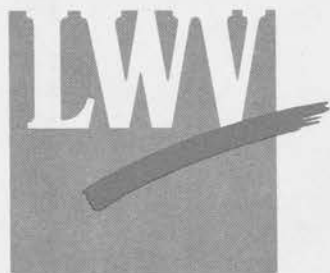




## League of Women Voters of Minnesota Records

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# FACTS and ISSUES

## HOW WE PAY FOR OUR SCHOOLS: *Financing Education in Minnesota*

### THE HISTORY

The social consciousness of the 1960s generated a movement to redress unequal educational opportunities in this country.

To this purpose, the governor of Minnesota and its legislature initiated the 1971 Omnibus Tax Act, popularly known as the "Minnesota Miracle." Its objective was to bring the Minnesota state school financing system more into spirit with its constitutional mandate "to establish a general and uniform system" of education. Its main goal sought to equalize the tax effort of property owners while promoting greater equalization of school revenues throughout the state.

Many amendments to the 1971 Omnibus Tax Act have attempted to equalize remaining differences between districts.

What has resulted is that the Minnesota basic education funding system is a complex quagmire that provokes more questions than answers. Generally speaking, the funding system causes intelligent persons to walk away baffled, content to abandon the muddle to the experts.

### THE TASK

The League of Women Voters of Minnesota Education Fund research committee (LWVMNEF) in this "Facts and Issues" will examine the 1990-91 Basic Education Funding Formula, its revenue sources and their distribution. It will attempt to provide a comprehensible simplification of a complex system and a solid foundation of public information.

The shortcomings and strengths of this funding system will be addressed in a second "Facts and Issues," Winter, 1990-91. Here the LWVMNEF committee will present questions on current funding and query the positive and negative characteristics of proposals for financing public education through grade 12 in Minnesota.

### THE PRESENT

Today, in Minnesota and across the nation, the social consciousness of the 1960s and the questioning of educational inequalities persists. It is evident from California to New Jersey. Most recently in May 1989, the Texas Supreme Court ruled its state's method of school finance unconstitutional. Wide gaps between the richest and poorest school districts violated the state's need for efficient delivery of education. By May, 1990 the Texas legislature must present a new school-financing plan (*Time*, October 16, 1989, p. 48).

In April 1990, Kentucky established new statutes that set a statewide \$2,900 minimum per pupil spending level. Under its old system, spending levels in that state ranged from \$1,800 to \$4,200 depending on a district's wealth (*Star Tribune*, April 12, 1990, page 2B).

### IN SUMMARY: FUNDING EDUCATION

Tax dollars become revenue to pay for Minnesota state agencies, public education through grade 12 and higher education, health and welfare, state assistance to local governments and other programs.

The sources of these tax dollars are state sales taxes, personal and corporate income taxes and local property taxes. All sources, other than local property taxes, when distributed to school districts are called state appropriations, i.e., state aids.

The Minnesota public education system provides for pre-school and family education in addition to kindergarten through grade 12. For handicapped children public education extends from birth to age 21.

Public education through grade 12 is funded by a combination of dollars from local property taxes and state aids.

The Basic Education Funding Formula determines what proportion of a public school district's revenue dollars comes from state aid versus property taxes.

This Funding Formula sets a base amount of dollars that the state guarantees each school district can spend per pupil unit, i.e. its basic allowance per pupil unit. This allowance is the largest source of revenue for Minnesota school districts.

To better assure equal opportunity to all students in the state, other components of financial aid are paid to some districts in addition to the Basic Allowance in an attempt to compensate for some specific cost differences between districts.

For additional funding, school districts have the ability to tax by passing local bond and levy referendums thereby raising local property taxes.

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While Minnesota addressed such spending inequalities with the 1971 "Minnesota Miracle," the questioning of funding equalities continues. Indeed, questions about the "Minnesota Miracle" and equitable funding of state-wide public education through grade 12 are now back in the courts.

In Minnesota there is still general agreement with the concept of providing equal educational opportunity to all students regardless of the property values of the districts in which they reside, but there is disagreement about what constitutes equality and how equality might be achieved.



## WHAT ARE THE SOURCES OF MONEY FOR PUBLIC EDUCATION?

The state of Minnesota taxes its residents to gather the majority of the revenue dollars to fund its programs, institutions, state agencies and personnel.

Each county acting with and for the state collects property taxes assessed by school districts, municipalities, cities and counties.

Public education is financed by tax dollars from a combination of two sources: *State Appropriations* (dollars from state income and state sales taxes, etc. set aside for or appropriated for education) and *Local Property Taxes*.

### STATE APPROPRIATION FOR EDUCATION

The State of Minnesota collects tax dollars for its general fund revenue (from which public education through grade 12 is funded) plus 40 to 50 other dedicated funds including the Highway Fund or the Game and Fish Fund.

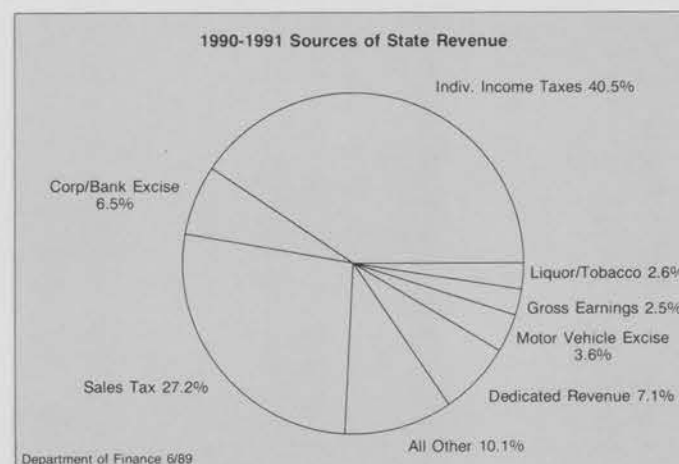
The state budgets for a two year period called a biennium. For the 1990-91 biennium the state will receive about 40.5% of its general fund revenue from personal income tax, 27.2% from sales taxes on items defined as taxable by the legislature, plus collecting 6.5% in corporate and bank excise taxes. Another 25.8% of its general fund revenue money will come from a combination of gross earnings taxes (for example, taxes on insurance and telephone/telegraph companies), motor vehicle excise taxes, certain "dedicated" monies and other areas.

All of these state tax sources are later distributed as "state appropriations." Dollars are appropriated to public education through grade 12.

In the 1988-89 school year, spending for elementary-secondary education came to 32.9% of the state's whole expenditure budget (Marx, p. 15). This includes tax credits which have been deducted from property taxes but restored to the school district with state aid.

Tax credits are a source of education dollars because money from sales taxes and personal income taxes is paid to school districts, counties, cities, etc. to make up for property tax credits/relief.

In the 1990-91 school year the state will set aside 28.1% of the dollars collected in state revenues for aid to school districts. Note the difference between the two years. It is not necessarily a lesser amount. Instead the 4.8% difference does not include tax relief/credits. The amount of tax relief/credits set aside for education for 1990-91 was not available at this printing.



In dollars: for the 1990-1991 biennium, it projected spending \$7.3 billion on education through grade 12 during the two year period (Marx, p. 7). For a yearly approximation, consider that in the 1989-1990 school year, the State of Minnesota dedicated \$3.5 billion to educating its students through grade 12 (Fin. Ed. in MN, p. 46).

### PROPERTY TAXES AND SCHOOLS

The county, acting with and for the state, collects property taxes assessed by the school district.

Property taxes are assessed on commercial, residential and agricultural properties. Taxes are based on the market value of these properties.

Taxes on commercial properties are based on the value of the deeded property but can be derived from their sales and income figures as well.

In the past two years, the state has changed the way it calculates residential property taxes. This "Facts and Issues" will work through calculations for homesteaded (owner occupied) residential property for taxes paid in 1990. There is little change between 1990 and 1991. Few are anticipated for 1992.

### Calculating Property Taxes

Five bits of information are needed to begin the calculation of property taxes: the market value of a property, the sale price, class rates, the Net Tax Capacity (NTC) and Tax Rates.

For taxes paid in 1990 (which fund the school year 1990-91), the county assessor estimates the market value of a property, i.e., what the property might sell for if it were for sale.

Essentially that part of the market value which will be taxed is called the tax capacity. According to mandate, property is to be valued at 100% of the market value. However, this is not always the case statewide (Minnesota Fair Share, Inc.).

Next, the market value is multiplied by a class rate. The product is the Net Tax Capacity (NTC) of the property.

For 1990, the class rate that produces the Net Tax Capacity (NTC) on a homesteaded residential property is a three-level index: 1% of the first \$68,000 of market value, 2% of the market value between \$68,000 and \$100,000 and 3% of the market value over \$100,000. For property taxes paid in 1991, the \$100,000 will be changed to \$110,000.

Another term to learn before proceeding further is Adjusted Net Tax Capacity (ANTC).

All property sales are reported by the county to the Department of Revenue which notes any discrepancy between the assessor's market value and the sale price of a property.

The Department of Revenue then computes the difference between the assigned market value and the sale price and determines a sales ratio. This sales ratio is a technical adjustment made by the Department of Revenue to correct any differences between the market value and a sale price.

If the sales price and assigned market value of a property match, the Adjusted Net Tax Capacity (ANTC) and the Net Tax Capacity (NTC) are the same. If they are different, then the Net Tax Capacity (NTC) is divided by the sales ratio. This figure produces the Adjusted Net Tax Capacity (ANTC) and it (the ANTC) is used to determine property taxes.

For the following "Facts and Issues" calculations, it will be assumed the sales ratio is 1, meaning that there is no difference between the sale price and the market value.

#### Example

Assume—Homeowner #1 resides in a house with a market value of \$50,000. Theoretically, the property taxes would be calculated as follows: multiply the market value of \$50,000 x 1% (Class Rate) = \$500. That \$500 is the Net Tax Capacity (NTC). It is not the property taxes due however.

To determine the property tax amount, one must first add together what the taxing bodies, i.e., the school district, county, city or township, etc. tax or levy. These are called Tax Rates (which used to be called mills or mill rates) and are the amount the taxing body uses to fund the services it provides.

#### School District Tax Rates

How is a school district's tax rate determined?

The single largest source of revenue to a Minnesota school district is the General Education Revenue Program.

The dollar amount that a school district can tax for this general education revenue (excluding excess levies from referendum) is determined by the state education formula. General education revenue is a by-product of the funding allowance times the number of pupil units in the school district.

Every year the State Department of Education computes the property tax effort a school district must make toward its share of the basic allowance. It is the base that a school district should tax its residents. The legislature sets a dollar value that is later converted into a rate or a percentage.

For 1990-91 the state set a school district's general education basic tax effort (tax rate) at 26.3% of the Adjusted Net Tax Capacity (ANTC).

This 26.3% (.263) is a major portion of the revenue a school district receives, but it is not all the property tax dollars a school district needs and uses. It does not include the property tax dollars raised for transportation, special education, early childhood and family education, community education, capital outlay or debt retirement.

Adding up all levies gives a school district a tax rate. It is not unusual that a school district's full Tax Rate can be 45%-55% (.45 to .55).

Note: it is tempting to assume here that the combined tax rates from all taxing bodies (school district, city, county, etc.) total 100% or 1.00. They do not. They can exceed 100% or 1.00.

Now let's go back to Homeowner #1 and with his/her \$50,000 house and

Assume—School District #000 levies a 50% (.5) tax rate on a piece of property. Assume further that the county taxes a 30% (.3) and the city has a 25% (.25) tax rate. This total Tax Rate is 105% (1.05). Now multiply 105% (1.05) x \$500 (its NTC, the taxable value of this residence with a \$50,000 market value), 1.05 x \$500 = \$525. This \$525 is what the owner owes in property taxes.

Assume—Homeowner #2 lives in a house with a market value of \$99,000. Its Net Tax Capacity (NTC) is \$680 or 1% of the first \$68,000 plus 2% of \$31,000 or \$680 + \$620. The taxable value of this residence, its NTC, is \$1,300.

Assume this school district, county and city also have a Tax Rate of 105% (1.05). Multiply 1.05 x \$1,300 = \$1,365. The property taxes owed on this property, \$1,365.

Assume—Homeowner #3 has a house valued at \$150,000.

This residence has a tax capacity of \$680 on the first \$68,000; plus 2% of the \$32,000 difference between \$68,000 and \$100,000 or \$640; plus, 3% of the \$50,000 over \$100,000 or \$1,500. The Net Tax Capacity (NTC) which is the taxable value of that house is \$680 + \$640 + \$1,500 = \$2,820.

Next, assume the school district, county and city here have the same Tax Rate as above, 105% (1.05). The property taxes owed on this property are \$2,961.

#### Summary

How property taxes paid in 1990 and 1991 on a residential homestead property are determined:

market value x class rate = NTC

NTC ÷ sales ratio = ANTC

ANTC x tax rate = property taxes payable



## TAX CREDITS

Tax credits are reductions in local property taxes. They are called property tax relief.

Recent changes to the tax laws have altered the method of calculating property taxes and tax credits (homestead credit, agriculture credit, etc.). Property tax relief per se has not been eliminated.

Because the words "Tax Credit" are politically volatile, the terms tax credit and tax relief have become interchangeable.

Tax credits/relief do reduce property taxes on residential homesteaded (owner occupied) property, but the school district, county and city do not lose revenue. Indeed, the state calls "tax credits" a source of education revenue.

