Sustainably Supporting a Sound Basic Education

Part 2

By Stevan Marcus, Research Associate

Summary

Flaws in New York State's school aid funding formulas stop the State from effectively distributing funds based on student need and local capacity. The Citizens Budget Commission's (CBC's) July 2024 report *Sustainably Supporting a Sound Basic Education* identified problems with Foundation Aid, expense-based aids, and the School Tax Relief (STAR) program, and made seven preliminary recommendations.

This report furthers those recommendations by:

1. Specifying three improvements to account for localities' circumstances and actions, in order to ensure the Foundation Aid formula:

■ More accurately measures a district's capacity and willingness to raise revenue, and uses the actual local contribution as the expected minimum local contribution when it exceeds the measure;

■ Accounts for a locality's other spending obligations—including State mandates such as Medicaid, and those driven by economic or social factors such as poverty and unhoused residents—by adjusting the expected local contribution; and

■ Ensures that indices of need and regional cost are updated regularly, are sufficiently granular to capture variation, and consider that a well-constructed metric with a limited number of weights may be more effective than a metric with many weights.

2. Supporting our recommendation to allocate more aid based on need with new analyses, including:

- An examination of the allocation of Building Aid and Transportation Aid;
- A discussion of how reallocating certain expense-based aids proportional to the current Foundation Aid formula shifts $135 million to the 268 districts—40 percent of districts—with the lowest wealth, which includes New York City[1]; and
- An analysis of how reallocating $3.3 billion in School Tax Relief (STAR) program funds proportional to the current Foundation Aid formula, rather than based on local property wealth and tax rates, would shift hundreds of millions of dollars to lower-wealth districts; and

  - STAR aid to the 201 lowest-wealth districts (bottom 30 percent) would double from $501 million to $1 billion, while aid to the 203 wealthiest districts (top 30 percent) would decrease from $942 million to $336 million.

Background: Preliminary Findings and Recommendations on State Education Aid in New York

CBC's July 2024 report *Sustainably Supporting a Sound Basic Education* identified the following problems with the allocation of State education aid:

- The Foundation Aid formula falls short on directing aid to districts based on student needs and local capacity;

  - The hold harmless provision provides funds even when the need goes down with enrollment declines;
  - The expected local contribution does not fairly assess districts' ability and willingness to pay;
  - Outdated poverty and regional cost measures reduce the accuracy of each district's estimated per-student cost; and
  - Arbitrary floors and ceilings distort funding distributions;

- Expense-based aids similarly suffer from outdated indices, arbitrary caps, and inappropriate or inadequate measures of local wealth;

  - Building Aid and Transportation Aid disburse 15 percent of State education aid and warrant further study to ensure allocation is appropriately targeted based on need and local capacity;
  - Minimum State funding shares limit effectiveness of distribution of Boards of Cooperative Educational Services (BOCES), vocational, and excess cost aids;
  - Library, Textbook, and Software Aids do not adequately adjust for district wealth; and
  - High Tax Aid directs funding mostly to higher wealth districts with no clear purpose; and

- The STAR program provides disproportionate benefits to wealthier districts.

CBC made preliminary recommendations for the State to:

- Quickly phase-out the hold harmless provision to align Foundation Aid with district enrollment;
- Revise the expected local contribution to be the higher of the district's actual contribution or the district's fiscal capacity, which should be better measured;

- Update district poverty estimates and regional cost measures for a more accurate assessment of need;
- Remove arbitrary floors and ceilings that distort the funding distribution of Foundation Aid and expense-based aid categories;
- Adjust aid for library, textbooks, and software to account for district wealth either by modifying the formula or folding the funding into Foundation Aid;
- Eliminate High Tax Aid; and
- Eliminate the STAR program to better allocate State resources to where they are needed most.

Three Improvements to Account for Local Circumstances

CBC recommends three improvements to the Foundation Aid formula to better account for local circumstances and actions:

- More accurately measure a district's capacity and willingness to raise revenue, and use the actual local contribution as the expected minimum local contribution when it exceeds the measure;
- Account for a locality's other spending obligations—including State mandates such as Medicaid, and those driven by economic or social factors such as poverty and unhoused residents—by adjusting the expected local contribution; and
- Ensure that indices of need and regional cost are updated regularly, are sufficiently granular to capture variation, and consider that a well-constructed metric with a limited number of weights may be more effective than a metric with many more weights.

Similar improvements should be made for indices of need and cost, and measures of local resources used in expense-based aid formulas, where they are relevant.

Local Contribution

A reasonable estimate of each district's local contribution is necessary to determine how much funding the State should provide to ensure that resources needed for a Sound Basic Education (SBE) are available. The current process to estimate this local contribution is faulty because it understates what districts can, and do, provide, and it does not account for local non-education spending obligations.

