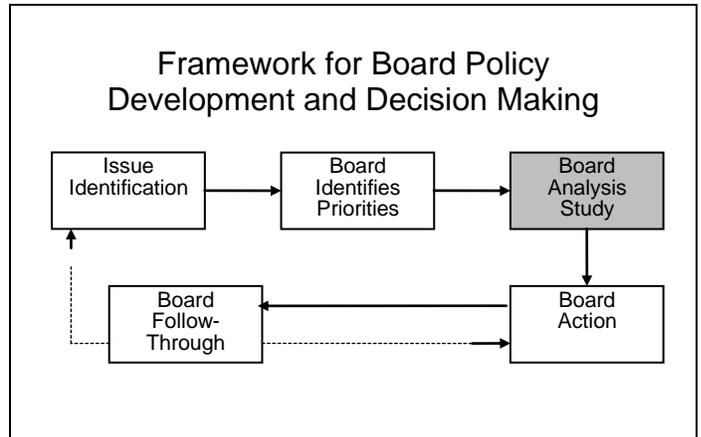


Iowa State Board of Education

Executive Summary

February 11, 2009



Agenda Item: School Finance in Iowa

Iowa Goal: All K-12 students will achieve at a high level.

Equity Impact Statement: Adequate and well-managed resources enable equal access to quality programs for all students.

Presenter: Jim Addy, Administrator
Division of School Support and Information

Attachments: 5

Recommendation: It is recommended that the State Board hear and discuss this information.

Background: Work sessions have been planned throughout the year to give the State Board background content knowledge on the areas they oversee. This presentation is a very basic Iowa school finance primer. It will begin by laying the foundation with some information about the school foundation aid formula and other district revenues. From there, the presentation will build upon itself spending the majority of time on specific topical issues relevant to State Board action and current discussions at the Legislature: negative unspent balance, the relationship between cash and authority, and allowable growth.



The Effectiveness of School District Sharing

➔ **What is this issue?**

Sharing is one strategy Iowa school districts have used to save costs. In 2001, the Iowa Department of Education conducted a “School District Reorganization and Sharing Incentive Study.” There were 438 school districts in 1983-1984. By 2000-01, 121 of the 438 districts had reorganized and two districts had dissolved. Of the 121 districts that reorganized, 103 or 85 percent were involved in sharing entire grade levels prior to reorganizing and 106 or 88 percent were involved in administrative sharing prior to reorganizing.

Of the 149 districts that were whole grade sharing, 103 or 69 percent of districts had reorganized as of July 1, 2000. Of the 302 districts that were involved with administrative sharing, 106 or 35 percent of districts had reorganized and of these 106 districts, 94 were also whole grade sharing prior to reorganizing.

From these historical data, it appears that whole grade sharing, not administrative sharing, is the driver in leading to reorganization. It must be noted that the greatest success for reorganization comes when *both* types of sharing occurred simultaneously. However, when these two types of sharing existed independently, it is clear that only a very small percentage of administrative sharing — only 7 percent — ever led to reorganization.

Activity During Fiscal Years 1983-1984 to 2000-2001 <i>(438 Districts in FY 1983-1984)</i>		
	Number of Districts	
Activity	Reorganized	Did NOT Reorganize
Participated in Whole Grade Sharing	9	12
Participated in Administrative Sharing	12	162
Participated in Both	94	34
Participated in Neither	6	107
<i>*Two districts dissolved in this period, one of which participated in administrative sharing.</i>		

(Continued)



LEGISLATIVE BRIEFING

Iowa Department of Education

➔ Where does this issue currently stand?

For districts operating with grades kindergarten through 12, there have been six reorganizations, two dissolutions, and one involuntary merger. In five of the six reorganizations, both partners were involved in sharing prior to reorganization. In the sixth, one of the two partners was involved in sharing. (As a point of clarification, sharing can go in “multiple directions” with multiple partners, but reorganizations rarely involve more than two districts.) Two other reorganizations between two sets of whole grade sharing partners have been approved for July 1, 2009, and July 1, 2010.

The last year of administrative sharing was in FY 1997-1998. Operational sharing, which is equivalent to administrative sharing in its composition, was not in effect until FY 2007-08. Therefore, comparisons between the two type’s effectiveness in resulting in reorganization would not be meaningful. Whole grade sharing has been the only supplementary weighting in place since the study to incent districts into reorganization.