### How and Why Tax Credits Changed

In 1989, the calculations to determine property taxes on homesteaded (owner occupied) residential property valued at less than \$68,000 began by multiplying 2.17% times the taxable value. Then, at the end of a series of calculations, a homestead tax credit was subtracted. The property taxes payable were what remained.

For taxes payable in 1990 and in 1991, taxpayers should think in terms of a class rate percentage that had been 2.17% of the first \$68,000 when tax credits were applied, but now is cut to 1% of that first \$68.00. This "cut" reflects the tax relief that homestead credits once did.

#### Example

Assume the market value of a property is \$50,000. The value subject to taxes in 1989 was 2.17% or  $\$50,000 \times 2.17\% = \$1085$ . In 1990 the value subject to taxing for a \$50,000 residence is 1% or  $\$50,000 \times 1\% = \$500$ .

Just like tax credits, this "cut" ultimately reduces property taxes for the taxpayer. And just like with tax credits, neither school districts nor the county nor the cities lose this revenue.

The state will still make up this revenue to the school district, city and county in 1990 with Homestead and Agricultural Credit Aid (HACA).

A hypothetical case: where property tax relief to a homeowner might lower property taxes by \$400, the state replaces that \$400 to the school district, the county or municipality with income and sales tax dollars and calls the replacement "state aid" (Fin. Ed. in MN, 1989-90, p. 40).

And when school districts, et al., are compensated for revenue lost to tax relief with dollars from income taxes and sales taxes, tax relief/credits once distributed to education are a state appropriation.

Why the change in "tax credits?" In 1988 and 1989, whenever voters approved property tax increases, their homestead credit would increase as well. In this way, any increase in levies also increased the homestead credit on a parcel.

From now on, the amount of Homestead Aid or tax relief will be determined by the legislature independent of the property tax increases local voters approve (House Research, Strom).

## Tax Increment Financing and School Revenue

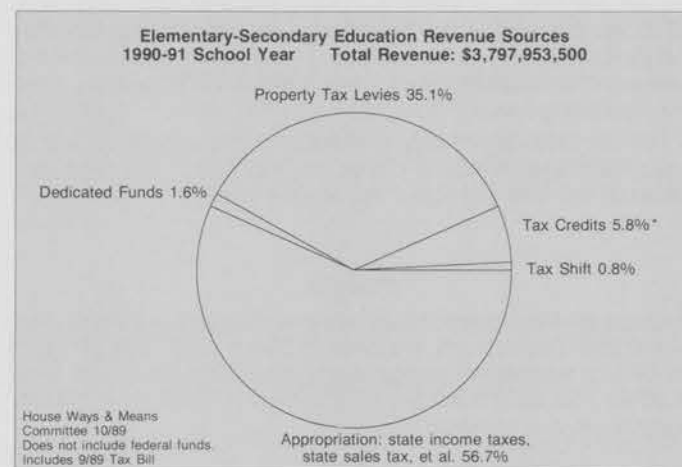
Tax Increment Financing (TIF), while it has no substantial bearing on school revenues, has provoked some questioning about school revenues.

Generally, when Tax Increment Financing occurs, a city has placed itself in debt or ultimately responsible for a debt to encourage residential and commercial development that might not occur without this municipality indebtedness.

Currently, once a Tax Increment Financed project is built, any added or new property tax dollars gained from this development first go to retire the bonds or debt the city/municipality has acquired because of the project. After the debt is paid, and after the 20 to 30 years specified to pay off the indebtedness has passed, the new property value can become part of the tax base of a school district.

However, a question has arisen about school district revenues and Tax Increment Financing because school districts do not have more immediate use of this source of property tax revenue.

If a school district received \$2,000 in property taxes from a parcel before development, it still receives \$2,000 after development even though the parcel may generate property taxes and pay off the debt in less than 20 to 30 years.



\* Tax credits are a source of education dollars because money from sales taxes and personal income taxes are paid to school districts, counties, cities, etc. to make up for property tax credits/relief.

### The Timetable

Property taxes payable in one year are based on property values determined almost two years earlier. Property taxes payable in 1990 are based on property values determined in 1988.

This means that even if the value of property within the district should skyrocket between the time the levy is decided and its collection, the school district would receive only the dollar amount it has levied. It cannot take instant advantage of increased property value until the next valuation period.

By fall of a given year, following public hearings on its proposed budgets, a school board votes on how many dollars it will need for its next year's budget. It includes the state's limits and voter-approved referendums. It next authorizes the tax or levy and certifies the amount to the county auditor. These levy dollars are then collected in property taxes in May and October of the following calendar year to be spent by the school district in the next school year.

Each year a school district levies a specific dollar amount rather than an absolute percentage. That dollar amount can be talked about as a percentage, but when it is levied, it is in dollars and cents.

Where the property taxes do not raise the minimum dollars assigned by the legislature to educate a pupil, the difference is funded (equalized) through state collected income and sales taxes. It is called a state aid and nearly all school districts receive some state aid.

Property tax dollars raised in one locale are used only by those taxing bodies. They do not supplement a school district, county, city, etc. in another locale. That is the role of state aid.

### Disparities

Differences between the state funding allowance for educating a pupil and what property taxes raise toward that allowance occur because the tax base in one school district, i.e., the value of the property in the area and what dollars that property can raise per pupil, may differ from another school district.

A school district in an area with a strong commercial and/or industrial base from shopping malls to power plants can raise more dollars for education with less tax effort or rate because the tax capacity of the area is higher than an area that is primarily residential property.

School districts in communities with little commercial and/or industrial base may receive the bulk of their property tax revenue from residential property. Here it takes a greater tax effort or rate to generate the same dollars it does in a heavily commercial/industrial area.

Disparities or differences in property taxes also occur because of the location of the property. If the house is located in an urban area, it may have a higher value than the exact same house located in non-urban Minnesota.

Consider a 4-bedroom colonial style house. In an urban area it could have a market value of \$200,000, far more than the same house in non-urban Minnesota. Subsequently, its tax capacity and its property taxes are higher because of its urban location.

### EXCESS LEVY REFERENDUM

Minnesota school districts can improve their financial picture through their own local referendums. With the approval of voters within the respective school district, and only with that approval, can a school board increase local property taxes above state limits to add revenue dollars to its general fund.

Similarly, voters approve bond referendums to finance the construction of new school buildings or major remodeling of existing structures. Property tax dollars dedicated to construction are not part of the school district's general fund. They are its Building Construction Fund. Paying off that bond is part of Debt Service, another fund separate from a school district's general revenue fund.

Voter-approved bond issues/referendums add to the property taxes a homeowner pays to support a school district's needs. For property taxes payable in 1990, 60% of Minnesota's school districts have a debt service for new construction or remodeled schools. It totals \$157 million dollars (House Research, Strom).

Although it is rarely easy to secure voter approval to raise property taxes, the number of approved referendums has risen. Nearly 65% of Minnesota school districts now have levy referendums to help fund their operating expenses. Excess levy referendums account for \$218 million and are a statewide 17% addition to property taxes payable in 1990 (*Star-Tribune*, May 14, 1990, p. 1B).

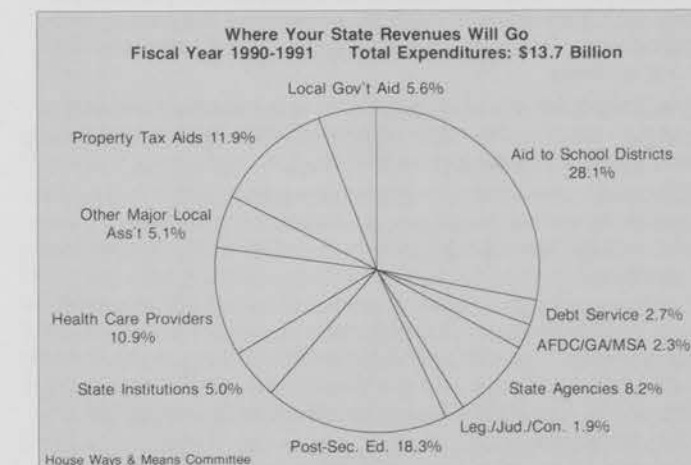
Levy referendums have also resulted in a range of difference in spending per pupil unit. While the excess levy referendum is not the only reason for this range in spending, this excess levy referendum ability does allow those school districts with successful referendums to expend more per pupil be it for teacher salaries or programs.

More districts with high property values than those with low property values have voter-approved levy referendums to increase the money available to their school district.

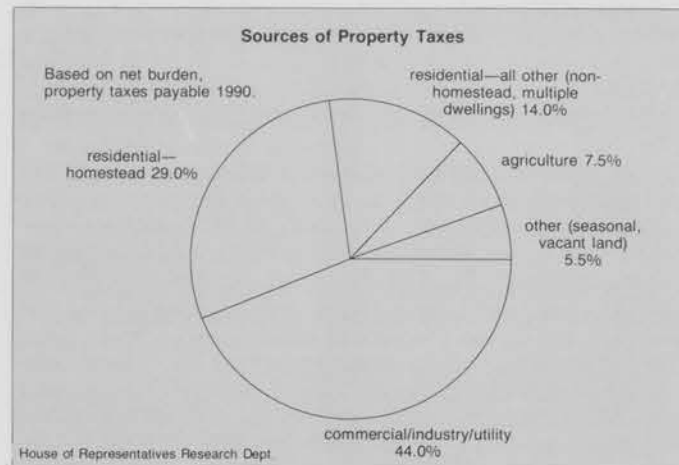
The state legislature has passed legislation to restrict a district's ability to hold local referendums. As of fall 1989, these special referendums may be held *only* on the Tuesday Election Day in November. The ballot must state the dollar amount of the proposed levy in tax capacity rate, the dollars raised by the rate the first year it is in effect, and the number of years it will be in effect.

### FEDERAL DOLLARS

The contribution of federal dollars to the schools, whether it is paid directly to the schools or through an intermediary, approximates about 4% of the education revenue in the state (*School District Profiles*, p. 8).







## HOW ARE TAX DOLLARS DISTRIBUTED TO EDUCATION?

Once all local property taxes and state tax dollars are collected, they can be distributed to the school districts, counties and cities and townships around the state.

## FORMULAS AND SCHOOL DOLLARS

A school district's share of these local property tax dollars and state tax revenues is based on all of its funding formulas.

These formulas include the Basic Education Funding Formula, but may also include formulas for transportation, limited English proficiency aid, secondary vocational education, cooperation programs with intermediate districts, community education, early childhood and family education, capital expenditures and debt service revenue.

The Basic Education Funding Formula is the largest source of any school district's financial support. It is also the base, and obviously not the sole source of money.

The base money the state will provide a school district, i.e., its "general education revenue," is primarily determined by the district's student enrollment. However, not all students count for the same value.

Pupils are weighted by their grade level. "Weighted pupil units" means each kindergarten student has a value of .5 per pupil unit; elementary students, 1.0 pupil units; and secondary students have a value of 1.35 per pupil unit. It is assumed the cost of educating at the grade 7-12 level requires more resources, therefore the greater weighting.

For 1990-91 the state legislature has set the base, its general education "formula allowance," at \$2,953 per pupil unit.

In theory and simple multiplication, the Gopherville school district with 1,000 students would receive about \$2,953,000 in minimum revenue for 1990-91. But recall all students do not count the same.

In theory, and a bit more complicated multiplication, if that 1,000 Gopherville students consisted of 50 kindergarteners, 475 elementary pupils and 475 secondary students, it would equal 1,141.25 pupil units and the school district would receive \$3,370,111 minimum revenue for 1990-91 because of this weighting of pupils.

It should be noted that school districts, although they are funded on a per pupil unit basis, do not have to spend accordingly ("School District Spending," p. 30).

## The Basic Education Funding Formula

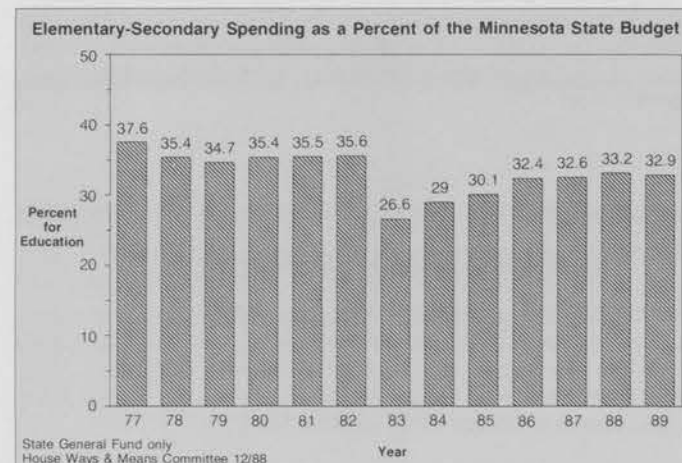
Money for this \$2,953 per pupil unit comes from a combination of local property taxes plus state appropriation, i.e., state aid (income and sales taxes).

Although the proportion of state aid to local tax dollars has changed over the past decade, the concept has remained constant.

The proportion of property tax dollars versus state aid dollars for a school district is determined by the property values in the district and the number of pupils.

Districts with relatively low or declining pupil enrollment and high property value (those with much industry, commercial enterprise, etc.) receive most, if not all, of their general education revenue from local tax levies. School districts with much non-taxable land or low property value and large student enrollments receive most of their education revenue from state aid (House Research, Strom).

