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SCHOOL FINANCE REFORM IN MICHIGAN

One of the most discussed public policy issues of the last two decades has been elementary-secondary school finance reform. The discussion has focused on reducing the per pupil expenditure disparity among school districts, and reducing reliance on the property tax as the principal revenue source to support K-12 education. The catalyst for the most recent discussion was a September 1987 report, prepared by a 42-member State Board of Education appointed commission, entitled Educational Quality in the 21st Century. The technical aspects of school finance are not difficult to resolve, but political problems involving several interest groups have prevented consensus on a school finance reform program. This **Council Comments** analyzes several factors that have made K-12 school finance reform difficult to achieve. **A more detailed 17-page report (No. 293) is available on request.**

School Finance Reform History

Serious school finance reform began with the publishing of a comprehensive school finance study in 1968 entitled School Finance and Educational Opportunity in Michigan. This report provided the framework for a comprehensive discussion of Michigan public and non-public education including school finance reform. In 1969, the Governor appointed a six-member Commission on Educational Reform, which held public hearings throughout the state to receive public testimony and collect facts relating to education issues.

In 1970, an effort was made to adopt a statutory remedy to the school finance issue. A two-year membership formula was adopted in Public Act 100 of 1970. The 1971-72 formula was a power equalizing formula, which guarantees a local school district an equal return in combined state and local funds for each mill levied. In the summer of 1971, the equal yield formula was repealed and was replaced with a traditional deductible millage formula.

The Governor and Attorney General had challenged the existing school finance system in the courts. In December 1972, the Supreme Court in **Milliken v Green** ruled by a 4-3 vote that the existing school finance system violated constitutional provisions. Through the adoption of Public Act 101 of 1973, the state adopted a new membership formula based on the power equalizing concept. The Supreme Court took cognizance of the adoption of the equal yield formula and vacated its 1972 decision in the latter part of 1973.

Beginning with the general election in November 1972 and ending with a special election in May 1981, there were five constitutional ballot issues, voted on by the electorate, that either were pure school finance proposals or major tax proposals with school finance implications. All five were defeated. There were single issues in 1972, 1978

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and 1981, and two issues in 1980.

Factors Inhibiting School Finance Reform

There are a number of factors which taken individually make elementary-secondary education school finance reform difficult to achieve. A combination of some or all of these factors has made it impossible to assemble a coalition that would support a viable reform package. Following is a discussion of several factors that have frustrated efforts to achieve school finance reform.

Cost of Equalization. If per pupil expenditure equalization is to occur, it is necessary to “level up” to the high expenditure districts, because to use an average figure would mean that 50% of the students in the state would have the amount expended on them reduced. The cost of “leveling up” to the amount spent by high expenditure districts is expensive (see **Table 1**).

Table 1

Estimated 1989-90 Cost of Equalizing Basic Education Revenue¹ at the 80th and 90th Revenue Percentile

<u>Percentile</u>	<u>Additional Cost (millions)</u>	<u>Pupils Equalized</u>	<u>Pupils Above Equalized Level</u>	<u>Revenue Per Pupil Equalized</u>
80	\$ 395	1,331,991	310,957	\$3,619
90	1,797	1,481,364	161,584	4,473

Source: Senate Fiscal Agency, unpublished data.

¹ Basic education revenue is defined as local property tax revenue plus state aid received through the basic membership formula.

Using 1986-87 data, which is the most recent available, the 90th percentile cost of \$1.8 billion is 32% of the \$5.6 billion current operating expenditure for all Michigan school districts. The actual cost would be higher than the figures shown in **Table 1**, because it would be necessary to provide significant increases for all districts below the equalization level. For example, a district with revenue of \$5 per pupil below the equalization level would expect more than a \$5 per pupil increase in a scenario where state school aid revenues increased by \$400 million. The problem is exacerbated if the per pupil revenue issue is combined with less reliance on the property tax. The current operating property tax revenue for K-12 schools is \$3.9 billion, and when combined with additional revenue needs, results in a potential major increase in state taxes such as the personal income tax, single business tax, and sales tax.