Operational sharing has been primarily leveraged by small to medium size districts, those districts with less than 1,509 and 1,523 actual enrollment in FY 08 and FY 09, respectively. The use of this type of sharing has grown significantly in these two years from 48 to 73 districts and from \$2.7 million to \$5 million. Correspondingly, this type of sharing jumped from 14 percent of total supplementary weighting dollars to 20 percent.

Observations:

- Whole grade sharing appears to be the type of sharing that needs to present to have the highest probability of reorganization – it’s the best incentive. Historical data support this observation.
- Conjecture is that operational sharing or administrative sharing between superintendents, the leaders at the top, most often lead to reorganization in these types of sharing arrangements. Other sharing may help, but it does not have the same impact.
- One possible addition to whole grade sharing to improve its effectiveness would be to commit those boards that enter into this agreement to a reorganization vote upon taking the third and final year of sharing money that is available prior to reorganization. Currently districts must only show progress toward reorganization to continue to receive the whole grade supplementary weighting that is available prior to reorganization.

➔ Where can I can I get more information?

Please contact the Iowa Department of Education at (515) 281-5293.



LEGISLATIVE BRIEFING

Iowa Department of Education

Cash and Authority in Local School Districts

→ What is this issue?

When looking at the financial condition of school districts in Iowa, it is valuable to look at the relationship between the amount of cash a district has and how much it is authorized to spend — cash versus authority.

The term “authority,” simply put, is the authorization to spend a certain amount of cash. Just because a district is given the authority to spend a certain amount doesn’t mean it has the cash. The authority that comes with the formula in part means the ability for a local district to levy local property taxes. Likewise, just because a district has cash and the authority to spend it does not necessarily mean that districts will spend the money.

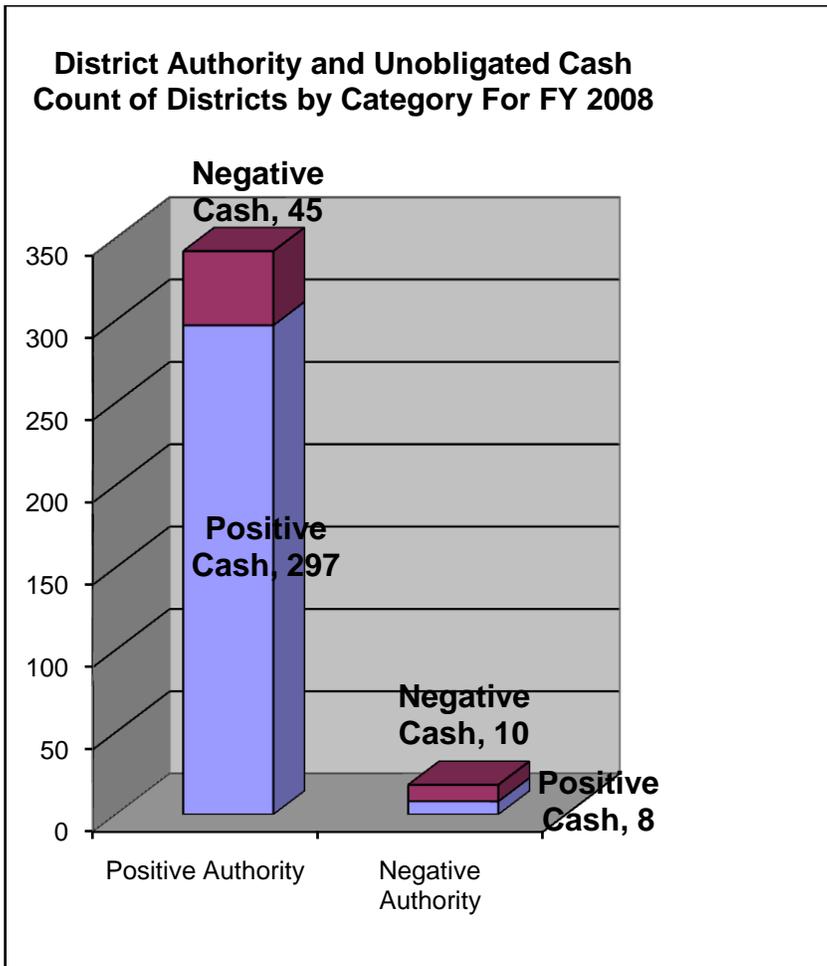
The authority left at the end of the year is referred to as the unspent balance, which may either be positive or negative. This unspent balance, either positive or negative, carries over from year to year, just like cash balances. Over time cash balances and the unspent balance can diverge.