In 1987-88 property taxes accounted for 70% to 80% of the general education revenue in Eden Prairie, Edina, St. Louis Park, Roseville, St. Anthony-New Brighton, Hopkins, West St. Paul and Wayzata. Becker, in Sherburne County, due to the property tax value of the SherCo III power plant, received 87% of its education revenue from property taxes. St. Francis, Black Duck, Glenville, Kensington, Foley, Barnum, Spring Valley, Peterson, Preston and North Branch school districts receive about 70% or more of their revenue from state aid (School District Profiles, 1987-88, MN Department of Education, pp. 22-43).



## Per Pupil Allowance

Recall that for 1990-91, the state set a school district's property tax effort for general education revenue at 26.3% of the Adjusted Net Tax Capacity (ANTC). School districts must levy at least 26.3% (.263) of the tax capacity of all property in their district. This does not include excess property tax levies from local referendums nor tax levies for transportation and other programs.

The amount of dollars per pupil unit (ppu) provided by property taxes versus state aid is determined by subtracting levied property tax dollars from the formula allowance.

$$\text{\$2,953 ppu} - \text{property tax dollars ppu} = \text{state aid ppu.}$$

### Example

Consider the school district of Gopherville in 1990-91 with its 1,000 pupils through grade 12.

$$\text{Basic Allowance Revenue} = \text{\$2,953 per pupil unit (ppu)} \\ \text{to Gopherville schools}$$

What proportion of that \$2,953 will come from local property taxes is determined by multiplying the education tax capacity rate (26.3%) x Gopherville's Adjusted Net Tax Capacity (ANTC).

Review Net Tax Capacity (NTC) and Adjusted Net Tax Capacity (ANTC) for a moment. Then recall Homeowner #3 who had a house valued at \$150,000. This homeowner's property has a Net Tax Capacity (NTC) of \$2,820. Recall, too, \$2,820 are not the property taxes due. Recall the sales ratio was assumed to be 1, no difference between the estimated market value and the sales price. Therefore the Net Tax Capacity (NTC) was the same as the Adjusted Net Tax Capacity (ANTC). Recall further that the tax rate was multiplied by this \$2,820 Adjusted Net Tax Capacity (ANTC) to determine the property taxes.

Theoretically, this homeowner pays at least 26.3% or a .263 tax rate of the Adjusted Net Tax Capacity (ANTC) of that property to the school. Recall excess levy referendums and levies required for transportation, building needs, community education, etc. These exceed the 26.3% and can boost the school district tax rate to 50% (.5) over the 26.3% (.265) that is the base for the general education revenue.

Back to Gopherville and its basic formula allowance per pupil: Assume—Gopherville has an Adjusted Net Tax Capacity (ANTC) of \$4,400,000. For Gopherville, that means:

$$26.3\% \times \$4,400,000 = \text{local school levy ppu} \\ 1,141.25 \text{ pupil units}$$

$$.263\% \times \$4,400,000 = \$1,157,200 = \$1,013.97 \text{ ppu} \\ 1,141.25 \text{ pupil units} \quad 1,141.25 \text{ pupil units}$$

Therefore, Gopherville, which raises \$1,013.97 ppu in property taxes toward the state education basic formula allowance, needs \$1,939.03 ppu in state aid to make up the difference between the per pupil allowance, \$2,953, and its levy dollars.

$$\text{\$2,953} - \text{\$1,013.97} = \text{\$1,939.03 ppu}$$

## ADDITIONAL EDUCATION MONEY

In addition to the formula allowance per pupil unit (ppu), some of the 435 Minnesota school districts can receive revenue dollars ppu in specific components or areas. Money for Compensatory Revenue, Training and Experience Revenue, Sparsity Revenue helps offset costs greater in one district than another.

Compensatory Revenue gives more dollars per pupil unit to 134 districts with high concentrations of students qualifying for AFDC (Aid to Families with Dependent Children).

In 1990-91 Training and Experience Revenue will go to 42 districts with more teachers at the upper end of the pay scale. This occurs because some areas of the state have easier access to advanced professional training, and/or declining enrollments resulting in layoffs of less senior teachers.

The state, recognizing the higher cost of operating an education program with lower enrollments, attempts to offset these costs. Secondary sparsity revenue goes to about 50 Minnesota school districts with fewer than 400 secondary students living in wide-spread geographic areas. Elementary sparsity revenue goes to 11 school districts whose grade levels average 20 or fewer pupils and whose school is located 20 or more miles from the next nearest elementary school.

Dollars in these three component areas are added to the basic allowance. A district receives dollars in these component areas from property taxes and state aid in the same proportion as their basic formula allowance.

### Example

We know Gopherville will receive at least \$2,953 ppu. But it also qualifies for \$40 ppu in compensatory aid for its AFDC pupils plus another \$30 ppu because it has some Ph.D. teachers (Training and Experience Aid). It gets no sparsity aid.

Gopherville's theoretical general education revenue is \$2,953 plus \$70 or \$3,023 per pupil unit.

Gopherville's property tax share of the general education revenue with these additional component aids is still computed the same way as it was without them.

## Supplemental Revenue

With the advent of the 1971 "Minnesota Miracle," certain school districts spending more per pupil than others were "grandfathered" in at a higher level of basic allowance revenue.

This was done to guarantee that those districts would not receive less revenue ppu under the new plan than they would have under the old plan. At one time it was called the "grandfather levy," but after several revisions it is now labeled the Supplemental Revenue Allowance. Additional revenues have been grandfathered in over the past 20 years and most recently in 1987 when some changes to the funding formula occurred. These are part of this supplemental revenue allowance.

For the 1990-91 school year, 66 school districts will receive this supplemental revenue ranging from \$1 ppu to over \$700 ppu.

Some of this revenue comes from property taxes, some from state aid just like the basic allowance.



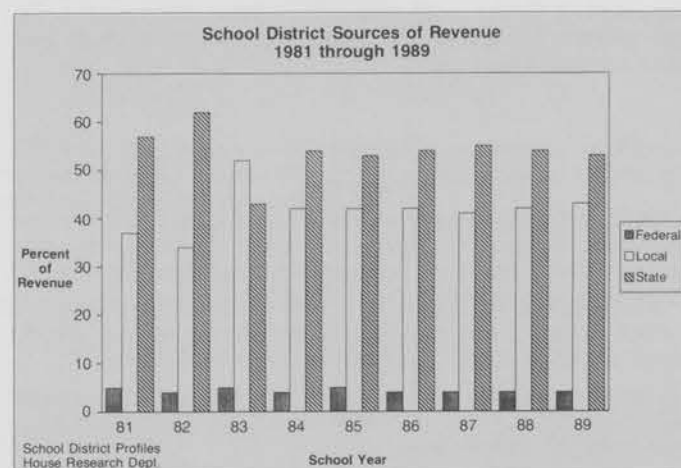
## Local Referendum Levies

School districts use voter-approved excess levy referendums to offset costs not covered by the basic funding allowance.

The original intention of local levy referendums was to allow school districts to tax themselves higher to provide extra educational programs beyond what was possible with formula dollars alone. However, many school districts now claim these excess levy referendums are necessary to meet basic needs and state requirements.

The state requires (mandates) and permits school districts to provide certain district programs and spend money to fund them. State dollars following these programs to the district have not funded the programs fully. Such programs include special education for handicapped/disabled children, summer school, art education, programs for the gifted and talented.

Where the increases in state aid and property tax levels set by the state have not covered education costs, be they higher teachers' salaries and/or benefits or educational programs, voters have gone to the polls and approved increases in their property taxes. In 1989, 75% of the school districts with referendums on the ballot received voter approval (School District Spending, p. 30).



## Special Education Aid

The state funds a school district's additional costs of special education for disabled children, but only in part. Funding in special education is not on a per pupil basis, although school districts do receive the basic education allowance per pupil unit for special education students.

The state describes and prescribes the program and then provides between 47% and 60% of a district's cost of special education, i.e., special education teachers/personnel salaries, supplies and materials, home-based services, etc. paying up to a point or capping its aid.

For example, the state will reimburse a special education teacher salary up to \$16,727 or it reimburses a school district for 60% percent of that salary whichever is less. However, if a school district pays its special education teachers more than \$16,727, the school district may levy for part of the difference (up to 6%) but then must also make up the rest. The state requires or mandates that school districts use other revenues, its general education revenue allowance, to pay the remainder (Fin. Ed. in MN, 1989-90, p. 27).

## Community Education

Other programs permitted and encouraged are local Community Education programs, which are open to all ages of residents, and Early Childhood Family Education, a community education program for children under age 5 and their parents. State funding is available to a district on a per capita basis with a prescribed property tax to aid ratio based on the tax capacity of the district (Fin. Ed. in MN, 1989-90). Money levied by the school district for community education must be spent on community education.

## Transportation

The state assists in paying regular transportation costs of students. The aid again is in a levy to aid ratio based on the number of students to be transported and the projected cost of transporting. If a district says it will cost \$200,000 to transport 800 of its 1,000 students, then a fixed percentage (1.9% in 1989) is levied against its Adjusted Net Tax Capacity (ANTC). The rest comes from state aid (Fin. Ed. in MN, 1989-90, pp. 25-26).

## STATE RESTRICTIONS

The state currently requires that 2.2% of a school district's general education revenue must be used to provide any part of any of the following programs: art education, chemical use prevention, programs for gifted and talented, summer school, interdistrict cooperation, baccalaureate and advanced placement programs. The school district has discretion on which programs to provide and how much to spend.

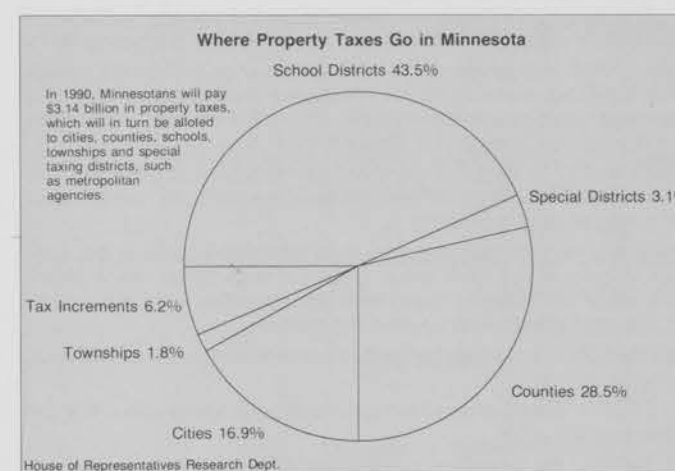
In addition \$10 per pupil unit is made available only if the district has a staff development plan and dedicates this \$10 ppu to that plan.

Another restriction limits the district fund balance or reserves to less than \$600 per pupil unit. Should reserves exceed this limit, the general education fund revenue the next year is reduced by no more than \$150 per pupil unit. This means the school district must deduct up to \$150 from the basic pupil allowance (\$2,935 - \$150 in 1990-91). Districts are thereby encouraged to spend their revenues and discouraged from building excessive reserves.

## RECORD KEEPING

All school districts use the same statewide reporting and recording system called Uniform Finance and Reporting System or UFARS.

However, UFARS presents some serious problems. The Legislative Audit Commission has concluded that UFARS instructions are "cumbersome, complex, and difficult to apply correctly" leading to gaps in and repetition between categories of expenses and misleading misinformation ("School District Spending," p. xiii).



## LOCAL SCHOOL BUDGETS

School Boards and administrators begin budget planning in the fall of the school year and vote on a final budget by June 30 unless an extension is granted. Citizens can become involved in the process at any point, but it is more effective to express interests and concerns early. Specific timelines and names of personnel involved in budgeting can be obtained from the school district superintendent.

Local school budgets in their entirety or summary are available upon request from a school superintendent or a district business office. Voluminous budget information might be less helpful initially than the summary form.

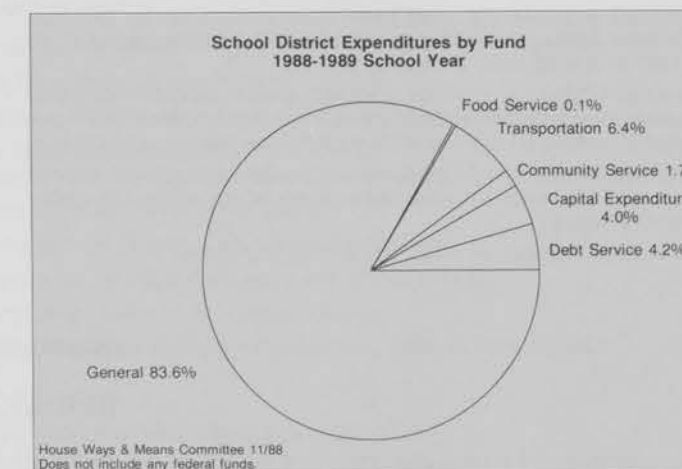
Budgets and budget summaries show district-wide revenues and expenditures organized into Operating Funds and Non-Operating Funds.

## Operating Funds are:

1. **General Fund**—covers salaries and related expenses, school supplies, custodial operations and special education revenue;
2. **Food Service**—revenue for school food service;
3. **Transportation**—buses and bus transportation;
4. **Community Services**—includes community education programs for early childhood and family education, adult high school, senior citizens and community recreation programs.

