

Revised on 4/13/11 based on amendments adopted through 4/13/11.

**FISCAL NOTE**  
**LEGISLATIVE FISCAL ANALYST ESTIMATE**

<b>ESTIMATE OF FISCAL IMPACT – STATE AGENCIES *</b>				
	<b>FY 2011-12</b>		<b>FY 2012-13</b>	
	<b>EXPENDITURES</b>	<b>REVENUE</b>	<b>EXPENDITURES</b>	<b>REVENUE</b>
GENERAL FUNDS	(\$188,667,319)		(\$221,750,941)	
CASH FUNDS				
FEDERAL FUNDS				
OTHER FUNDS				
<b>TOTAL FUNDS</b>	(\$188,667,319)		(\$221,750,941)	

\*Does not include any impact on political subdivisions. See narrative for political subdivision estimates.

LB 235 changes the formula which provides state aid to schools pursuant to the Tax Equity and Educational Opportunities Support Act (TEEOSA). The following narrative describes the changes made in the act.

**CHANGES TO NEEDS IN THE TEEOSA FORMULA:**

**Base Limitation/Cost Growth Factor:** The base limitation rate or basic allowable growth rate in the aid formula is decreased from 1.5% to 0% for FY2011-12 and .5% for FY2012-13. A decrease in the rate reduces the cost growth factor in the formula which is used to inflate school district expenditures for purposes of calculating aid. The cost growth factor is also adjusted to eliminate an additional factor which is currently added to the basic allowable growth rate for the aid year plus the basic allowable growth rate for the prior aid year. The 1% factor is eliminated. (Note that the factor is normally 1% but it has been changed to 1.5% for aid distributed in FY2011-12 and FY2012-13). These changes result in a calculated cost growth factor of .25% for FY12 and .5% for FY13. The decrease in the cost growth factor decreases the amount of state aid that is provided as basic funding.

**Averaging Adjustment:** The averaging adjustment increases need for districts whose basic funding per student is less than the averaging adjustment threshold. The bill decreases the averaging adjustment threshold by 5% in FY12. It also permanently eliminates an additional .5% that is added to increase the threshold in the calculation each year. The reduction in the threshold used to compute the averaging adjustment reduces state aid for districts receiving the averaging adjustment.

**Needs Stabilization:** LB 235 changes the calculation of needs stabilization in FY2011-12. The bill reduces the lower and upper limits for the needs stabilization by 5%. Currently, the amount of need is stabilized at the prior year's level, if need is calculated to be less than the prior year. The bill provides that needs will be stabilized at 95% of the prior year's amount if needs for a district are calculated to be less than 95% of the prior year.

The upper limit on needs stabilization is also adjusted in FY12. Currently, if calculated needs for a district are greater than 112% of the prior year, then needs are adjusted to 112%. The stabilization limit is changed to 107% by the bill. Districts receiving a student growth adjustment are excluded from the reduction. The change in needs stabilization reduces state aid for districts that are eligible for stabilization aid.

**Elementary Class Size Allowance:** The bill repeals language which eliminates the elementary class size allowance beginning in FY2013-14. Generally, allowances attribute expenditures for such purposes to school districts incurring the expenditures which reduces the amount of basic funding available in the formula. In FY11, the elementary class size allowance was \$105.4 million of the needs calculation.

The retention of the allowance should not increase or decrease the overall amount of state aid distributed, unless the interaction with the averaging adjustment or needs stabilization changes the amount, but it will alter the amount of aid received by individual districts.

**Summer School Allowance:** The bill incorporates the provisions of LB 287 which change the computation of the summer school allowance. Summer school units for the purpose of the allowance are to include students enrolled in an early childhood education program in a summer session (kindergarten eligible students), in the most recently completed data year, beginning with the state aid calculation for FY2012-13. The number of summer school units calculated for early childhood education students shall be six-tenths of the number calculated for students in other grades. An additional six-tenths of a summer school student unit is added for each early childhood education child in a free lunch and free milk program.

An allowance in the formula for a particular activity (i.e. summer school) attributes expenditures for that purpose to a school district actually incurring the expenditures. This reduces the amount of basic funding available in the formula by the amount of the allowance and increases funding for schools able to take advantage of the allowance. Generally, the expansion of an allowance should not increase or decrease the overall amount of state aid distributed, but it will alter the amount of state aid received by individual school districts. It is possible total state aid could increase by an indeterminate amount depending upon how the change in basic funding interacts in the formula with the averaging adjustment or needs stabilization.

Comparison Groups: The calculation of basic funding for districts is changed in the bill. Currently, basic funding for a district is determined by comparing the formula students of the five larger and five smaller districts to a district. The highest and lowest spending districts are excluded from the calculation. The comparison group is changed beginning in FY2011-12 to be the ten larger and ten smaller districts, with the two highest and two lowest spending districts excluded from the comparison group.

The fiscal impact of the change in comparison groups is unknown, but not anticipated to be significant in terms of overall state aid. However, the change of the comparison group for an individual district may increase or decrease state aid for that district.