How do districts’ cash and authority track over the course of a year? Do they have the authority they need to spend the cash they have? To shed light on these questions, the unspent balances left at the end of Fiscal Year (FY) 2008 are compared to the unobligated cash balances at the end of FY 2008 as reported on the Certified Annual Report (CAR). Unobligated cash balances in this instance are technically undesignated, unreserved fund balances per the Uniform Financial Accounting definition. Districts with negative cash may still have cash, but their cash is already designated or reserved for a purpose.

→ Where does this issue currently stand?

There were 297 local school districts that had both positive cash and some positive authority at the end of FY 2008. This means there were 297 districts that still had unobligated money and ability to spend some of that money. What was the relationship between the unobligated cash and the unused authority for these districts?

(Continued)





LEGISLATIVE BRIEFING

Iowa Department of Education

Districts with Left-over Positive Cash and Positive Authority Per FY2008 CAR Ending Balances (N=297)
Three-quarters of the districts had the authority to spend at least 36% of the unobligated cash they had on hand.
One-half of the districts had the authority to spend at least 57% of the unobligated cash they had on hand.
One-quarter of the districts had the authority to spend at least 83% of the unobligated cash they had on hand.
16.8% of the districts had the authority to spend all the unobligated cash they had on hand.

In these 297 districts remaining authority (unspent balances) ranged from \$15,569 to \$25 million and unobligated cash (undesignated, unreserved) ranged from slightly over break even — at \$845 — to \$21 million.

Of course, a local school district or business cannot spend all the cash it has on hand. They need a reserve or float so they can cash flow expenditures when money is not coming in. Just like businesses, districts have an uneven cash flow: they only receive state aid payments 10 out of the 12 months in a year. This is why local school districts have the ability to levy for a reserve. However, the amount of districts' reserves is not an agreed upon or set percentage — the reserve percentage is conceptualized as a percent of its annual expenditure. In fact, the School Budget Review Committee has been studying the issue and debating the merits of setting a percentage and what that percentage would be.

Therefore, to realistically consider the relationship between the remaining authority and the unobligated cash on hand, one must account for districts' reserves. Following is a table that subtracts different reserve percentages — 25, 20, 16.7, 15, and 10 percent — from the unobligated cash districts have on hand and then reports the cumulative amount left over (e.g., the overage). All of the districts included in the cumulative overages had the authority remaining to cover or expend the amount of the overage according to their FY 2008 CARs.

Unobligated Cash Available to Spend Once Reserves Filled					
	Overage @ 25% reserve of expenditures	Overage @ 20% reserve of expenditures	Overage @ 16.7% reserve of expenditures	Overage @ 15% reserve of expenditures	Overage @ 10% reserve of expenditures
Districts that have cash remaining after various reserve thresholds covered	30	57	80	95	158
Total sum of districts' overages	\$8,899,580.97	\$18,883,415.44	\$30,430,394.49	\$38,539,368.43	\$85,367,438.17

Note: The definition of cash is such that anything reserved or designated by districts is NOT included. Also note all these districts have the remaining authority (unspent balance) to spend the amounts beyond their reserves.

Analysis Notes:

These are the best available data at the time of the analysis. The CAR data are from 12/23/08. At that time, 34 districts were not certified. In addition, the data are "dirty": for instance, edits — computer script that checks for accounting errors — has not been fully run yet. Data will not be final for several more months. Further, while the edits are designed to catch inadvertent errors, some districts have more experienced professional staff and there are some others that have staff who may be inexperienced and book something so unusual that Iowa Department of Education could have never conceived of it.

→ Where can I can I get more information?

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LEGISLATIVE BRIEFING Iowa Department of Education

Allowable Growth Scenarios

Current Status of Education Budgets

The budgeting process for education in the state of Iowa is a multi-year process. In regard to the legislative process, those years that are being affected simultaneously are: 1) the current fiscal year — FY2009, 2) next fiscal year — FY2010, and 3) FY2011.