## Non-Operating Funds are:

1. **Capital Outlay**—covers land acquisition, building repair, purchase/lease of equipment, textbooks, computer software;
2. **Building Construction Fund**—pays for new building construction;
3. **Debt Service**—money to retire the school district's debt obligation should a school district issue bonds to pay for capital improvements, new buildings, additions or remodeling;
4. **Trust and Agency Fund**—money or property, most commonly dedicated scholarship funds or student activity accounts, held in trust by a school district.



## CURRENT CONCERNS

The LWVMN education research committee asked local leagues to interview their school superintendents about the major public school finance issues confronting them. A statewide cross-section of 45 superintendents responded. They listed equitable funding, especially focusing on whether local levy referendums should be a local right, as their primary concern.

Next came the need for adequate and consistent state funding of schools with less reliance on property taxes.

Their third concern was inadequate and shrinking funding for state and federal mandated programs like special education which are not fully funded.

Additionally, they mentioned the need for increased state funding to compensate for the salaries of older tenured staffs in those locales where declining enrollments have necessitated teacher layoffs and adjustments in salary for staff due to differing cost of living in various areas of the state.

Other concerns included the costs associated with AFDC students, differing school facility needs including upgrading technology, vocational education, transportation and sparsity aids. All are partially funded at this time.

Analysis and implication of these and other issues form the basis of "Facts and Issues II," Winter, 1990-91.

## GLOSSARY

**ADJUSTED NET TAX CAPACITY (ANTC):** the tax capacity of a property which results when the Net Tax Capacity is divided by the sales ratio. Adjusted Net Tax Capacity is the figure used to determine property taxes.

**APPROPRIATION:** money set aside for a specific use. State aid to education is an appropriation of state sales tax dollars and state income tax dollars.

**CLASS RATE:** an index which when multiplied by the market value of a taxable property produces the Net Tax Capacity (NTC). The index applied to residential homestead property has three levels: 1% of the first \$68,000 of market value, 2% of the market value between \$68,000 and \$100,000 and 3% of the market value over \$100,000. For property taxes paid in 1991, the \$100,000 will be changed to \$110,000.

**CAPITAL OUTLAY:** revenue dollars used for land acquisition, building repair, purchase/lease of equipment, textbooks, computer software.

**DEBT SERVICE:** money used to retire a school district's debt obligation should a school district issue bonds to pay for capital improvements, new buildings, major additions or remodeling.

**FUNDING ALLOWANCE:** that base dollar amount set by the state legislature that is guaranteed to a school district to educate a pupil unit. In 1990-91 it is \$2,953 per pupil unit.

**FUNDING FORMULA:** a method of equalizing aid to education using both property taxes and state appropriations. The funding formula is the proportion of property taxes versus state aid that funds any one school district.

**GENERAL FUND:** school district revenue used to cover teacher salaries and related expenses, school supplies, custodial operations and special education revenue.

**LEVY:** a tax imposed on property, i.e., property taxes.

**NET TAX CAPACITY (NTC):** the market value of a property multiplied by the class rate index. That value of the property subject to property taxes.

**PUPIL UNITS:** in determining the funding allowance, the student population is weighted, meaning each kindergarten student has a value of .5 pupil units; each elementary student, 1.0 pupil units; and each secondary student has a value of 1.35 pupil units.

**SALES RATIO:** a technical computation made by the Department of Revenue to correct any difference between the estimated market value and a sale price of a property.

**STATE AID:** dollars collected from state personal income taxes, sales taxes, corporate and bank taxes, gross earnings taxes, motor vehicle taxes, liquor and tobacco taxes, dedicated revenues and other monies that are appropriated to a specific expenditure.

**TAX CAPACITY:** the value of property that school districts, counties, cities, townships, etc. tax.

**TAX CREDIT:** a state allowed reduction in local property taxes. It is called property tax relief.

**TAX RATES:** the amount a taxing body (school district, city, county, township) uses to fund the services it provides.

**TAX INCREMENT FINANCING:** a method of encouraging municipal development whereby a city places itself in debt or ultimately responsible for a debt to encourage residential and commercial development that might not occur without this municipality indebtedness.

**UFARS (UNIFORM FINANCIAL ACCOUNTING AND REPORTING SYSTEM):** a single statewide accounting procedure used by all school districts to record and report financial data to the state Department of Education.

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# FACTS and ISSUES: EDUCATION HOW WILL WE PAY FOR OUR SCHOOLS? FINANCING PUBLIC EDUCATION IN MINNESOTA (K-12)

League of Women Voters of Minnesota

August 1982

## I. Current Status of Financing of Public Education

### A. Introduction

#### Reform Movement

The social consciousness of the mid-Twentieth Century generated a movement to redress unequal educational opportunities in this country. Many people recognized that being black or white made a difference in the education an individual could expect; being rich or poor made a difference; being from a community that valued or did not value education made a difference; living in a property-rich or property-poor school district made a difference. Numerous court challenges reflected the general consensus that an overhaul of school funding was due.

In Minnesota the Governor and Legislature initiated changes which brought the state's school financing system more into spirit with the constitutional mandate "to establish a general and uniform system" of education. Widely known as the "Minnesota Miracle," the 1971 Omnibus Tax Act had as its main goals to equalize tax effort of property owners while at the same time promoting greater equalization of school expenditures throughout the state. The Legislature continues to have a large role in the joint state-local effort to finance schools.

#### Amendments to the 1971 Law

In the decade since, numerous amendments to the original Act have reflected significant changes in schools and society not anticipated by those who drafted the 1971 law. Inflation, declining enrollment, the increasing needs of special groups, and, most recently, declining state revenues in a recessionary economy have prompted these amendments. Some believe the amendments have "fine-tuned" the law; others think the changes have turned the Minnesota Miracle into an unwieldy instrument, difficult to understand and unresponsive to present needs.

The League of Women Voters of Minnesota (LWVMN) was actively involved in efforts to pass the 1971 law, lobbying from its 1969 position on equal opportunity in education. Details of that position have enabled LWV lobbyists to support many of the changes made in the law during the past decade.

Have these "adjustments" caused a loss of many of the law's original features, those designed to distribute funds equitably and reduce reliance on the local property tax? Educators and the concerned public have begun to ask for a reexamination of Minnesota's school financing system. What was appropriate in 1971 may not be what schools need in the '80s.

### B. Minnesota Law and Some Problems With It

Schools in Minnesota are financed by a combination of state and local monies (with some additional funds, about 6%,

which we will not discuss here, from federal sources). The state share of this money is divided among three aid programs, Foundation aids, categorical aids, and tax relief aids.

#### The Foundation Formula

The Foundation Formula includes Foundation aid from state tax sources and property tax revenues from local levies. The state portion of this formula, Foundation aid, constitutes 70% of the total state aid to school districts. Local districts are unrestricted in their use of this aid and the related property tax revenues to meet their current operating costs.

The local property tax portion of the formula is based on district ability to pay as measured by property valuation in the district. An equalization factor determines what proportion of the funds comes from state aid and what from property tax in each district. The higher the property valuation, the less a district gets from state aid, and vice versa. Some districts, with high local property valuation, raise all their Basic Foundation amount from the local property tax: they are, thus, "off-the-formula."

"Equalization . . . refers to an equal minimum rate of taxation among school districts which supports a minimum guarantee of equal dollars per pupil unit. Above these minimums both tax rates and dollars per pupil vary greatly among districts depending upon varying student needs, district costs, and district education and tax choices."

#### Illustration of Formula

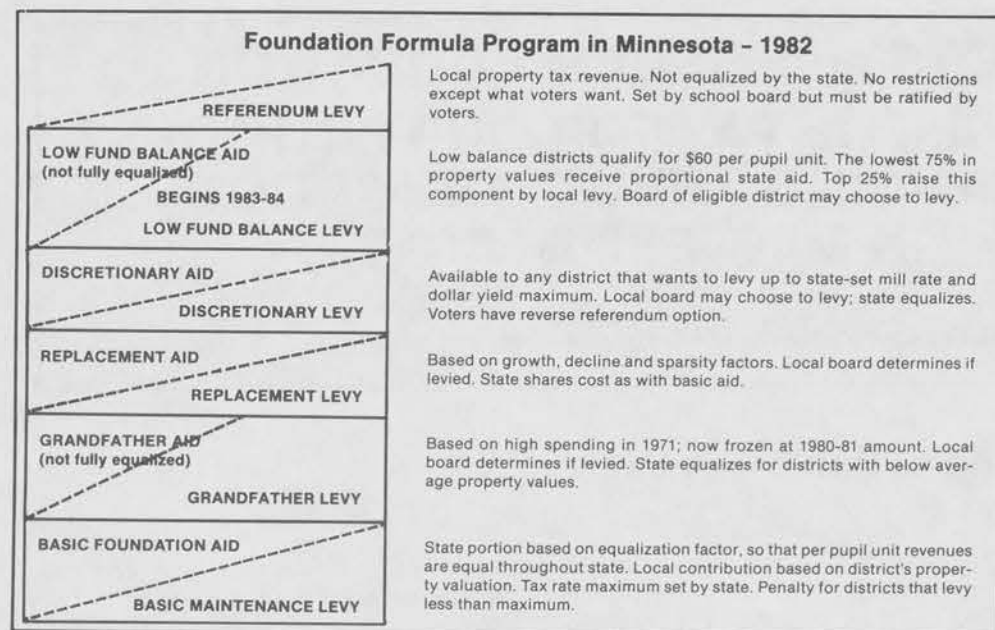
There were in 1981-82 five parts to the Foundation Program. All but one could be made up of both state and local monies. Beginning in 1983-84, a sixth part, Low Fund Balance Aid and Levy, will be added. The accompanying chart entitled "Foundation Formula Program," based on one provided by the State Department of Education (SDE), illus-

#### Method of Study

In carrying out this study, the LWVMN research committee read widely and interviewed many state leaders in government and education. They also used the results of interviews conducted by local League members with school personnel and concerned citizens to provide a sense of the thinking around the state. A summary of the responses to this survey appeared in the June-July 1982 *Minnesota VOTER* and is included in the more detailed version of this study published by LWVMN in August 1982. The more extensive version also includes the sources of information for the study. Additional copies of this paper, as well as the more detailed, computer-printed version may be obtained from:

League of Women Voters of Minnesota  
555 Wabasha St.  
St. Paul, MN 55102  
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trates how state aid and tax levies are combined to arrive at the total formula amount for each district.

The illustration is not proportionally accurate. The Basic Foundation Aid and Levy usually represents about 77% of a district's monies. The supplementary components are not equal either. For example, in 1982-83 the local referendum will account for 3.2% of the total Foundation Program statewide, up from under 1% in 1981-82.

The diagonal lines dividing the boxes are not meant to imply that state and local shares of a component are equal. The shares are, of course, different for each district, depending on the district's ability to pay as measured by property valuation.

Some definitions:

**Levy** – money raised from tax on local property.

**Aid** – state funds from the income and sales taxes.

**Pupil Units** – weighted count of students in a district, taken each year and used as basis for the guaranteed dollar amount of the Foundation Formula. The weighting depends on several factors, including the grade level of the student and whether the student's family receives Aid to Families with Dependent Children. The weighting is an attempt to take into account the differing costs of educating different children.

#### Legislature sets allowance and tax rate

The amount of the Basic Foundation Formula is determined by the state Legislature. Increases have been made through the decade, partially in response to inflation, but considerably below the inflation rate. The 1971 average pupil unit cost was \$663, and the formula was set at

\$600 for 1971-72. The formula for 1981-82 was set at \$1333. For 1982-83, districts were to be guaranteed \$1346 per pupil unit, until the 1982 Legislature required a 1.5% budget cut because of the state's fiscal problems.

One of the criticisms of the Foundation Program is based on the somewhat arbitrary means used for arriving at the formula allowance. Education committees of both the House and Senate tend to bargain on this point, arriving at an amount that the state budget will bear which has little direct relationship to the real costs of educating students (although they may take costs into account).

The Legislature also sets a required rate of taxation (mill rate) that must be levied locally to provide the district's tax portion of the basic formula. The 1971-72 rate was 30 mills. In 1981-82 the rate was 21 mills, and the rate for 1982-83 was set at 23 mills plus one optional mill. Aids for 1982-83 are computed using 24 mills applied to equalized property valuations (adjusted for varying assessment practices around the state).

#### Added Components

Because it is recognized that there are cost differences from district to district, adjustments in the total Foundation Program have been made over the last 10 years. Some of the adjustments have made the distribution of funds more equitable; others have tended to dis-equalize the distribution. Each of these adjustments has added a component to the basic Foundation Formula.

The first supplement to the basic foundation formula is the *Grandfather Aid and Levy*. It has become one of the most controversial parts of the law in recent years. In 1971, when the greatest effort was

made to equalize spending throughout the state's school districts, those districts that had been spending over the state's average were allowed to continue raising that amount through local property taxes. That additional levy is now equalized with state aid for districts with below average property values. For other eligible districts, the full amount comes from the property tax.

The original intent was to gradually reduce the Grandfather allowance so that high-spending districts would be brought down to the state's average within 40 years. In fact, that reduction never occurred, and districts that were high spenders in 1971 still have the option to maintain a higher spending level today. The disequalizing effect is obvious. In 1981, 177 districts of the state's 432 received a Grandfather allowance of between \$1.00 and \$475.00 per pupil unit. The other districts had no Grandfather allowance.