General Fund Operating Expenditures: The provisions of LB 148 are included in the bill. Beginning with state aid calculated for FY2012-13, general fund operating expenditures are to exclude amounts paid by school districts for lobbyist fees and expenses. LB 235 also excludes expenditures for voluntary terminations occurring on or after July 1, 2011 and on or before June 30, 2013 from general fund operating expenses.

These exclusions from general fund operating expenses reduce the amount of need calculated for school districts by the amount of the fees and expenses. The report of lobbyist fees and expenses filed with the Nebraska Accountability Disclosure Commission for 2010 (as of January 24, 2011), shows 14 school districts expended about \$410,000 for lobbyists. Assuming a few more 4<sup>th</sup> quarter reports will be filed, it is estimated schools spent about \$475,000 for this purpose in CY2010. The amount that will be expended for voluntary terminations is unknown.

A reduction of \$475,000 of need may reduce the amount of basic funding in the formula by an unknown amount. Exclusions decrease the need for districts with lobbyist expenditures and voluntary terminations. The exclusions may also reduce basic funding for other school districts in the same comparison group which receive equalization aid. How the decrease in need is reflected in the determination of basic funding for a district with the exclusions and the other districts in the same comparison group depends upon: whether the districts with the exclusions are the high or low spending district in the comparison group, in which case they are excluded from the averaging mechanism to determine basic funding; and, how much the decrease in general fund operating expenditures changes the average for the comparison group. In addition, it is possible that a decrease in basic funding pursuant to the bill for a district may be offset by increases in the averaging adjustment or needs stabilization components of the formula. Based on these interactions, the actual fiscal impact of the exclusions is indeterminate.

The bill also extends an exclusion from general fund operating expenses for the amount of school district contributions to retirement systems. The exclusion is extended for FY14-15, FY15-16 and FY16-17. Any school district contributions to retirement in excess of 7.35% for the state teacher retirement system or 7.37% for the Class V school retirement system made in these fiscal years are excluded from general fund operating expenses for the purposes of calculating state aid.

Cumulative NEEDS Fiscal Impact: The interaction of the NEEDS components of the formula makes it difficult to isolate the impact of a change to the cost growth factor, averaging adjustment, needs stabilization or the other formula changes in the bill. It is estimated the cumulative impact of changes to NEEDS in LB 235 is a general fund savings of about \$137 million in FY12 and \$168.8 million in FY13.

#### **CHANGES TO RESOURCES IN THE TEEOSA FORMULA:**

Local Effort Rate: The local effort rate is increased from \$1.00 to \$1.0395 for the calculation of aid in FY12 and FY13. An increase in the local effort rate decreases the amount of state aid provided to school districts by the amount of additional resources that can be raised from the increased rate. The estimated general fund savings is \$49.7 million in FY12 and \$52 million in FY13.

Property Tax Refunds: Formula resources for a school district are reduced by the amount of property tax refunds paid by a district beginning in FY13. The adjustment decreases resources for a district which will increase state aid for most affected districts by the amount of the refunds.

Income Tax: The bill continues a reduction in the amount of income tax rebate in FY12 and FY13. The amount of income tax rebate is reduced by \$21 million in each fiscal year. The reduction in FY11 is \$20 million. A reduction in income tax rebate decreases resources to schools and state aid by \$21 million but the aid reduction is restored as equalization aid to equalized districts. The estimated net general fund savings is \$1.9 million in FY12 and FY13.

Converted Contract Option Students: The bill includes the provisions of LB 273 which makes changes in the option enrollment provisions of the formula and the computation of local formula resources. The bill provides that tuition receipts from districts where nonresident students have been converted from being contracted students to option students will not be included as a local formula resource. The converted contract must be an expired contract that was in effect for at least 15 years.

Districts having converted contract option students must apply to the State Department of Education (NDE) on or before March 1 for converted contract option students for FY2011-12 and on or before November 1<sup>st</sup> thereafter. NDE is to determine the amount of tuition receipts from converted contracts to be excluded from the calculation of formula resources for each of the first two years for which the converted contract is not in effect and determine the number of converted contract option students attributed to the receiving district and a like number is attributed to the resident district as students optioning out.

NDE indicates there has been an agreement between two school districts (Grand Island and Grand Island Northwest) which provides that if Grand Island annexes land in the G.I. Northwest district, and children desire to remain at Northwest, then G.I. pays tuition to Northwest for the students. This agreement ends after the FY2010-11 school year.

State aid payments are based on data elements from the annual financial report of the second preceding school year and the number of option students in the preceding year. In the absence of the bill, in the determination of state aid for FY2011-12, Northwest would have tuition received from Grand Island in FY2009-10 showing as a resource for state aid purposes, but would no longer actually be receiving the tuition payment. The resource would offset the equalization aid that the district would receive by including the students in membership for purposes of the needs calculation.

The bill provides that tuition receipts will not be counted as a formula resource for Northwest, so state aid for Northwest will not be reduced in FY2011-12 by the amount of tuition that Grand Island paid in FY2009-10. The students attending Northwest will become option students and the aid for Grand Island will decrease by a like amount, so it is assumed the changes will have no net fiscal impact.

