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Budget Information Brief / 2004-2

An Overview of the K-12 Budget

The Oregon Constitution directs the Legislature to “provide by law for the establishment of a uniform and general system of common schools.” General state support for K-12 schools and education service districts (ESDs) is provided through the State School Fund. The Department of Education makes distributions of state support to districts that meet all legal requirements (Chapter 327, Oregon Revised Statutes).

Allocations to school districts include a transportation grant, a facility grant, and a general-purpose grant. The general-purpose grant follows a legislatively prescribed distribution formula that reflects number of students, additional student weighting for specific greater education costs, teacher experience, and available state and local revenues. This formula was designed to equalize allocations to schools. It was phased-in over time through the use of flat and stop-loss grants designed to ease the transition for certain school districts. Full implementation of the equalization formula occurred in the 2001-03 biennium. The 2001 Legislature adopted a phase-in plan to equalize ESD funding. Final equalization for ESDs begins in 2005-06.

Each regular session, the Legislature typically approves modifications to the distribution of funding for schools. Changes made by the 2003 Legislature can be found in SB 550. Among other changes, the 2003 Legislature added a high-cost disability grant to the school equalization formula. It also increased the transportation grants for districts with high transportation costs as defined in the bill.

Voter approval of Measure 5 in 1990 and Measure 50 in 1997, both of which limited local property tax revenues, caused a significant shift in funding sources for K-12 education. The proportion of state support for K-12 education has increased from about 28% in 1990-91 to about 69% in 2002-03. Given the shift in funding sources, a key issue is how to balance local control of expenditures with accountability to the Legislature, the taxpaying public, and others. High academic standards, student assessments, school and district report cards, and the Oregon Department of Education’s Database Initiative Project – which provides public access to school spending data – are steps towards accountability. The federal No Child Left Behind Act of 2001 reinforces and adds to these accountability requirements.

State Funding Sources for the State School Fund and Other K-12 Grants

The following chart shows state funding levels and sources of funds for the State School Fund and certain targeted K-12 grants for three biennia (including the Governor’s 2003-05 recommended budget). Amounts shown for 2001-03 reflect special session adjustments, which are discussed in the following section of this document.

	1999-2001 Actual	2001-03 Legislatively Approved	2003-05 Governor's Recommended	2003-05 Legislatively Adopted
General Fund	4,272,212,291	3,802,166,368	4,755,152,014	4,737,607,754
Lottery Funds	295,962,708	614,555,682	222,401,387	452,100,536
Other Funds	193,494,942	268,460,516	73,830,569	17,191,710
Total	4,761,669,941	4,685,182,566	5,051,383,970	5,206,900,000

General Fund represents the primary source of state support for the State School Fund. General Fund for 2001-03 also included \$108 million for grants in 2001-02 from the School Improvement Fund, which targeted funds to improve students' math and reading skills.

Lottery support began in the 1995-97 biennium. Lottery Funds in 2001-03 included \$262 million in transfers from the Education Stability Fund (ESF) in addition to \$353 million from net unobligated lottery resources. The Governor's budget did not include any transfers from the ESF, but the 2003 Legislature approved a budget that includes an estimated \$122 million transfer in May 2005 (HB 3642) as well as net unobligated lottery resources of \$330 million.

To achieve desired levels of funding for K-12 education, the Legislature has used resources other than General Fund and Lottery Funds. In 1999-01, the majority of Other Funds were for technology and other grants funded with proceeds from the sale of lottery-backed bonds (\$127 million) and for grants from the School Technology Account established by Senate Bill 622 (\$41.4 million). For 2001-03, the majority of Other Funds were Medicaid Upper Payment Limit (MUPL) resources (\$242 million) for schools' health-related costs.

In the Governor's budget, the sole Other Funds source was MUPL funds; however, the 2003 Legislature did not include this as a resource for the 2003-05 State School Fund budget due to the federal government's concern about Oregon's mechanism by which it calculates MUPL revenue. Other Funds in the 2003-05 legislatively adopted budget include local tax revenues deposited in the State School Fund, primarily from property taxes generated from a reduced discount for early payment of such taxes.

2001-03 Budget Reductions

During the 2002 special sessions to balance the state's General Fund budget, school support was reduced from the 2001-03 legislatively adopted level of \$5.2 billion by a net \$227 million General Fund, after backfilling with Other Funds sources such as the Education Stability Fund, MUPL funds, and increased Common School Fund distributions. More specifically, School Improvement Fund grants of \$112 million for the 2002-03 school year were eliminated during the second special session and the State School Fund was increased by \$30 million through the third special session, for a cumulative reduction of \$82 million. Subsequently, HB 4056 from the third special session, which was to have provided \$50 million in proceeds from cigarette tax revenue bonds, was vetoed by the former Governor. During the fourth special session, the Legislature did not override the veto. The result was to bring the net reduction to \$132 million. In the fifth special session, another \$95 million General Fund was disappropriated, pending the outcome of the vote on the January 2003 tax measure. The failure of this measure brought the total 2002 legislatively approved reductions to \$227 million.

