Overview

- Minnesota has one of the most complex school funding systems of any state
- Not a logical, cohesive, or fair system; developed gradually over many years, through messy political processes involving special interests and compromises
- For new superintendents and business officials, learning the system can be overwhelming
- Using best practices starts with an understanding of how Minnesota school finance works
Overview

• What we will cover today – our emphasis will be on school district revenues, with a few other topics
  – Pupil counting – the basic building block of MN school finance
  – Measures of property value
  – School revenue sources
  – Basic concept of equalization
  – General education revenue in all its forms
  – Special education and other categorical revenues
  – The importance of fund balance
  – UFARS and fund accounting
  – Federal revenues
  – Audits and budgets
Pupil Counting

• Average Daily Membership (ADM) – unweighted headcount of students (each student is counted for portion of the year enrolled or “in membership”)
  – Resident ADM – ADM of students who reside in the district, including those enrolled in other districts through open enrollment or tuition
  – Adjusted ADM – The ADM of students served by the district, including adjustments for open enrollment

• Pupil Units – ADM multiplied by “weighting factors” based on the grade level of the student
  – Resident Pupil Units
  – Adjusted Pupil Units

• Weighting Factors
  – Grades K – 6 – 1.0
  – Grades 7 -12 – 1.2
Pupil Counting Matters

• Since most revenue formulas depend on pupil counts, over- and under-estimating has implications …..

• Initial revenue during any fiscal year is paid based on estimated pupil counts

• Final revenue is adjusted for actual pupil counts, through
  – “Final” aid payments – paid during the next fiscal year but recognized as revenue in the fiscal year earned
  – Levy adjustments – recognized as revenue in a subsequent fiscal year
Property Values

• Various measures of property value (value of all taxable property in the district) are used in calculation of state aid and property tax levies:
  – Estimated market value (EMV)
  – Taxable market value (TMV)
  – Referendum market value (RMV)
  – Net tax capacity (NTC)
  – Adjusted net tax capacity (ANTC)

• Minnesota also has one of the most complex property tax systems in the nation
School Revenue Sources

• General Education Revenue
  – Legislatively authorized formulas, primarily pupil driven
  – Voter approved operating referendums

• Categorical Revenue
  – Legislatively authorized formulas pupil and cost driven

• Levies
  – Voter approved
  – Board approved with legislative authorization
  – Levied against NTC or RMV
  – Some are equalized with state aid

• Federal ("Title" programs, other programs)

• Other - Fees (lunches, activities, etc.), donations, earnings on deposits and investments
Equalization

• The goal of equalization is to equalize property tax burdens between school districts for similar property types / values and levy amounts.
• This has been a key concept in school finance formulas in MN and other states for over 50 years.
• In general, districts with lower property values receive more state aid (and lower tax levies) than higher value districts.
• In practice, statutory provisions and economics have significantly reduced the level of equalization aid available for many programs.
  • Growing property values
  • Fixed equalizing factors
# Simple Example of Equalized Aid and Levy Formula

First Tier of Referendum Revenue

<table>
<thead>
<tr>
<th>Step</th>
<th>Description</th>
<th>District A</th>
<th>District B</th>
<th>District C</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Allowance per Pupil</td>
<td>$300</td>
<td>$300</td>
<td>$300</td>
</tr>
<tr>
<td>2.</td>
<td>Resident and Adjusted Pupil Units</td>
<td>1,000</td>
<td>1,000</td>
<td>1,000</td>
</tr>
<tr>
<td>3.</td>
<td>Total Revenue (#1 x #2)</td>
<td>$300,000</td>
<td>$300,000</td>
<td>$300,000</td>
</tr>
<tr>
<td>4.</td>
<td>Referendum Market Value (RMV)</td>
<td>$300,000,000</td>
<td>$600,000,000</td>
<td>$950,000,000</td>
</tr>
<tr>
<td>5.</td>
<td>RMV per Pupil Unit (#4/#2)</td>
<td>$300,000</td>
<td>$600,000</td>
<td>$950,000</td>
</tr>
<tr>
<td>6.</td>
<td>Statewide Equalizing Factor</td>
<td>$880,000</td>
<td>$880,000</td>
<td>$880,000</td>
</tr>
<tr>
<td>7.</td>
<td>Levy Ratio (#5/#6)</td>
<td>34.1%</td>
<td>68.2%</td>
<td>100.0%</td>
</tr>
<tr>
<td>8.</td>
<td>Levy (#3 x #7)</td>
<td>$102,273</td>
<td>$204,545</td>
<td>$300,000</td>
</tr>
<tr>
<td>9.</td>
<td>Aid (#3 - #8)</td>
<td>$197,727</td>
<td>$95,455</td>
<td>$0</td>
</tr>
<tr>
<td>10.</td>
<td>Tax Rate (#8/#4)</td>
<td>0.03409%</td>
<td>0.03409%</td>
<td>0.03158%</td>
</tr>
<tr>
<td>11.</td>
<td>Tax per $100,000 of Value</td>
<td>$34</td>
<td>$34</td>
<td>$32</td>
</tr>
</tbody>
</table>
School District Revenue, All Sources