Current year — FY2009: Prior to the last Revenue Estimating Conference (REC) estimates, there were projections that the state would finish the budget year with \$5 million on hand. After the latest round of economic bad news the Governor instituted an across the board cut, since revenues were under projections and he is required to balance the budget by law. The Governor has since submitted his budget to the Legislature.

This fiscal year for education is also subject to other forces. If the budget worsens, the Legislature may make deappropriations from state funding. Additionally, districts may be absorbing some or all of the 1.5 percent across-the-board cuts with their reserves: some districts have put different sources of money — teacher compensation and Phase II — into salary schedules so they are contractually obligated to pay the full amount.

Next fiscal year — FY2010: The REC budget projections that the Governor based his budget upon show negative growth: there are less tax receipts than had been expected. Projections of the state budget shortfall range from \$500 to \$700 million.

FY2011: There is no extra money in the state budget. The Governor has proposed a 2 percent allowable growth. For the first time, four allowable growth rates will be set: state foundation aid and three categorical roll-ins — early intervention, professional development, and teacher salaries. For state foundation aid it has been proposed to authorize a higher allowable growth rate, but not fully funding it, thereby giving local districts the authority, but no state aid to back it¹.

Other Factors to Consider

Special education numbers came in lower than projected in previous state aid runs². This had a positive impact, but not a one to one reduction in state aid — the state's monetary commitment to education.

Considerable attention is being paid to how much cash districts have on hand and what are their reserves? Of course, a local school district or business cannot spend all the cash it has on hand. They need a reserve or float so they can cash flow expenditures when money is not coming in. Just like businesses, districts have an uneven cash flow: they only receive state aid payments 10 out of the 12 months in a year. This is why local school districts have the ability to levy for a reserve. However, the amount of districts' reserves is not an agreed upon or set percentage — the reserve percentage is conceptualized as an amount equal to a certain percent of a district's annual expenditure. In fact, the School Budget Review Committee has been studying the issue and debating the merits of setting a percentage and what that percentage would be.

¹ Another brief in your packet explores the relationship between districts' authority and cash relationships.

² Another brief in your packet discusses the lower special education numbers explicitly.



LEGISLATIVE BRIEFING
Iowa Department of Education

Following is a table that subtracts different reserve percentages — 25 percent, 20 percent, 16.7 percent, 15 percent, and 10 percent — from the unobligated cash districts have on hand and then reports the cumulative amount left over (e.g., the overage)³.

Unobligated Cash Available to Spend Once Reserves Filled					
	Overage @ 25% reserve of expenditures	Overage @ 20% reserve of expenditures	Overage @ 16.7% reserve of expenditures	Overage @ 15% reserve of expenditures	Overage @ 10% reserve of expenditures
Districts that have cash remaining after various reserve thresholds covered	30	57	80	95	158
Total sum of districts' overages	\$8,899,580.97	\$18,883,415.44	\$30,430,394.49	\$38,539,368.43	\$85,367,438.17
Note: The definition of cash is such that anything reserved or designated (technically undesignated, unreserved balances) by districts is NOT included.					

This Year's Deficit and Next Year's Rate

The allowable growth rate set last session will cost the state \$112 million. As has been mentioned, that allowable growth rate was actually for FY 2010. At this point in time, the state now conservatively has a gap between original projections and receipts of revenue in the neighborhood of \$600 million. Given that and the fact that the allowable growth rate has been reduced after across-the-board cuts historically, there is near certainty that the Legislature will revisit the rate.

Following is a table that sets out the FY2009 and FY2010 allowable growth rate projections and their impact. It also provides what the impact would be for FY2010 at a lower allowable growth rate than the enacted last session.

³ These are the best available data at the time of the analysis. The Certified Annual Report data are from 12/23/08. At that time, 34 districts were not certified. In addition, the data are "dirty:" for instance, edits – computer script that checks for accounting errors – have not been fully run yet. Data will not be final for several more months. Further, while the edits are designed to catch inadvertent errors, some districts have more experienced, professional staff and there are some others that have staff who may be inexperienced and book something so unusual that DE could have never conceived of that.