Additionally, during the 2003 regular session, the Legislature enacted (through SB 859) an allotment rule adopted in response to the December 2002 economic and revenue forecast, which projected an additional \$112 million statewide budget shortfall for 2001-03. The rule reduced the State School Fund budget by another \$46.2 million General Fund. This brought total reductions to \$273.2 million. This total does not include an additional \$211 million reduction that was intended to be offset by statutory accrual provisions that allowed school districts to use 2003-04 state resources to pay for 2002-03 services. (If the \$211 million is included, the total reduction is \$484.2 million.) The 2003-05 roll-up effect of the permanent reductions in state support was approximately \$500 million.

In response to these budget reductions, with most affecting the 2002-03 school year, school districts reported plans to layoff staff and reduce the number of school days. In Spring 2003, 90 school districts reported that they were cutting days due to budget reductions. Although the average number of days cut was five, some districts, such as Hillsboro at 17 days, were much higher than the average. Thirty-one of those districts reporting fewer school days indicated they would be below the minimum number of hours required in Oregon.

2003-05 Legislatively Adopted Budget

The 2003 Legislature approved a base amount of \$5.2 billion for State School Fund grants to school districts and ESDs in 2003-05. This funding level is essentially the same as that approved by the 2001 Legislature for K-12 support (including the School Improvement Fund) prior to 2002 special session reductions, but it represents an increase of approximately \$522 million, or 11%, over the 2001-03 legislatively approved level of \$4.7 billion after special session reductions. (If all districts used statutory provisions to accrue, collectively, up to \$211 million as revenue for 2002-03 so that 2001-03 resources were \$4.9 billion, the 2003-05 adopted budget of \$5.2 billion represents a 6.3% increase over 2001-03 resources.)

The adopted budget includes \$4.74 billion General Fund, \$452.1 million Lottery Funds, and \$17.2 million Other Funds from local revenues deposited into the State School Fund. As noted earlier, Lottery Funds include an estimated \$122 million transfer to the State School Fund from the Education Stability Fund in May 2005. Also included in Lottery Funds is \$67 million that is contingent upon the effects of legislation passed to expand the number of lottery machines at authorized locations and other actions to be taken by the Lottery Commission to increase lottery revenues.

The 2003-05 legislatively adopted budget is about \$150 million higher than the \$5.05 billion level in the Governor's recommended budget. The Governor's budget of \$5.05 billion did not include funding for salary increases nor did it include inflation on services and supplies. The Education Subcommittee of the Joint Committee on Ways and Means discussed at length whether increases in salary and health benefits costs should be included in the budget, noting that bargaining takes place at the local level and that districts and their employees are not bound by the statewide salary freeze. The Subcommittee also discussed the savings from using a school district PERS rate of 11.11% that was approved by the PERS Board for the 2003-05 biennium rather than the 16.71% used in the Governor's budget. There also was discussion on whether it was reasonable to eliminate the inflation allowance from the State School Fund budget as was done for state agencies. Ultimately, the Legislature did not approve any specific cost factors when it adopted the \$5.2 billion budget for schools, although there was general acknowledgement of the lower PERS employer contribution rate. Whether the legislatively adopted budget allows for actual growth in salaries and wages, health benefits costs, inflation, and other factors affecting school budgets will depend upon an individual school district's circumstances.

The 2003-05 state support monies, along with property tax and other local funds distributed through the equalization formula, increase revenues available to schools and ESDs above the 2002-03 school year (not including accrued state resources) by 14.4% in 2003-04 and by an additional 2% in 2004-05. If accrued resources are included in the funding total for 2002-03, the increase from 2002-03 to 2003-04 is 7.4%.

The statewide average for per-student (weighted) spending in 2003-04 is projected to be \$5,286. This is about a 13% increase over the 2002-03 statewide average of \$4,695, which reflects special session reductions without any accrued resources. With accrued resources, 2002-03 per student funding is about \$5,004. The 2003-04 amount then becomes about a 6% increase.

