

EDUCATION FUNDING FORMULA REVIEW COMMITTEE

Senate Bill No. 2065 (2019) created an Education Funding Formula Review Committee consisting of the chairmen of the standing Education Committees of the House of Representatives and the Senate; three additional members of the Senate, two of which must be appointed by the Majority Leader of the Senate and one of which must be appointed by the Minority Leader of the Senate; and three additional members of the House of Representatives, two of which must be appointed by the Majority Leader of the House of Representatives and one of which must be appointed by the Minority Leader of the House of Representatives. Members appointed to the committee were required to have a secure knowledge of the current K-12 funding formula. The committee was required to study the K-12 education funding formula, including the components, adjustments, and weighting factors of the formula.

In addition, the committee was assigned the following responsibilities:

1. Senate Bill No. 2013 (2019) provided for a study of school transportation, including district routes, expenditures, reimbursement, and possible efficiencies.
2. The Legislative Management assigned the committee the responsibility to receive the following reports from the Superintendent of Public Instruction regarding:
 - a. The financial condition of school districts (North Dakota Century Code Section 15.1-02-09); and
 - b. Annual school district employee compensation reports (Section 15.1-02-13).

Committee members were Senators Donald Schaible (Chairman), Joan Heckaman, Nicole Poolman, and David S. Rust and Representatives David Monson, Marvin E. Nelson, Mark S. Owens, and Mark Sanford.

ELEMENTARY AND SECONDARY EDUCATION STATE AID AND FUNDING FORMULA STUDY

Senate Bill No. 2065 directed a study of the K-12 education funding formula, including the components, adjustments, and weighting factors of the formula. The committee invited several school district superintendents and business managers to participate in the funding formula study.

Background

North Dakota Constitutional Directives

Section 1 of Article VIII of the Constitution of North Dakota provides:

A high degree of intelligence, patriotism, integrity and morality on the part of every voter in a government by the people being necessary in order to insure the continuance of that government and the prosperity and happiness of the people, the legislative assembly shall make provision for the establishment and maintenance of a system of public schools which shall be open to all children of the state of North Dakota and free from sectarian control. This legislative requirement shall be irrevocable without the consent of the United States and the people of North Dakota.

Section 1 has been unchanged since its enactment in 1889.

Section 2 of Article VIII of the Constitution of North Dakota follows with the directive that:

The legislative assembly shall provide for a uniform system of free public schools throughout the state, beginning with the primary and extending through all grades up to and including schools of higher education, except that the legislative assembly may authorize tuition, fees and service charges to assist in the financing of public schools of higher education.

Section 3 of Article VIII of the Constitution of North Dakota requires "instruction shall be given as far as practicable in those branches of knowledge that tend to impress upon the mind the vital importance of truthfulness, temperance, purity, public spirit, and respect for honest labor of every kind."

Section 4 of Article VIII of the Constitution of North Dakota directs the Legislative Assembly to "take such other steps as may be necessary to prevent illiteracy, secure a reasonable degree of uniformity in course of study, and to promote industrial, scientific, and agricultural improvements."

History of Education Funding

Since the 1930s the Legislative Assembly has attempted to meet its constitutional directives by providing some level of financial assistance to school districts. In the late 1950s the Legislative Assembly initiated a foundation aid program

based on a uniform 21-mill county levy and a supplemental state appropriation to ensure school districts would receive 60 percent of the cost of education from nonlocal sources.

For several years, the foundation aid program remained essentially unchanged. However, federal and state courts were beginning to address issues of spending levels for elementary and secondary education and whether those levels should be dependent upon the wealth of the school district in which a student resides. The Legislative Assembly, in an attempt to preempt such issues in North Dakota, responded by amending the foundation aid program in a way that evidenced a higher level of sophistication. Per student payments were more than doubled and weighting factors that recognized four classes of high schools were made part of the education formula. By the late 1970s, a new funding category encompassing seventh and eighth grade students had been created and fiscal protections were instituted for school districts that experienced declining enrollment. In 1979, the Legislative Assembly appropriated \$208.4 million for the foundation aid program and added an additional \$1 million to pay for free public kindergartens.

The next major development affecting education finance occurred with the approval of Initiated Measure No. 6 at the general election in November 1980. This measure imposed a 6.5 percent oil extraction tax and provided 45 percent of the funds derived from the tax must be used to make possible state funding of elementary and secondary education at the 70 percent level. To meet this goal, the 1981 Legislative Assembly allocated 60 percent of the oil extraction tax revenues to the school aid program. Initiated Measure No. 6 also provided for a tax credit that made the 21-mill county levy inapplicable to all but the owners of extremely high-value properties. The Legislative Assembly eliminated the 21-mill county levy and increased state aid to compensate for the revenues that otherwise would have been derived from the levy.

Discussions continued on issues of funding inequities among school districts. Districts spending similar amounts per student and having similarly assessed valuations were not levying similar amounts in property taxes to raise the local portion of education dollars. It was alleged the system encouraged some districts to levy much smaller amounts than their spending levels and assessed valuations would seem to justify. Both the Legislative Assembly and legislative interim committees continued to evaluate the impact of weighting factors, considered the effects of increasing the mill levy equalization factor, and explored the excess mill levy grant concept. While individuals and organizations articulated the need to alter the state's education funding system, little agreement was reached beyond recommending increases in the level of per student aid.

Litigation

In 1989 several school districts and parents joined in suing the state to have North Dakota's system of public school financing declared unconstitutional. The complaint in *Bismarck Public School District No. 1 v. State of North Dakota* charged that disparities in revenue among the school districts had caused corresponding disparities in educational uniformity and opportunity and those disparities were directly and unconstitutionally based upon property wealth. Four years later a district court declared the state's system of education financing to be in violation of Sections 1 and 2 of Article VIII and Sections 21 and 22 of Article I of the Constitution of North Dakota. The decision was appealed and in January 1994, by a one-vote margin, the North Dakota Supreme Court did not uphold the lower court's ruling. The Supreme Court indicated areas in need of legislative attention but, unlike courts in other states, it did not mandate specific legislative action.

Within a decade after the court decision, the Legislative Assembly's commitment to education funding had exceeded \$665 million. In 2003, the state was providing educational services to 99,174 public school students--50 percent of whom were being educated in the state's eight largest school districts. The remaining students were distributed across 205 other districts. Best estimates indicated that by 2013, the number of enrolled students could fall below 90,000. Against a backdrop of declining student numbers, rising expectations for services, and a belief the available resources were both insufficient and inequitably distributed, another lawsuit was brought against the state by the school districts of Williston, Devils Lake, Grafton, Hatton, Larimore, Surrey, Thompson, United, and Valley City.

Williston Public School District No. 1 v. State of North Dakota did not go to trial. Instead, the plaintiffs and the defendants entered a settlement agreement in which it was stated:

[I]t is desirable and beneficial for them and for the citizens of the State of North Dakota to stay this Act and provide the North Dakota Legislative Assembly the opportunity to settle, compromise, and resolve this Action in the manner and on the terms and conditions set forth in this Agreement. The terms and conditions required that the Governor, by executive order, create the North Dakota Commission on Education Improvement and submit to the Legislative Assembly in 2007 an executive budget that includes at least \$60 million more in funding for elementary and secondary education than the amount appropriated by the Legislative Assembly in 2005.

North Dakota Commission on Education Improvement

The North Dakota Commission on Education Improvement, as initially configured, consisted of the Lieutenant Governor--as the governor's designee, the Superintendent of Public Instruction, four members of the Legislative Assembly, four school district administrators, and three nonvoting members representing education interest groups. The commission was instructed to recommend ways in which the state's system of delivering and financing public elementary and secondary education could be improved, and to specifically address the adequacy of education, the equitable distribution of funding, and the allocation of funding.

The recommendations of the North Dakota Commission on Education Improvement became the basis for Senate Bill No. 2200 (2007), which provided a new education funding formula. The bill consolidated education funding that had been assigned to a variety of existing funding categories and established new weighting factors that reflected the added costs of providing education to certain categories of students and the added costs of providing various statutorily mandated services. In addition, the new formula factored in the variable cost of providing services and programs in small, medium, and large school districts. The Legislative Assembly increased the availability of capital improvement loans for needy school districts, provided increased funding for new career and technical education centers and programs, and provided funding for full-day kindergarten programs. The Legislative Assembly reauthorized the North Dakota Commission on Education Improvement and directed it focus its attention on developing recommendations regarding educational adequacy.

2007-08 Interim

After the 2007 legislative session, the North Dakota Commission on Education Improvement contracted with Lawrence O. Picus and Associates (Picus) to identify the resources needed to ensure an adequate education for all students. Picus began with the premise that adequacy requires all students to be taught the state's curriculum and strategies must be deployed to use resources in ways that would double student performance on state tests over 4 to 6 years. Picus determined very early in its efforts that while North Dakota students performed reasonably well on state tests, only 30 to 40 percent of North Dakota students performed at or above the proficiency standard measured by the National Assessment of Educational Progress. It was Picus' determination that North Dakota students would need to achieve at much higher levels if they were to be deemed fully prepared, upon high school graduation, for either college or the workplace. Picus concluded existing state per student payments, coupled with the yield of 185 mills on 88.5 percent of the state average imputed valuation per student, amounted to approximately \$7,024 per student, and to achieve adequacy, the expenditure per student would need to be \$7,293.