The second supplement to the basic foundation formula is the *Replacement Aid and Levy*, which is a system of shared state and local funding for the costs associated with sparsity and enrollment change. These aids were computed separately and fully paid by the state prior to 1980-81. The amount comes from aid and levy in the same proportion as the basic foundation formula. This revenue was received by 424 of the 432 school districts in 1981-82. The highest per pupil amount from Replacement revenue was \$284.

Declining enrollment has been one of the major problems to hit the state schools in the last decade. Recently many districts have learned that decline may be more difficult to deal with financially than increased enrollment. A district may lose a substantial amount of money as its pupil units decline, yet incur no reduction in costs. For example, a district with a K-12 enrollment of 500 students might lose 50 pupils and, therefore, realize a 10% loss in aids. Yet, if those students were lost at the rate of four per class, it is possible that there would be no reduction in staff, no cost savings in equipment and utilities, and little savings in supplies.

When reduction in staff does take place, by Minnesota law the teacher with least seniority (who is, typically, the lowest salaried teacher) is the one to leave. The savings are less than if a teacher getting an average or high salary were dropped.

The third added component, dating from 1979, is the *Discretionary Aid and Levy*. Bowing to those who call for more local control, this component is optional.

High staff costs or expanded program offerings might be reasons why a district would opt for this aid and levy.

Under the Discretionary component a mill of tax levy is equalized by the state to provide the same number of dollars per pupil unit as would a mill raised under the basic formula, subject to a legislative limit on the number of mills a district may levy. In 1981, 314 of the state's 432 districts used this option. The maximum allowance set by the Legislature for 1982-83 is 2.25 mills guaranteed to raise \$138.52 per pupil unit. The law allows for a reverse referendum by voter petition on this levy.

The fourth supplement to the Foundation Formula, added during the 1982 legislative session but not available until 1983-84, is the *Low Fund Balance Aid and Levy*. Fund balances in many school districts were depleted following the withholding of school aids during the 1981-82 state deficit crisis. This allowance is the Legislature's attempt to make up for some of that loss. Only districts with balances below \$316 per pupil unit will qualify.

The final supplement to the Foundation Program is the *Referendum Levy*, locally generated and unmatched by state aids. The only limit on this is what the local voters will accept. Ballot proposals are expressed in mills and the amount raised by that millage in the first year, for a specific year or years or ongoing. In 1981, 171 of the state's school districts had money raised from local Referendum levies, passed in that year or earlier, which they used to supplement their Foundation funds. The amounts varied from \$21.20 per pupil unit to \$1411.34 per pupil unit. Since 261 districts had no money raised from referendum levies in 1981 and most districts face financial crises, a large number of districts are likely to hold referenda to ask for additional tax money in the near future.

#### Categorical Aids

Categorical aids are distributed to local districts to support specific categories of programs agreed upon by the Legislature, the SDE and local districts. Some of these are mandated programs, some are optional. They are designed to address certain problems not dealt with under the original 1971 Omnibus Tax Act. Many of them have been supported by the League of Women Voters.

A percentage of the costs, different for each type of aid, is paid by the state. These aids are akin to the idea of Program-Based Funding (see section on that subject), which is espoused by some who are dissatisfied with the Foundation system of funding by pupil unit.

The major categorical aids are Transportation aid, Special Education aid, and Secondary and Post-Secondary Vocational aid. There are over a dozen other miscellaneous categorical aids, for such programs as Gifted and Talented Students, Indian Education, English As a Second Language, and Community Education.

*Transportation aid* is a large and growing portion of state aids to local districts. Even though enrollments in both public and nonpublic schools have declined since 1971, the number of students transported has increased every year. These increases are due to desegregation efforts in the three major urban districts, pairing or consolidation between districts, increases in programs for handicapped pupils, increases in shared time between public and nonpublic schools, and high energy costs. Transportation costs for extracurricular activities or field trips are borne solely by the local districts out of their general funds (Foundation monies). The proportion of transportation costs covered by the state was decreased in 1981-82 as part of the legislative response to increasing costs of transportation and decreased state revenues.

*Special Education aids* go to school districts based on their costs of instruction and supplies (one of the few current programs for which funds are tied to real costs, although the state's percentage contribution was recently decreased). These are mandated programs and they are costly. Districts must provide educational services for the speech impaired, mentally retarded, physically handicapped, hearing and vision impaired, learning disabled, emotionally disturbed, and pupils with special behavioral problems.

*Vocational Education aids*, both secondary and post-secondary, are also appropriated to districts according to the costs of instruction and equipment. Some of the costs of post-secondary vocational education are met by tuition.

Although the *other categorical aid programs* have a minimal impact on total state financing, they address some problems specifically that might otherwise be ignored. Total monies spent on Gifted and Talented Student programs have not been great, but the LWV has been a long-standing proponent of this kind of state aid. Similarly, the special needs of the recent immigrant population in Minnesota schools have been addressed by the English As a Second Language and the Bilingual Education programs.

Some legislators argue that categorical aids, the scope of which has been ex-

panding throughout the past decade, violate the spirit of the 1971 Tax Law. They claim that these aids are disequalizing. Some school officials as well as legislators complain that, in some cases, programs are mandated at the state level that local districts may not want to provide or be able to afford.

#### Tax Relief Aids

Tax relief aids are non-equalized components which constitute about 15% of the state aid distributions to Minnesota school districts. They provide property tax relief to owners of both homestead and agricultural property. School districts also get aid in lieu of taxes for some types of property within their districts which are exempt from local taxation, e.g., Tac-onite tax revenues and Attached Machinery aid.

Tax relief aids reduce the levy certified by a school board; thus districts that are "off the formula" in terms of Basic Foundation aid actually get a considerable amount of state aid for tax relief. The effectiveness of these tax relief aids in guaranteeing equitable tax burdens statewide is debated. It is possible that they will be the next components of the financing formula to undergo "adjustments."

#### In Summary

Together the components of the Foundation Formula add up to varying amounts of revenue per pupil unit and varying tax rates, all as a result of historical spending levels, funding needs recognized by legislative decisions, and local decisions on tax levies. Total Foundation revenue per pupil unit in 1981-82 ranged from \$1344 to \$2894, due to differing district entitlements in the components that supplement the Basic Foundation Aid and Levy.

We have provided an overview of the current Minnesota school financing law with a few of its problems. According to the SDE, the Foundation Program "assures that all school districts will have an adequate educational program."<sup>2</sup> Is each district's educational program "adequate"?

People frequently complain about the complexity of the funding system. But if the complexity is necessary to provide equitable funding, it should not be criticized. Is the complexity necessary? Is the funding system providing equal educational opportunity for Minnesota students?

#### Notes

1. Joyce Krupey, *The Foundation Formula*, draft of unpublished paper, (St. Paul: Office of Senate Research, June 1982), 1-2.
2. "ABC's of Minnesota School Finance, The," *SDE Special Report*, 13:4, June 1979 (St. Paul: Minnesota State Department of Education), p. 10.



### C. Recent Demographic and Economic Developments

School children are becoming a decreasing proportion of the nation's population. During the '70s the percentage of respondents to the Gallup Poll of Public Attitudes toward Public Schools who had children in school dropped from 50% to 32%. Public school enrollments were increasing in Minnesota through the 1971-72 school year, when our current financing law was passed, and have decreased steadily since.

Minnesota Enrollment  
in Public Schools (K-12)

Year	Number of Students	Percent of Peak Year
1971-72 (peak)	916,355	100%
1981-82	736,000	80%
1984-85 (projected)	708,649	77%
1990-91 (projected)	738,757	81%

Source: Minnesota State Department of Education

#### Economic Changes

Political and economic forces affecting the state, both internal and external, have had a generally negative impact. Minnesota was one of nine states to index personal income taxes between 1978 and 1980. Six of these, including Minnesota, experienced a loss in state revenues by the end of 1981. Some critics argue that Minnesota over-indexed, but the most likely cause for this decline in revenues is the severe national recession which began in 1981.

Minnesota personal income rose 10.3% in 1980-81, while the national average income rose 11.6% and there was a 10.4% inflation rate. At the same time that Minnesotans are experiencing both a reduced personal income and reduced state tax revenues, the New Federalism of the current national administration is creating major cutbacks in federal aid to states and localities.

In funding for elementary and secondary education, the federal share of Minnesota's education dollar has generally been around 6%. In 1981-82 the percentage dropped to 5.2 (while the national average was 8.1%). School programs that lose federal funding must either be eliminated or their costs must be picked up at the district level, where competition for dollars is growing.

Federal cutbacks in all areas of local and state services have, in 1982, been about 4%. In the previous two years, federal aid to Minnesota had grown 12.2% and 10%, respectively, making the 4% reduction seem even greater in comparison. Indications are that the reduction in

federal dollars will continue.

When cutbacks at the federal level occur more rapidly than they can be absorbed at the local level (or when local expenditures increase), the state is in the middle, suffering the major shock. Since states are constitutionally required to maintain balanced budgets, this squeeze may demand some fancy footwork.

School aids represent such a major percentage of the overall state budget that periods of fiscal crisis for the state affect school financing greatly. As one school board lobbyist put it, referring to the combined effects of the changes in population and the drop in state revenues, "I can see us being put in the position of fighting for tax dollars with the elderly and the handicapped . . . Not a pretty picture."

### D. The Courts and School Finance Reform: Legal Opinions of the Last Decade

Pressure from the courts was and is a factor influencing legislators to take action to improve equality of access to good public education in the United States. Curtailing of educational expenditures on the basis of property wealth, household income, municipal overburden, education overburden, or local votes to keep property taxes low have all been successfully challenged in court. Some court decisions require a state to consider education need and/or to implement some affirmative duty.

#### Serrano v. Priest

" . . . in a democratic society free public schools shall make available to all children equally the abundant gifts of learning."

*Serrano v. Priest*, California, 1971

Landmark school finance reform cases were *Serrano v. Priest I and II* (487 P.2d1241-1971<sup>1</sup> and 557 P.2d929-1976). The first case invalidated the California system of school finance on constitutional grounds. Relying predominantly on the local property tax, the financing system discriminated against the poor, making the quality of a child's education dependent on the wealth of his or her parents and neighbors. The California Supreme Court called for fiscal neutrality: an equal tax levy must mean equal amounts of money to spend on each pupil in every district.

In *Serrano v. Priest II*, the California Supreme Court accepted the proposition that a positive correlation exists between expenditures per pupil and the quality and extent of availability of educational

opportunities. While some difference in spending levels is necessary because of differing educational needs, the court ruled that the disparity existing then in California violated the state constitution's equal protection clause. The doctrines of fiscal neutrality and equal expenditures to provide equal opportunity were accepted as guides for the reform of school financing systems in several other states.

#### Other Court Decisions

Other decisions have followed, based on wording in each state's constitution or interpretations of the Fourteenth Amendment, with somewhat contradictory assertions of the level of equal opportunity that must be achieved by a state's school finance laws.

In the most recent ruling, the U.S. Supreme Court held that illegal alien children have a constitutional right to a free public education. The court announced in June 1982 that a 5-4 majority had upheld two lower federal court decisions which declared unconstitutional a Texas law refusing state funds for the education of the children of illegal aliens.

Associate Justice William Brennan stated for the majority that education is not a right under the U.S. Constitution, but that once a state provides it for some children, it must make education available for all children. Education plays a fundamental role "in maintaining the fabric of our society" and must be given special protection.

In an unusually clear example of the sharp difference of opinion within the court (and among other students of the issue), Chief Justice Warren Burger wrote for the minority, "the Constitution does not provide a cure for every social ill, nor does it vest judges with a mandate to try to remedy every social problem."<sup>2</sup>

Is either wealth or geography a permissible base for classifying children for the purpose of determining how much is to be spent on their education? Is wealth or geography so related to maintaining local control over the schools as to be considered "reasonable"?

Conflicts over school finance methods pit beliefs in a democratic society's need for equal opportunity for all of its children to receive the full benefits of education against beliefs in individual freedom and local control of schools. This conflict in values is discussed further in following sections.

#### Notes

1. References to court decisions list volume number, court reporter series title, and page for beginning of case. In series title, P.2d is *Pacific Reporter*, second series.
2. "Illegal aliens win right to schooling," *Minneapolis Star and Tribune*, June 16, 1982, p. 1.

## II. Conflicting Goals: The Legal, Legislative and Social Context

### A. School Responsibility for Social Concerns

What is the school's responsibility for social concerns, that is, nonacademic programs or services or targeted academic programs which benefit society as well as individuals (examples are drug abuse programs and hot breakfasts)? If there is a limited number of dollars, what is most important for schools to do? Are schools the best place to reach the most children and targeted adults with social service programs? If they are, should basic education funding be separated from the funding for these programs? If so, how?

Since the mid-Seventies, the emphasis in education has been on cost containment. Because of inflation and the sagging U.S. economy, people bearing the financial burdens are, in turn, exerting pressures on every level of government and on institutions such as the school system. As Robert S. Zais, Kent State University associate professor of curriculum and instruction, has stated, "personal financial distress is a most effective cure for an acute case of social consciousness."<sup>1</sup>

#### Social Programs in the Schools

The dilemma of education is that the schools have been delegated multiple responsibilities, often without adequate means to carry them out. Schools have been given these tasks because a) the students are a captive audience, hence easy to identify and reach out to; b) the thinking has been to identify and meet the needs of the poor, disadvantaged and/or handicapped early in life, so that they may develop their potential as individuals and fully functioning members of society; and c) they are well known, accessible places in almost every community. And, while there are constituent pressures for the schools to maintain their social programs, there are also pressures to "return to the basics"—reading, writing, arithmetic—and abandon other roles.

