number of students by 2 percent and multiplying the number of students represented by the reduced percentage by \$4,000. The Superintendent may not award more than \$3,000,000 in grants during the 1<sup>st</sup> year of the 2017-19 biennium and if funding is not sufficient to provide all of the eligible grants, the SPI must prorate the payment based on the percentage of the total amount to which the school district is entitled. A district is precluded from receiving a rapid enrollment grant if the district is not eligible to receive state aid because its general fund ending balance exceeds the unobligated general fund balance limits provided in Section 15.1-27-35.3.

## **Foundation Aid Stabilization Fund**

Prior to December 8, 2016, the principal of the foundation aid stabilization fund was available only upon order of the Governor to offset foundation aid reductions made by executive action due to a revenue shortfall. Section 54-44.1-12 provided the Director of the Budget may order an allotment to control the rate of expenditures of state agencies. This section provided an allotment must be made by a specific fund and all departments and agencies that receive money from a fund must be allotted on a uniform percentage basis, except that appropriations for foundation aid, transportation aid, and special education aid only may be allotted to the extent the allotment can be offset by transfers from the foundation aid stabilization fund.

In November 2016 voters approved a measure proposed by Senate Concurrent Resolution No. 4003 (2015), which amended the Constitution of North Dakota to allow the Legislative Assembly to appropriate or transfer the principal balance of the foundation aid stabilization fund in excess of 15 percent of the general fund appropriation for state school aid for education-related purposes.

In 2017 the Legislative Assembly approved Senate Bill No. 2272 and House Bill No. 1155, which amended Section 54-44.1-12 to provide any reductions to the general fund appropriation to the Department of Career and Technical Education for grants to school districts due to allotment also are offset by funding from the foundation aid stabilization fund. In addition, Senate Bill No. 2272 created a new section to Chapter 54-27 to provide for purposes of Section 24 of Article X of the Constitution of North Dakota, education-related purposes means purposes related to public elementary and secondary education and state aid to school districts means general fund appropriations for state school aid, transportation aid, and special education aid in DPI, as well as general fund appropriations for career and technical education grants to school districts and area centers in the Department of Career and Technical Education.

## **Elementary and Secondary Education State Aid Formula - Selected Provisions**

### **School District Hold Harmless Calculations - Minimum and Maximum Adjustments**

The committee reviewed the use of transition minimum and maximum adjustments in the state school aid formula. When the state school aid formula was implemented during the 2013-15 biennium, hold harmless calculations were included to avoid disrupting school budgets. Districts with formula adjustments for transition minimum and maximum adjustments are not considered to be on the state school aid formula.

Transition minimum adjustments apply to those districts that were above the per-pupil payment rate when the formula was implemented. Districts above the formula amount were subject to a transition minimum to hold the districts harmless under the new formula. These districts received a 2 percent increase each year of the 2013-15 and 2015-17 bienniums to provide a minimum of 108 percent of the district's baseline funding per weighted student unit multiplied by the district's prior year weighted student units, or 100 percent of the district's baseline funding dollars whichever is greater. There was no increase in the transition minimum adjustment during the 2017-19 biennium. Two hold harmless minimum calculations--baseline funding per weighted student unit and total baseline funding dollars--guarantee school districts will not receive less funding per weighted student unit or in total than the funding received during the 2012-13 school year.

Transition maximum adjustments apply to those districts that were below the per-pupil payment rate in the 2012-13 base year when the formula was implemented. Districts below the formula amount were subjected to a transition maximum to avoid excess funding. For these districts the maximum was increased 10 percent each year of the 2013-15 and 2015-17 bienniums to 140 percent of the district's baseline funding per weighted student unit multiplied by the district's prior year weighted student units. There was no increase in the transition maximum adjustment during the 2017-19 biennium.

Districts on the formula--those not subject to minimum or maximum adjustments--were given 3 percent increases each year of the 2013-15 and 2015-17 bienniums as the integrated formula payment was adjusted annually. There was no increase in the integrated formula payment rate during the 2017-19 biennium.

The total formula amount is adjusted for school district minimum and maximum calculations and the local contribution of 60 mills and local in lieu of revenue is deducted. State school aid is reduced for districts with ending fund balances that exceed 35 percent of expenditures plus \$50,000 (\$100,000, if the district is in a cooperative agreement for 2 years). The amount remaining after deductions is provided by the state. Hold harmless calculations are applied to total state and local funding, which is divided by total weighted student units to determine state and local funding per weighted student unit. Districts with state and local funding per weighted student unit equal to \$9,646 are on the formula and do not have adjustments for minimum or maximum payments. Districts with state and local funding per weighted student unit above \$9,646 receive transition minimum funding. Districts with state and local funding per weighted student unit below \$9,646 are subject to the transition maximum calculation.

The Department of Public Instruction reported, for the 2017-18 school year, 98 of the 173 school districts receiving state school aid were not on the formula. The department reported 11 school districts were subject to transition maximum deduction adjustments and 87 school districts were subject to transition minimum increases. Of the 87 school districts receiving transition minimum funding, 22 school districts are subject to the minimum hold harmless in baseline funding dollars.