FY 16 School District Revenue Sources
Total Revenue: $12.4 Billion

- State Aid/Credits: 68%
- Property Taxes: 20%
- Federal: 6%
- Fees: 6%

General Education

- Largest share of school district revenue
- Mostly aid, but levy portion in the some components
- Composed of multiple formulas for individual components, most of which are “non-restricted;” for FY17:

<table>
<thead>
<tr>
<th>Basic</th>
<th>Extended Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gifted and Talented</td>
<td>Small Schools</td>
</tr>
<tr>
<td>Basic Skills</td>
<td>Declining Enrollment</td>
</tr>
<tr>
<td>Secondary/Elementary Sparsity</td>
<td>Pension Adjustment</td>
</tr>
<tr>
<td>Transportation Sparsity</td>
<td>Operating Capital</td>
</tr>
<tr>
<td>Equity</td>
<td>Local Optional</td>
</tr>
<tr>
<td>Operating Referendum</td>
<td>Transition</td>
</tr>
</tbody>
</table>
Basic

- Basic General Education formula is the largest source of revenue for school districts
- The basic allowance is set each year in legislation
- "Basic Allowance (per adjusted pupil unit)
  - FY 2015 $5,831
  - FY 2016 $5,948 +2%
  - FY 2017 $6,067 +2%
- Almost all revenue provided as state aid – small "student achievement levy" - will be eliminated beginning in FY19
Extended Time

- For students in extended day, week or year programs
- Students may generate up to 0.2 ADM, which is weighted by the standard weightings to generate the district’s Extended Time pupil count
- Revenue is all aid, and equals the Extended time pupil count times $5,117
Gifted and Talented

• For districts to identify and serve gifted and talented students and provide professional development for teachers of those students
• Revenue is all aid, and equals $13 times APU
Basic Skills

• Basic skills revenue is intended to fund at risk students, and is calculated based on two formulas, Compensatory Revenue and English Learner Revenue

• Compensatory Revenue
  – Calculated by site, based on the concentration of free and reduced price lunch students at the site
  – All state aid
  – Varies by concentration of free and reduced students, and by total numbers
  – 5% may be reserved by the district for use at different sites
  – Restricted for certain expenditures
Basic Skills (cont.)

• English Learner revenue
  – Calculated in two parts:
    • A fixed amount per English Learner
    • A concentration calculation that provides additional funding for districts with higher concentrations of English Learners
  – All state aid
  – Restricted for certain expenditures
Elementary and Secondary Sparsity

• Additional revenue for small and isolated schools
• Calculated in two parts:
  – Elementary Sparsity based on 20 or fewer students per grade, and more than 19 miles to next nearest elementary
  – Secondary Sparsity based on enrollment and “Isolation Index,” which is based on square miles of area and distance to nearest high school

• All state aid
• Unrestricted revenue
Pension Adjustment

- A grandfathered revenue based on PERA and TRA adjustments from 1984, 1997, 1999 and 2007, compared with the state average adjustment in FY 2014
- All state aid
- Unrestricted revenue
Transportation Sparsity

- Additional revenue for districts with sparse population
- Calculated based on an isolation index and a density index that are a function of the ratio of the square miles in the district to the number of pupils in the district
- All state aid
- Unreserved revenue
Operating Capital

- Funding for district capital needs, including repair and betterment, equipment purchases, books, technology and other allowable expenses
- Calculated per pupil times an equipment component ($79) and a facilities component ($109) multiplied by a maintenance cost index (one plus the ratio of average building age to 100)
- Mix of state aid and local levy, but highly equalized so that most of the revenue is paid as state aid
Declining Enrollment