Some of the programs and services are federal- or state-mandated. Others have been initiated at the local level. They are funded by federal, state, and/or local money. Complex problems of overlap can result, which sometimes lead to objections at the local level about the burdens of administering them.

They include:

- special education for handicapped, mandated by federal and state legislation;
- vocational education;

- cocurricular and extracurricular activities, including sports, music groups;
- community education, including classes for adults, summer school, recreation programs, and day care;
- child nutrition, including lunch, breakfast, and milk programs;
- ESEA Title I, the federal program for improvement in basic skills;
- migrant education;
- Indian education;
- pupil personnel services, including counseling, health, and career planning;
- preschool screening for health and developmental problems;
- early childhood and family education programs;
- bilingual education and English as a second language;
- chemical dependency education;
- driver education;
- family life, including sex education.

Title IX is a mandated but not funded federal program to regulate educational equality between the sexes in schools. It requires certain administrative procedures which do represent a cost to a district.

Desegregation as one method to help provide equal educational opportunity has been a social concern of the state. To comply with state regulations, Minneapolis, St. Paul, and Duluth school districts have instituted measures, including busing, to achieve numerical desegregation. While there is no evidence to suggest any return to pre-1974 segregation, some people are concerned about equal educational opportunities as districts face budget constraints.

Reductions are being made by the Legislature in aids for special education, through more restrictive definitions of those who qualify. Restrictive definitions on services for the handicapped are also being applied by the federal level. On June 28, 1982, the U.S. Supreme Court ruled that federal law entitles handicapped children to a public education from which they can derive "some educational benefit," but that local districts are not obligated to provide such services as handicapped children may need to reach their full academic potential. The decision may potentially affect four million handicapped children receiving education and special services in the public schools.<sup>2</sup>

#### Task Force Conclusions

The main question for the public to deal with at this time is: If there are limited dollars for the public schools,

what is most important for them to do? The following are some of the conclusions and recommendations of the Governor's Task Force on Educational Policy (1981) to the Legislature:<sup>3</sup>

"The primary purpose of schools is instruction. Therefore a clear distinction must be made between the primary areas . . . and the supporting services which public policy determines that schools should also provide . . .

"Any new charge to public schools should be preceded by an impact statement which expresses its effect on the time, staff, and dollars available for instruction . . .

"Schools are asked to fulfill multiple goals as defined by a wide variety of constituent groups. It is likely that the number of required missions will increase. These expanded functions may erode resources available for instruction.

"The public school is increasingly being used as a vehicle to deliver social service programs. These programs need to be identified and the most appropriate agencies for their implementation and funding defined.

"It is imperative that the instructional role of schools remain primary. A precise definition of the role and purpose of schools involves areas which are beyond the purview of the Governor's Task Force on Educational Policy (e.g. interagency relationships in the provision of support services). The Task Force believes, therefore, that a blue ribbon legislative commission with specifically-designated staff support is the most effective vehicle to develop recommendations to the Legislature."

These recommendations, formulated by a representative body of Minnesota citizens, suggest the trend, in hard times, toward a clearer definition of what we want from our schools and what we can afford.

#### Notes

1. Robert S. Zais, "In One Era and Out Another: Anti-School Philanthropy and the Sociology of Curriculum Change," *NASSP Bulletin*, Vol. 64, April 1980, (National Association of Secondary School Principals), 17.
2. Article in *Minneapolis Star and Tribune*, June 29, 1982, 1 and 4.
3. *Focus on Learning: Volume I: Conclusions and Recommendations*, 5-11.

### B. Public Funding of Nonpublic Schools

Nonpublic schools: How, and how much, do the state and nation finance them? Is this appropriate?

During the 1979-80 school year, 10% of the school-age population in Minnesota



attended the nonpublic schools, as compared to 10.9% for the United States as a whole. About 91,000 Minnesota students attended nonpublic elementary and secondary schools in 1981.

Proponents of public aid for nonpublic schools claimed in the late '60s that parochial schools in the nation were under financial strain and faced huge tuition increases, which would drive away pupils. Between 1968 and 1973 these schools lost a quarter of their students. Since then nonpublic school enrollments have remained fairly stable nationally as public school enrollments have declined.

#### Federal Legislation Provides Support

Since the passage of the Elementary and Secondary Education Act (ESEA) of 1965, public financial support for programs, projects, instruction, services and textbooks in nonpublic schools has increased at both federal and state levels.

ESEA and the other federal legislation that followed (for school lunch and breakfast programs, for example) aimed to meet the increasingly diverse needs of this country's educational system, yet stay within constitutional limits. Materials and services were offered to students of both public and nonpublic institutions. The Courts have upheld the constitutionality of this legislation when it has met the judicial criteria: the materials and services were secular and benefitted the child, not the institution; and the programs did not entangle government with religion.

The administration, benefits and services are generally provided through and under the supervision of the State Department of Education (SDE) and the local public school. This supervision is required in order to keep the public funds separate from the sectarian institution.

Not all nonpublic school administrators choose to use every program from which their students could benefit. If it does adopt a program, the nonpublic school is subject to regulations and accountability measures similar to those required in the use of public funds by public schools.

Some of the federal legislation of the 1960s and 1970s has been changed or phased out. The momentum of the 1980s swings toward tuition tax credits, tax vouchers, consolidation of federal and categorical grants, or even the elimination of the federal role in elementary and secondary education.

#### State Funding

At the time of the federal legislation cited above, similar laws were being passed by the Minnesota Legislature. Each of these statutes was, and is, "provided in order to promote equal educa-

tional opportunity for every school child in Minnesota and to assure all Minnesota pupils and their parents freedom of choice."<sup>1</sup> The state now appropriates money for busing of nonpublic school students; shared time; textbooks, individualized instructional materials and standardized tests; health services; guidance and counseling services; and special education. Most of these services are provided at the public school or at a neutral site.

#### Income Tax Deduction

Minnesota is the only state in the nation where parents of nonpublic school children receive a standard deduction on their state income taxes for costs of nonpublic education. Those with children who attend Minnesota, North Dakota, South Dakota, Wisconsin or Iowa elementary or secondary nonpublic schools may deduct up to \$500 for each child in grades K-6 and up to \$700 for each child in grades 7-12, if those amounts are spent for tuition, nonreligious books, or transportation.

This legislation has been upheld as constitutional by the Minnesota Supreme Court, while similar legislation has been declared unconstitutional in other states. The case is being appealed to the U.S. Supreme Court by the Minnesota Civil Liberties Union.

In a 1981 speech,<sup>2</sup> Van D. Mueller, past president of the Minnesota Parent-Teacher-Student Association stated that the "expenditure of public funds amounts to an average of \$180 for each of the 90,954 students in the nonpublic schools. The use of funds for the support of nonpublic schools amounts to a little over 1 percent of annual appropriations for elementary and secondary education." He added that during 1979-80, Minnesota spent \$16.4 million in nonpublic school aid, including the \$2.2 million for the tax deduction available to parents whose children attend nonpublic schools.

#### Tuition Tax Credits

Tuition tax credit proposals have been introduced in Congress since the early '50s. Such credits allow eligible taxpayers to subtract from their income tax bills for a given year a designated portion of the tuition they had paid to certain nonpublic schools. Debate on the subject intensified with the 1980 Republican Party platform plank favoring the concept and the Administration's recent proposal.

The President's bill, introduced in Congress in June 1982, would allow parents of private and parochial elementary and secondary students a tax credit equal to 50% of tuition paid, up to a maximum of \$100 per child in 1983, \$300 per child in

1984, and \$500 per child thereafter. Those families with adjusted gross income of up to \$50,000 could claim the full credit; those earning up to \$75,000 would be eligible for part of it. Families with incomes above \$75,000 would not be eligible. The proposal denies credits for schools that practice racial discrimination.

One estimate is that the tax break would cost the Treasury \$100 million in 1983, and the cost would grow to \$1.5 billion in 1987.<sup>3</sup> This would not appear in the federal budget as an expenditure, since tax credits limit government income.

Credits to special groups have increased over the years, and their cost is considerable. Once in place credits are rarely removed; each has a strong lobby on the lookout for further increases.

The League of Women Voters of the United States has opposed tuition tax credits since 1978 on the grounds that they would thwart equal access to education. The organization is working with other groups in a coalition to defeat the Administration's bill.

#### Questions Raised

The issue of aid to parents of nonpublic school students produces many questions: Who should control education, the family or education professionals? Should taxpayers have to pay more through tuition tax credits to extend the power of choice to families who cannot now afford private education? Is such aid constitutional? Do children rather than religious institutions benefit from these public expenditures?

Private and parochial schools are not bound by federal, state, and local mandates; they control the composition of their student bodies; and they are not officially accountable to the public. Can a public education policy that subsidizes the maintenance of two sets of standards, one for public and one for nonpublic schools, be consistent with democratic principles?

There has been a great deal of litigation over the appropriateness of financial support to those in nonpublic schools. The main argument made by proponents of aid is that parents of nonpublic school students pay for both public and private schooling and should get some relief from this double burden. They also claim that aid promotes competition and quality among all schools by encouraging choice.

The position of the Minnesota Education Association (and other opponents of aid) is that the primary responsibility for public education is granted to the state Legislature by the Minnesota Constitution and that "the only appropriate edu-

cation expenditure of tax monies is for public education."<sup>4</sup>

The Minnesota Legislature has continued to grant support for nonpublic school students through income tax deductions and categorical aids legislation, a majority believing that the expenditures promote equal educational opportunities. There is a strong lobby for such aid.

As the financial woes of public education increase, so do complaints about the administrative burden on the public schools as they carry out the directives of state and federal laws which provide for the nonpublic school student. According to one administrator, the up-to-5% allowed by state law does not truly cover administrative costs; and a local district's general fund sometimes must cover for a late appropriation (or, as in 1982, a cut-back in state allocations). Finally, public school officials find themselves having to pass judgment on what is "secular, neutral, and nonideological."

The challenge of the 1980s is how to maintain equal educational opportunity for all school-age children without incurring religious, political, and administrative entanglements.

#### Notes

1. *Minnesota Statutes on Nonpublic School Aids*.
2. Van D. Mueller, "Are Nonpublic Schools a Threat to the Survival of Public Schools in Minnesota?", speech, 1981.
3. "Reagan urges tax credits for private schools," *Seattle Times*, June 24, 1982.
4. *Report of MEA Task Force on Nonpublic Schools*, Minnesota Education Association, 1981, 1.

### C. Equal Opportunity and Quality

What is the philosophical base for our belief in equal opportunity for all children to get a good education? How do we define "equal opportunity"? How do we measure it? How can we balance this goal with the other basic goals with which it may be in conflict?

Equality denotes sameness, uniformity. It generally means things are the same or becoming the same. Equal treatment does not necessarily provide equal ends, since the members of a group (students, school districts, taxpayers, etc.) do not begin at equal places.

Equity is fairness. It means that the potentials are equal. Equal opportunity and equal access refer to equity. In the interest of equity, members of a group may receive unequal treatment.

Crucial to the theory on which our Constitution is based is the idea that individuals have the self-critical ability, developed through education, to choose their own ways of life. Equal opportunity is a core value in American society.

#### Results of Research

Is it possible to select a reasonable

measure of equality of educational opportunity? Some researchers measure equality of educational opportunity in terms of school services, "inputs"; others choose student achievements, "outputs."

Over the past two decades, studies have demonstrated that certain schooling experiences do make a difference for children: money spent on schools contributes to the quality of the school experience offered. In what is probably the most comprehensive survey of research done on equality of educational opportunity through the 1960s, James Guthrie established several important relationships:<sup>1</sup>

1. Socioeconomic status is an excellent predictor of available school services.
2. A positive relationship exists between the quality of school services provided to a pupil and his/her academic achievement. Also, school staff and children's access to the staff are important.
3. Post-school opportunities of students are related to their achievement in school.

More recently, studies have attempted to isolate the factors which may produce a quality school experience for children, measured by such outputs as higher test scores and number of college bound students in a school. Declines in test scores closely parallel the enrollment declines in subjects such as regular English, American history, math and science courses. Public high school students spend a small amount of time doing homework when compared to their private school peers (Coleman, et al., 1981). Yet college-bound students in more traditional courses in public schools do not show the precipitous drop in test scores that has occurred recently among the general student population. Schools apparently can make a difference, but attention must be paid to their staff, course content and overall morale.

#### Equity and Quality—In Conflict?

When we talk about equity, we must realize that there are many different kinds. Taxpayer equity was what the state Legislature had in mind in 1971. A teacher might rather see a focus on salary equity. Most likely student equity is program equity, or comparable access to educational programs regardless of local community tax wealth.

Are both equity and quality possible? "... equity ... is not the only value by which our society lives. Do we not aspire to quality, or even the possibility of excellence? ... A democratic society built upon a free enterprise system must live with this dilemma, that equality (of opportunity) and quality are perennially in

tension one with another. Wisdom resides in understanding that the dilemma can never be fully resolved without destroying what we are."<sup>2</sup>

Others argue that not only is it possible to have equity and quality, it is in fact really not possible to have one without the other. For these people, equity is adequate funding of different costs of providing an equivalent quality education. Unless we plan to fence off our school district from the rest of the world, a loss of equal access to good education for any of our children anywhere diminishes all of us.