Picus also insisted expending a specific dollar amount per student would not achieve the desired results unless the expenditures were linked to certain programmatic strategies that guaranteed the desired results. Without such linkages, the final effect would be nothing other than the existing education system at a much higher cost to taxpayers. Picus' recommendations were centered around prototypical schools having 432 students in the elementary grades, 450 students in the middle grades, and 600 students at the high school level.

2009 Legislative Session

In 2009, after reviewing the Picus report, the North Dakota Commission on Education Improvement made recommendations to the Legislative Assembly, many of which were enacted in House Bill No. 1400. At the conclusion of the 2009 legislative session, the North Dakota Commission on Education Improvement began its third and final interim effort and provided its recommendations to the 2011 Legislative Assembly.

2011 Legislative Session

As had its predecessors, the 2011 Legislative Assembly incorporated the recommendations put forth by the North Dakota Commission on Education Improvement through the enactment of Senate Bill No. 2150 and Senate Bill No. 2013. The amount appropriated for the grants - state school aid line item was \$918,459,478. In addition, the Legislative Assembly provided \$16 million for special education contracts and \$48.5 million for transportation.

Property Tax Relief Legislation

While educational equity and adequacy continued to be dominant legislative concerns, additional time and attention was now being given to the desire for property tax relief. In 2007, the Legislative Assembly enacted property tax relief through the use of income tax credits and transferred \$115 million from the permanent oil tax trust fund to the state general fund to offset anticipated revenue losses resulting from the credits. Due to inherent administrative difficulties resulting from the use of income tax credits for property tax relief, the 2009 Legislative Assembly instituted a statewide system of property tax relief through state-funded school district mill levy reductions. The biennial cost of the program was \$299 million. By 2011 the program's price tag had risen to \$341.8 million and there existed concerns regarding the overall effectiveness of the mill levy reduction grant program as a mechanism for property tax relief, the program's potential to result in the rededication of locally generated revenues to other purposes, and long-term sustainability.

State School Aid and Integrated Property Tax Relief

2013 Legislative Session

When the Legislative Assembly convened in January 2013, the principal education funding package contained a new proposal for funding elementary and secondary education, which included property tax relief provided through an integrated formula. Introduced as House Bill No. 1319, the new proposal was defeated on the morning of the 80th day of the legislative session, but the content was attached later as an amendment to House Bill No. 1013 and enacted. The legislative appropriation for the state school aid program followed substantially the executive budget recommendation to integrate property tax relief in the K-12 state school aid funding formula. The formula change discontinued the mill levy reduction grant program and provided the state will determine an adequate base level of support necessary to educate students by applying an integrated payment rate to the weighted student units. This base level of support will be provided through a combination of local tax sources, local revenue, and state integrated formula payments. The local funding requirement is set at 60 mills and a percentage of identified local in lieu of property tax sources and local revenues. Base level support not provided by local sources is provided by the state through the integrated formula payment. In addition, school districts are allowed an additional 10-mill levy for general fund purposes, an additional 12-mill levy for miscellaneous purposes, and a 3-mill levy for a special reserve fund. The legislation provided for a district's weighted student units to be multiplied by integrated formula payment rates of \$8,810 during the 1st year of the 2013-15 biennium and \$9,092 during the 2nd year, an inflationary increase based on total expenditures per student suggested by Picus during the 2008 study conducted for the North Dakota Commission on Education Improvement.

Minimum and maximum payment levels were established using a statutorily defined baseline funding level that includes:

- All state aid received by the district in accordance with Chapter 15.1-27 during the 2012-13 school year;
- The district's 2012-13 mill levy reduction grant, as determined in accordance with Chapter 57-64, as it existed on June 30, 2013;
- An amount equal to that raised by the district's 2012 general fund levy or that raised by 110 mills of the district's 2012 general fund levy, whichever is less;
- An amount equal to that raised by the district's 2012 long-distance learning and educational technology levy;
- An amount equal to that raised by the district's 2012 alternative education program levy; and
- An amount equal to:

75 percent of all revenue received by the school district and reported under code 2000 of the North Dakota School District Financial Accounting and Reporting Manual, as developed by the Superintendent of Public Instruction in accordance with Section 15.1-02-08;

75 percent of all mineral revenue received by the school district through direct allocation from the State Treasurer and not reported under code 2000 of the North Dakota School District Financial Accounting and Reporting Manual, as developed by the Superintendent of Public Instruction in accordance with Section 15.1-02-08;

75 percent of all tuition received by the school district and reported under code 1300 of the North Dakota School District Financial Accounting and Reporting Manual, as developed by the Superintendent of Public Instruction in accordance with Section 15.1-02-08, with the exception of revenue received specifically for the operation of an educational program provided at a residential treatment facility and tuition received for the provision of an adult farm management program;

75 percent of all revenue received by the school district from payments in lieu of taxes on the distribution and transmission of electric power;

75 percent of all revenue received by the school district from payments in lieu of taxes on electricity generated from sources other than coal;

All revenue received by the school district from mobile home taxes;

75 percent of all revenue received by the school district from the leasing of land acquired by the United States for which compensation is allocated to the state under 33 U.S.C. 701(c)(3);

All telecommunications tax revenue received by the school district; and

All revenue received by the school district from payments in lieu of taxes and state reimbursement of the homestead credit and disabled veterans' credit.

From this baseline total, the legislation called for a subtraction of 60 mills multiplied by the district's taxable valuation, not to exceed the amount in dollars subtracted the prior year plus 12 percent, and a subtraction of the specified portion of the in lieu of taxes revenues listed in the preceding paragraph.

School district boards had been authorized to levy an amount sufficient to cover a multitude of expenses; however, the enactment of House Bill No. 1013 provided for the consolidation of these levies. The bill authorized the board of a school district to levy:

- A tax not exceeding the amount in dollars the school district levied for the prior year, plus 12 percent, up to a levy of 70 mills on the taxable valuation of the district, for any purpose related to the provision of educational services;
- No more than 12 mills on the taxable valuation of the district, for miscellaneous purposes and expenses;
- No more than 3 mills on the taxable valuation of the district for deposit into a special reserve fund; and
- No more than the number of mills necessary, on the taxable valuation of the district, for the payment of tuition.

2013-14 Interim

During the 2013-14 interim, the Education Funding Committee was assigned a study, pursuant to Section 58 of House Bill No. 1013 (2013), of state-level and local-level responsibility for the equitable and adequate funding of elementary and secondary education in the state. The dollar amounts by which a district's weighted student units were multiplied, to arrive at a funding level for the 2013-15 biennium, were determined by applying an inflationary increase to the "adequate" funding level the Picus study recommended as part of its final report to the North Dakota Commission on Education Improvement in 2008. Given the passage of 5 years and changes in the state's economic and demographic circumstances, the Legislative Assembly determined it would be appropriate to review and clarify state-level and local-level responsibility for the equitable and adequate funding of elementary and secondary education. To meet its study directive, the interim Education Funding Committee asked Picus to review its 2008 recommendations and conduct a recalibration using an evidence-based model and the most recent data available. Based on available information and assumptions, Picus recommended recalibrated weighting factors and increased payment rates from the 2013-15 biennium levels of \$8,810 and \$9,092 to \$9,347 and \$9,442. The interim committee did not recommend the Picus funding model. The committee recommended Senate Bill No. 2031 (2015) relating to the funding of elementary and secondary education. The bill set per student funding rates of \$9,482 for the 1st year of the biennium and \$9,766 for the 2nd year. The rate of \$9,482 was determined by subtracting \$236, which represented the 8 days of professional development Picus had recommended, but which the committee did not require, from the Picus recommendation of \$9,442. The remainder was then increased by 3 percent to arrive at \$9,482. A 2nd year increase of 3 percent brought the 2nd year payment rate to \$9,766.

2015 Legislative Session

In 2015, the Legislative Assembly approved Senate Bill No. 2031 which provided increases in the integrated payment rate of 3 percent per year during the 2015-17 biennium, based on the integrated formula payment rate during the 2nd year of the 2013-15 biennium. Integrated payment rates were set at \$9,365 during the 1st year and \$9,646 for the 2nd year of the 2015-17 biennium. In addition, the bill removed the sunset clause on the K-12 integrated formula for state school aid, adopted by the 2013 Legislative Assembly. The 2015 Legislative Assembly also approved Senate Concurrent Resolution No. 4003, which proposed a constitutional amendment to allow the Legislative Assembly to appropriate or transfer the principal balance of the foundation aid stabilization fund in excess of 15 percent of the general fund appropriation for state school aid for the most recently completed biennium for education-related purposes. The resolution was approved by voters in November 2016. In 2016, due to revenue shortfalls during the 2015-17 biennium, the Governor ordered two allotments totaling 6.55 percent and transfers from the foundation aid stabilization fund to offset foundation aid reductions made by executive action totaled \$116,053,293.

2017 Legislative Session

In 2017, the Legislative Assembly approved House Bill No. 1324, which included an adjustment to set the integrated payment rate at \$9,646 for each year of the 2017-19 biennium, the same as the 2nd year of the 2015-17 biennium.

