

# Vermont Legislative Joint Fiscal Office

One Baldwin Street • Montpelier, VT 05633-5701 • (802) 828-2295 • Fax: (802) 828-2483

## *FISCAL NOTE*

Date: March 5, 2015

Prepared by: Mark Perrault

### **Education Funding, Spending, and Governance House Bill No. 361 – As Introduced**

#### **Summary**

#### **Education Tax Rates – Secs. 6 and 7**

Section 6 sets the FY2016 base education tax rates at \$1.53½ for nonresidential property, \$1.00 for homestead property, and 1.94% for household income and section 7 sets the base education amount at \$9,459. Statewide education taxes would increase by \$31 million at these tax rates.

#### **Education Tax Cap – Secs. 27 and 28**

Section 27 limits growth in per pupil education spending to 2% over the prior year for three years beginning in FY2017. If this provision had been in effect in FY2016, 162 districts would have exceeded the cap collectively by \$37 million.

#### **Integrated Education Systems – Secs. 10-12, 17, 18-22, 25**

Section 17 require districts to merge into “integrated education systems” offering prekindergarten through grade 12 instruction to no fewer than 1,100 pupils by FY2020. The other sections provide incentives or remove impediments to the formation of larger districts. Cash incentives available to integrated education systems would require an appropriation of \$-- million from the Education Fund in FY2016. If efficiencies achieved through consolidation enabled districts to increase the State’s 4.7 pupil-to-staff ratio to between 4.8 and 4.9, education spending could be reduced by \$32 to \$54 million.

#### **Tuition Payments – Secs. 15-16**

These sections prohibit the payment of publicly-funded tuition to schools outside Vermont except in certain situations. Payments to schools outside Vermont would drop from \$5.7 million to \$1.7 million.

#### **Education Oversight Committee – Secs. 33-34**

Section 33 authorizes the payment of per-diem compensation and reimbursement of expenses for members.

#### **Moratorium – Sec. 26**

Section 26 imposes a moratorium through FY2016 on State mandates that would increase statewide education tax rates.

#### **Transparency – Secs. 2-5, 8-9, and 13-14**

These sections have no measurable fiscal impact, but provide information intended to help school boards and voters better understand the relationship of per pupil education spending to homestead tax rates.

#### **Studies – Secs. 24, 29-32, and 35**

Sec. 32 authorizes a General Fund appropriation of \$300,000 for a study of an adequacy-based education finance system in Vermont.

## **Section by Section Analysis**

### **Sec. 1. Policy Goals**

This section would have no measurable fiscal impact.

### **Secs. 2–5. Yield or “Dollar Equivalent” – FY2017**

These sections replace the base education amount used to calculate homestead tax rates each year with a yield or “dollar equivalent” that States the amount of per pupil education spending that can be supported with base tax rates fixed at \$1.00 for homestead property and 2.0% for household income.

Although this provision would have no measurable fiscal impact, fixing the base homestead tax rates would have advantages. First, since the base homestead tax rates would remain constant, it might become more apparent to voters that their collective spending decisions determine homestead tax rates rather than the Legislature.

Second, it would be easier for homeowners to estimate their homestead tax when presented with board-approved budgets. For example, if a school board proposed spending per equalized pupil that was 50% more than the yield, the spending-adjusted homestead tax rate would be 50% higher than the base homestead tax rate of \$1.00 or \$1.50.

### **Secs. 6–7. Education Tax Rates – FY2016**

These sections set the education tax rates and the base education amount for FY2016 as follows:

- Nonresidential property – \$1.53½ per \$100 of equalized value
- Homestead property – \$1.00 per \$100 of equalized value
- Household income – 1.94%
- Base education amount – \$9,459 per pupil

Based on preliminary board-approved school budgets, FY2016 Statewide education taxes will increase by roughly \$31 million over FY2015 at these tax rates. See the Education Fund Outlook at:

<http://www.leg.state.vt.us/ifo/education/EF%20Outlook%20-%20Town%20Meeting.pdf>

### **Secs. 8–9. Ballot Language – FY2017**

These sections repeal the so-called “two-vote” provision and require that the Warning for a district’s proposed budget States the total budget in terms of spending per equalized pupil and the percentage change in spending per equalized pupil from the prior year.

Ballot language would have no measurable fiscal impact; however, since homestead tax rates are based on per pupil education spending rather than budgets this additional information might help homeowners better understand the tax consequences of their vote.

### **Secs. 10–11. Merger Support Grants for Small School Districts – FY2017**

These sections allow a district to retain its small schools support after merging with another district even if that district is no longer eligible to receive small school support under current law:

(1) Sec. 10 allows the support grant to continue unless the merged district closes the school that created the original eligibility. However, if closure of the school is tied to consolidation, the support grant continues until the bonded indebtedness is retired.