#### Notes

1. in *Schools and Inequality*, (Boston: MIT Press, 1971).
2. Tom Sabal, Superintendent of Schools, Scarsdale, New York, speaking about an *amicus curiae* brief filed with the New York Court of Appeals in *Levittown v. Nyquist*. Quoted in letter from education chairperson of LWV of Scarsdale.

### D. Local Control

Local control is something many people want more of, but defining what it is and how to attain it is very difficult. Local leeway, local participation in decision-making, local incentive, local governance, local choice, local voice, local responsibility are all terms used synonymously with local control. But all are open to interpretation. Control over taxation and/or control over management of schools may be clearer definitions of "local control."

Questions raised by the concept of local control are many: Who exactly do we mean by "local"? The school board? Parents? All the citizens of the school district? Are school board members representatives of the people who elected them or are they spokespeople for the school district? How much control is desirable—total, or some degree of leeway within state and federal regulations?

Fiscally, the question is who pays and why. Central issues today in Minnesota are levy authority and limitation, mandates, collective bargaining, quality education, and equal opportunity.

Local control is not mandated in the Minnesota Constitution. "Local participation in decision-making is a product of statute and tradition."<sup>1</sup> Local boards, local long-range planning committees, and local referendum levies are all permitted by state statutes. However, there are other statutes which limit local flexibility in fiscal management.

#### Two Facets of Control

The two major facets of local control, finance and governance, are, theoretically, independent of each other. However, there is a general feeling (which was clearly expressed in the survey con-



ducted by LWVMN) that increased reliance on local revenues brings increased local control over the governance of the school district. In practice, this may or may not be true.

A number of Minnesota school districts are "off the formula." However, these districts are no more free to use the funds in any way they wish than is a district which raises very little of its Foundation revenue locally, and thus receives a great deal of state aid. Each district must conform to state and federal requirements.

State law also requires that money for operation of the schools be in separate funds. In general they may not transfer the money received for one fund to another.

The Referendum Levy allowed by the state law does provide some amount of local control. In many cases, school boards must "sell" the voters on the increased levy with extensive publicity about how the money will be used.

Many complaints about lack of local control are not concerned with financing at all, they are expressions of frustration at a perceived excess of federal and state program and reporting requirements. Many local school people feel that they have too little leeway to tailor educational programs to their own needs. Their demands are not necessarily for unrestricted local control, but for more freedom to choose their own options within a basic framework.

Pros and Cons

In addition to definition problems, the idea of local control raises perplexing issues of quality and equity. Proponents of local control insist that it would allow more variation and innovation in educational programs, that instead of being rigidly circumscribed by state and federal regulations, each school district could be responsive to local needs and desires. Opponents of local control are afraid that instead of innovation there would be stagnation, and there is concern that some school districts would not offer an adequate curriculum if it were not required.

Some districts are more able to support schools adequately than others. The property tax is perceived as an unfair tax. Those concerned about equity are not necessarily opposed to local fiscal control provided that local levies are equalized or "made fair," disparities are not great, and the level of support ensures a quality education.

Whether people favor or oppose local control probably depends greatly on how they perceive their own school district and its citizens, and how they perceive state actions on education. Local control is likely to look good or bad according to

whether the individual agrees or disagrees with the school district's philosophy and actions.

Does every child have a right to some basic level of education? If so, must local control be curtailed to some degree in order to assure that it is provided? At what point does a locality's lack of ability or desire to finance a basic or high quality education mean that its children are disadvantaged simply because they live there?

Note

1. The Condition of Education, Minnesota State Department of Education, 1980.

E. Responsible Taxation

The State of Minnesota raises revenue to finance state and local services by levying several kinds of taxes. Minnesotans pay taxes on individual and corporate income, retail sales, real estate valuation and inheritances, as well as excise taxes on a host of products, and a variety of other fees.

Comparison of Minnesota state and local tax collections to those of other states and localities shows that in 1980 Minnesota relied more on the taxation of income, considerably less on sales, and somewhat less on property taxes than the national average. These percentages may not reflect today's reality, since sales taxes have been added and the Legislature has shifted some of the burden of funding education and local government back to the property tax.

In 1979-80 Minnesotans paid a larger part of their income as state and local taxes than did residents of 41 other states.<sup>1</sup> In that year Minnesota's state and local tax collections of \$1124.73 per capita ranked ninth highest in the nation.<sup>2</sup>

Criteria often used to judge the desirability of a tax include the concepts of equity, convenience, certainty, economy and incidence.<sup>3</sup>

Tax equity is often defined as equal treatment of similarly situated taxpayers. Application of this criterion is difficult because it is hard to determine the conditions under which two taxpayers are similarly situated. Students of taxation have expanded the concept of equity further to include vertical equity; i.e., unequally situated taxpayers should be treated differently. Those with greater ability to pay should pay a larger part of the total taxes. The most commonly used measure of ability to pay is income.

Taxes can be further described in relation to income as being progressive, proportional or regressive:

**Progressive Tax:** The proportion of income paid for tax increases as income increases.

**Proportional Tax:** The proportion of income paid for tax remains constant as income increases.

**Regressive Tax:** The proportion of income paid for tax decreases as income increases.

A tax is deemed *convenient* if it can be easily assessed, collected, administered and paid by the taxpayer.

The taxpayer should know with reasonable *certainty* how much tax is owed. Historically this criterion has also implied that the taxing unit should be able to predict with accuracy the amount of revenue that will be raised by the tax.

A good tax should be relatively inexpensive to collect and administer (*economy*).

Consideration must be given to who finally pays the tax (*incidence*). For example, a tax on resources owned and used by a Minnesota farmer, such as the agricultural land tax, may be borne by the farmer or shared by his/her customers in the form of higher product prices. Tax experts often disagree on the incidence of taxes levied on products, business profits, and resources used in production.<sup>4</sup>

An additional concern in levying state and local taxes must be the effect of the tax on the level of economic activity in the area. Since businesses, property investments and people are mobile, excessively high taxes levied in one locality can often be avoided by moving to another locality. Concerns about the "business climate" in Minnesota are being heard with increasing frequency.

Who Should Pay?

What level of government should support primary and secondary education? The Correspondence Principle of public finance suggests that, ideally, jurisdictional boundaries for governments should be drawn so that the people who participate in the government are the same people who enjoy the benefits and incur the costs of the services provided. Achieving the ideal is, of course, impossible. We would have different taxing units for each public service. Using a limited number of governmental units inevitably results in cost and benefit spillovers.

Of particular relevance in determining benefit from primary and secondary education is the mobility of persons educated by any particular school district. The people educated in Hibbing do not live out their lives in Hibbing and are involved in decisions affecting people living elsewhere; outsiders are responsible for the wellbeing of Hibbing residents. Therefore, the benefit profile extends far beyond the town. The Correspondence Principle suggests that responsibility for basic education should likewise extend

Percent of Funds for K-12 Education in Minnesota from State and Local Sources\*

Year	Total Revenue (In millions)	% State Aids	% Local Property Tax
1971-72	1,181+	55.1	44.9
1972-73	1,222+	63.5	36.5
1973-74	1,302+	64.8	35.2
1974-75	1,435+	67.8	32.2
1975-76	1,542+	66.4	33.6
1976-77	1,656+	67.6	32.4
1977-78	1,782+	64.6	35.4
1978-79	1,877+	66.1	33.9
1979-80	1,961+	66.0	34.0
1980-81	2,085+	68.4	31.6
1981-82	2,235+	73.1	26.9
1982-83	2,265+	63.3	36.7
(1982-83 after property tax shift)	2,265+	57.2**	42.8

\*includes post-secondary vocational education; excludes federal revenues. Percentage local property tax reflects amount actually certified and paid by taxpayers after reductions for all credits. (State tax aids to reduce the levy increased 355% over the 11-year period.)

\*\*state aids reduced \$137.6 million (estimate) and same amount of payable 1983 property taxes shifted from FY 1984 to FY 1983 to increase local share of costs. (Total state aids, after the property tax shift, increased 99% over the 11 years.)

Source: Joyce Krupey, Office of Senate Research, State of Minnesota.

beyond the boundaries of the local school district.

Problems With Local Funding

Financing education on the local level also presents several practical difficulties, beyond the tax philosophy reasons against it. Local school districts are allowed to use only the local property tax to raise revenue. This tax is perceived by citizens as being one of the "least fair" taxes.<sup>5</sup>

Local financing also invites the problems associated with flight of capital from high tax jurisdictions. "If rate differences exist, investors will prefer to locate prop-

erties in low tax rather than high tax areas, and a cumulative set of forces may be set in motion that can greatly increase fiscal disparities among different government units. As more and more taxable property leaves high-tax areas, rates in those areas may be forced higher and higher."<sup>6</sup>

Problems With State Funding

Increased use of state funding also presents difficulties. State revenues are dependent on sales and income tax collections, which tend to fluctuate with the level of economic activity. Recently school districts have been forced to

III. Other Ways to Finance Schools

A. Reform in Other States 1970-80

During the last decade, more than half the states overhauled their structures for financing elementary/secondary education. Reformers tried to make schools even more an equalizing force in America for both taxpayers and students. Five major themes characterize the finance reforms enacted during the 1970s:

1. **General operating and equalization aid programs were broadened and strengthened.** Low wealth districts were "leveled up" by state aids rather than high spending districts being leveled down. To accomplish this, 13 states, including Minnesota, enacted *higher level foundation programs*. Seven states enacted formulas which *reward equal local effort with equal revenue yield* (see section on District Power Equalization). Under a method which *combines these approaches*, local districts in five states may choose
2. **Income has been added to property wealth in seven states as a measure of fiscal capacity.**
3. **States have instituted or dramatically increased support for high cost programs for special populations** (the physically or mentally handicapped, economically or educationally disadvantaged).
4. **States have also designed formula adjustments and factors to assist school districts with particular characteristics**, such as sparse population,

absorb cutbacks in state funding as tax collections responded to recession and declining farm incomes. In times of crisis that diminish the state's ability to support education, the local property tax may be perceived by some as a good base for financing education, despite its drawbacks.

Funding Education in Minnesota

Funds for primary and secondary education in Minnesota have in recent years come primarily from the State. The State uses taxes on income and sales as its primary sources of tax revenue. In 1971 44.9% of school revenue was generated from local property taxes. As the table shows, the trend toward reduced reliance on local property taxes which began in 1972 continued through 1981-82. Projections for 1982 and beyond indicate a dramatic reversal of this trend due to the state's fiscal problems.

Notes

1. U.S. Department of Commerce Bureau of the Census, *Governmental Finances in 1979-80*, GF 80 No. 5, p. 94.
2. Ibid., p. 90.
3. Minnesota State Department of Education, *The ABC's of Minnesota School Finance*, pp. 9-10.
4. Ray M. Sommerfeld, et al, *An Introduction to Taxation*, 1982, pp. 1/16-1/17.
5. Survey conducted by Opinion Research Corp. of Princeton, N.J. for the Advisory Commission on Intergovernmental Relations, Washington, D.C. 20575. Annual reports are available.
6. Wayland D. Gardner, *Government Finance, National, State and Local* (Prentice Hall, 1978), p. 389.

one-room schools, few pupils, low wealth with high tax rates, municipal overburden, or high-priced education resources.

5. **Tax and spending limitations on local school districts have been established in nearly two-thirds of the states.**

Litigation Continues But Reform is Slowing

School finance litigation continues in many states. Most cases are brought either on state equal protection or state equal education clauses. Several states are undergoing reviews of their finance structures. Citizen groups are keeping a variety of general and specific goals alive. Clearly, the job of devising equitable systems of school finance is not complete.

Given inflation, dropping enrollments, and declining political support, however, increases in education expenditures in the '80s are unlikely to match those of the '70s. Competition among various levels of



government and among various public services for the shrinking public dollar will also have an impact on the pace of education finance reform.

### Financing Options

The next four sections explore briefly some of the financing methods adopted by states or developed by theorists that

are different from Minnesota's Foundation Formula approach. The accompanying chart, which compares the major alternatives, will help clarify the differences among them.

Comparison of School Finance Structures

	Minnesota Foundation Formula	Full State Funding	District Power Equalization	Program-Based Funding	Vouchers
Government level that sets tax rates and type of tax	state: income, sales; state & district: property	state: income property &/or sales	district: property; may be state limit	state: any state tax (& district if local supplement is allowed)	state: any; consumer chooses level of school support
Level that collects taxes	state: income, sales; county: property	state	state & district or local	state & district or local	state
Level at which policy is made	state & district	state & district	state & district	state standard curriculum; local options	state standards; each school chooses own
Level at which expenditures are made	district	district	district	district	individual school
Effects	equal minimum resources per pupil unit; additional local levies, some power-equalized, state pays % of categorical aids; uncapped local option to raise & spend more with non-equalized referendum levy	substantially equal funding per pupil; some extra funding is possible as needed	substantially equal funding per pupil for equal tax effort; if districts choose different tax rates, unequal funding per pupil results	equalizes services available to students up to a minimum level	consumers choose among schools with different per pupil costs & get equal buying power for equal economic sacrifice

## B. Full State Funding

Full state funding allows money for schools to be collected where taxable income can be found and then redistributed where it is needed to provide an acceptable and uniform standard of education. In 1972, James B. Conant wrote, "... removing consideration of financing from the local level would ... allow both parents and school authorities to concern themselves with the real matters of education and make decisions on the basis of educational worth."<sup>1</sup>

After completing a two-year study, the Fleischmann Commission recommended full state funding for the state of New York in 1972.<sup>2</sup> According to the Commission's plan, revenues would have come either from a statewide property tax or more intensive use of state income taxes and sales taxes.