In House Bill No. 1013, the Legislative Assembly provided an appropriation of \$1,935,204,163, of which \$1,334,657,258 was from the general fund, \$295,000,000 from the foundation aid stabilization fund, and \$305,546,905 from the state tuition fund for state school aid integrated formula payments. Of the \$295,000,000 provided from the foundation aid stabilization fund, \$185,000,000 was considered one-time funding. This level of funding represented an increase of \$18,564,163, including a decrease in funding of \$246,795,449 from the general fund and increases in funding of \$178,946,707 from the foundation aid stabilization fund and \$86,412,905 from the state tuition fund, from the 2015-17 biennium adjusted appropriation for integrated formula payments of \$1,916,640,000. Increases in state school aid integrated formula payments included the cost to continue the 2015-17 biennium 2nd year integrated formula payment increase (\$54,000,000), cost of projected student growth (\$57,700,000), and cost associated with an increase in the English language learner weighting factors approved by the 2015 Legislative Assembly and effective July 1, 2017

(\$900,000). The increased costs were partially offset by increases in the local cost-share, including local property tax sources and local revenue. The Legislative Assembly, in Senate Bill No. 2272, also provided one-time funding of \$6,000,000 from the foundation aid stabilization fund to the Superintendent of Public Instruction for rapid enrollment grants during the 2017-19 biennium.

2017-18 Interim

During the 2017-18 interim, the Education Funding Committee was assigned, pursuant to House Bill No. 1318 (2017), a study of how state aid for elementary and secondary education is determined and distributed under the state aid funding formula; the impact of state aid; potential changes to the funding formula to ensure equity, adequacy, and sustainability; the delivery and administration of elementary and secondary education in the state; and the short- and long-term policy and statutory changes that may result from or be necessitated by 21st century technological advances and global economics. In addition, pursuant to House Bill No. 1423 (2017), the committee was assigned a study of the in lieu of property tax portion of the elementary and secondary education funding formula for the purpose of identifying and addressing any inequities in the application of the formula. The committee did not make a recommendation regarding these studies; however, information gathered by the committee was the basis for several bills introduced during the 2019 legislative session.

2019 Legislative Session

In 2019, the Legislative Assembly approved Senate Bill No. 2265, which included several funding formula changes and Senate Bill No. 2013, which provided \$2,098,202,429, of which \$1,610,438,429 is from the general fund, \$110,000,000 is from the foundation aid stabilization fund, and \$377,764,000 is from the state tuition fund, for state school aid integrated formula payments. This level of funding represented an increase of \$162,998,266, including increases in funding of \$275,781,171 from the general fund and \$72,217,095 from the state tuition fund offset by a decrease in funding from the foundation aid stabilization fund of \$185,000,000, from the 2017-19 biennium appropriation for integrated formula payments of \$1,935,204,163. Increases in integrated formula payments included \$54,000,000 for costs associated with projected student growth and \$109,000,000 for state school aid formula changes. Senate Bill No. 2265 included adjustments to:

- Convert the school calendar from days to hours;
- Provide rapid enrollment grants in the 1st year of the biennium and for a phase-in of on-time funding beginning with the 2020-21 school year;
- Reset baseline funding to the 2018-19 school year;
- Provide increases in transition minimum payments of 1 percent over the new baseline in the 1st year of the biennium and 2 percent over the new baseline in the 2nd year of the biennium;
- Reduce, beginning with the 2020-21 school year, total baseline funding and baseline funding per weighted student unit for districts that become elementary school districts;
- Phase out, beginning in the 2021-22 school year, the baseline funding per weighted student unit minimum. The changes provide for a 15 percent reduction of the amount by which the district's baseline funding per weighted student unit exceeds the payment provided per weighted student unit. For each year after the 2021-22 school year, the reduction percentage is increased by an additional 15 percent until it is equal to the payment provided per weighted student unit. The changes also provide weighted student units over the baseline weighted student units are reimbursed at the formula payment rate, instead of the baseline funding per weighted student unit rate;
- Phase out, beginning in the 2021-22 school year, the dollar amount transition minimum. The changes provide for a 15 percent reduction in the dollar amount transition minimum for the 2021-22 school year and an additional 15 percent reduction each school year thereafter;
- Increase the per student payment rate by 2 percent each year of the biennium, to provide \$9,839 per weighted student unit in the 2019-20 school year and \$10,036 per weighted student unit in the 2020-21 school year;
- Increase transition maximum payments by 5 percent each year of the 2019-21 biennium;
- Increase the local property tax deduction calculation each year over a 5-year period, beginning in the 2020-21 school year, to transition all districts to a deduction of 60 mills in the 2025-26 school year;
- Allow school districts, for taxable years beginning after December 31, 2018, to levy additional tax to recover the increase in the property tax deduction in the state school aid formula until all districts are levying and deducting 60 mills in the state school aid formula;
- Reduce the deduction for in lieu of revenue to 75 percent for all revenue types listed, exempt tuition from nonresident students residing in a state with which the state has not entered a cross-border education contract, exempt tuition received from an adjacent school district by certain accepting school districts, and reduce all in lieu

of revenue types by the percentage of mills levied in 2018 by the school district for sinking and interest relative to the total mills levied in 2018;

- Provide the Superintendent of Public Instruction use funding provided for state aid to pay South Dakota if more North Dakota students attend South Dakota schools; and
- Require admitting school districts meeting certain criteria to charge 200 percent of the statutory tuition payment calculation or \$4,000, whichever is greater, and that the tuition received by these school districts is not deducted in the formula.

Foundation Aid Stabilization Fund

Prior to December 8, 2016, the principal of the foundation aid stabilization fund was available only upon order of the governor to offset foundation aid reductions made by executive action due to a revenue shortfall. Section 54-44.1-12 provided the director of the budget may order an allotment to control the rate of expenditures of state agencies. This section provided an allotment must be made by a specific fund and all departments and agencies that receive money from a fund must be allotted on a uniform percentage basis, except that appropriations for foundation aid, transportation aid, and special education aid only may be allotted to the extent the allotment can be offset by transfers from the foundation aid stabilization fund.

In November 2016, voters approved a measure proposed by Senate Concurrent Resolution No. 4003 (2015), which amended the Constitution of North Dakota to allow the Legislative Assembly to appropriate or transfer the principal balance of the foundation aid stabilization fund in excess of 15 percent of the general fund appropriation for state school aid for education-related purposes.

In 2017, the Legislative Assembly approved Senate Bill No. 2272 and House Bill No. 1155, which amended Section 54-44.1-12 to provide any reductions to the general fund appropriation to the Department of Career and Technical Education for grants to school districts due to allotment also are offset by funding from the foundation aid stabilization fund. In addition, Senate Bill No. 2272 created a new section to Chapter 54-27 to provide for purposes of Section 24 of Article X of the Constitution of North Dakota, education-related purposes means purposes related to public elementary and secondary education and state aid to school districts means general fund appropriations for state school aid, transportation aid, and special education aid in the Department of Public Instruction (DPI), as well as general fund appropriations for career and technical education grants to school districts and area centers in the Department of Career and Technical Education.

The 2017-19 biennium appropriation for integrated formula payments, transportation aid, and special education grants totaled \$2,009,904,163, of which \$1,409,357,258 is provided from the general fund. In addition, general fund appropriations for career and technical education grants to school districts and area centers in the Department of Career and Technical Education totaled \$22,854,100 during the 2017-19 biennium. Based on this level of funding from the general fund during the 2017-19 biennium, the Office of Management and Budget, in its 2019-21 executive budget documents, reported a required reserve balance of \$214,831,704 for the 2019-21 biennium.

The Legislative Assembly, in Senate Bill No. 2013 (2019), appropriated \$111.2 million from the foundation aid stabilization fund for integrated formula payments (\$110 million) and for a one-time state automated reporting system rewrite (\$1.2 million). In addition, the Legislative Assembly, in Senate Bill No. 2265 (2019), provided one-time funding from the foundation aid stabilization fund for music education grants (\$800,000) and rapid enrollment grants in the 1st year of the biennium (\$3 million). The Legislative Assembly also approved Senate Bill No. 2214 (2019) to provide for a transfer of \$75 million from the foundation aid stabilization fund to the school construction assistance revolving loan fund during the 2019-21 biennium. In addition to the transfer, Senate Bill No. 2214 provides legislative intent that the 67th Legislative Assembly appropriate \$110 million from the foundation aid stabilization fund to DPI for providing ongoing funding for state school aid and transfer \$75 million from the foundation aid stabilization fund to the school construction assistance revolving loan fund during the 2021-23 biennium.

In 2019, the Legislative Assembly provided \$2,178,702,429 for integrated formula payments, transportation aid, and special education grants during the 2019-21 biennium, of which \$1,690,938,429 is provided from the general fund. In addition, general fund appropriations for career and technical education grants to school districts and area centers in the Department of Career and Technical Education totaled \$24,887,780 during the 2019-21 biennium. Based on this level of funding from the general fund during the 2019-21 biennium, it is anticipated the required reserve balance in the foundation aid stabilization fund for the 2021-23 biennium will be approximately \$257,373,931, \$42,542,227 more than the reserve required for the 2019-21 biennium.

Elementary and Secondary Education State Aid Formula - Selected Provisions

School District Hold Harmless Calculations - Transition Minimum and Maximum Adjustments

The committee reviewed the use of transition minimum and maximum adjustments in the state school aid formula. When the state school aid formula was implemented during the 2013-15 biennium, hold harmless calculations were included to avoid disrupting school budgets. Districts with transition minimum and maximum adjustments are not considered to be on the state school aid formula.

