Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873
Email: fiscal.bureau@legis.wisconsin.gov • Website: http://legis.wisconsin.gov/lfb

May, 2019 Joint Committee on Finance Paper #556

Secondary Cost Ceiling (DPI -- General School Aids and Revenue Limits)

[LFB 2019-21 Budget Summary: Page 320, #10]

CURRENT LAW

A major objective of the equalization aid formula is tax base equalization. The formula operates under the principle of equal tax rate for equal per pupil expenditures. In pure form, this means that a school district's property tax rate does not depend on the property tax base of the district, but rather on the level of expenditures. The provision of state aid through the formula allows a district to support a given level of per pupil expenditures with a similar local property tax rate as other districts with the same level of per pupil expenditures, regardless of property tax wealth. There is an inverse relationship between equalization aid and property valuations. Districts with low per pupil property valuations receive a larger share of their costs through the formula than districts with high per pupil property valuations.

The equalization aid formula is calculated using school district data (pupil membership, shared costs, and equalized valuations) from the prior school year. There are three guaranteed valuations used in the equalization formula that are applied to three different expenditure levels. The rate at which shared costs are aided through the formula is determined by comparing a district's per pupil property value to the three guaranteed valuations. Equalization aid is provided to make up the difference between the district's actual tax base and the state's guaranteed tax base.

Primary tier. The first tier is for shared costs up to the primary cost ceiling of $1,000 per member. State aid on these primary shared costs is calculated using the primary guaranteed valuation of $1,930,000 per member. Both the primary cost ceiling and the primary guarantee are set in statute. Primary aid is based on a comparison of the school district's equalized valuation per member to the $1,930,000. Primary aid equals the amount of costs that would be funded by the missing portion of the guaranteed tax base. Every district whose equalized valuation per member is below $1,930,000 receives at least the primary aid amount. Primary aid cannot be reduced by negative aid generated at the secondary or tertiary aid levels. This feature of the formula is referred to as the primary aid hold harmless.

Secondary tier. The second tier is for shared costs that exceed $1,000 per member but are less than the secondary cost ceiling, which is equal to $9,729 per member in 2018-19. By law, the secondary cost ceiling is set equal to 90% of the prior year statewide shared cost per member. The state's sharing of secondary costs is calculated using the secondary guaranteed valuation. By law, the secondary guarantee is set at the amount that generates equalization aid entitlements that are equal to the total amount of funding available for distribution. In 2018-19, the secondary guaranteed valuation is $1,241,233 per member.

Tertiary tier. The third tier is for shared costs that exceed the secondary cost ceiling of $9,729 per member in 2018-19. State aid on tertiary shared costs is calculated using the tertiary guarantee, which, by law, is set at the statewide average equalized valuation per member. The tertiary guarantee is $594,939 per member in aid year 2018-19. If a school district's tertiary aid is a negative number, this amount is deducted from its secondary aid. As noted above, if the sum of a district's secondary and tertiary aid is a negative number, this amount is not deducted from its primary aid amount.

GOVERNOR

Set the secondary cost ceiling at 100% of the prior year statewide shared cost per member, beginning in with the 2020-21 distribution of general school aids.

DISCUSSION POINTS

1. The secondary cost ceiling has been set at 90% of the prior year statewide shared cost per member since the 2001-02 general aid distribution. Prior to that time, the secondary cost ceiling was adjusted for inflation annually. Under that provision, the secondary cost ceiling consistently declined relative to the statewide average shared cost per member. To address this issue, the 2001-03 biennial budget act set the secondary cost ceiling at its current law 90% amount, which is approximately the level where it was at the time.

2. Prior to the imposition of revenue limits, the highest tier of the equalization formula (previously the secondary tier, now the tertiary tier) was intended to serve two purposes. First, it was intended to serve as a disincentive for higher spending levels by causing districts to receive aid at much lower levels for costs incurred above the secondary cost ceiling. Second, it attempted to narrow the per pupil spending disparities among school districts by redistributing aid to districts that spent at lower levels.

3. Under revenue limits, those two purposes are arguably less important. Revenue limits control the amount that districts can raise from the combination of state general aid and the local property tax levy. Thus, any changes in a district's general aid would tend to result in opposite changes in the district's levy, to the extent that districts levy the maximum amount allowed under revenue

limits, which most do. In addition, the primary method for narrowing spending disparities since the imposition of revenue limits has been increases to the low revenue adjustment, which provides additional revenue limit authority to low revenue districts.

4. The bill provision would increase the amount of shared costs that would be aided at the secondary level of the formula with its higher guarantee, and reduce the amount of shared costs that would be aided at the tertiary level with its lower guarantee. To distribute the same amount of aid, however, the state would not provide as generous of a guarantee at the secondary tier compared to current law.

5. The current secondary cost ceiling establishes an aid disincentive for below average costs. Under the bill, only if costs exceed the statewide average would districts be subject to a lower aid rate or negative tertiary aid. In the 2018-19 aid distribution, 41 of the 422 districts had a shared cost per member below 90% of the statewide average cost, while 176 had a shared cost per member below the statewide average. It could be argued that any penalty or disincentive features of tertiary aid are lessened when the vast majority of districts in the state are subject to it.