(2) Sec. 11 allows the support grant to continue as provided in section 10 in districts that merge under section 17 of this bill as long as the merger receives final approval by November 30, 2017 and becomes operational by FY2020.

The cost of continuing to provide the support grant to small schools after merger would be small; however, this provision would remove the potential loss of small schools support as an impediment to mergers. See section 12.

### **Sec. 12. Small Schools Support – FY2020**

Under current law, small school districts operating at least one school are eligible for (1) a support grant if their two-year average enrollment is less than 100 or if the average grade size is 20 or fewer and (2) a financial stability grant if there is a 10% decrease in the two-year average enrollment in any one year.

This section repeals the requirement that a district's two-year average enrollment is less than 100, but requires participation in a merger study and an annual determination that the district remains eligible due to its high student-to-staff ratios, geographic isolation, and success in meeting EQS. In addition, this section repeals the financial stability grant beginning in FY2017.

The fiscal impact of these proposed changes to small schools support beginning in FY2020 would be very small, especially if affected districts vote to replace any lost grant revenue by increasing their locally voted education spending. However, this provision would remove the potential loss of small schools support as an impediment to mergers.

In FY2015, 95 districts received small schools support grants amounting to roughly \$7.4 million, and five districts received small schools financial stability grants amounting to roughly \$90,000.

### **Secs. 13–14. Equalized Pupils; Hold–Harmless Provision – FY2017 and FY2018**

Under current law, the loss of equalized pupils is limited to 3.5% annually. This provision was originally intended to help districts navigate annual swings in enrollment; however, after years of steadily declining enrollment, this provision has resulted in the inclusion of 773 so-called “phantom” pupils in the equalized pupil count in FY2015.

These sections reduce the number of phantom pupils included in a district's equalized pupil count in two ways:

(1) Sec. 13 requires districts with no phantom pupils to apply the hold-harmless provision to the *actual* number of equalized pupils in the prior year; and

(2) Sec. 14 requires districts with phantom pupils to reduce their equalized pupil count to no less than 90% of the prior year in FY2017 and 80% of the prior year in FY2018.

The state-wide fiscal impact of eliminating most phantom pupils would be small; however, districts with phantom pupils might choose to reduce spending since their homestead tax rates would increase. Eliminating phantom pupils from the calculation of homestead tax rates would also allocate the homestead tax burden among districts more equitably.

### **Secs. 15–16. Tuition Payments – FY2017**

These sections prohibit the payment of publicly funded tuition dollars to schools outside Vermont except in certain situations.

Any savings achieved by prohibiting these tuition payments would be small. There could be savings if pupils who would have attended school outside Vermont attended a school in Vermont with excess capacity or if the tuition paid to schools in Vermont is lower than the tuition that would have been paid to schools outside Vermont.

In FY2014, \$5.7 million was paid to schools outside Vermont for 473 full-time-equivalent pupils. If this prohibition had been in place in FY2014, the amount of tuition paid to schools outside of Vermont would have dropped to \$1.7 million for 147 full-time equivalent pupils.

### **Sec. 17. Integrated Education Systems – FY2020**

This section requires 290 existing districts to merge into “integrated education systems” (IES) offering prekindergarten through grade 12 instruction to no fewer than 1,100 pupils by FY2020. Currently, only 15 districts have over 1,000 pupils.

Salaries and benefits paid to school teachers and staff in Vermont account for nearly 80% of current expenditures, so any significant long-term savings under this legislation would be achieved primarily through reductions in the number of teachers and staff made possible by consolidation.

In FY2011, the most recent year that comparable data are available, Vermont’s pupil-to-staff ratio was 5.2, the lowest in the nation. In other New England states, pupil-to-staff ratios ranged from 5.8 to 7.8. In Maine and New Hampshire, pupil-to-teacher ratios were 5.8 and 5.9, respectively.

More recent data available from AOE indicate that Vermont’s pupil-to-teacher ratio was 4.664 in FY2013. If the pupil-to-teacher ratio had been between 4.8 and 4.9, state-wide education spending would have been \$32 million to \$54 million lower and the number of staff would have declined by 409 to 819 full-time equivalents. See the analysis here:

<http://www.leg.state.vt.us/jfo/education/Impact%20of%20Pupil-to-Staff%20Ratios%20on%20Total%20Compensation.pdf>

Vermont has extraordinarily small districts even when compared to Maine and New Hampshire, both rural and sparsely populated states. In FY2009, the most recent year that comparable data is available, nearly two-thirds of Vermont’s districts had fewer than 300 pupils and more than one-quarter of Vermont’s pupils belonged to districts with fewer than 300 pupils.