Transition Minimum Adjustments

Transition minimum adjustments apply to those districts that were above the per student payment rate when the formula was implemented. Districts above the formula amount received a transition minimum to hold the districts harmless under the new formula. Two hold harmless minimum calculations--baseline funding per weighted student unit and total baseline funding dollars--guaranteed school districts would not receive less funding per weighted student unit or in total than the funding received during the 2012-13 school year. The total dollar baseline guaranteed funding regardless of enrollment decline and the per student baseline provided a district could not receive less money per student than the district received in the 2012-13 school year, even if the per student payment from all sources exceeded the formula per student payment. In addition, new students generate the same per student funding as the baseline set during the 2012-13 school year. In 2019, the Legislative Assembly reset school district baseline funding to the 2018-19 school year which, for districts receiving minimum payments, was the same minimum based on the 2012-13 school year. Transition minimum school districts received a 2 percent increase each year of the 2013-15 and 2015-17 bienniums to provide a minimum of 108 percent of the district's baseline funding per weighted student unit multiplied by the district's prior year weighted student units, or 100 percent of the district's baseline funding dollars, whichever is greater. There was no increase in the transition minimum adjustment during the 2017-19 biennium. In 2019, the Legislative Assembly provided a 1 percent increase over a new baseline in the 1st year of the biennium and a 2 percent increase over the new baseline in the 2nd year of the biennium.

The committee reviewed school districts continuing to receive transition minimum payments. During the 2018-19 school year, 86 school districts received a transition minimum adjustment, of which 22 school districts received the total dollar baseline minimum. For the 2019-20 school year, 101 of the 173 school districts operating in the state received a transition minimum adjustment, of which 49 school districts received the total dollar baseline minimum. The number of school districts receiving a transition minimum adjustment is anticipated to decrease from 101 school districts during the 2019-20 school year to 90 school districts during the 2020-21 school year. Recent increases in the integrated formula payment rate may bring some school districts onto the formula or some school districts may gain enough students to move from the total dollar minimum baseline to the formula.

In 2019, the Legislative Assembly approved a plan to bring all transition minimum school districts onto the formula over the next 7 years. Provisions were made to begin phasing out the dollar amount transition minimum by reducing the adjustment by 15 percent each year beginning in the 2021-22 school year. Formula changes also will reduce the amount by which the district's baseline funding per weighted student unit exceeds the payment provided per weighted student unit by 15 percent each year beginning in the 2021-22 school year. Weighted student units over the baseline weighted student units will be reimbursed at the formula payment rate, instead of the baseline funding per weighted student unit rate. It is anticipated the transition minimum adjustment, costing \$49.5 million during the 2019-20 school year, will be eliminated in the 7th year.

The committee recognized smaller school districts do not benefit from the economies of scale of larger school districts and school districts in certain sparsely populated areas of the state are considered essential to avoid unreasonable travel times for students. The committee reviewed information regarding viable school districts and small, but necessary isolated school districts. The state has two definitions for isolated school districts. School districts with a land mass greater than 275 square miles and fewer than 100 students receive an additional weighting factor of .1 for each student. School districts with a land mass greater than 600 square miles and fewer than 50 students receive an additional weighting factor of 1.10. There are 16 districts that qualify for the .1 weighting factor for districts greater than 275 square miles with fewer than 100 students and no districts with over 600 square miles and fewer than 50 students. The National Center for Education Statistics defines remote rural as rural territory more than 25 miles from an urbanized area.

The committee studied various methods of providing additional assistance to school districts anticipating significant state aid formula reductions when transition minimum adjustments are phased out, including a three-tiered sparsity funding system used by South Dakota and potential changes to the school size weighting factors.

The committee received information regarding the effects of adopting a three-tiered funding system in the state school aid formula. The South Dakota sparsity formula provides additional funding for smaller school districts. Criteria for payment includes enrollment, enrollment per square mile, land area, and distance to the nearest high school. To be eligible for payment under the South Dakota model, school districts also must offer grades through high school and levy the maximum property tax. The sparsity formula separates school districts into three categories--enrollment under

83 students, enrollment from 83 to 232 students, and enrollment over 232 students but fewer than 500 students. The committee was informed the formula seemed to generate more funding for school districts with enrollment ranging from 83 to 232 students and smaller payments to districts with fewer than 83 students and more than 232 students. Districts qualifying for sparsity formula funding receive 75 percent of the general state aid per student up to a maximum payment of \$110,000. Because the per student payment is higher in North Dakota than it is in South Dakota, many of the North Dakota districts would reach the maximum payment when applying the same sparsity formula to North Dakota schools.

The committee received information showing under the previous state school aid formula, payment rates were lower and the formula weighting factors had less impact. Whether weighting factors accurately reflect the cost of services was not addressed when the current formula was adopted. Under the current formula school districts' ability to levy property tax is limited and school districts are not able to rely on property tax to supplement state school aid as in the past. Because smaller school districts are less efficient, the school size weighting factor has become more important under the new formula. A substantial number of school districts continue to receive transition minimum adjustments indicating weighting factors may not accurately reflect the cost of educating certain students.

The committee reviewed the number of years it would take school districts receiving transition minimum adjustments to move to the formula. Given no change in enrollment and 2 percent annual increases in the per student payment, it is estimated 42 school districts could transition to the formula within 10 years. The remaining 36 school districts would require between 11 and 42 years to transition to the formula. If annual per student payment rate increases are more than 2 percent, school districts will move onto the formula faster and if the per student payment rate increases are less than 2 percent, school districts will move onto the formula slower.

The committee reviewed an analysis, prepared by DPI, of adjustments to the school size weighting factors for each school district, which would be required to eliminate the transition minimum adjustment and move the district to the formula. The analysis resulted in a wide range of school size weighting factors needed to eliminate the transition minimum adjustment in each school district. After removing outlier districts, the committee reviewed the impact of various sets of new school size weighting factors that could be applied to all school districts. The new school size weighting factors would eliminate or significantly reduce the transition minimum adjustment for most school districts. The new school size weighting factors included in the analyses would increase the state's cost of state school aid. Although the factors would not increase funding for districts with a transition minimum, school districts on the formula would receive additional funding due to increases included in the proposed new sets of school size weighting factors. Even if the transition minimum adjustments for some districts were not eliminated, the adjustments could be reduced with a new set of school size weighting factors. Increasing the school size weighting factors would mitigate some of the negative impact of the phase-out of the transition minimum adjustment scheduled to begin in the 2021-22 school year. The committee was informed some districts are close to being on the formula and the weighting factor adjustment is slight. However, other districts would require a significant increase in the size weighting factor to generate the same funding as the transition minimum adjustment.

The committee analyzed the cost of the various weighting factor scales based on data from the 2019-20 school year, which is based on 2018-19 enrollment. The data was used to analyze the phase-in of proposed sets of school size weighting factors over the same 7-year period the transition minimum will be phased out. Proposed sets of school size weighting factors reviewed by the committee resulted in net savings related to the phasing out of the transition minimum adjustments. The goal of the analysis was to keep the school size weighting factor adjustments cost neutral when compared to the reduction in transition minimum adjustments which is estimated to save the state \$8 million in the 1st year the adjustments are reduced. Reorganized districts benefit from a special factor for 4 years to prevent the school district from losing funding through reorganization or by entering a cooperative agreement. These special factors will require consideration when adjusting the school size weighting factors.

Transition Maximum Adjustments

Transition maximum adjustments apply to those districts that were below the per student payment rate in the 2012-13 base year when the formula was implemented. Prior to the 2019-20 school year, every school district received a baseline funding calculation that included a baseline for total dollars received, a weighted student unit baseline, and a per student payment baseline that were established using 2012-13 school year finance and student data. If a school district had a baseline per student payment rate less than the statutory per student payment rate for the 2013-14 school year, the school district received a transition maximum adjustment to its formula calculation to prevent significant changes in school district budgets due to the implementation of the funding formula change. In 2019, the Legislative Assembly reset school district baseline funding to the 2018-19 school year. However, the legislation did not provide for a phase-out of transition maximum adjustments. For these districts, transition maximum payments were increased 10 percent each year of the 2013-15 and 2015-17 bienniums to 140 percent of the district's baseline funding per weighted student unit multiplied by the district's prior year weighted student units. There was no increase in the transition maximum adjustment during the 2017-19 biennium, and in 2019 the Legislative Assembly increased transition maximum payments by 5 percent in 2019-20 and 5 percent in 2020-21. During the 2019-20 school year, 11 school districts, mostly Native

American schools impacted by federal funds, received a transition maximum adjustment resulting in a reduction to the formula of \$10.5 million compared to the 2013-14 school year when 41 school districts received a transition maximum adjustment totaling \$19.5 million. As increases in the transition maximum adjustment have been approved, school districts have moved onto the formula.