Historical Trend in Support for K-12 Education

The table on the following page shows the trend in support for K-12 education since 1990-91. The table does not include federal or local resources not subject to the distribution formula. Local resources do include Common School Fund distributions to schools by the Department of State Lands. The Department's 2003-05 legislatively adopted budget includes \$27.1 million Nonlimited Other Funds for this purpose. The table also includes certain targeted state support, as noted in the footnotes.

K-12 Support: 1990-91 through 2004-05

\$ in millions)														LAB (g)	
	90-91	91-92	92-93	93-94	94-95	95-96	96-97	97-98	98-99	99-00	00-01	01-02	02-03	03-04	04-05
State funding (a)	626	818	1100	1132	1427	1750	1760	2078(b)	2252(c)	2329(d)	2437(d)	2537(e)	2358(f)	2591	2616
Local funding	<u>1598</u>	<u>1561</u>	<u>1490</u>	<u>1343</u>	<u>1178</u>	<u>902</u>	<u>956</u>	<u>870</u>	<u>888</u>	<u>964</u>	<u>995</u>	<u>1040</u>	<u>1086</u>	<u>1109</u>	<u>1159</u>
Total	2224	2379	2590	2475	2605	2652	2716	2948	3140	3293	3432	3577	3444	3700	3775
Percent change		7.0%	8.9%	-4.4%	5.3%	1.8%	2.4%	8.5%	6.5%	4.9%	4.2%	4.2%	-3.7%	7.4%	2.0%
STATE SHARE	28%	34%	42%	46%	55%	66%	65%	71%	72%	71%	71%	71%	69%	70%	69%
<small>a State funding includes juvenile corrections for 1992-93 through 2003-05; Common School Fund distributions are reflected as local revenues</small> <small>b Includes one-time funding of \$50 million for classroom needs and \$5 million for security; reflects reduction for \$26 million excess property taxes over cap</small> <small>c Includes \$150 million from lottery bond sale for school facilities</small> <small>d Includes \$127 million lottery bond proceeds, \$50 million in SB 622 proceeds, and \$4 million GF to schools with more than 50,000 ADMw; assumed distribution: \$83 million in 1999-00, \$98 million in 2000-01</small> <small>e Includes \$108 million School Improvement Fund and \$225,000 for local option matching grants</small> <small>f Includes \$225,000 for local option matching grants; includes potential accrual of \$211 million by school districts from 2003-05 resources (SB 1022 – 2002 Third Special Session); without the accrual, the percentage change from 2001-02 is -9.4%; reflects failure of Measure 28 (\$95 million) and \$46 million allotment reduction</small> <small>g Does not include potential \$100 million in 2004-05 generated under legislatively adopted trigger language; both 2003-04 and 2004-05 include state funding for local option matching grants (biennial total of \$400,000)</small> <small>Source: Legislative Revenue Office & Legislative Fiscal Office; historical data adjusted to actual and comparable funding sources</small>															

Potential Changes in the 2003-05 Funding Level

To potentially reach a K-12 funding level of \$5.3 billion, the Legislature provided that the State School Fund could receive additional funding if economic recovery occurs. If General Fund growth occurs, and as long as the state's 2003-05 General Fund ending balance is at least \$100 million as of the June 2004 forecast, then the State School Fund is eligible to receive 50% of any excess over the \$100 million ending balance, until the State School Fund support reaches a total of \$5.3 billion. Even absent any General Fund growth, if lottery revenues exceed those allocated by the Legislature during the 2003 regular session, the State School Fund will receive 100% of the excess net lottery revenues up to a capped amount. Thus, an additional \$100 million over the legislatively adopted budget could be from the General Fund, lottery revenues, or both.

On the other hand, if the temporary graduated income tax assessments adopted by the Legislature in HB 2152 are rescinded through the voter referral, then \$284.6 million will be disappropriated from the State School Fund based on the provisions of HB 5077. If the statewide disappropriation amount of \$544.6 million is not adequate to maintain a balanced budget, additional allotment reductions across all appropriation categories, including the State School Fund, may be implemented by the Governor. Additionally, referral and defeat of the cap on the property tax discount will result in a reduction of about \$14.3 million in Other Funds for the State School Fund.

Recent growth in the Common School Fund's value will result in increased funding to schools from this source. The Fund's value as of December 31, 2003, which determines distributions for 2004-05, has increased significantly from the estimated value that was used to develop the distributions included in the 2003-05 legislatively adopted budget. As a result, the 2004-05 amount will increase from \$13.8 million to \$40.2 million, bringing the total for 2003-05 to \$53.5 million. The Common School Fund is one of many local revenue sources included in the statutory distribution formula. These sources often change from the original estimates that are considered when establishing the legislatively adopted budget for K-12.

**For additional information, contact:
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