Another problem is that expenditures by out-of-formula school districts have become the standard for measuring educational quality. An out-of-formula district is one that raises more revenue per pupil through the local property tax than is guaranteed through the state aid membership formula. The high expenditure standard is driven

by SEV growth in high-valuation districts. The issue is further complicated by the disproportionate growth of the property tax base (see **Table 2**).

Table 2
State Equalized Valuation Comparison
State and Selected School Districts

	<u>1978-79</u>		<u>1987-88</u>		<u>Percent Change</u>	
	<u>SEV¹</u>	<u>SEV Pupil</u>	<u>SEV</u>	<u>Pupil</u>	<u>SEV</u>	<u>SEV Pupil</u>
State	\$64,863.9	\$32,998	\$111,037.6	\$ 66,733	71.2	102.2
Birmingham	767.7	69,391	1,589.8	209,509	107.1	201.9
Bloomfield Hills	555.8	68,580	1,329.6	227,595	139.2	231.9
Farmington	608.8	45,880	1,684.7	164,430	176.7	258.4

Source: Department of Education 1978-79 Bulletin 1013, and 1987-88 unpublished data; State Tax Commission 1987 Ad Valorem Property Tax Levy Report.

¹ In millions.

Because of the disproportionate SEV growth in some high-valuation districts, the revenue gap between in-formula and out-of-formula districts continues to grow. If the per pupil revenue disparity issue is dealt with but nothing is done to relieve local reliance on the property tax, disproportionate growth in the property tax base will continue to occur and create another per pupil disparity scenario.

Local Control. The concept of local control simply means that Michigan citizens desire maximum decision making control at the local government level, including school districts, with minimum interference from state government. One indication of local control is the resistance to school district consolidation. Many educators believe that Michigan has too many K-12 districts. In 1986-87, there were 525 K-12 districts, one less than there was 20 years earlier although there had been a pupil decline of 422,259, or 20.3%, during the same period.

Fewer school districts would allow for economies of scale and more comprehensive educational programs, especially at the secondary level. A substantial reduction in the number of school districts could be a significant step in the direction of equalizing the property tax base of school districts.

Out-of-Formula School Districts. The clear beneficiaries of the current school finance system are the out-of-formula school districts. With lower tax rates than in-formula districts, they have more revenue per pupil to spend. The Birmingham school district raises \$6,954 per pupil with an operating levy of 28.3 mills. An in-formula district with the same levy would generate \$2,549 per pupil in combined state and local funds. In 1987-88, there were 165 out-of-formula districts with a membership of 361,000.

High-valuation districts are organized to protect their interests. Effective with the 1980-81 fiscal year, the Legislature added a \$15.5 million recapture provision to the state aid act. This was a small attempt to reduce the per pupil revenue disparity between in-and out-of-formula districts. The recapture figure reached a peak of \$26 million in 1983-84, but by 1988-89 was reduced to \$20.2 million. The reduction occurred as a result of the effective lobbying of high-valuation districts.

Other Factors. There are a number of other factors that inhibit school finance reform. Some education officials oppose abandoning the property tax because of its stability as a revenue source for K-12 education. These officials point to the reduction in state support beginning in 1980-81 and continuing through 1982-83. Between 1979-80 and 1982-83, state school aid dropped \$283 million, while school operating property tax revenue increased \$900 million.

Other factors include: (1) as a result of legislative recalls, the state personal income tax is not available, (2) the growth of the educational lobbying corps, (3) different needs brought about by geographic diversity, and (4) the need to provide educational accountability. When combined with other issues, such as voter approval of any sales tax increase, efforts at school finance reform have been frustrated.

Conclusion

Historically, school finance reform has involved reducing the per pupil expenditure disparity and reducing reliance on the property tax to finance K12 education. More recently there has been a move to add educational accountability as a third side to the school finance reform triangle.

Proponents of property tax relief often are interested in a tax reduction. In the middle are those supporting some additional funds for education. At the other end of the spectrum are those whose primary goal is to generate more money for education. School officials have the added problem of sorting out their various attitudes, beliefs, and objectives which often are in conflict.

Clearly, there is no consensus on a solution to the school finance issue, and there can be no political solution until there is consensus among the affected communities. In light of the existing environment, elected officials should receive some credit for caning as close as they have to getting a two-thirds majority for two recent proposed constitutional proposals.