LEGISLATIVE BRIEFING
Iowa Department of Education

Options for the Upcoming Fiscal Year										
Fiscal Year	Allowable Growth Rate	Budget Enrollment	Combined District Cost	State Aid Without Preschool State Aid	Preschool State Aid	Total State Aid	Property Taxes	Add. Prop. Tax Levy Aid	Budget Guarantee	Number Receiving Budget Guarantee
FY2009 (In progress)	4%	480,608.8	3,385,922,280	2,207,372,179	17,057,280	2,224,429,459	1,178,704,480	17,999,912	12,123,808	155
Impact of Different Allowable Growth Rates for Next Fiscal Year										
FY 2010	0%	477,494.8	3,413,302,045	2,169,766,509	36,819,453	2,206,585,962	1,243,535,579	23,999,995	54,269,600	313
FY 2010	1%	477,494.8	3,426,615,313	2,197,388,642	36,819,453	2,234,208,095	1,229,226,718	24,000,040	35,163,573	271
FY 2010	2%	477,494.8	3,445,690,463	2,225,576,430	36,110,894	2,261,687,324	1,220,114,080	23,999,899	20,965,379	219
FY 2010	3%	477,494.8	3,469,784,875	2,253,211,339	36,819,453	2,290,030,792	1,216,573,579	24,000,110	12,189,390	164
FY 2010 (Enacted)	4%	477,494.8	3,498,203,929	2,281,398,899	36,819,453	2,318,218,352	1,216,805,073	23,999,849	7,062,247	124

Assuming that allowable growth for FY2010 will be reduced, the question becomes what will the rate be? Focusing on the Total State Aid column in the preceding chart brings an appreciation for the decision the Legislature may make. Resetting the FY 2010 rate to zero percent would actually be a reduction in total state aid to districts compared to last year due to the decline in budget enrollment. Looking at 1 percent and 2 percent allowable growth would mean an increase of approximately \$10 million or \$37 million, respectively. Ultimately, the answer to the allowable growth rate question subsumes how much does the Legislature have to spend or reallocate in this area?

Setting the FY 2011 Allowable Growth

The allowable growth rate is required to be set within 30 days of the submission of the Governor’s budget. If the Legislature uses the entire time allotted, then this decision will be made much later in the session this year compared to last year. The longer it takes to make this decision, the more information and analysis will be available about tax receipts and the state’s revenue picture.

The school foundation aid formula builds on itself from one year to the next: the costs the previous year feed into the allocation made the next year. A positive allowable growth rate makes the point readily evident to everyone. Hence, to do meaningful projections for FY2011, the allowable growth rate for FY2010 is needed. To provide a frame of reference for what could be two separate tables have been prepared to look at FY2011 allowable growth projections using two different FY2010 projections.



LEGISLATIVE BRIEFING
Iowa Department of Education

Maintain Commitment to Allowable Growth – 4% FY 09 & FY10								
Fiscal Year	Allowable Growth Rate	Budget Enrollment	Combined District Cost	State Aid Without Preschool State Aid	Preschool State Aid	Total State Aid	Property Taxes	Add. Prop. Tax Levy Aid
FY2009 (In progress)	4%	480,608.8	3,385,922,280	2,207,372,179	17,057,280	2,224,429,459	1,178,704,480	17,999,912
FY2010 (Enacted)	4%	477,494.8	3,498,203,929	2,281,398,899	36,819,453	2,318,218,352	1,216,805,073	23,999,849
Impact of different allowable growth rates								
FY2011	0%	477,132.8	3,539,954,344	2,256,589,839	58,206,498	2,314,796,337	1,283,364,547	24,000,138
FY2011	1%	477,132.8	3,556,870,376	2,285,886,086	58,206,498	2,344,092,584	1,270,984,331	23,999,871
FY2011	1.5%	477,132.8	3,567,555,868	2,300,260,255	58,206,498	2,358,466,753	1,267,295,653	23,999,939
FY2011	2%	477,132.8	3,579,039,928	2,314,657,069	58,206,498	2,372,863,567	1,264,382,903	23,999,963
FY2011	4%	477,132.8	3,640,421,908	2,372,798,363	58,206,498	2,431,004,861	1,267,623,587	23,999,926
FY2011	6%	477,132.8	3,708,584,370	2,430,939,799	58,206,498	2,489,146,297	1,277,644,616	23,999,939