The committee reviewed various methods of phasing out transition maximum adjustments and the cost of bringing all transition maximum school districts onto the formula. Given increases in the transition maximum payments, the length of time to get all school districts onto the formula will vary. If transition maximum school districts were given a percentage increase each year, a few school districts would take significantly longer to transition than the others. One school district, which accounts for more than one-half of the estimated 2020-21 transition maximum adjustment total of \$9.8 million, will take significantly longer to transition to the formula. The length of time to transition these districts also is dependent on the gap between the percentage increase in the transition maximum payment and the percentage increase in the per student payment rate. If the 5 percent annual increase in the transition maximum payment is continued into the 2021-23 biennium, the cost to the state would be approximately \$5.4 million. If transition maximum districts received increases of 7 percent in the 1st year and 8 percent in the 2nd year of the 2021-23 biennium, the cost would be approximately \$7.6 million. If transition maximum districts receive 10 percent annual increases during the 2021-23 biennium, the cost would be approximately \$10.2 million. The number of districts transitioning to the formula with the proposed increases would depend on potential changes to the per student payment.

The committee was informed that to ensure all the school districts are on the formula, the deduction could be adjusted by a percent of the difference over 7 years rather than providing percentage increases each year. A hybrid method of bringing transition maximum school districts onto the formula could include allowing transition maximum school districts to receive the statutory per student rate for new students as opposed to the lower transition rate or by providing a percentage increase, but also requiring the formula gap be reduced by a certain percentage to ensure all districts are transitioned to the formula over 7 years.

Districts on the formula

Districts on the formula, those not subject to minimum or maximum adjustments, were given 3 percent increases each year of the 2013-15 and 2015-17 bienniums as the integrated formula payment was adjusted annually. There was no increase in the integrated formula payment rate during the 2017-19 biennium. The per student payment was increased by 2 percent each year of the 2019-21 biennium, to provide \$9,839 per weighted student unit in the 2019-20 school year and \$10,036 per weighted student unit in the 2020-21 school year.

The total formula amount, adjusted for school district minimum and maximum calculations, the local contribution of 60 mills, and local in lieu of revenue, is reduced further for districts with excess ending fund balances. The amount remaining after deductions is provided by the state. Total state and local funding is divided by total weighted student units to determine state and local funding per weighted student unit. Districts with state and local funding per weighted student unit equal to \$9,839 during the 2019-20 school year are considered on the formula and do not have adjustments for minimum or maximum payments. Districts with state and local funding per weighted student unit above \$9,839 receive transition minimum funding. Districts with state and local funding per weighted student unit below \$9,839 are subject to the transition maximum calculation. The Department of Public Instruction reported, for the 2019-20 school year, 62 of the 173 school districts receiving state school aid were on the formula.

Excess Ending Fund Balance Deduction

The committee reviewed school district ending fund balance limitations. The ending fund balance of a school district is limited under Section 15.1-27-35.3 to 35 percent of its actual expenditures, plus \$50,000 (\$100,000, if the district is in a cooperative agreement for 2 years). State school aid is reduced by the amount by which a school district's ending fund balance exceeds the limit. In addition, Section 15.1-07-29 provides the amount carried over by a school district in the ending fund balance may not exceed 45 percent of the current annual budget for all purposes other than debt retirement and amounts financed from bond sources plus \$20,000. There is no consequence for exceeding the threshold in Section 15.1-07-29.

The committee was informed the ending fund balance limitation is a challenge for transition maximum districts because the districts have little property tax revenue and funding is dependent on federal revenue, the timing of which may be inconsistent. The excess ending fund balance deduction in the state school aid formula also is problematic for school districts that receive significant unpredictable revenue.

A school district may reduce an ending general fund balance by transferring funds from the general fund to the building fund; however, transfers from the building fund to the general fund are restricted. The Coronavirus (COVID-19) pandemic, which closed school buildings in March 2020 and limited school districts to online instruction, resulted in some school districts, mostly smaller districts, being at risk of accruing larger than anticipated ending fund balances as of June 30, 2020. The early spring closure of several small school districts resulted in lower than anticipated expenditures

and higher than anticipated amounts of cash on hand. In addition, ending fund balance limits are lower because the limits are based on a percentage of the lower than anticipated expenditures. The committee determined it was not prudent for school districts to spend funds unnecessarily to meet the limits set in statute when the districts may need the additional funding to address expenses related to the COVID-19 pandemic in the fall. The committee determined it would be appropriate to allow the excess ending fund balance to remain with school districts and not reduce state school aid during the 2020-21 school year.

The committee considered a bill draft to amend Section 57-15-17 to allow school districts, which transferred funding from their general fund to their building fund between March 13, 2020, and July 1, 2020, to avoid an excess fund balance deduction to their state school aid, to return the funding to their general fund, if the transfer is done before June 30, 2021. The exception would be temporary to allow school districts to keep excess funding resulting from school district closures during the COVID-19 pandemic. It is estimated 33 small school districts would benefit from the increased transfer flexibility. The committee determined school boards wanting to transfer excess funds related to the COVID-19 pandemic school facility closures, could identify those funds and the reason for the transfer in school board minutes. If a school district transfers excess funding from its general fund to the building fund before June 30, 2020, the district would not have an excess general fund balance at the end of the 2019-20 school year and would not be subject to a state school aid deduction during the 2020-21 school year. If the bill draft is not approved by the Legislative Assembly in 2021, the funding remains available to the school district in the building fund, where it will not affect the state school aid calculation. If the bill draft is approved by the Legislative Assembly, the school district would be able to return the funding to the general fund without limitation.

School District Mill Levy and In Lieu of Property Tax Revenue and Other Local Revenue

The committee gathered information regarding property tax revenue, in lieu of property tax revenue, and local revenue received by each school district and deducted in the state school aid formula. During the 2018-19 school year, property tax provided 20 percent of state school aid formula payments, in lieu of revenue provided 5 percent of state school aid formula payments, and the state provided the remaining 75 percent of the state school aid formula. The committee received information indicating while state funding has accounted for almost 80 percent of the state school aid formula in the past, higher property values have increased local funding. As property values increased during the 2017-19 biennium, there were no increases to the per student payment rate, resulting in a decrease in the state's share of formula funding to approximately 75 percent. Increases in the per student payment rate, approved in 2019, could increase the state's share of the formula. Federal funding and other sources, including a miscellaneous levy and other state grants, are not considered in the formula. When these additional sources of revenue are considered, the state's contribution to K-12 funding is approximately 60 percent. The funding sources vary significantly by district and the statewide percentage of 75 percent is not accurate in districts that receive significant amounts of local revenue. Local in lieu of revenue contributions are deducted in the state school aid formula; however, are not considered when determining the 60-mill requirement. The 60-mill deduction requirement and local in lieu of revenue deductions increase the percentage of local contribution in the state school aid formula.

The committee received a report regarding the general fund levy and value of one-mill levy in each school district in 2018 and the total 2018 taxable valuation, including taxable valuation per student. The value of one mill is equal to the taxable valuation of the school district multiplied by .001. In 2018, the value of one mill varied from just over \$3 at the Grand Forks Air Force Base to \$481,058 in Bismarck, the statewide average value of a mill levy was \$26,700, and the median value is \$11,500. The range of revenue generated by one-mill levy in school districts across the state poses funding challenges. According to the report, because mill levies raise more funding in property rich districts, those districts may be able to raise funding for school construction at a lower mill rate than property poor districts.

Annual increases in property tax are limited to 12 percent of prior tax or the amount of new growth, whichever is greater. Although new property qualifying as tax exempt is included in the new growth of the county in the year it is put into service, other taxable properties are paying the amounts related to the tax exempt property until it is taxed. The committee reviewed the maximum levy worksheet for taxable year 2019 for school districts' general fund, including example worksheets and worksheet instructions. Calculation 1 on the worksheet determines if the prior year assessment plus 12 percent, or 70 mills applied to the current taxable valuation, yields the higher maximum mill levy. Calculation 2 on the worksheet determines the new property value. Even with large commercial properties added to the tax base, the 12 percent increase calculation typically provides for the larger allowable increase. As a result, calculation 1 on the maximum levy worksheet is applied most commonly, and calculation 2 is rarely used even in the western part of the state where there has been rapid growth. New property additions would have to be substantial for the tax increase related to the new property to exceed the 12 percent increase limitation. The committee was informed there was discussion before the 2019 legislative session regarding whether new property should be added to the 12 percent increase when determining the property tax increase limitation. Counties have been collecting data on new property, and if approved by the Legislative Assembly, the Tax Department could build the necessary changes into the maximum mill levy worksheet to apply the 12 percent increase limitation only to existing property. If school districts are allowed to exclude

new property when determining the 12 percent limit on property tax increases, the same exclusion will need to be provided when calculating the local property tax deduction in the state school aid formula.

An adjustment certified by DPI has been added to the 2019 worksheet to account for the phase-in of the 60-mill deduction from the state school aid formula. This adjustment is necessary for districts unable to levy 60 mills because of the 12 percent limitation on annual increases in both taxation and the state school aid formula deduction. If a school district is not on the formula because it does not levy 60 mills, state funding is provided to meet the total funding determined by the formula. The 2019 Legislative Assembly approved a provision to phase in the 60-mill deduction for all districts starting in the 2020-21 school year. The property tax deduction for districts deducting fewer than 60 mills will be increased by 10 percent of the difference in the first 2 years of the phase-in period and 20 percent of the difference in each of the remaining 4 years of the phase-in period. The committee received information regarding the 60-mill local property tax contribution included in the state school aid formula and the fiscal impact of changes to the 60-mill contribution for districts with a deduction below 60 mills. The analysis includes districts deducting fewer than 60 mills during the 2019-20 school year and includes the estimated property tax deduction each year of the phase-in period. Based on 2019-20 property valuations, the cumulative increase in the deduction for all districts currently deducting fewer than 60 mills would be a savings to the state of an estimated \$22.5 million. The difference between current deductions for local property tax and deductions at 60 mills could be higher as property values increase in future years resulting in additional savings to the state. The volatility of property values will make it difficult to budget for the 60-mill local property tax deduction in the formula.