**CHANGES TO BUDGET LIMITATIONS:** The bill modifies the budget limitation for school districts in FY2011-12. The general fund budget of expenditures is limited to the greater of: the FY2010-11 general fund budget of expenditures less exclusions in section 79-1028.01, for FY11 increased by 1.115% of the formula need for FY11; plus any student growth adjustment; or, 110% of formula need for FY12, less special education budgeted expenditures for FY11 increased by the basic allowable growth rate for FY12.

Under current law, in FY11, the budget limit is the maximum of the prior year budget (less grant funds and special education expenditures) increased by .0075% plus the applicable allowable growth rate; or, 116.5% of formula need (less special education expenditures) increased by the basic allowable growth rate.

In FY2012-13 and thereafter, the budget limitation is modified to be the greater of: the prior year general fund budget of expenditures less exclusions in section 79-1028.01 increased by the basic allowable growth rate; plus any student growth adjustment; or, 110% of formula need for the school year for which the calculation is made less prior year special education expenditures increased by the basic allowable growth rate for the school year being calculated.

A new budget lid exclusion is included allowing schools to exceed their lid in the amount of expenditures for voluntary terminations occurring on or after July 1, 2011 and on or before June 30, 2013. The bill also eliminates the allowable growth range for districts which is currently up to 3% above the base limitation.

An existing exclusion from the budget lid is extended by the bill for FY2014-15, FY2015-16 and FY2016-17. Expenditures by school districts to pay for employer contributions to the School Retirement System or the Class V School Employees Retirement System are excluded from the budget lid when the expenditures are in excess of what would have been spent at a rate of 7.35% or 7.37%, respectively. The current exclusion goes through FY2013-14.

The unused budget authority which may be accessed by school districts is also changed. Currently, unused budget authority is carried over to the next fiscal year. LB 235 limits the use of unused budget authority in any fiscal year to 2% of the difference of the general fund budget of expenditures (less grant funds, special education expenditures and certain exceptions) for the preceding school year.

It is assumed the changes in budget authority will have an impact in terms of reducing the annual increase in school spending. Any change in school spending impacts state aid paid two years later. The budget limit changes will impact state aid beginning in FY2013-14. It is difficult to project the impact of the changes in the budget limitation. It is assumed the bill will reduce school spending from an estimated 5.5% increase in FY12 (affects FY14 aid) to 1%. A 2.5% increase in school spending is estimated in FY13 (affects FY15 aid) pursuant to the bill. If so, the general fund savings will be \$131.6 million in FY14 and \$231.8 million in FY15.

The budget limitations in the bill allow for about a 3% growth in spending in FY12. However, it is assumed the combination of low growth in property valuations, limited unused tax rate capacity, and a \$128 million reduction in state aid lowers the resources to schools to the point where spending will only increase by about 1%. It is assumed a growth in resources in FY13 allows school spending to increase by 2.5% per LB 235 budget limitations.

**FISCAL IMPACT:** In summary, it is estimated the bill decreases the amount of state aid distributed in FY12 by \$188.7 million and the amount distributed in FY13 by \$221.8 million of general funds. The savings become greater, as shown on the following chart, when the impact of the changes in budget lids for schools occur in FY14 and FY15.

	FY2010-11 certified	FY2011-12 estimated	FY2012-13 estimated	FY2013-14 estimated	FY2014-15 estimated
<b>Total TEEOSA</b>					
Current Law*	<b>950,221,736</b>	<b>1,010,479,640</b>	<b>1,101,107,086</b>	<b>1,206,149,298</b>	<b>1,303,726,553</b>
LB 235 Formula Changes:					
- NEEDS Changes		(136,997,960)	(168,838,269)	(127,409,132)	(88,246,939)
- Local Effort Rate Increase		(49,732,549)	(50,975,862)	0	0
- Income Tax Rebate		<u>(1,936,810)</u>	<u>(1,936,810)</u>	<u>0</u>	<u>0</u>
Total Formula Changes		(188,667,319)	(221,750,941)	(127,409,132)	(88,246,939)
LB 235 Budget Lid Changes		0	0	<u>(131,631,096)</u>	<u>(231,815,512)</u>
<b>LB 235 Total General Fund Savings</b>		(188,667,319)	(221,750,941)	(259,040,228)	(320,062,451)
<b>LB 235 TEEOSA Aid</b>	<b>950,221,736</b>	<b>821,812,321</b>	<b>879,356,145</b>	<b>947,109,070</b>	<b>983,664,102</b>
General Funds	796,734,561	807,469,661	864,654,919	932,040,313	968,218,626
Insurance Premium Taxes	13,200,000	14,342,660	14,701,226	15,068,757	15,445,476
ARRA Federal Funds	<u>140,287,176</u>	0	0	0	0
<b>Total TEEOSA</b>	950,221,737	821,812,321	879,356,145	947,109,070	983,664,102

\* March 2011 Estimate