### **School District Mill Levy Limitations**

The committee reviewed limits on property tax increases and the impact of limits on mills levied by school districts and property tax revenue deducted in the state school aid formula. During the 2015-16 school year, statewide, school districts levied \$274.2 million on \$4.1 billion of 2015 taxable valuation for their general funds. During the 2016-17 school year, statewide, school districts levied \$289.2 million on \$4.4 billion of 2016 taxable valuation for their general funds. Based on the 2015 tax levy, the local property tax contribution deducted in the state school aid formula for all districts during the 2016-17 school year was \$219.7 million, \$54.4 million less than the property tax levied for the 2015-16 school year and \$69.5 million less than the property tax levied for the 2016-17 school year.

While dollars levied based on 2016 property valuations are distributed to school districts in the 2016-17 school year, the integrated state school aid formula uses 2016 property valuations for purposes of calculating the local property tax deduction for the 2017-18 school year formula payment. Based on the 2016 tax levy, the local property tax contribution deducted in the state school aid formula for all districts during the 2017-18 school year was \$237.9 million.

"Property poor" districts are required to meet a minimum local effort. If a district's taxable valuation per student is less than 20 percent of the statewide average valuation per student, the formula will use an amount equal to 60 mills times 20 percent of the statewide average valuation per student multiplied by the number of weighted student units. This results in computed mills in the formula that are higher than 60 mills for seven districts. The statewide average taxable valuation per pupil for the 2016-17 school year was \$33,396. During the 2016-17 school year the formula deduction for 41 districts was below 60 mills, 74 districts were levying below 60 mills, and 33 districts were levying 70 mills or more. The Department of Public Instruction reported 89 school districts levy for miscellaneous purposes, generating \$22.5 million annually, that is not offset in the funding formula. The department noted that if a district does not levy up to the same increase deducted in the state school aid formula, the district will lose the difference between the amount deducted in the formula and the actual amount based on the levy. The state school aid formula statutorily deducts up to the 12 percent increase whether it is levied or not.

The committee reviewed the impact of the 12 percent limit on the increase in property tax revenue assessed and deducted in the state school aid formula. Districts unable to tax at the full 60 mills, due to increases in school district property valuation that result in property tax revenue increases in excess of 12 percent over the prior year, could be considered not on the formula. The 12 percent restriction effectively lowers the mill rate to below 60 mills for districts with rapidly increasing property valuations. When growth in the taxable valuation of a school district exceeds the 12 percent limit on growth in the formula, the state is required to increase its share of state school aid because the local share of property tax deducted in the formula is below the 60 mills provided by the formula. Removing the 12 percent limit on the growth of the general fund mill levy would not change the total state school aid provided to districts, but would decrease the state's cost because more local property tax revenue would be deducted in the formula. If districts, for which the deduction is less than the full 60 mills due to the 12 percent annual limitation, were deducted at the full 60 mills in the formula in the 2017-18 school year, an estimated \$29.7 million in state school aid funding would be shifted from state to local resources. Removing the 12 percent limit on property tax increases would remove the taxpayer protection provision in the formula. Increasing assessments in all districts to 60 mills may create hardships for taxpayers in certain districts.

The committee reviewed the impact of new property growth on the limits placed on property tax increases. The committee examined school district general fund maximum levy worksheets presented by the Tax Department. More than one section of law determines the calculation of maximum general fund levy authority. The Tax Department's maximum levy worksheet for the school district general fund summarizes these calculations to determine which calculation provides the most dollars for the fund. School district general fund maximum levy worksheets are created by the headquarter county for each school district. If districts cross county lines, only one worksheet is completed for the district with information provided by the other counties. Mill levy rates are calculated by the headquarter county and shared with the other counties to apply to their tax statements. The committee reviewed the calculations on two sample school district general fund maximum levy worksheets, one worksheet for a district experiencing significant growth in taxable value and one for a district with a relatively stable taxable valuation. Calculations included determining districts' 12 percent limit on property tax increases, base year taxable value adjustments, voter-approved excess mill levy adjustments, and maximum mill levy calculations. Base-year tax is the higher of taxes levied in the past 3 years. The base-year tax is adjusted for new construction or losses to taxable valuation. Base-year tax calculations protect districts by allowing the districts to maintain a level of funding by increasing the mill rate when property values decrease. The additional property tax potential of the new growth is added to base-year taxes. New property includes property added

to the district since the base year, including property added through annexation and local discretionary exempt property. Adjustments for new property increase base-year taxes and can protect taxpayers by allowing districts to collect the same amount of funding at a lower mill levy rate. However, districts may certify higher budgets in the year of the new growth in property value to collect additional property taxes rather than certifying similar budgets as the prior year and reducing the mill levy rate to collect the same amount of revenue. Maximum general fund levy authority is determined by comparing the largest of the prior year taxes plus 12 percent, adjusted base year taxes, and voter-approved excess levy worksheet calculations. School districts are most often limited by the maximum 12 percent increase provided in Section 57-15-14.2, because it results in more levy authority. The final levy is the lesser of the maximum general fund levy authority or the school district's certified budget. Districts above 60 mills will likely use the prior year taxes plus 12 percent calculation if there are no significant changes in taxable value due to property value added to or removed from the base year. The Tax Department reported a substantial amount of new property would have to be added to a district for the tax on the new property to exceed the 12 percent limit on growth.