The committee also reviewed the impact of the minimum local effort on state aid which requires if a school district's taxable valuation per student is less than 20 percent of the state average valuation per student, the Superintendent of Public Instruction, for purposes of determining state aid, must deduct an amount equal to 60 mills times 20 percent of the state average valuation per student multiplied by the number of weighted student units in the district. The committee received testimony that the minimum local effort deduction may result in further reductions in state school aid for certain school districts deducting the transition maximum adjustment. Because the local effort is based on the state average taxable valuation, 60 mills is deducted in the formula even though the "property poor" district does not collect the additional property tax funding. The 12 percent limit on increases in the deduction also applies when the taxable valuation is imputed.

Status of State School Aid - 2019-21 Biennium

The committee received reports from DPI regarding student enrollment and the status of funding for state school aid for the 2019-21 biennium.

In 2019, DPI estimated integrated formula payments during the 2019-21 biennium based on 2019-20 school year average daily membership (ADM) of 112,630 students and 2020-21 school year ADM of 116,634 students. The department estimated state school aid integrated formula payments will total \$2,714,393,010 during the 2019-21 biennium, of which \$537,999,973 was estimated to be provided through local property tax contributions, \$100,049,326 was estimated to be provided through local in lieu of taxes and revenue contributions, and \$2,076,343,711 was estimated to be provided by the state. In addition to the state's share of state school aid integrated formula payments, the appropriation for 2019-21 biennium integrated formula payments included funding for costs related to child placement, regional education association grants, the gifted and talented program, estimated cross-border tuition payments to South Dakota, and budget variances. The department estimated these expenditures and budget variances would total \$21,858,718, for a total of \$2,098,202,429 charged to the integrated payment line item for the 2019-21 biennium. Based on total integrated formula payments, the state's share of funding for state school aid was expected to shift from 54 percent in 2009 to 77 percent during the 2019-20 school year.

The committee received updated 2019-21 integrated formula payment estimates from DPI. The Department of Public Instruction estimates state school aid for the 2019-20 school year, based on 2019-20 school year ADM of 112,165 students, will total \$1.314 billion, of which \$263.9 million, or 20 percent, is provided by local property tax, \$58.3 million, or 4.4 percent, is provided by local in lieu of revenue, and \$991.6 million, or 75.2 percent, is provided by the state through integrated formula payments. Because state school aid is paid based on the prior year enrollment, DPI estimates for the 2020-21 school year are based on 2019 fall enrollment. State school aid for the 2020-21 school year, based on 2020-21 school year ADM of 114,788 students is estimated to total \$1.387 billion; of which \$279.6 million, or 20.2 percent, is estimated to be provided by local property tax; \$55 million, or 4 percent, is estimated to be provided by local in lieu of revenue; and \$1,052.3 million, or 75.8 percent, is estimated to be provided by the state through integrated formula payments. The local property tax contribution to 2020-21 state school aid is known because it is based on 2019 property values; however, the contribution from in lieu of revenue will not be known until August or September 2020. Lower than anticipated enrollment, increased contributions from in lieu of property taxes, and a large ending fund balance deduction resulted in budget savings of \$19.5 million during the 2019-20 school year and based on preliminary estimates, state school aid payments for the 2nd year of the biennium are anticipated to be \$13.3 million less than budgeted.

Projected State School Aid - 2021-23 Biennium

Cost to Continue

The committee reviewed a preliminary estimate of funding required to continue current state school aid integrated formula payments during the 2021-23 biennium. The report, prepared by DPI, was based on:

- ADM projected using a 5-year cohort survival routine with 2019-20 fall enrollment as the base year;
- Taxable valuation for fiscal year 2020-21 based on taxable year 2019 and taxable valuations for 2021-22 and 2022-23 projected based on a 2-year average increase with a maximum increase of 8 percent and a minimum increase of 0 percent;
- The implementation of delayed formula changes approved in 2019, including on-time funding, the phase in of the 60-mill deduction and the phase out of transition minimum adjustments; and
- Other statistical data and weighting factors based on data supporting the 2019-20 payment year.

The Department of Public Instruction is projecting a 2.2 percent increase in ADM each year of the 2021-23 biennium and estimates the cost-to-continue integrated formula payments for an estimated 10,151 additional students will total \$131.3 million. The cost of enrollment increases is partially offset by savings related to reductions in transition minimum adjustments (\$20.9 million) and savings related to adjustments to school districts' property tax contribution to bring all school districts to a 60-mill contribution (\$12.7 million). Projections do not include the impact of COVID-19 in March 2020. Of this increase, an estimated \$85.8 million will be provided locally through estimated increases in property tax contributions and in lieu of property tax revenue. The remaining \$45.5 million of estimated cost-to-continue integrated formula payments will be provided by the state. Funding available from the common schools trust fund is estimated to increase by \$52 million and may offset the funding required to continue state aid.

Committee Recommendation

The committee recommends a bill draft to allow a school district to temporarily transfer excess funds, accruing as a result of the COVID-19 pandemic, between the general fund and the building fund of the school district.

ELEMENTARY AND SECONDARY EDUCATION TRANSPORTATION STUDY

Senate Bill No. 2013 directed a study of school transportation, including district routes, expenditures, reimbursements, and possible efficiencies.

Background

The 1957 Legislative Assembly approved a provision for transportation reimbursement that ranged from 25 cents per day for students living at least two miles from school to 80 cents per day for students living at least six miles from school and provided an additional 10 cents per day for each one-half mile over six miles. In the 1980s state transportation aid was paid to school districts according to the number of miles traveled, the size of schoolbuses being operated, and the number of students transported. State transportation aid steadily increased as a percentage of all transportation costs incurred by school districts. By the 1985-86 school year, state transportation aid payments totaled \$20,189,000 or 88.6 percent of all school district transportation expenditures. There was a disparity in the percentage of transportation costs reimbursed to school districts. In general, rural school districts with fewer students and longer routes received the highest ratio of state aid to actual costs. Many such districts received state aid in excess of 100 percent of their actual costs. The largest school districts with large student populations and relatively short bus routes received the lowest ratio of state aid to actual transportation costs. These districts typically received state aid in amounts varying between 40 and 75 percent of their transportation costs.

An issue that surfaced during the 1985 legislative session concerned certain school districts that charged for the transportation of rural school children. State law did not require school districts, other than those that have been reorganized, to provide transportation to schools. Therefore, in school districts that had not been reorganized, certain costs of school transportation were charged to the parents of children who were being bused to school. This practice was challenged by a Bismarck Public School District patron in *Bismarck Public Schools v. David Walker*, 370 N.W.2d 565 (N.D. 1986). In that case, the North Dakota Supreme Court refused to determine whether there is a state constitutional right to free transportation to schools because it found the Bismarck Public School District patrons had signed a contract agreeing to pay transportation costs and thereby waived any rights to receive that transportation free of charge. This practice was challenged by a Dickinson Public School District patron in *Kadrmas v. Dickinson Public Schools*, 402 N.W.2d 897 (N.D. 1987). The assertion was that Section 15-34.2-06.1, which allowed nonreorganized school districts to charge for transportation, violated the North Dakota constitutional provision providing for a uniform system of free public schools. The North Dakota Supreme Court held the constitutional provision mandating a uniform system of free public schools does not require the state or school districts to provide free transportation for students to and from school. On appeal, the United States Supreme Court affirmed the constitutionality of the statute.

The transportation formula continued to be criticized because there was a wide disparity in the percentage of transportation costs reimbursed to school districts. The range in cost per mile was due to various factors. For example, some school districts held costs down by hiring mechanics, buying used buses and used or rebuilt parts, paying immediate attention to maintenance, paying drivers to use their own cars, and planning and limiting routes. Other variables that affect the cost of transportation from district to district included types of roads, replacement schedules for buses, and salaries of bus drivers. In addition, some school districts receiving over 100 percent of their transportation costs were not factoring in administrative costs or depreciation as part of their transportation costs.

The Legislative Assembly approved House Bill No. 1003 (1993), the appropriations bill for the Superintendent of Public Instruction. This bill became the principal 1993 education funding enactment and capped state transportation payments at 100 percent of transportation costs for the 1st year of the 1993-95 biennium and at 90 percent for the 2nd year of the biennium. The bill provided any savings resulting from imposition of the 90 percent cap during the 2nd year of the biennium be used by the Superintendent to increase the per student transportation payments. The Legislative Assembly, in Section 9 of the bill, provided \$100,000 from the general fund and \$60,000 from other funds to DPI for the purpose of studying school transportation services during the 1993-95 biennium. The department was to develop, by December 1, 1994, a school transportation system database that included the network of usable roads, school district boundaries, and the location of all schools and related facilities. The department was to negotiate with North Dakota State University to utilize any available information the university had regarding the study.