• Additional revenue for districts with declining enrollment
• Calculated (only if pupil counts decline) as 28% of the formula allowance times the change in adjusted pupil units since the prior year
• All state aid
Equity

- Additional revenue linked to referendum revenue – intended to provide additional revenue to districts with low referendum allowances
- Calculated in four parts:
  - Regular Equity revenue ranks metro and non-metro districts separately, by Operating Referendum amount, and provides more revenue for the lowest ranking districts
  - Low Referendum Equity revenue gives districts with a referendum levy of less than 10% of the state average referendum an amount equal to 10% of the state average referendum minus their referendum amount
Equity

• Calculated in four parts (cont.):
  – Supplemental Equity revenue provides $50 per pupil to all districts
  – Regular and Low Referendum equity are increased by 25% for districts in the seven county metropolitan area; for districts in the rest of the state, by 16% for FY 17-19, and by 25% for FY 20 and later
  – Revenue is a mix of aid and levy
  – Levy is spread on Referendum Market Value
  – Equalized at the same level as the 2nd tier of referendum revenue
Small Schools

• Additional revenue for small districts (under 960 enrollment), or rural districts with multiple high schools and small school buildings

• Calculated in two parts:
  – District calculation
    • $544 \times APU \times (960-(APU/960))
  – School calculation (if the district has multiple high schools and qualifies for Secondary Sparsity revenue)
    • $544 \times \text{High School Building APU} \times (960-(\text{High School Building APU}/960))

• All state aid
Transition

- An aid grandfather that holds districts harmless in revenue for changes in state education revenue formulas
- Includes components for hold harmless general education and special education funding Revenue is a mix of aid and levy
  - Levy is spread on Referendum Market Value
  - Equalized at the same level as the 2\textsuperscript{nd} tier of referendum revenue
Local Optional Revenue

- All districts may receive board-approved revenue of up to $424 per APU
- For referendum authorities approved before 2014, LOR allowance is subtracted from referendum authority
- Taxes spread on RMV
- Equalized formula – equalized at same level as the 2nd tier of referendum revenue
Operating Referendum

• Board approved (up to $300 per APU) and voter approved (up to a maximum total of $1,891 in 2016-17)
  – No maximum for secondary sparsity districts
  – Higher maximum for a few “grandfathered” districts

• Three tier equalization aid formula, with percent of aid based on each district’s referendum market value (RMV) per RPU

  • 1st tier
    – Up to $300 of revenue per pupil unit
    – Equalized at a relatively high level ($880,000)
    – Most districts receive some aid
Operating Referendum (cont.)

• 2\textsuperscript{nd} tier of aid
  – Revenue between $300 and $760 per APU
  – Equalized at $510,000 of value per pupil
  – Many districts receive aid

• 3\textsuperscript{rd} tier of aid
  – Revenue above $760 per APU, up to 25% of the basic formula allowance ($1,451.50), with no limit for districts that qualify for sparsity revenue
  – Equalized at $290,000 of value per pupil
  – Most districts do not receive any aid
Operating Referendum (cont.)

- FY 2015 conversion of allowances complicates revenue
  - Basic calculation is FY 2015 old law revenue divided by new APU
  - Must include alternative attendance (open enrollment) adjustment
  - Intent was no loss of revenue, no loss of aid
  - Pupil count estimates and property value estimate changes (due to the alternative attendance calculation) have the potential to continue changing a district’s allowance until the fall of 2015

- Location Equity Revenue
  - Functions as an offset to Operating Referendum revenue
  - $424 for metro districts, $212 for outstate districts larger than 2,000
Special Education

• Districts qualify for State and Federal funding for special education costs, but it may not cover all costs. Costs not covered must be funded out of the district’s general fund.

