Introduction into categorical aid and "Taking money off the top of the Education Fund"

House Committee on Education

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March 29, 2022

Review: District tax rates depend on spending decisions

- Vermont's education finance system is a Statewide funding formula coupled with local decision
  - Education spending is determined at a local level
  - School boards set budgets which must be approved by voters

- Education property tax rates are set annually by the legislature
  - Rates are set at the level necessary to fund all voter-approved school budgets
  - Each district's homestead property tax rate depends on its education spending
    - The higher its education spending per equalized pupil, the higher its education tax rates

Review: Local education tax rates are based on 3 factors

- 3 factors determine a school district's equalized tax rate:
  - District's locally voted education spending
  - District's equalized pupil count
  - The statewide yield

Spending adjusted tax rates:

$$\text{District's property tax rate} = \$1.00 \times \frac{\left(\text{District's Education Spending}\middle/\text{District's Equalized Pupils}\right)}{\text{Statewide Property Yield}}$$

$$\text{District's income tax rate} = 2\% \times \frac{\left(\text{District's Education Spending}\middle/\text{District's Equalized Pupils}\right)}{\text{Statewide Income Yield}}$$

What is Education Spending and how is it calculated?

- Districts receive some money that is not included in its Education Spending
  - These funds are referred to as "offsetting revenues"

- Calculating Education Spending:

$Total\ voted\ education\ budget\ ^*$
$\quad -Federal\ categorical\ aid$
$\quad -\ State\ categorical\ aid$
$\quad -\ Tuition\ revenues$ *Offsetting revenues*
$\quad -Prior\ year\ surpluses\ or\ deficits$
$\quad -\ Reserve\ Fund$
$\overline{\qquad\qquad\qquad\qquad\qquad\qquad}$
$Education\ Spending$

Note:* This includes the voter approved budget plus any separately warned articles approved by the voters

What is categorical aid?

- Categorical aid is included in offsetting revenues

- Categorical aid is state aid to school districts* for specific purposes
  - In other words, categorical aid grants offset direct expenditures by school districts for explicit purposes

- Existing State categorical aid includes:
  - State placed students
  - Transportation
  - Technical Education
  - Small school support
  - Essential early education
  - Flexible pathways
  - Special education aid

Note: * Technically, categorical aid is state aid to school districts, supervisory unions, or schools

How does categorical aid affect local tax rates?

Increasing categorical aid to a district *reduces* its local tax rate because the categorical aid is subtracted from its education spending

Recall:

$$\text{District's property tax rate} = \$1.00 \times \frac{\left(\text{District's Education Spending} \Big/ \text{District's Equalized Pupils}\right)}{\text{Statewide Property Yield}}$$

$$\text{District's income tax rate} = 2\% \times \frac{\left(\text{District's Education Spending} \Big/ \text{District's Equalized Pupils}\right)}{\text{Statewide Income Yield}}$$

Example #1 – How does categorical aid affect local tax rates?

Assume:

- 2 almost identical districts - District A and District B
  - Both districts approved a $10 million budget
  - Both districts have 500 equalized pupils
  - The property yield is $11,000

- Difference between districts:
  - District A has $1 million in offsetting revenue
  - District B has $2 million in offsetting revenue

Example #1 – District A

Assume:

- Locally voted education budget: $10 million
- Equalized pupils: 500
- Property yield: $11,000
- Offsetting revenue: $1 million

$$\text{District } A\text{'s property tax rate} = \$1.00 \times \frac{\left(\text{District } A\text{'s Education Spending} \middle/ \text{District } A\text{'s Equalized Pupils}\right)}{\text{Statewide Property Yield}}$$

$$\text{District } A\text{'s property tax rate} = \$1.00 \times \frac{\left(\text{District } A\text{'s Education Spending} \middle/ 500\right)}{\$11,000}$$

Example #1 – District A

- To calculate Education Spending, subtract all offsetting revenues from the total voted education budget:

District A's total voted education budget $10,000,000

     −Federal categorical aid

     − State categorical aid

     − Tuition revenues   −$1,000,000

     −Prior year surpluses or deficits

     − Reserve Fund

          District A's Education Spending $9,000,000

- Calculate tax rate:

$$\text{District } A\text{'s property tax rate} = \$1.00 \times \frac{\left(\$9{,}000{,}000 / 500\right)}{\$11{,}000} = \$1.64$$

Example #1 – District B

- Assume District B is identical to District A, except it has *$2 million* in offsetting revenues:
  - Locally voted education budget: $10 million
  - Equalized pupils: 500
  - Property yield: $11,000
  - Offsetting revenue: $2 million

$$\text{District } B\text{'s property tax rate} = \$1.00 \times \frac{\left(\text{District B's Education Spending}\middle/\text{District B's Equalized Pupils}\right)}{\text{Statewide Property Yield}}$$

$$\text{District } B\text{'s property tax rate} = \$1.00 \times \frac{\left(\text{District B's Education Spending}\middle/500\right)}{\$11,000}$$

Example #1 – District B

Calculate Education Spending:

District B's total voted education budget		$10,000,000
–Federal categorical aid		
– State categorical aid		
– Tuition revenues		$-$2,000,000
–Prior year surpluses or deficits		
– Reserve Fund		
District B's Education Spending		$8,000,000

Calculate tax rate:

$$\text{District } B's \text{ property tax rate} = \$1.00 \times \frac{\left(\$8{,}000{,}000 / 500\right)}{\$11{,}000} = \$1.45$$

Example #1 – Summary

- Increasing categorical aid *reduces* the tax rate at the <u>local</u> level for the district receiving the aid
  - This is because any categorical aid a district receives is subtracted from their education spending

	District A	District B
Approved Budget	$ 10,000,000.00	$ 10,000,000.00
Offsetting Revenues	$ 1,000,000.00	$ 2,000,000.00
Education Spending	$ 9,000,000.00	$ 8,000,000.00
Equalized Pupils	500	500
Statewide property yield	$ 11,000.00	$ 11,000.00
Tax rate	$ 1.64	$ 1.45

How is State Categorical Aid Paid For?

- Categorical aid affects the state's education finance system in two ways:
  - State categorical aid lowers homestead property tax rates in school districts that receive the aid, which lowers statewide education property tax revenues
  - State categorical aid increases statewide education spending by the cost of the categorical aid program

- These two impacts create an obligation in the Education Fund that must be offset with additional revenue
  - Assuming no change in policy or education spending, an obligation in the Education Fund is addressed by increasing the statewide property taxes by lowering the property yield

- In other words, categorical aid is paid for "off the top of the Education Fund"
  - If the categorical aid increases the total uses of the Education Fund, the additional cost would be shared by homestead and nonhomestead property taxpayers across the state

Discussion of S.100