### In Lieu of Property Tax Revenue and Other Local Revenue Deductions

The committee gathered information regarding total revenue from in lieu of property taxes and local revenue received by each school district in the state, compared to the contribution from in lieu of property tax and local revenue deducted in the state school aid formula. Information regarding in lieu of revenues is reported to DPI by counties each August. The Department of Public Instruction provided a statewide summary of in lieu of property taxes and local revenue received during the 2015-16 school year by revenue type deducted in the state school aid formula. Total revenue for these types of in lieu of property taxes and local revenue was \$68.0 million during the 2015-16 school year, resulting in a contribution from in lieu of property taxes and local revenue deducted in the state school aid formula of \$53.7 million during the 2016-17 school year. The cost to the state of deducting 75 percent of all in lieu of property taxes and local revenue in the state school aid formula would be approximately \$3 million per year, or \$6 million per biennium. If all in lieu of property taxes and local revenue were deducted at 100 percent in the state school aid formula the state would save approximately \$15 million per year, or \$30 million per biennium.

Department of Public Instruction guidance relating to school district financial accounting provides 100 percent of oil and gas production, coal production, and coal conversion tax revenue be deposited in the school's general fund. Revenue from federal flood control and oil and gas production, coal production, and coal conversion tax revenue, deposited into the school's general fund are deducted at 75 percent in the state school aid formula. A majority of the remaining revenues, deducted in the state school aid formula at 100 percent, are deposited into various school district funds based on mill levy distribution. Some districts reported using oil and gas production revenue for capital projects. This could result in the deduction of certain revenue at 100 percent in the formula even if only a portion of the revenue is deposited in the school district's general fund. The department provided the following summary of in lieu of property tax and local revenue received by school districts during the 2015-16 school year, including the method by which the revenue is distributed to various school funds and the percent deducted in the state school aid formula.

In Lieu of Property Tax and Local Revenue Type	Distribution Method	2015-16 Revenue Received	Percent Deducted in the Formula	2016-17 Potential Revenue Deducted in the Formula
Homestead credits	Mill levy	\$2,303,228	100%	\$2,303,228
Game and Fish land	Mill levy	315,392	100%	315,392
Land owned by Board of University and School Lands or State Treasurer	Mill levy	54,028	100%	54,028
National Guard land	Mill levy	13,717	100%	13,717
Land owned by nonprofit organizations for conservation purposes	Mill levy	21,427	100%	21,427
Land acquired by the State Water Commission	Mill levy	6,806	100%	6,806
Workforce Safety and Insurance building	Mill levy	75,474	100%	75,474
Mobile home taxes	Mill levy	1,466,841	100%	1,466,841
Other revenue in lieu of property taxes	Mill levy	953,999	100%	953,999
Disabled veterans' property tax credits reimbursed by the state	Mill levy	1,187,850	100%	1,187,850
Compensation for flood land leased by the United States under 33 U.S.C. 701(c)(3)	General fund	2,508,202	75%	1,881,152
Electric generation, distribution, and transmission tax	Mill levy	4,279,354	75%	3,209,516
Telecommunications tax	General fund	4,805,328	100%	4,805,328
Oil and gas production tax	General fund	32,714,414	75%	24,535,811
Coal production tax	General fund	2,230,651	75%	1,672,988
Coal conversion tax	General fund	1,012,222	75%	759,167
Tuition	General fund	14,084,450	75%	10,563,338
Total		\$68,033,383		\$53,826,062 <sup>1</sup>

<sup>1</sup>School districts with sufficient local revenue do not receive a state school aid payment due to the local revenue deduction. The in lieu of property taxes and local revenue deduction cannot result in negative state school aid, therefore the potential total revenue deducted in the formula of \$53.8 million is slightly higher than the in lieu of revenue actually deducted in the state school aid formula for the 2016-17 school year.

Of the \$68.0 million of in lieu of property tax and local revenue received by school districts during the 2015-16 school year, under the current policy, an estimated \$57.4 million (84 percent) was deposited into districts' general funds. The next year \$53.8 million was deducted in the formula, which allowed districts \$3.6 million of the in lieu of property tax and local revenue deposited in the general fund which was not deducted in the formula. Statewide, the average percent of property tax mill levies deposited into districts' general funds is 67.4 percent. The Department of Public Instruction reported if the policy were changed to allocate all in lieu of property tax and local revenue based on property tax mills, \$45.9 million of the \$68.0 million would be deposited into the general fund and, if a 100 percent deduction were maintained, the entire \$45.9 million would be deducted in the state school aid formula. If the state school aid deduction were 75 percent, \$34.4 million would be deducted in the state school aid formula, allowing districts \$11.5 million of the in lieu of property tax and local revenue deposited in the general fund which would not be deducted in the formula. If in lieu of property tax and local revenue were distributed based on the proportion of property tax mills levied and a 100 percent deduction were maintained, the difference between the \$53.8 million deducted in the state school aid formula during the 2016-17 school year and the \$45.9 million, that would have been deducted, or (\$8 million) would represent additional cost to the state for 1 year (\$16 million per biennium). If the formula deduction were 75 percent, the difference between the \$53.8 million deducted in the state school aid formula during the 2016-17 school year and the \$34.4 million, that would have been deducted, or (\$19 million) would represent additional cost to the state for 1 year (\$38 million per biennium). The department noted the estimated cost is based on the statewide average for mill levies assessed and the amounts would vary when each district is calculated separately and totaled statewide.