Vermont also has many small schools that may have higher fixed costs. In FY2009, the average number of pupils per elementary school was 200 pupils, the lowest average in New England and well below the national average of 475 pupils. The average number of pupils per secondary school was 575 pupils. In New England, only Maine had a lower secondary school average.

A 2014 report prepared by voluntary merger committee of the Chittenden East Supervisory Union included an estimate of potential savings to be achieved by closing an elementary school in the union district. Estimated savings ranged from \$0.5 million to \$1.9 million depending on the size of the school. This report is available here:

<http://www.leg.state.vt.us/jfo/education/FINAL%20DRAFT%20REPORT%20APPROVED%20%207-28-14%20%282%29.pdf>

**Sec. 18. Tax Incentives – FY2020**

This section allows an IES that is created before FY2020: (1) to reduce its homestead tax rate and equalize the homestead tax rates of its members; or (2) to receive an incentive payment. It also makes two small facilitation grants available to an IES.

(1) During the first four years after merger, homestead tax rates in member municipalities may not change more than five percent in a single year and the IES's equalized homestead property tax rate is reduced as follows:

- 8 cents in the first year
- 6 cents in the second year
- 4 cents in the third year
- 2 cents in the fourth year

There is a corresponding reduction in the tax rates on household income in the IES over this period.

(2) Alternatively, an IES may opt to receive a payment from the Education Fund equal to \$400 per pupil based on the combined enrollment of the participating districts during the first year after merger.

In addition, an IES is eligible for two grants: (a) a consulting services reimbursement grant and (b) a transition facilitation grant. The combined amount of both grants is paid from the Education Fund and may not exceed \$150,000.

These tax rate incentives would have a negligible fiscal impact in the short-term since any reduction in homestead taxes in districts that are part of an IES would be offset by an increase in those districts that are not yet part of an IES. However, these provisions would create an incentive for districts to merge sooner rather than later in the transition period.

*The cash incentives need an appropriation in FY2016; however, the appropriated education payment in FY2015 exceeded expenditures by nearly \$5 million. AOE has suggested that these funds could be used for this purpose.*

**Sec. 19. Repayment of State Construction Aid – FY2016**

This section repeals a current-law requirement that, upon sale of any building for which State construction aid has been awarded, a district must refund a percentage of the sale price equal to the percentage of aid received – generally 25%. Forgoing these refunds would remove a potential impediment to consolidation into larger districts.

**Secs. 20–21. Technical Corrections**

This section would have no fiscal impact.

**Sec. 22. Recently Merged Districts – Articles of Agreement**

This section would have no fiscal impact, but it removes a potential impediment this legislation might introduce into the merger process under current law.

**Sec. 23. Data; Quality Assurance; Accountability – FY2016**

This section requires AOE to implement state-wide systems to maintain financial and accounting data and longitudinal student data. This requirement would impose no *additional* cost since AOE currently has sufficient funds to cover the cost of its ongoing work.

**Sec. 25. Employee Transition**

This section would have no measurable fiscal impact.

**Sec 26. Moratorium – FY2016 only**

This section imposes a moratorium through FY2016 on mandates that would increase education tax rates. Legislation setting the base education tax rates and the base education amount is exempted.

**Secs. 27–28. Education Spending Cap – FY2017 to FY2019**

These sections limit growth in a district's *per pupil* education spending to 2% over the prior year for three years beginning in FY2017 and prohibit a district from borrowing any amount for operating costs to keep education spending under the limit. *Note that this section needs to be amended to allow districts to borrow to meet short-term cash flow needs.*

Preliminary board-approved budgets submitted to AOE for FY2016 would increase education spending by 2.95% over FY2015. If this provision had been in place for FY2016, 162 districts would have collectively exceeded the spending limit by roughly \$37 million.

For an analysis of the impact of the education spending cap assuming that it had been effective for FY2016 go to: <http://www.leg.state.vt.us/jfo/education/Capped%20Per-Pupil%20Spending%20at%202%20Percent.pdf>

**Secs. 24, 29 – 32, 35**

These sections authorize studies on collective bargaining laws, special Education Funding, the roles of superintendents and principals, current-year property tax adjustments, and health care costs. Section 32 appropriates \$300,000 from the General Fund for a study of an adequacy-based education finance system in Vermont.

**Secs. 33–34 Joint Legislative Education Oversight Committee**

These sections create an oversight committee and authorize the payment of per-diem compensation and reimbursement of expenses for members pursuant to 2 V.S.A. §406.