The 1995-96 interim Education Finance Committee found that while transportation payments were limited to 90 percent of a district's current transportation operating cost, plus the 8-year average cost of transportation equipment, districts affected by the cap complained that reported transportation costs were not uniform among the districts. Superintendents from smaller districts said they spent considerable time on busing--time not reflected in the cost calculations. Other districts charged costs to other users of transportation services on an ability-to-pay basis. For example, an extracurricular program not having a budget for transportation may be subsidized by the regular transportation program in one district and not reported in another. Recognizing these inconsistencies, the 1995 Legislative Assembly directed the Superintendent of Public Instruction to develop and require school districts to use a uniform cost accounting system for the transportation reimbursement program. The document, *Guidelines for Student Transportation Costs*, was issued in April 1996, and addressed contracted services, bus drivers, fuel, family transportation, repairs, maintenance, insurance, equipment costs, and the allocation of costs related to the district superintendent, business office, and school board.

In 2001, the Legislative Assembly moved Century Code sections related to K-12 education, including the transportation funding formula, from Title 15 to Title 15.1 during a rewrite of K-12 education provisions. These changes were not effective until after June 30, 2001. As a result, the formula for transportation grant distribution as of June 30, 2001, would be state statute as it existed after the 1999 session. Provisions, existing in 1999, regarding transportation aid included sections related to definitions, transportation aid calculations, transportation aid for vocational education and special education, certification of information by the school district business managers, determination and payment of transportation aid, including a 90 percent limitation, and distribution of transportation payments in the event of school district closure.

The 2001-02 interim Education Committee was informed data envelopment analysis, which involves an analysis of comparable operating units, could provide an alternate method for measuring and encouraging efficiency, as well as provide a basis for funding transportation. All school districts in the state would be divided into categories or peer groups. Once the categories or groups are established, the next step would be to standardize the factors. School district transportation factors may include costs for administrators, drivers, mechanics, repairs, and fuel. Through use of a mathematical formula, variables would be analyzed to determine the relative efficiency of each district. Each district is compared to the other districts in its category or group. If funding is made a part of the formula, the funding is then based on the operational cost of the most efficient district in the category. In addition to providing a basis for funding, it also is able to assist school districts in reconfiguring transportation routes so that the greatest possible degree of efficiency may be attained. A data envelopment analysis project had been in a stage of partial completion for a number of years. An initial appropriation of \$50,000 was made for the project during the 1997 legislative session, but not supplemented in 1999 or 2001.

The 2003 Legislative Assembly repealed Century Code sections related to payments for school district transportation of students, payments for school district transportation of special education students, payments for school district transportation of vocational and technical education students, certification of information for transportation payments, distribution of transportation payments in the school closure, and state transportation payments to school districts. The Legislative Assembly, in Section 31 of Senate Bill No. 2421 (2003), provided DPI distribute transportation aid to each school district in the state in an amount equal to the transportation aid payments received by the school district during the 2001-03 biennium. In addition, the Legislative Assembly approved Senate Bill No. 2032 (2003) to appropriate \$50,000 to the Superintendent of Public Instruction for the completion of the data envelopment analysis project.

The 2003-04 interim Education Committee once again reviewed data envelopment analysis as an alternate method for measuring and encouraging efficiency, as well as providing a basis for funding. The interim committee recommended House Bill No. 1033 (2005) to require the Superintendent of Public Instruction to use data envelopment analysis as the basis for calculating school district transportation payments; however, the bill was not approved by the Legislative Assembly. Instead, the Legislative Assembly, in Section 25 of House Bill No. 1154 (2005), required that for the 1st year of the 2005-07 biennium, DPI apply the transportation formula as it existed on June 30, 2001, except provide reimbursement for in city mileage at the rate of 50 cents for schoolbuses having a capacity of 10 or more students and reimbursement for vehicles having a capacity of 9 or fewer students and transporting students who live outside the incorporated limits of a city at the rate of 40 cents per mile. The Superintendent was to use the latest available student counts in determining transportation payments. During the 2nd year of the biennium, the Superintendent was to distribute the same amount to each school district as the district received during the 1st year of the biennium.

The 2007 Legislative Assembly continued to provide funding based on the state transportation formula, as it existed on June 30, 2001, during the 1st year of the biennium and to provide funding for the 2nd year of the biennium be distributed to each school district in the same amount the district received for the 1st year of the biennium. Reimbursement rates, in Section 48 of Senate Bill No. 2200 (2007), were adjusted to provide 51.5 cents per mile for schoolbuses having a capacity of 10 or more passengers and transporting students within city limits and 40 cents per mile for vehicles having a capacity of 9 or fewer passengers and transporting students in rural areas. A rate of 73.5 cents per mile for schoolbuses having a capacity of 10 or more passengers and transporting students in rural areas was added during the 2007-09 biennium.

The 2009 Legislative Assembly provided \$43.5 million from the general fund for transportation aid, \$10 million more than the 2007-09 biennium. Section 54 of House Bill No. 1400 (2009) provided DPI was to distribute transportation aid for the 2009-11 biennium based on the state transportation formula as it existed on June 30, 2001, except DPI was to provide reimbursement at the rate of 92 cents per mile for schoolbuses having a capacity of 10 or more passengers and 44 cents per mile for vehicles having a capacity of 9 or fewer passengers. The 2009 Legislative Assembly also adjusted the formula to resume funding based on the number of students transported. A reimbursement of 24 cents per student for each one-way trip was added to the transportation aid formula. Beginning with the 2009-11 biennium, there is no longer a distinction between transporting students in rural areas and transporting students within city limits and funding during the 2nd year of the biennium is distributed based on the formula, instead of funding provided during the 1st year of the biennium.

The 2011 Legislative Assembly provided \$48.5 million from the general fund for transportation aid. This level of funding was the same as the 2009-11 biennium, which included a contingent \$5 million appropriation from the general fund for supplemental transportation aid payments. The appropriation was contingent on the Office of Management and Budget projecting during the 2009-11 biennium that the June 30, 2011, ending balance of the state general fund will be at least \$30 million more than estimated by the 2009 Legislative Assembly. The February 2011 executive revenue forecast estimated the conditions would be met and the contingent supplemental transportation aid payments would be made. Reimbursement for two types of family transportation were added in 2011 and Section 36 of Senate Bill No. 2150 (2011) required DPI to distribute transportation aid for the 2011-13 biennium based on the state transportation formula as it existed on June 30, 2001, except DPI is to provide reimbursement at the rate of \$1.03 per mile for schoolbuses having a capacity of 10 or more passengers; 46 cents per mile for vehicles having a capacity of 9 or fewer passengers; 46 cents per mile round trip for family transportation of a student with a disability whose individualized education program plan requires that the student attend a school outside the student's school district of residence; 46 cents per mile one way for family transportation if the student lives more than two miles from the public school the student attends; and 26 cents per student for each one-way trip.

Except for reimbursement rate increases, the transportation formula continued, based on the state transportation formula as it existed on June 30, 2001, for the 2013-15 and 2015-17 bienniums. The formula, still based on the state transportation formula as it existed on June 30, 2001, continued during the 2017-19 biennium; however, reimbursement rates and funding were reduced.

The 2019 Legislative Assembly reviewed funding for transportation aid. In testimony provided to the Legislative Assembly, DPI reported statewide, transportation aid provides approximately 50 percent of the cost of transportation to school districts. Members of the House Appropriations Committee expressed concern regarding the formula and multiple reimbursement for the same miles on certain routes when districts cross paths and family transportation is reimbursed. Concern also was expressed regarding the transportation formula subsidizing districts transporting students from other districts and the inability to verify routes and reimbursement. The Legislative Assembly provided \$56.5 million from the general fund for transportation aid during the 2019-21 biennium. This level of funding is \$1.1 million more than 2017-19 biennium funding of \$55.4 million from the general fund and will allow reimbursement rates to remain the same as the 2017-19 biennium. Section 10 of Senate Bill No. 2013 (2019) requires DPI to distribute transportation aid for the 2019-21 biennium based on the state transportation formula as it existed on June 30, 2001, except DPI is to provide reimbursement at the rate of \$1.11 per mile for schoolbuses having a capacity of 10 or more passengers; 52 cents per

mile for vehicles having a capacity of 9 or fewer passengers; 50 cents per mile round trip for family transportation of a student with a disability whose individualized education program plan requires that the student attend a school outside the student's school district of residence; 50 cents per mile one way for family transportation if the student lives more than two miles from the public school the student attends; and 30 cents per student for each one-way trip.

Transportation Demand

The committee reviewed a summary, based on information published by DPI, of transportation data from the 1992-93 school year through the 2017-18 school year, including number of students, transportation cost, change in annual cost, state payments, percent of state support, cost per student, cost per mile, total annual mileage, fall enrollment, number of operating school districts, and percent of all state support. The number of students transported ranged from a high of 49,117 students during the 1998-99 school year to a low of 37,257 students during the 2004-05 school year. During the 2017-18 school year, 43,613 students were transported. From the 1992-93 school year through the 2017-18 school year, the number of students transported decreased by 1 percent. In addition to a reduction in the number of routes, there was a 10 percent reduction in annual miles traveled during the same time period and the number of school districts declined from 257 to 178. The local cost of transportation increased to \$65.7 million during the 2017-18 school year. A shortage of qualified bus drivers has forced both school districts and contractors to increase wages and benefits. During the 2017-18 school year, the average transportation cost per student was \$1,507 and the average cost per mile was \$2.95 per mile. During the 2017-18 school year, state payments to school districts for transportation totaled \$26.8 million, or 40.8 percent of the cost of transportation. While the percentage of state support for all programs, including per student payments, transportation, career and technical education, special education and others, has increased, the percentage of state support for transportation has been decreasing.