In lieu of property tax and local revenues that are not for a specific purpose are not distributed by mill levy, but are deposited in the general fund pursuant to DPI guidelines. In some counties, the in lieu of property tax and local revenue is identified for school districts, but in others the amount is not delineated and is included in the funding provided by property tax assessments. The department provided an analysis of the effects of distributing the various types of in lieu of property tax and local revenue in the same proportion as property tax mills on the state school aid of select school districts. The effects of a policy change regarding the deposit of in lieu of revenues and the percent deducted in the formula would vary by school district, depending on the types of in lieu of revenue each district receives and the percentage of property tax mill levies deposited into the general fund. The department reported counties deposit the various in lieu of property tax and local revenue differently and any change to the deduction of in lieu of property tax and local revenue deposited in other funds in the formula would require legislation, including legislation to require counties to report the deposit data.

The committee reviewed the effects on state school aid and property taxes of imputing in lieu of property tax and local revenue into taxable valuation in the state school aid formula. The Department of Public Instruction collaborated with the Tax Department to prepare an analysis for select school districts. Instead of deducting in lieu of property tax and local revenue from the state school aid formula, the department was asked to determine the effects of imputing the taxable valuation of the in lieu of property tax and local revenue and adding it to the actual taxable value of the district prior to calculating the deduction for 60 mills. The committee determined if in lieu of property tax and local revenue is imputed for purposes of the state school aid formula, the effects of the increased property valuation on local property tax assessment and the 12 percent limit on property tax increases also would have to be considered. The calculations provided by the department were an estimate of one way to implement the policy of imputing the in lieu of revenue into taxable valuation. The department reported there may be other methods, but establishing a base year was determined to be important. Because the level of funding per weighted student unit is set, any increase in property tax deducted in the formula will result in a decrease in the amount of state school aid paid by the state. The department reported that with the exception of hold harmless calculations and the 12 percent limit on annual increases, the current formula is easy to calculate, and imputing value from in lieu of property tax and local revenue would make the formula more complicated. In addition, because imputing value in the current formula would impact county levies, there was concern the calculation would require consistent application by county auditors, school superintendents, and school boards.

The committee also reviewed a report illustrating the impact of allocating, based on mill levies, a portion of fiscal year 2016-17 in lieu of property tax to school districts' sinking and interest funds and exempting the funding from the state school aid formula deduction. The Department of Public Instruction provided an analysis for school districts levying taxes for a sinking and interest fund. The analysis determined the sinking and interest levy as a percent of the school district's total levy and deducted that percentage of in lieu of property tax from total in lieu of property tax revenue before determining the amount of in lieu of property tax revenue deducted in the state school aid formula. Based on 2016-17 in lieu of property tax and district mill levies, if in lieu of property tax revenues were allocated to school district sinking and interest funds and excluded from the state school aid formula deduction, the cost of the state's share of state school aid would increase by approximately \$1.23 million per year or \$2.46 million per biennium. The cost of exempting a pro rata share of in lieu of property tax related to bonding would vary each year based on school district debt.

### **Rapid Enrollment Grants/On-Time Funding for State School Aid**

The committee reviewed the use of rapid enrollment grants and the benefits and challenges of on-time funding for state school aid. School districts expressed concern that a separate appropriation for rapid enrollment grants, based on

forecasts, is subject to large variances in actual versus forecasted enrollments. Rapid enrollment grants, limited to \$3 million each year of the 2017-19 biennium, were intended to provide \$4,000 per eligible student for the 2017-18 school year, but instead provided approximately \$2,350 per eligible student. When rapid enrollment grant calculations totaled \$5.1 million for the 2017-18 school year, DPI was required to prorate the grant funds. Over 1,270 students qualified for the grant, 520 more than the 750 students estimated to calculate the appropriation.

The committee reviewed the benefits, challenges, and cost of transitioning the state school aid formula to on-time funding. On-time funding provides state school aid based on fall enrollment for each school year. The current state school aid formula provides funding based on the previous spring enrollment. State school aid based on fall enrollment would provide additional funding to districts experiencing increasing enrollment.

The committee considered a proposal to adjust the current funding formula for the greater of fall enrollment or the prior year's average daily membership. Full funding for on-time enrollment in the proposal provided support for growing districts, while maintaining the current model of paying for the prior year's student enrollment in school districts with declining enrollments. In addition to spring average daily membership, the current state school aid formula uses prior year property tax data to calculate state school aid. Assuming a hold harmless provision at 2017-18 school year levels, transitioning to "on-time" funding, using the higher of 2016-17 school year spring average daily membership or fall enrollment each year of the current biennium, would have resulted in an additional one-time state school aid funding cost of approximately \$69 million in the 2017-19 biennium. The estimate is based on using property tax contributions from the prior year. If the formula were to use current year property tax contributions in each of the school years, the transition cost would be less. The Department of Public Instruction noted if the formula were transitioned to both "on-time" enrollment and "on-time" property tax contributions, the true state school aid formula payment amounts would not be known until property tax information becomes available in December or January. The department's "on-time" funding estimate provided schools with declining enrollment would be held harmless at the 2016-17 average daily membership levels. If all schools were moved to "on-time" funding for fall enrollment, the one-time cost would be less.