• Starting in FY 2016, funding has moved to a more pupil based distribution that takes into account total pupils, concentrations of poverty, district size and the costs of educating students with different primary disability identification.
Long Term Facilities Maintenance Revenue

- New category of revenue created by legislation in 2015; replaced previous health & safety, deferred maintenance and alternative facilities programs.
- Creates greater equity among districts in funding for facilities maintenance – districts that did not qualify for previous “alternative facilities revenue” have access to additional revenue.
- Can be used for facilities maintenance, accessibility, health and safety, and improvements for Pre-K programs.
- Phasing in over 3 years, with limits per APU ($193 for 2016-17, $292 for 2017-18, $380 for 2018-19).
- Revenue is lower for districts with average building age < 35 years.
Long Term Facilities Maintenance Revenue

- Revenue is provided through an equalized formula - property tax levies, some state aid for most districts.
- Can access revenue above per pupil funding amounts for certain projects.
- Revenue can be used in multiple ways:
  - to fund project costs on an annual basis
  - district can issue bonds and use revenue to make annual payments
  - can build up a fund balance to use for larger projects in later years.
Other Categorical Revenues

- Telecommunications Access Revenue
- Achievement and Integration Revenue
- Safe Schools
- School Breakfast and Lunch Aid
- Lease Levy
- Alternative Teacher Compensation (Q-Comp)
- Community Education
- Early Childhood and Family Education
- School Readiness
- Debt Service
- Capital Project Levy
Fund Balances

• Advantages of a Larger Fund Balance
  • Provides financial flexibility
  • Improves cash flow – avoid cash flow borrowing and increase revenue from investments
  • Can lead to a higher credit rating and lower borrowing rates

• Potential Disadvantages of a Larger Fund Balance
  • Could become a target in negotiations
  • State’s tendency to “go after” fund balance

• Fund balance policy
  • Importance of having a policy setting a target for minimum fund balance
  • Fund balance range / level varies by school district
Accounting Requirements

• Accounting of school district finances is governed by state law and by the state Uniform Financial Accounting and Reporting Standards (UFARS)

• UFARS requires that school district revenues and expenditures be recorded in separate funds, with different revenue sources and uses of funds for each
Funds

• Common funds for most districts:
  – Fund 01 – General
  – Fund 02 – Food Service
  – Fund 04 – Community Service
  – Fund 06 – Building Construction
  – Fund 07 – Debt Service

• Other funds used by some districts:
  – Fund 03 – Transportation*
  – Fund 05 – Capital Expenditures*
  – Funds 08 & 09 – Trust and Agency
  – Fund 47 – OPEB Debt Service
  – Internal Service Funds

* Funds 3 and 5 have not been used for state reporting or in audited financial reports since 1997, but many districts still use them internally to record transactions related to these purposes
Federal Revenues

- **Title I**: Based on students qualifying for free and reduced lunch, and funds reading and math for economically disadvantaged students
- **Special Education**
- **Title II**: Eisenhower, audio visual, equipment, vocational education
- **Title III**: English Language Learning Programs
- **Impact Aid**
Audited Financial Reports

- Annual report required by law, summarizing revenues, expenditures, fund balances, and other financial information
- Management Discussion and Analysis (MDA) and Notes provide additional information
- Reports must comply with state law and with Governmental Accounting Standards Board (GASB) standards
- Independent auditor must review financial practices, records and reports; and issue opinion on compliance with GASB, state law, and certain federal requirements
- Auditor usually assists with preparation of statements
- Some districts prepare Comprehensive Accounting and Financial Reports (CAFRs) with more extensive information
- Process: starts July or August, is completed and approved by school board in October-December
Budget

• State law requires that School Board approve a budget for the upcoming fiscal year by June 30th. This gives district staff legal authority to spend budgeted funds.

• Budget summary must be published in district’s official newspaper.

• Most districts also prepare one or more revised or amended budgets, to incorporate changes since June (enrollment, staffing, contract settlements, federal program entitlements).
Multi-Year Budget Forecasting

• State law does not require multi-year budget forecasts, but there are lots of advantages
  – Gives administration and school board ability to make decisions knowing the long-term financial implications
  – May prevent the initiation of new programs that are not financially sustainable in the long run
  – Helpful in demonstrating need for increased referendum revenue
  – Demonstrates financial responsibility to your public

• A number of forecasting tools are available to districts
Additional Resources

- Lots of helpful information on MDE web site [http://education.state.mn.us/MDE/dse/schfin/](http://education.state.mn.us/MDE/dse/schfin/)
- MASBO conferences and annual MASBO Institute (2017 session running this week)
- Ehlers annual School Finance Seminar (April 21, 2017)
- Graduate school classes
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