6. To the extent that the disincentive aspects of the tertiary tier still influence the decisions of individual districts, however, increasing the secondary cost ceiling could, in isolation, reduce the disincentive for higher spending by districts with shared costs per member between the current secondary cost ceiling and the proposed higher cost ceiling. This could redistribute state aid from districts with per pupil costs below the current secondary cost ceiling to districts with higher costs.

7. The bill provision modifying the secondary cost ceiling would be made in conjunction with a number of other changes to the aid formula. A March 28 memorandum from this office to the members of the Wisconsin Legislature provided background information on K-12 school finance, described the general aid and tax credit provisions of the bill, and provided distributional information on those provisions had they been in place for the 2018-19 aid distribution.

8. In isolation, had this option been effective for the 2018-19 aid year, the secondary cost ceiling would have been $10,810 per pupil, rather than $9,729 per pupil as under current law. A total of 242 districts would have received more aid, 117 districts would have received less aid, and 63 districts would have had their aid unchanged. A total of $57.4 million in funding would have been redistributed among districts, which is 1.3% of total net general aid payments.

9. Districts with shared cost per member above the statewide average (the proposed cost ceiling) would generally tend to receive more aid compared to current law. Districts with shared cost per member below the statewide average would generally tend to receive less aid compared to current law. Aid eligibility for higher value districts would tend to remain unchanged.

10. Rather than increasing the secondary cost ceiling in one year, the Committee could also choose to phase the increase in over a longer period. One such alternative would be to increase the secondary cost ceiling by 2.5 percentage points over a four-year period, beginning with the 2020-21 aid distribution (Alternative 2). Had the secondary cost ceiling been set at 92.5% of the prior year statewide average shared cost per member for the 2018-19 aid year, only $11.8 million in funding would have been redistributed among districts, rather than the $57.4 million under the 100% option.

11. In their report to the Legislature, the Blue Ribbon Commission on School Funding recommended that the Legislature consider addressing the issue of negative tertiary aid with one or more of three options, one of which was the Governor's recommendation to set the secondary cost ceiling at 100% of the prior year statewide shared cost per member.

12. Another option was a more narrowly-focused alternative to specify that any additional costs generated by a referendum (debt, operating, or both) would be excluded from aidable cost for negative tertiary aid districts (Alternative 3). The effect of additional aidable costs, such as from a referendum, differ based on the property value per pupil of the district. A district with costs at the tertiary tier and a property value per pupil below the statewide average would receive additional equalization aid for increased costs. A district with property value per pupil above the statewide average would lose aid for those costs. Districts with property value per pupil above roughly twice the statewide average would likely be subject to the hold harmless provisions that would result in no aid change on additional costs.

13. The effect on district levies under revenue limits would also vary. As an example, if a below-average value district raises an additional $100 under a referendum, it might receive $20 of positive aid for those costs, meaning it would have to levy $80 under revenue limits to fund the expenditures. If an above-average value (negative tertiary aid) district raises that additional $100, it might lose $30 in negative tertiary aid, meaning it would have to levy $130 dollars to fund the expenditures. If a very high-value district raises the additional $100, the hold harmless provisions would mean that its aid would likely be unaffected, meaning it would have to levy only the $100 raised.

14. This alternative would thus exclude additional referenda expenditures for negative tertiary aid districts. Under this alternative, equalization aid could be shifted among districts for costs attributable to such referenda, if they would have been offered and passed under current law. To the extent that referenda would be offered and passed in negative tertiary districts under current law, there would be a redistribution of aid related to the treatment of the additional costs under the alternative. To the extent that referenda would not be offered and passed in negative tertiary districts under current law, there would be no redistribution of aid under the alternative.

15. A final option identified by the Commission was to add a secondary aid hold harmless to the formula, similar to the current law primary aid hold harmless (Alternative 4). This would mean that negative tertiary aid could not reduce positive secondary aid. This would maintain a tertiary aid concept but address the discontinuity described above. Had this option been effective for the 2018-19 aid year, 77 districts would have received more aid, 297 districts would have received less aid, and 48 districts would have had their aid unchanged. A total of $72.7 million in funding would have been redistributed among districts, which is 1.6% of the funding appropriated.

ALTERNATIVES

1. Approve the Governor's recommendation to set the secondary cost ceiling at 100% of the prior year statewide shared cost per member, beginning in the 2020-21 aid year.

2. Modify the Governor's recommendation to set the secondary cost ceiling at the following percentages of prior year statewide shared cost per member: (a) 92.5% in the 2020-21 aid year; (b) 95% in the 2021-22 aid year; (c) 97.5% in the 2022-23 aid year; and (d) 100% in the 2023-24 aid year and each aid year thereafter.

3. Delete the Governor's recommendation and instead specify that, beginning in the 2020-21 aid year, any additional costs generated by the following type of referendum would be excluded from aidable cost if the result of the exclusion would be an increase in a district's aid.

a. Debt referenda

b. Operating referenda

c. Both debt and operating referenda

4. Delete the Governor's recommendation and instead add a secondary aid hold harmless feature to the equalization aid formula, beginning in the 2020-21 aid year.

5. Take no action.

Prepared by: Russ Kava