The committee considered options to fund the transition to on-time funding. The adjustment could be accomplished through a weighting factor applied to the qualifying number of students. The weighting factor could be set to provide \$4,000 per eligible student and increased over time until the incremental cost of moving to full funding is negligible. A .40 weighting factor applied to students eligible under the rapid enrollment grant program would have increased state school aid by \$5.1 million during the 2017-18 school year, or \$2.1 million more than the \$3 million provided for rapid enrollment grants. Funding provided for the rapid enrollment grant program (\$6 million for the 2017-19 biennium) would be sufficient to implement a factor of approximately .25 per eligible student. Any variable, including the weighting factor, percentage deduction, number of students deducted, or any combination of variables, could be modified to achieve on-time funding over a number of years. Adjustments could be made to the factor and thresholds for payment over time until eventually all districts would be receiving on-time funding and the factor could be removed. The committee also considered continuing the rapid enrollment grant program. Rapid enrollment grant funding per student could be adjusted while continuing to require minimum student and percentage increases.

The committee explored possible funding sources for the one-time cost of transitioning the state school aid formula to on-time funding, including unspent 2017-19 biennium general fund appropriations, rapid enrollment grant funding, or a weighting factor. In addition, the committee considered ways to mitigate the impact of a transition to on-time funding of state school aid on school districts with declining enrollment, including the use of the greater of spring or fall enrollment or a 3-year rolling average enrollment. Formula provisions could be adopted to require school districts to use the spring or fall enrollment count for a number of years, instead of having the ability to change each year.

### **Cross-Border Tuition**

The committee reviewed policies related to the cross-border education of nonresident students. Cross-border education with South Dakota is addressed in an agreement; however, there are no agreements with Montana or Minnesota. North Dakota pays to educate all the students along its border with South Dakota, including South Dakota students. South Dakota pays to educate all the students along their northern border, including North Dakota students. At the end of the school year there is an accounting of the cost of cross-border students. Traditionally DPI has paid South Dakota because North Dakota has sent more students to South Dakota schools than it has received from South Dakota. The payment varies depending on the number of North Dakota students educated in South Dakota compared to the number of South Dakota students educated in North Dakota. The payment to South Dakota is allocated to each North Dakota school district sending more students to South Dakota than it received. Districts do not receive foundation aid for students educated in South Dakota, but are required to pay for the net allocation. For a school district that received more students from South Dakota than were sent to South Dakota, there is no payment but the district receives the state school aid associated with those students.

The committee reviewed Section 15.1-29-01 related to Minnesota and Montana students. Pursuant to this section, a student attending an out-of-state school is deemed to be enrolled in the student's school district of residence for purposes

of determining average daily membership. School districts receive funding through the state school aid formula for North Dakota students attending Minnesota or Montana schools and it is the responsibility of the North Dakota school district to negotiate the tuition it will pay the out-of-state district. A North Dakota school district does not receive credit in its average daily membership for Minnesota and Montana students attending a North Dakota school, but negotiates tuition from the out-of-state school district sending the student. The tuition paid by the out-of-state school district for the nonresident child is subject to the 75 percent tuition deduction in the state school aid formula, leaving the district 25 percent of the tuition revenue to educate the student. Generally, North Dakota school districts accept only a few students from a neighboring state because of the 75 percent tuition deduction which causes financial shortfalls to educate more out-of-state students. When a neighboring out-of-state school closes and the number of students is significant, the 75 percent deduction can make absorbing the additional students too expensive for the North Dakota school district.

To address these concerns, the Department of Public Instruction suggested the state school aid formula could be changed to either:

- Exclude tuition related to out-of-state students from the local revenue deduction in the state school aid formula; or
- Include nonresident students in the North Dakota school district's average daily membership, while continuing to deduct 75 percent of the tuition related to the out-of-state students from the school district's state school aid payment.

The department has not collected data regarding the source of tuition payments, and the cost of any change to the formula for cross-border tuition is not known.

### **Integrated Formula Per Pupil Payment Rates**

The committee reviewed the integrated formula per pupil payment rate. For the 2017-19 biennium, the integrated payment rate remained at \$9,646 for each year of the biennium, the same as the 2<sup>nd</sup> year of the 2015-17 biennium. Stakeholders indicated increasing the per-pupil payment benefit is the most important funding challenge. Unlike other changes to the state school aid formula that may impact schools differently, all school districts benefit from a per-pupil payment increase.

### **Adult Learning Center Funding**

The committee reviewed funding for adult learning centers. There are 11 adult learning centers in the state, including 8 regional centers and 3 satellite programs. Services also are provided in 6 correctional facilities across the state. The Department of Public Instruction reported some adult learning centers are located in career and technical education buildings and on college campuses. Approximately 40 percent of adult learners are English language learners. Based on the state's definition of 1 hour of service, 3,200 students have been served during fiscal year 2018. The state's GED program passing rate is 88 percent, the second highest in the country. Grant funding for adult education totals \$5.13 million for the 2017-19 biennium, including \$3.1 million from the general fund, \$1.86 million of federal funds, and \$170,000 of special funds from the displaced homemaker fund. Funding from the general fund for adult education grants was reduced from \$4.11 million during the 2015-17 biennium. Federal funding also has decreased resulting in some adult learning centers closing. The department reported 88 percent of all federal and state funding provided to adult learning centers is used for salaries and benefits.