Reducing Previously Enacted Allowable Growth – 4% FY09 & 2% FY10								
Fiscal Year	Allowable Growth Rate	Budget Enrollment	Combined District Cost	State Aid Without Preschool State Aid	Preschool State Aid	Total State Aid	Property Taxes	Add. Prop. Tax Levy Aid
FY2009 (In process)	4%	480,608.8	3,385,922,280	2,207,372,179	17,057,280	2,224,429,459	1,178,704,480	17,999,912
FY2010	2%	477,494.8	3,445,690,463	2,225,576,430	36,110,894	2,261,687,324	1,220,114,080	23,999,899
Impact of different allowable growth rates								
FY2011	0%	477,132.8	3,472,899,637	2,200,762,562	58,206,498	2,258,969,060	1,272,137,114	24,000,128
FY2011	1%	477,132.8	3,489,567,936	2,229,505,609	58,206,498	2,287,712,107	1,260,062,366	23,999,890
FY2011	1.5%	477,132.8	3,499,890,602	2,243,324,195	58,206,498	2,301,530,693	1,256,566,448	23,999,916
FY2011	2%	477,132.8	3,511,345,864	2,278,195,101	58,206,498	2,315,902,516	1,253,649,889	24,000,041
FY2011	4%	477,132.8	3,571,108,968	2,314,657,069	58,206,498	2,372,863,567	1,256,451,943	23,999,963
FY2011	6%	477,132.8	3,637,919,875	2,371,690,098	58,206,498	2,429,896,596	1,266,229,819	23,999,852



LEGISLATIVE BRIEFING
Iowa Department of Education

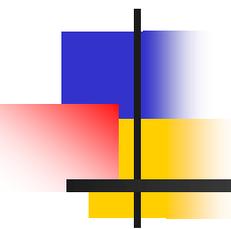
One position presented for FY2011 has been to set the allowable growth rate high, 6 percent, and then have the state not fully fund it. The implications of this particular course of action are many. It gives districts unfunded authority. How authority plays out at the district level is a local decision and there will be a variety of responses. Some districts do not back their authority with cash. In other words, they have considerable authority for which they have not levied and therefore it does not make its way into the educational program. Some districts will secure the cash to back the authority and spend it: short-term capital market financing and then property tax levies. The millage rates for districts obviously play out differently for property tax rich versus property tax poor districts. A small number of districts have negative authority and the unfunded authority would improve their unspent balances without the district having to make any financial adjustments (cuts).

Even if the state were to set the allowable growth rate at 6 percent and then not fully fund it, at some point the state would have to determine how much they were going to actually fund. The previously provided tables have what funding the different allowable growth percentages for FY2011 would cost. Also remember that the allowable growth rate set for FY2011, whether or not it is fully funded, affects the FY2012 state aid cost.

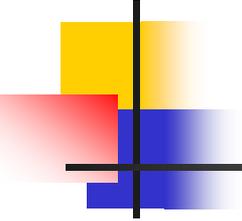
Besides setting the allowable growth rate for the state foundation aid, the Legislature will have to set a separate allowable growth rate for each of the three categorical pots of money. Following is a table setting out what a variety of different allowable growth rates for the categoricals would cost. Note these estimates are based on the amounts that were expected to be rolled into these categorical pots before the 1.5 percent across-the-board (ATB) cut was made. At the time the analysis was run how those cuts would explicitly impact these monies had not been delineated or implemented, so they could not be used in the estimate.

Categorical Allowable Growth Rates

Fiscal Year	Allowable Growth	Teacher Salary Supplement	AEA Teacher Salary Supplement	Professional Development Supplement	AEA Professional Development Supplement	Early Intervention Supplement
FY2010	Base Prior to ATB	237,122,173	14,129,590	26,848,791	1,650,930	29,249,722
Impact of different allowable growth rates						
FY2011	0%	238,807,749	14,221,047	27,036,605	1,661,961	29,453,834
FY2011	1%	241,921,011	14,221,047	27,334,861	1,661,961	29,738,919
FY2011	2%	246,386,985	14,331,367	27,774,210	1,661,961	30,175,445
FY2011	3%	251,570,664	14,669,104	28,242,494	1,661,961	31,121,320
FY2011	4%	256,333,234	14,742,651	29,194,024	1,661,961	31,597,937
FY2011	5%	261,099,320	14,742,651	29,670,630	1,661,961	32,075,045
FY2011	6%	265,865,741	14,896,344	30,147,400	1,661,961	32,552,180