### Pros and Cons

Arguments against full state funding usually begin with the claim of loss of control by local boards of education. The Commission argued that studies have concluded that centralization of financing and decentralization of policy making are not inconsistent concepts. The Commission recommended several specific plans for maintaining and/or increasing local control of policy making, including strong local citizen advisory groups and parent organizations. Local boards of education would continue to hire teachers and plan curriculum.

Supporters of other funding methods debate proponents of full state funding over. . . "whether deliberate funding

inequality, which is what ensues from district choice, more nearly approaches a 'just' system than does some imposed 'equality.' This debate, in turn, revolves around the extent to which the desires of parents are to be considered in discussing what is justice among children . . . the needs of children themselves will probably be more determinative when finance decisions are made by a unit of government that is less responsive to direct parental pressure than is the school district."<sup>3</sup>

As of today, no state has adopted full state funding. Hawaii has centralized finance, but operates its schools as one big district, so most authors discount this as being true full state funding. According to Walter Garms, the high level foundation plans of Minnesota and New Mexico have come closest to full state funding.<sup>4</sup>

Without a greater concern for tax and expenditure equity and a willingness to yield some local decision-making on expenditures, it is unlikely that full state funding in its purest form will become popular with state legislatures.

### Notes

1. James B. Conant, "Full State Funding," *Financing Public Schools: Selected Papers from New England School Development Council Conference*. (Cambridge: Federal Reserve Bank of Boston, January, 1972.)
2. *The Fleischmann Report on the Quality, Cost and Financing of Elementary and Secondary Education in New York State*. (New York: The Viking Press, 1973).
3. S. Michelson, "What is a 'Just' System for Financing Schools? An Evaluation of Alternative Reforms," *Law and Contemporary Problems*. Winter-Spring 1974, Vol 38, No. 3, p. 442.
4. Walter I. Garms, "Measuring the Equity of School Finance Systems," *Journal of Educational Finance*, Vol 4, No. 4, Spring 1979, p. 199.

## C. District Power Equalization

In the book *Private Wealth and Public Education*, John E. Coons and associates held that the quality of a child's education should not be a function of wealth except the wealth of the state as a whole.<sup>1</sup> The book emphasized the importance of fiscal neutrality with regard to district wealth<sup>2</sup> as a basis for school finance and supported local choice in the level of funding. The authors outlined the theory of district power equalizing and gave some practical applications of this method of funding. By 1980, more than 20 states were using some form of district power equalizing (DPE).

### Equity and Local Choice

The distinguishing factor of DPE is the attempt to deal simultaneously and constructively with the usually conflicting principles of taxpayer equity and local choice. Pure DPE allows each district to elect to support its schools at the tax rate it chooses. A type of taxpayer equity is achieved by "neutralizing" the property wealth, or income level (or both, depending on the type of tax or taxes used) of all school districts, theoretically producing equal reward (amount of revenue) for equal effort (locally chosen tax rate). This is viewed as giving each school district equal "power" (ability) to raise revenue. The state guarantees a certain amount of revenue for a given tax rate.

In property-poor school districts, the state makes up the difference between what is raised locally and what the state guarantees. In property-rich districts, where the given tax rate would raise more

than the guaranteed amount, excess funds may or may not be "recaptured" by the state and redistributed to the poorer districts.

Recapture enhances the equity principle where there are wide disparities among districts in actual tax base, and it can help offset state costs. This feature tends to be unpopular with wealthy districts. Equity in DPE may also be enhanced by reorganizing districts to create ones with more nearly equal tax bases.

A state can impose constraints consistent with statewide goals; however, equity and local control may be undermined by too many restrictions. If a state adds many constraints, the formula can become extremely complex. Achieving true wealth neutrality has proved difficult under DPE programs in use today, mainly because of 1) political and judicial opposition to recapture provisions, and 2) cost controls imposed by legislators who fear high state expenditures.

### Power-Equalized Supplements

Power equalizing is used not only as a major method of school finance, but also as a supplement to other finance systems. For example, in addition to offering Foundation aid, Minnesota could power equalize its Referendum Levy, making it more "wealth neutral." Currently Minnesota's Discretionary Levy is power equalized, although there is a limit to the tax rate a local district can adopt (up to 2.25 mills for 1982-83). The state determines a guaranteed amount of revenue, proportionate to the mill rate chosen by the district.

### Notes

1. John E. Coons, William H. Clune III, and Stephen D. Sugarman, *Private Wealth and Public Education*. (Harvard Belknap Press, 1970).
2. Fiscal neutrality concepts: 1) *Ex ante*: the ability of a district to support schools should not depend on its wealth; 2) *Ex post*: actual level of education support must not correlate with wealth.

## D. The Voucher System

The most frequently discussed voucher system would bring the goals of district power equalization down to the individual family. It would supply public dollars to power equalize each family's decision on how much to spend on their children's education. Coons, Sugarman, and Clune, the originators of DPE, have lobbied steadily for a voucher system as a means of empowering poor families and encouraging new ways of educating.

Their voucher system would create school offerings at several different levels of per pupil cost. Schools, public and/or private, would compete for the business of education consumers. These consumers would have been given equal buy-

ing power for equal "economic sacrifice" through vouchers. Anyone could go to any school within the system. Every family choosing a particular school would make an equivalent economic sacrifice, regardless of family income. A sliding scale (based on financial need) would determine how much the voucher would cost (like food stamps). Thus vouchers with the same market value would have different purchase prices depending on the consumer's income.

Proponents of a voucher system maintain that schools would offer a variety of educational programs with differing costs, thus providing choice and incentive for a quality education. Opponents argue that under a voucher system, social, racial and religious segregation might increase. In the competition for students, schools that stress achievement might tend to select only good students and promote academic segregation.

Some people question whether the voucher system would have any validity in small rural school systems. Choice becomes pointless if there is little diversity. And, it is argued, if the system were implemented in the metropolitan area only, where there are sufficient options to allow a "marketplace" approach, it would create divisions between metropolitan and rural districts.

## E. Program-Based Funding

### (Foundation Service Program)

A report produced in 1981 for the Minnesota Senate Education Committee<sup>1</sup> outlined a new method, the Foundation Service Program (FSP), which would fund by *program* rather than by *pupil*. This is not a total school financing system; it says nothing about how the money for public schools would be raised, or whether there would be local options to spend above the FSP level. Program-based funding, as visualized in the study, would include the following concepts:

1. Foundation revenue provided to a school district would be the dollars necessary to fund a standard set of instructional and support services for that district. However, the local school board, working within the dollar limits of this funding method, could put curricular emphasis where it believed it was needed. (A program-based system could, however, require that all or part of the standard curriculum be offered by the school in order to get state funding.)
2. Assuming that the basic cost of providing such a standard program is people cost, the FSP is described in terms of full-time equivalent (FTE) professional

staff by program area that are required for each 1,000 students. The standards used were not hypothetical ideals but were based on what was actually happening in Minnesota schools in 1977-78.

3. A "training/experience index" for teachers and regional salary schedules would be developed. The number of FTE staff needed to supply the model curriculum multiplied by the overall training/experience index for the individual school district multiplied by the regional salary base would determine the revenue allocated to a particular district for licensed regular instruction.

Looking at actual practice in the state, the researchers found that Minnesota students did not have comparable access to school-provided professional services as of 1977-78. Wide variations among districts were found in, for example, ability to deliver instruction in such special service subjects as art and foreign languages. Implementation of FSP in 1977-78 would have required a 12% overall increase in licensed instructional staff and a 7% increase in funding.

Variations of the program-based funding system outlined above are possible, of course. An example is funding of a minimum program with no weighting for statewide salary differences and allowing a power-equalized levy for any amounts above the minimum.

### Pros and Cons

Some of the arguments for the use of a program-based school financing method using FTE teachers per 1,000 pupils as the funding unit are that funding would be sensitive to enrollment change. Service capability is a better measure of quality and equal opportunity than number of electives, class size, or dollars per pupil unit. Significant curriculum control would be left at the local level.

Arguments against program-based funding are that developing the specialized data base necessary to manage the system and increasing staff levels to achieve a pupil/teacher ratio of 20/1 would be expensive. For small school districts of under 300 students, it would be difficult to supply a full program of services using the FSP formula, unless the ratios were adjusted downward, resulting in substantially greater cost statewide. The public might not accept the inclusion of local cost differences in the funding formula. Some of the major beneficiaries of the program would be those districts which have the most experienced teachers, districts often thought to be over-advantaged already. Finally, if a previous year's data on teacher training/experi-



ence levels and regional salary scales were used to determine the current year's funding, existing cost differentials might be perpetuated.

#### Note

1. Joyce Krupey, director, *Foundation Service Program Study*. (St. Paul: Education Committee, Minnesota Senate, 1981).

## F. Policies That Affect Financing

### Disparities in Staff Salaries

A discussion of school finance that considers only revenues and legislative attempts to equalize them is incomplete. In most school districts nearly 80% of income is used to pay salaries and benefits. In 1980-81, average professional staff salaries in Minnesota ranged from \$11,308 to \$25,370 among the school districts. The reasons for this wide range include staff maturity, staff level of postgraduate achievement, and the effectiveness of contract negotiations.

Solutions to the problem of vastly differing salary costs from district to district are beyond the scope of this study. But, as we attempt to provide equal opportunity in education, a labor-intensive business, Minnesotans cannot overlook the disparities in labor costs among districts. Equal dollars do not necessarily deliver equal services throughout the state.

### School District Reorganization

To determine whether or not reorganization is an answer to some of the financial problems facing the Minnesota educational system in the 1980s, let us look at the three aims of the advisory commission which guided local groups in the consolidation of school districts following 1947 legislation. These goals were restated in a 1977 bill which would have dissolved present districts and established 92 county-sized school districts. (That proposal was strongly opposed and soundly defeated.)

1. Does consolidation offer "better educational opportunities"? Reorganized districts reported to the Commission on School Reorganization appointed by the 1947 Legislature several advantages, including the following: expanded curriculum, better trained faculty and improved holding power, i.e. more students graduate. Optimum size studies conducted by the State Department of Education (SDE) argue that a minimum basic program would require a secondary teaching staff of 12 to 14. To support such a staff, the enrollment would have to be at least 200 secondary students. There are several school districts in Minnesota that have fewer than 200 students, K-12.

Although the Commission on School Reorganization seems to have succeeded in its mission, there was one goal unfulfilled in 1971, when the work was finally completed. That was, according to the commission, the "merging of inefficient secondary districts into stronger units of operation." Since 1971 there has been little progress in that direction. Now, more than a decade later, that unfinished business may need to be tended to.

The explosion of knowledge that has occurred in the mid-Twentieth Century makes greater demands than ever before on both students and faculty. There are no easy career choices any more, and a limited secondary curriculum puts high school graduates at a disadvantage that is not only unfortunate but may be challenged in court.

2. Does reorganization offer "more economical and efficient operation"? Although the best answers to this may have to await the results of a study undertaken by the Blue Earth County districts on this specific question, a partial answer can be derived from reports to the SDE on paired districts. Statutes enable two or more districts to enter into a pairing agreement and permit them to discontinue some grades and to cooperate on programs and services. Sometimes this pairing leads to consolidation. Paired districts report savings from fewer staff and administrators, while additional elective choices are available. There are, of course, some increases in costs due to pairing, the largest being for transportation.
3. Will reorganization ensure a "more equitable distribution of school revenues"? Under the current per pupil unit funding, the size of a school district does not affect the distribution of state funds. There are certain categorical aids, however, that would be more equitably distributed if smaller districts were reorganized.

At present, if there are too few pupils in a program to fund at least one FTE position, either the program cannot be offered (and needs are not met) or a funding floor allows any district to receive at least a minimum number of dollars. This is, of course, inequitable distribution of revenues—all in the name of equitable opportunity for students.

Reorganized districts, i.e. larger districts, would tend to even out the highs and lows in district property values, so property tax revenue collections would tend to equalize.

## Opposing Arguments

Those who have opposed consolidation usually argue:

1. The school is the "heart of the community", often serving as the center of the town's social activities. Therefore, to lose the school would be to destroy the community.
2. There are virtues of "smallness," and students who attend small schools are given greater opportunities to lead and participate in extracurricular activities.
3. Long bus rides are detrimental to children's health, the time spent limits students' participation in activities, and bus maintenance and energy costs are increased.
4. Local control over schools must not be lost; consolidation would weaken local control.

Proponents of changes in Minnesota's district organization must respect such local concerns even as they cite what they consider are overriding advantages of reorganization.

## Summary

The purpose of this study has been to reexamine The 1971 Omnibus Tax Act and its amendments to determine its current effectiveness. We have also investigated some options to the current school financing system.

What this study has attempted may have distorted the education picture somewhat. Constraints of space, time and energy forced the committee to address the financial questions with little attention to the related issues of taxes and educational policy.


To study public school finance in Minnesota was our task. It is now the task of other Minnesota citizens to educate themselves on this issue and either reconfirm their satisfaction with the financing law we have or determine the next step: more reform? a new financing scheme? a new "miracle"?

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