The Department of Public Instruction reported the Every Student Succeeds Act state plan includes the GED as a factor in graduation rates and a student dropping out of a traditional school may be encouraged to complete a GED at an adult learning center. The department anticipates an increase in the number of adult education students ages 16 through 21 and expressed concern regarding the capacity of adult learning centers to serve the additional students. State funding for a student dropping out of a traditional high school is prorated for the time spent in high school and does not follow the student to an adult learning center. The department reported a committee has been formed to review the possibility of providing supplemental funding to adult learning centers through the state school aid formula. The department suggested the state school aid formula could be changed to provide funding for adult education students between the ages of 16 and 21 who earn a GED and who are included in a school district's graduation rate. The proposed formula change would allow funding to follow students who drop out of the traditional K-12 education system to complete their education at an adult education center. The department suggested the funding provided through the state school aid formula would be in addition to the general fund appropriation for adult learning center grants. The department is considering a funding model similar to those used for special education and regional education associations. The department suggested funding could be based on a weighting factor and provided to school districts for distribution to adult learning centers. The department estimates the additional funding through the state school aid formula would total \$850,000 per year. The funding provided through the state school aid formula combined with the current appropriation would total \$2.4 million per year or \$4.8 million per biennium for adult learning centers. Total funding would depend on the weighting factor, number of eligible students, and the number of hours eligible students attend class. The department reported the additional funding could be used to add staff and reopen centers that have closed.

## **Status of State School Aid - 2017-19 Biennium**

The committee received reports from the Department of Public Instruction regarding student enrollment and the status of funding for state school aid, transportation grants, and special education contracts for the 2017-19 biennium.

To project future enrollment, DPI analyzes resident births and determines cohort survival rates by examining annual changes in enrollment by grade for the previous 2 years. In the years from 2007 to 2011, the annual increase in resident births ranged from 43 births to 202 births. In 2012, resident births increased by 838 from 2011 and since then resident births have increased at a lesser rate. Fall enrollment for the 2017-2018 school year totaled 108,945 students. Fall 2019 enrollment was projected to grow by 2,945 students; however, updated estimates are that the increase will be between 1,900 and 2,200 students.

The Department of Public Instruction estimates state school aid integrated formula payments will total \$2,513,809,497 during the 2017-19 biennium, of which \$488,444,521 will be provided through local property tax contributions, \$116,018,096 will be provided through local "in lieu of" taxes and revenue contributions, and \$1,909,346,880 will be provided by the state. In addition to the state's share of state school aid integrated formula payments, the appropriation for 2017-19 biennium integrated formula payments includes funding for costs related to child placement, regional education associations, and the gifted and talented program. The department estimates these expenditures will total \$9,522,119, for a total of \$1,918,868,999 charged to the integrated payment line item for the 2017-19 biennium, \$16,835,164 less than appropriated. The department reported the state's share of funding for state school aid shifted from 54 percent in 2009 to 77 percent during the 2016-17 school year. Because there was no increase in the per pupil integrated payment rate during the 2017-19 biennium and property tax revenue is likely to increase, the state's share of state school aid funding is estimated to decrease to 75 percent.

The Department of Public Instruction estimates transportation grant expenditures will total \$54.4 million during the 2017-19 biennium, \$1 million less than appropriated.

The Department of Public Instruction estimates special education contract expenditures will total \$22.3 million during the 2017-19 biennium, \$3 million more than appropriated. Special education contract expenditures are more than estimated due to increases in the number of claims and in the cost of cases. In addition, because special education contract claims exceeded the 2015-17 biennium appropriation, the department used \$2 million of 2017-19 special education contract authority to pay 2015-17 claims. In the past, the department has had the authority to receive funds from the Bank of North Dakota for any shortage in funding for state school aid. Due to the timing of state school aid payments, the department never has used Bank funding. As a result, the Legislative Assembly repealed this provision and directed the department to request a deficiency appropriation if necessary. As provided by the Legislative Assembly in 2017, the department anticipates requesting a deficiency appropriation of approximately \$3 million from the general fund for 2017-19 biennium special education contracts.

The Department of Public Instruction anticipates excess funding in the integrated formula payments line item and the transportation grants line item totaling approximately \$17.8 million from the general fund will not be spent. However, if the department is allowed to use excess foundation aid payment funding authority to pay special education contracts in excess of the department's 2017-19 biennium appropriation, unspent appropriation authority will total \$14.8 million, and there would be no need for a deficiency appropriation.

## **Projected State School Aid - 2019-21 Biennium**

### **Cost to Continue**

The committee reviewed a preliminary estimate of funding required to continue current state school aid integrated formula payments during the 2019-21 biennium. The report, prepared by DPI, was based on:

- Average daily membership projected using a 3-year cohort survival routine with 2017-18 fall enrollment as the base year;
- Taxable valuations for fiscal years 2019-20 and 2020-21 projected based on the change from the 2016 to 2017 tax year limited to the state average;
- No change to formula minimum and maximum adjustments; and
- Other statistical data and weighting factors based on data supporting the 2017-18 payment year.

The Department of Public Instruction estimates the cost-to-continue integrated formula payments for an estimated 3,000 additional students each year of the 2019-21 biennium, including child placement, regional education associations and the gifted and talented program, will total \$125.9 million during the 2019-21 biennium. Of this increase, an estimated \$48.7 million will be provided locally through estimated increases in property tax contributions and "in lieu of" property tax revenue. The remaining \$77.2 million of estimated cost-to-continue integrated formula payments will be provided by the state. In addition to funding required to continue integrated formula payments at the same level during the 2019-21

biennium, additional funding will be required to replace one-time funding provided for state school aid payments during the 2017-19 biennium, including \$185 million from the foundation aid stabilization fund and \$4.3 million from the state tuition fund. Funding available from the common schools trust fund is estimated to increase by \$78.1 million and will offset a portion of the funding required to continue state aid and to replace one-time funding. The estimated net increase in funding required to continue integrated formula payments at the current level and to replace one-time funding from special funds will total approximately \$188.4 million for the 2019-21 biennium.