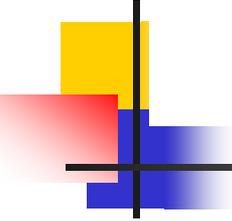
Very Basic School Finance



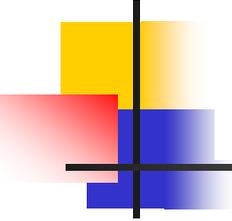
Goals and Principles

- Equity in Expenditure
- Property Tax Relief
- Equalize Taxation
- Uniform State Aid Allocation Formula
- Predictable
- Pupil Driven
- Provide for Local Discretion/Incentives
- Establish Maximum Spending Control
- One Funding Formula AEA + K-12

School District Finance Components



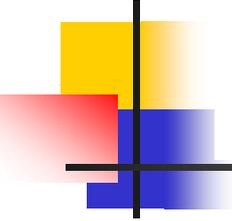
- Combined District Cost (Formula)
Regular, Guarantee, Supplementary
Weighting, Special Education, AEAs
- Instructional Support
- Management Levy
- Physical Plant and Equipment Levy
- Public Education and Recreation Levy
- Debt Service Levy
- Statewide Sales and Services Tax
- State/Federal Categoricals



Combined District Cost

- Regular Program Cost
- + Weighted Enrollment Funding
- + Budget Guarantee (Budget Adjustment)
- + AEA Program Funding
- + SBRC Funding

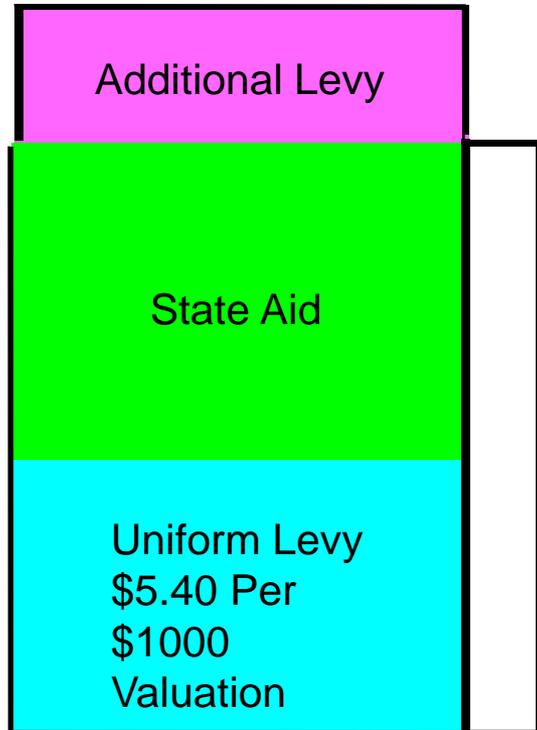
Combined District Cost



Revenue - Foundation Formula

- Required Local Levy - Uniform Levy
 - \$5.40 per \$1,000 Valuation
 - Total **\$583.8 Million**
- State Aid
 - Increase Funding for Districts
 - “Fair” Method to Distribute State Aid
 - Provide Property Tax Relief
 - Equalize Effort
 - Total **\$2,145 Million**
- Additional Levy
 - Total **\$536.8 Million**