The committee received information regarding transportation challenges, including the cost of buses and bus repair, bus driver shortages, wages and benefits increases, fluctuating fuel prices, and recent changes to certification requirements.

Transportation Aid Distribution

The committee was informed school districts are required to submit two transportation reports by June 30 each year. The vehicle inventory report includes information regarding license number, capacity, year manufactured, year purchased, vehicle type, ownership, and vehicle purpose--activity, regular, or standby. The routes report provides information regarding total miles, total rides, maximum ride time, primary vehicle, and route type--rural, city, or special education. Schools are reimbursed for several types of routes, including rural, in-city, family to school, family to bus, special education, vocational education, extended year, public transit, and other routes, including between schools. Elementary and K-8 districts are reimbursed for transportation to high schools outside their districts. School districts are asked to report miles for activities, but the miles are not reimbursed.

The Department of Public Instruction provides reimbursement based on the rates in Senate Bill No. 2013 (2019). Reimbursement is limited to 90 percent of general fund transportation expenditures less equipment cost, plus the 8-year average of transportation equipment expenditures and an allocated percentage of the expenses of the school board, superintendent, and business manager offices. The allocation is based on the percentage of general fund transportation expenditures to total general fund budget. Although reimbursement rates no longer distinguish between rural and in-city routes, the department collects information regarding whether the route is rural or in-city. The department does not collect data regarding open enrollment rides. Transportation for open enrollment students is not identified and is reimbursed with resident students. The department does not audit the information provided by school districts. School districts and contractors are expected to determine the number of students transported each day. Transportation grants are distributed on the same schedule as the state school aid payments. Payment for school transportation is based on data from the previous year. Transportation payments for the 2018-19 school year were based on 2017-18 rides and ranged from a low of \$6,352 paid to Earl 18 Public School to a high of \$1.2 million paid to Bismarck Public Schools. Separate payments also are made to numerous special education units for qualified transportation services. The committee reviewed guidelines available in DPI's accounting manual regarding student transportation services-related costs.

The committee received information regarding a performance audit of transportation grant reimbursement by DPI. An audit report issued by the State Auditor in September 2020 included a finding relating to lack of guidance and monitoring for school district transportation reimbursement. The department indicated that although the department does not have staff resources to perform a detailed review of each school district transportation report, the department does some comparisons to prior years and communicates with school districts to resolve questions. The Department of Public Instruction does not have the authority to reject a request for reimbursement, but there is a penalty for fraudulent reporting. The department will update guidance regarding miles and rides, review processes, and document correspondence with districts.

The committee compared transportation reimbursement in North Dakota to transportation funding provided by South Dakota. The committee received information showing South Dakota does not provide funding for student transportation,

nor is there a weighting factor associated with transportation in the South Dakota general aid funding formula. South Dakota provides additional funding for districts that meet the state's definition of a sparse school district. In South Dakota, if access to bus service is not furnished by the school district to which the student is assigned, the student is entitled to a transportation or a room and board allowance which is provided by the school district. In South Dakota, families are reimbursed by school districts for distances traveled in excess of 5 miles each way. In North Dakota, travel in excess of 2 miles each way is reimbursed by the school district and may be submitted for state reimbursement. While North Dakota requires family reimbursement be made to a family member, South Dakota allows for reimbursement when families redishare.

The committee received information regarding transportation grants provided during the 1st year of the 2019-21 biennium; the impact of the COVID-19 pandemic on transportation funding during the 2nd year of the 2019-21 biennium; and an estimate of the cost-to-continue transportation aid during the 2021-23 biennium.

During the 2019-20 school year, \$28.5 million, or 50.4 percent of the \$56.5 million appropriation for transportation grants was distributed to school districts based on miles and ridership reported by school districts for the 2018-19 school year. Beginning on March 16, 2020, due to the COVID-19 pandemic, buses were not used to transport students to and from school for the remainder of the 2019-20 school year. The Department of Public Instruction informed districts they would not be reimbursed for meal delivery costs through the state transportation grant program. Although funding from the federal Elementary and Secondary School Emergency Relief Fund could be used to offset the cost of meal delivery, it would not be reimbursed on the same basis as traditional transportation grants.

The committee was informed transportation grant payments for the 2020-21 school year will be impacted by the COVID-19 pandemic because the payments will be based on lower miles and rides reported by school districts for the 2019-20 school year. The Department of Public Instruction is reviewing transportation reports submitted for the 2019-20 school year and the impact on transportation grants during the 2020-21 school year. Preliminary information submitted through the state automated reporting system application indicates transportation grant payments will total approximately \$21.7 million for the 2020-21 school year, 24 percent less than 2019-20 school year transportation grants. Based on this estimate, approximately \$6.3 million of the transportation grant appropriation would remain unspent.

The Department of Public Instruction's preliminary estimate of the cost-to-continue transportation grant payments for the 2021-23 biennium is approximately \$57 million (2 years at \$28.5 million per year). However, reimbursement for miles and ridership during the 1st year of the 2021-23 biennium will be impacted by distance and hybrid schedules, social distancing guidance, and family safety concerns impacting transportation during the 2020-21 school year.

The committee considered whether it is appropriate to reimburse school districts for the transportation of students participating in open enrollment and tuition waiver agreements. To prohibit reimbursement for these students, the committee determined legislation would be needed to establish the transportation formula which does not currently exist in statute.

The committee considered a bill draft to codify student transportation aid payment sections as the provisions existed on June 30, 2001, update provisions to reflect current practices and reimbursement rates included in Section 10 of Senate Bill No. 2013 (2019), and prohibit school districts from receiving transportation reimbursement for certain students participating in open enrollment and tuition waiver agreements. If the bill draft is approved by the Legislative Assembly, future changes to transportation reimbursement rates would require an amendment to the Century Code.

Committee Recommendation

The committee recommends a bill draft to codify student transportation aid payment sections as the provisions existed on June 30, 2001, update provisions to reflect current practices and reimbursement rates, and prohibit school districts from receiving transportation reimbursement for certain students participating in open enrollment and tuition waiver agreements.

OTHER COMMITTEE RESPONSIBILITIES

The committee received, pursuant to Section 15.1-02-09, a report from the Superintendent of Public Instruction regarding the financial condition of schools. The annual report is published in February for the preceding school year and includes information regarding mill levy rates, taxable valuation, revenues, expenditures, student enrollment, ADM, average cost per student, teachers, average salaries, and number of graduates.

The committee received, pursuant to Section 15.1-02-13, a report from the Superintendent of Public Instruction regarding school district employee compensation. The report is based on data reported by school districts for school years ending in June of 2017, 2018, and 2019. The report includes teachers, administrators, and other district employees, but does not include part-time teachers. The department collects compensation information for all school districts; however, for comparison purposes the report only includes full-time licensed school district employees who

have worked more than 172 days. Although the department collects the information, districts that have transitioned to 4-day weeks are not included in the report. As more districts transition from days to hours, the department will evaluate how the data for those districts can be reported. Administrators include principals, superintendents, directors, assistant principals, assistant or deputy superintendents, and assistant directors. The average base salary for administrators increased from \$96,372 to \$99,337, or 3.07 percent, from 2017 to 2019. Teachers include coordinators, library media specialists, student personnel, school counselors, school psychologists, speech and language pathologists, supervisors, instructional programmers, special education consultants, and tutors in training. The average base salary for teachers increased 1.68 percent, from \$53,261 to \$54,154, over the same period. The number of administrators statewide increased from 625 in 2017 to 643 in 2019, while the number of teachers increased from 8,936 to 9,176 during the same period.

OTHER REPORTS AND INFORMATION RECEIVED BY THE COMMITTEE

In addition to the committee's other responsibilities, the committee received other reports, including reports from:

- DPI regarding special education contract costs and challenges of the special education contract system and student placement including challenges related to determining financial responsibility, unaccompanied refugee minors, calculating the actual cost of education per student, timely notification of placements and contracts by agencies still using paper forms, and residency determination, including the definition of custodial parent and legal guardian;
- North Dakota Council of Educational Leaders regarding K-12 tuition calculations, open enrollment, tuition agreements, agency-placed students, graded elementary and rural districts, air base tuition, and the Wyoming model for students educated outside their resident district;
- DPI regarding a federal Every Student Succeeds Act report on per student expenditures by school district, including cost information by building, available on the department's website;
- DPI regarding the impact of funding made available to school districts through the federal Coronavirus Aid, Relief, and Economic Security (CARES) Act and distributed on a reimbursement basis;
- Superintendent of Public Instruction regarding a study, assigned to DPI, the Indian Affairs Commission, and the Kindergarten Through Grade Twelve Education Coordination Council pursuant to Section 24 of Senate Bill No. 2265 (2019), regarding the effect of impact aid on the funding formula of reservation schools;
- North Dakota Center for Distance Education regarding the impact of the COVID-19 pandemic on enrollments;
- Department of Career and Technical Education regarding the impact of the COVID-19 pandemic on enrollments;
- DPI regarding the impact of on-time funding factors on the state school aid formula; and
- DPI regarding the impact of distance learning on school districts' ability to fulfill school calendar hour requirements and the impact of distance learning on school districts' state school aid calculation.