The committee reviewed enrollment projections for the 2019-21 biennium. The Department of Public Instruction anticipates 2018-19 enrollment will be less than previously estimated. When fall 2018 enrollment is finalized, the department will recalculate the cost-to-continue state school aid. If actual 2018-19 fall enrollment is 900 students fewer than anticipated in the department's projections, the cost-to-continue state school aid in the 2019-21 biennium will be approximately \$27 million less.

The committee also received a report from DPI regarding 2019-21 biennium funding concerns. Based on current formulas and policies related to transportation grants, rapid enrollment grants, and special education contracts, an additional \$5.7 million may be needed to fully fund special education contracts and an additional \$5 million may be needed if rapid enrollment grants are continued using criteria similar to the 2017-19 biennium. If transportation rates are not adjusted, the funding level would not change significantly for the 2019-21 biennium.

### **Estimated Cost of Integrated Formula Per Pupil Payment Rate Increases**

The committee gathered information regarding the estimated cost of increasing the integrated formula per pupil payment rate during the 2019-21 biennium. The Department of Public Instruction reported with no other formula changes, a 1 percent increase in the integrated formula payment each year of the 2019-21 biennium resulting in integrated formula payment rates of \$9,742 and \$9,839 during the 1<sup>st</sup> and 2<sup>nd</sup> year of the biennium respectively, would cost approximately \$31 million. With no other formula changes, a 2 percent increase in the integrated formula payment each year of the 2019-21 biennium, resulting in integrated formula payment rates of \$9,839 and \$10,036 during the 1<sup>st</sup> and 2<sup>nd</sup> year of the biennium respectively, would cost approximately \$62.9 million. These increases would be in addition to the estimated \$77.2 million cost-to-continue state school aid related to increased enrollment.

### **State School Aid - 2021-23 Biennium Projected**

The committee reviewed information regarding the cost-to-continue state school aid during the 2021-23 biennium. The Department of Public Instruction reported based on current weighting factors and minimum and maximum adjustments, no increase in the integrated formula payment of \$9,646, and an approximate 3.5 percent increase in property values, the cost-to-continue state school aid due to population growth during the 2021-23 biennium is estimated to total \$125.5 million. The increase is based on enrollment growth of approximately 4,000 students each year of the 2021-23 biennium. The department does not expect the significant increases in enrollment to continue beyond 2023 because the student influx related to the oil boom will begin graduating. If the integrated formula payment is increased during the 2019-21 biennium, the cost to continue the increases in the 2021-23 biennium is approximately \$13 million for each percentage increase provided in the 2019-21 biennium. If property tax growth does not meet the 3.5 percent estimate included in the department's projections, the state's cost would be more.

### **Committee Recommendation**

The committee makes no recommendation related to its study of the state school aid funding formula.

### **OTHER COMMITTEE RESPONSIBILITIES**

The committee received, pursuant to Section 15.1-02-09, a report from the SPI regarding the **financial condition of schools**. The annual report is published in February for the preceding school year and includes information regarding mill levy rates, taxable valuation, revenues, expenditures, student enrollment, average daily membership, average cost per pupil, teachers, average salaries, and number of graduates.

The committee received, pursuant to Section 15.1-02-13, a report from the SPI regarding **school district employee compensation**. The report is based on data reported by school districts for school years ending in June of 2015, 2016, and 2017. The report includes teachers, administrators, and other district employees, but does not include part-time teachers. Administrators include principals, superintendents, directors, assistant principals, assistant or deputy superintendents, administrative assistants, and assistant directors. The average base salary for administrators increased from \$90,598 to \$96,372, or 6.37 percent, from 2015 to 2017. Teachers include coordinators, library media specialists, pupil personnel, school counselors, school psychologists, speech and language pathologists, supervisors, and instructional programmers. The average base salary for teachers increased 6.4 percent, from \$50,057 to \$53,261, over the same period. The number of administrators statewide increased from 603 in 2015 to 625 in 2017, while the number of teachers increased from 8,691 to 8,936 during the same period.

The committee, pursuant to Senate Bill No. 2037 (2017), received a report from the SPI regarding the use of **teacher loan forgiveness funds**. The Superintendent reported \$2,103,393 from the general fund was appropriated to the North Dakota University System for the teacher shortage loan forgiveness program during the 2017-19 biennium. The University System and the SPI collaborated to implement the program. Policies and procedures for the program were established and University System procedure 508.1.2 relating to the teacher shortage loan forgiveness program is posted on the University System website. Loan forgiveness benefits are allowed for recruiting for a vacant position or to retain a teacher in a position that is filled and school districts were to apply for the position regardless of whether it was filled. The maximum benefit is 4 years and the school district determines which teacher will receive the loan forgiveness benefits.

To determine critical need and shortage areas, the SPI reviewed alternative and provisional licensing through the Education Standards and Practices Board and district surveys. The Superintendent identified critical need areas for the 2017-18 school year (in order of priority) as science, business and office technology, agriculture education, technology and engineering education, and computer science. In addition, the department identified 13 shortage areas. Applications were made available in January 2018 and due April 15<sup>th</sup>. Districts were allowed to apply after the deadline, but applications submitted by April 15<sup>th</sup> were given priority. Under the new program, school districts are responsible for the applications and could apply for up to two teaching positions. Districts were allowed to determine which positions were hardest to fill and to submit those positions for loan repayment under the program. Elementary and science teachers were the most applied for positions. When determining which positions to approve for funding, the SPI and the University System considered whether the position qualified as a critical need or shortage area, whether the position was rural or urban, and the amount of funding available. Urban districts could apply only for teaching positions in the critical need areas.