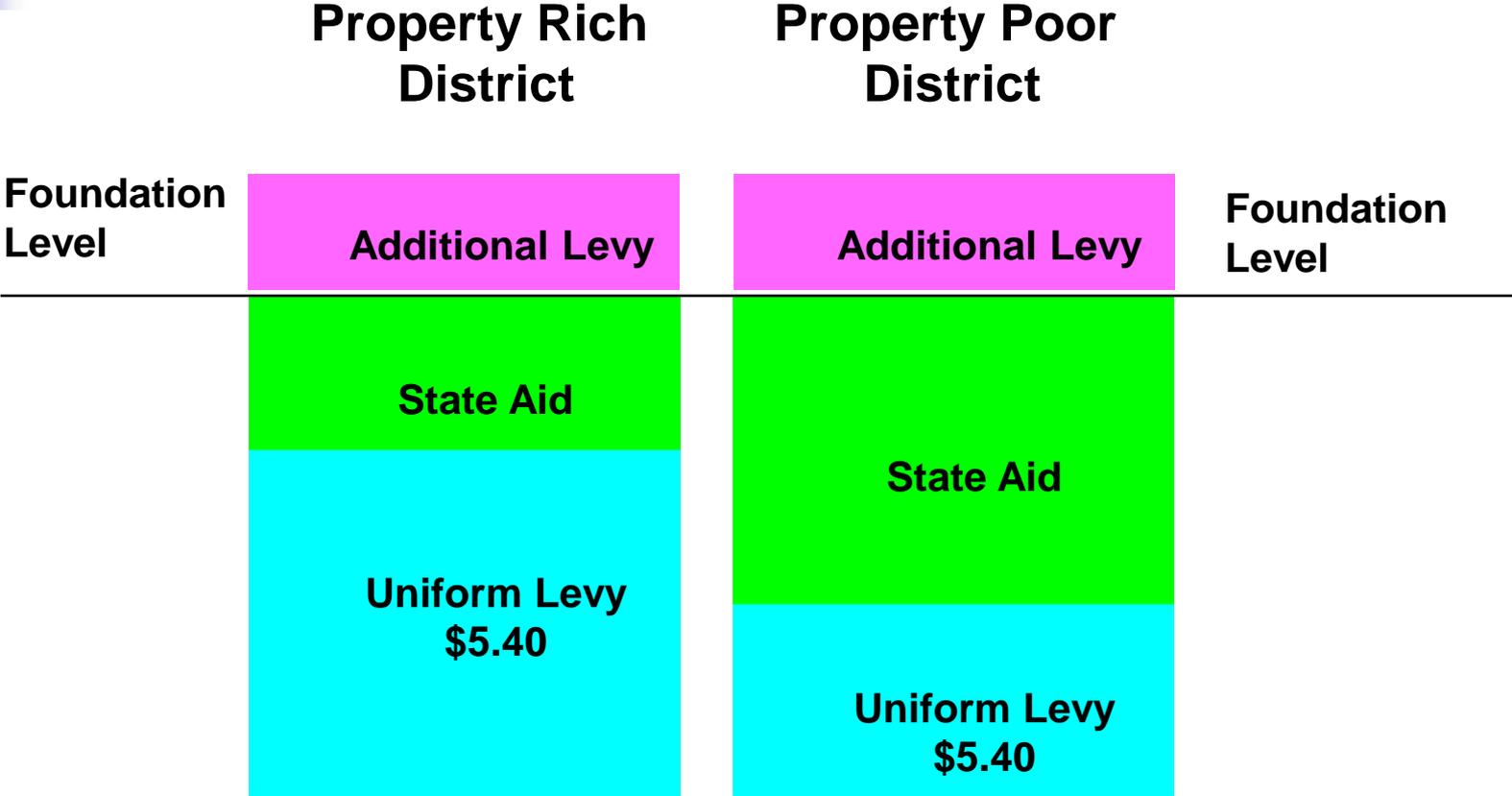
Foundation Formula

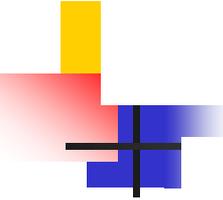


Foundation Level

87.5% of State Cost

Foundation Formula





Additional District Revenues

- Categorical
 - State:
 - Some are about to become part of the formula – “roll-ins”
 - Others HSAP
 - Federal: Title I, Title II, and IDEA
- Instructional Support Program
- Miscellaneous Sources
- Management Fund
- Physical Plant and Equipment Levy
- Statewide Sales and Services Tax

Unspent Balance and General Fund Cash Matrix		
Authority	General Fund (GF) Cash	Plausible explanations - Individual situations vary
Negative Unspent Balance (Negative Authority)	Negative GF	Have spent beyond the authority and more than cash on hand, so some other fund(s) is(are) cross-subsidizing [interfund loan or spending out of other accounts].
	Positive GF	Have spent more than authorized to, but have a cash "float" potentially from the reserve levy.
Positive Unspent Balance (Positive Authority)	Negative GF	Have not levied for all the authority given - districts only have to spend up to the state cost per pupil threshold, even if their district cost per pupil is higher.
	Positive GF	Authority and Cash have tracked fairly well over the years: levying and spending highly correlated.
Technically, mathematically a district could have zero unspent balance and zero authority, too.		

Points to remember:

Both cash and authority balances roll over from year to year, thereby allowing divergence.

There are many funds on the books of which the general fund is one and the general fund has funds within it.