The Superintendent of Public Instruction reported loan forgiveness amounts could range from \$3,000 to \$6,500 per year for up to 4 years depending on whether the district was rural or nonrural and if the teaching position was in a critical need area or a shortage area. Of a total of 227 districts (public and nonpublic), 170 districts applied. The Superintendent reported 149 rural districts applied for 295 positions, of which 270 positions were approved at a cost of \$1,389,000. The Superintendent reported 21 urban districts applied for 41 positions, none of which were approved. The Superintendent reported 183 positions were approved for the \$4,500-per-year award and 87 positions were approved for the \$6,500-per-year award. Because the awards are for a 4-year period, unless additional appropriations are provided, no new positions will be approved. The Superintendent reported to fully fund a program that provides each district with two teaching position awards at the highest level, an estimated \$5.2 million would be needed each biennium.

In addition to the report from the SPI, the committee received a report regarding the results of a school district survey related to the teacher shortage loan forgiveness program. Stakeholders reported 80 districts responded to the survey. Over 50 percent of the districts responding indicated the scholarships were used to retain teachers. In schools responding to the survey, the new program resulted in a loss of benefits for 186 teachers receiving awards under the previous loan program. Stakeholders expressed concern regarding the timing of the application. The April application deadline is prior to districts knowing which teaching positions will need to be filled.

## **OTHER REPORTS AND INFORMATION RECEIVED BY THE COMMITTEE**

### **Medicaid-Covered Services Provided by School Districts**

The committee received a report from the Department of Human Services regarding policy changes allowing expanded reimbursement for Medicaid-covered services provided by school districts. Pursuant to the federal Individuals with Disabilities Education Act, the Department of Human Services is responsible for the payment of services for Medicaid-eligible children who receive Medicaid-covered services described in the child's Individualized Education Program. The Department of Public Instruction receives a monthly Medicaid payment report from the Department of Human Services for Medicaid-covered services included in a student's Individualized Education Program and provided by the school district. The Department of Public Instruction withholds the 50 percent of the state share Medicaid payment from the school district's state aid payment. If the district's state aid payment is not sufficient to cover the Medicaid withholding, the school district must pay the difference to DPI. The amount withheld is certified and paid to the Department of Human Services. Approximately \$1.7 million is withheld and remitted to the Department of Human Services each biennium. Most of the state match is made by the offset to state school aid. However, some districts are providing services in schools, but claims for reimbursement are not made through the school. The match for services billed in this manner is not included in the match certified by DPI, resulting in the use of state general fund dollars for the state match. Covered services include physical, occupational, and speech-language pathology therapies; audiology; behavioral health; skilled nursing services provided to children with complex medical needs; transportation to and from Individualized Education Program services from school; and applied behavior analysis.

The committee also received a report regarding regional education association collaboration with special education units to develop a Medicaid billing consortium. Verifying Medicaid eligibility for students is difficult and a number of special education units either were not maximizing Medicaid reimbursements or not submitting for Medicaid

reimbursement. A regional education association recruited partners, invested in software, and provided training and support to establish and expand the consortium. The consortium includes 12 special education units, including 67 school districts. The regional education association assists and supports special education units accessing Medicaid reimbursement for services the units are required to provide.

### **Other Reports Received by the Committee**

In addition to the committee's other responsibilities, the committee received other reports, including reports from the:

- Superintendent of Public Instruction regarding a summary of the various entities responsible for the delivery and administration of elementary and secondary education in the state;
- Governor's office regarding the Governor's elementary and secondary education initiative, including the Governor's Summit on Innovative Education;
- Indian Affairs Commission and the SPI regarding the elementary and secondary education funding system for Native American children and achievement challenges;
- Education Commission of the States regarding a comparison of the state's elementary and secondary education funding and outcomes to the national average and bordering states;
- Department of Public Instruction regarding the status of the innovative education program established pursuant to Senate Bill No. 2186 (2017);
- Department of Public Instruction regarding the student contract system used to reimburse school districts for high-cost students and for students in placement for reasons other than education;
- Department of Public Instruction regarding the increasing cost and number of special education contracts;
- Tax Department regarding property tax budget deadlines for school district preliminary budgets and budget adjustments;
- Regional education associations regarding course offerings and the structure and funding of regional education associations;
- Great Western Network Interactive Television regarding the delivery of K-12 video distance learning in the state and an interactive television distance learning consortium;
- North Dakota Center for Distance Education regarding the center's role in the delivery of elementary and secondary education in the state and SmartLab tours;
- Department of Career and Technical Education regarding the role of career and technical education in the delivery of elementary and secondary education in the state;
- North Dakota Small Organized Schools regarding transportation challenges and funding;
- North Dakota State College of Science regarding a strategic plan for the Career Workforce Academy; and
- North Dakota Council of Educational Leaders regarding a comparison of resources across school districts and other items including; the impact of funding formula changes, funding for school districts incurring tuition costs for students placed in summer programs outside the district, property tax limits, school safety, behavioral and mental health services in schools, funding for an administrator mentor program, and the cost to school districts of bus driver physicals.