New York State approaches the local contribution with two methods—one measures what could be raised based on local wealth, and the second measures what share of the total cost the locality should cover.[2] The formula uses whichever results in the lowest contribution—maximizing State aid even when the locality could and does contribute more local aid than the formula identifies. Because almost all districts raise more revenue than the formula expects, the State provides aid beyond what is needed to support an SBE for many districts.

Rather than having multiple formulas with the district selecting the most advantageous, the Foundation Aid formula should be based on district wealth. Many states have a school aid funding model similar to New York's Foundation Aid formula: The State determines the total cost for a district and reduces that amount by how much the school district is expected to contribute, largely based on the district's local property wealth and a statewide expected tax rate.[3] This method is simple and more directly approximates a district's ability to contribute to the Foundation amount than the alternative sharing ratios used by New York.

Often a district contributes more than the formula determines it can or should. In the 2023-24 school year, almost all districts did that, and 152 of those contributed enough to provide an SBE without any State aid at all.[4] Some of the difference between the formula and the actual contribution is due to the formula being faulty. However, even when improved, this may continue to be the case for some districts. In these cases, the formula should use the actual local revenue when determining how much the State should contribute.

Even an improved formula that better identifies districts' ability to raise revenue still ignores the different spending obligations districts face due to circumstances not directly within their control. While local preferences play a role in how much a jurisdiction spends overall and how it allocates its funds, local finances are also strained by the cost of providing other services that are mandated by the State or based on external economic or social factors. For instance, local governments are required to cover a portion of the State's Medicaid program cost, and localities may have high rates of poverty or unhoused residents.

The Foundation Aid formula should adjust for the non-discretionary cost of these local services that draw on the same underlying tax base. Providing some discount to a district's local contribution to education to account for these other, often mandated, services would help more equitably provide an SBE.

Indices

Several indices used in the Foundation Aid formula, as well as other expense-based aid formulas, are outdated and imprecise. The regional cost index is outdated and geographically broad; it may not capture differences between urban, suburban, and rural areas in the same region, for example. The pupil need index relies on outdated measures of poverty, imprecise measures of qualification for free and reduced lunch, and English Language Learner (ELL) enrollment. It does not account for other factors that could increase student need—thereby a district's cost to provide an SBE—such as residing in transitional housing, special education needs, or the negative impacts of concentrated poverty.

However, merely adding factors to the index may not necessarily improve it. The best approach would be to develop a streamlined index with a limited number of key variables—and ensuring the right and sufficient weights to them—to accurately capture the varying levels of cost or need across districts. Furthermore, transparency about the index development and a routine review process is essential to ensure stakeholder buy-in.

Ineffective Allocation of Building Aid and Transportation Aid

Building and Transportation Aid are the two largest expense-based aid categories, together totaling nearly $6 billion in the coming school year. Both are allocated by similar formulas that reimburse the district for a portion of their eligible expenditures—with that portion adjusted for a district's local fiscal capacity, regional cost variance, and, for transportation, the district's residential sparsity.[5]

Regardless of how funds are allocated, New York schools' cost of providing transportation service is exceptionally high. Statewide student transportation expenditures totaled $1,805 per student in 2022, the highest of any state.[6] This figure exceeds the second-highest cost state, Connecticut, by 40 percent, and is nearly triple the U.S. average. In the 2024-25 school year, the State will reimburse school districts for 61 percent of total eligible student transportation costs, with almost half of all school districts set to receive the maximum reimbursement rate of 90 percent.

School districts' building and transportation costs should be explored further to identify reforms that would:

- Incentivize efficiency of spending on student transportation and building projects; and
- Improve the funding distribution to better reflect local needs and resources.

Impact of Shifting to Need-Based Allocation of Library, Textbook, Software, and High Tax Aid

CBC recommends changing the allocation of dollars provided by four categories of aid that currently have no wealth or need factor determining their distribution. These four aid categories—Library, Textbook, Software, and High Tax Aid—are set to total $447 million in the 2024-25 school year. Library, Textbook, and Software aids provide schools with a fixed per-student allocation regardless of student need or local resources. High Tax Aid is allocated based on prior district funding levels and has been frozen since 2014; it therefore no longer serves its original purpose of incentivizing districts to raise more local revenue.

CBC modeled the impact of a formula-based allocation, finding that reallocating these funds in proportion to each district's share of Foundation Aid would substantially shift funding from higher-wealth districts to lower-wealth districts and New York City, which receives no High-Tax Aid currently. When accounting for need and local resources, the share flowing to the districts in the four lowest deciles based on wealth, which includes New York City, increases from 45 percent to 75 percent (an increase of $135 million), while the share flowing to districts in the top three deciles based on wealth decreases from 30 percent to 10 percent (a decrease of $90 million).[7]

On a per-student basis, funding in districts in the lowest wealth decile would increase from $191 to $327 (72 percent). At the other end of the spectrum, per-student funding would decrease from $204 per student to $50 (76 percent). (See Figure 1.)

Figure 1: Library, Textbook, Software, and High Tax Aid Allocation Per Student Currently, and Reallocated Proportional to Foundation Aid
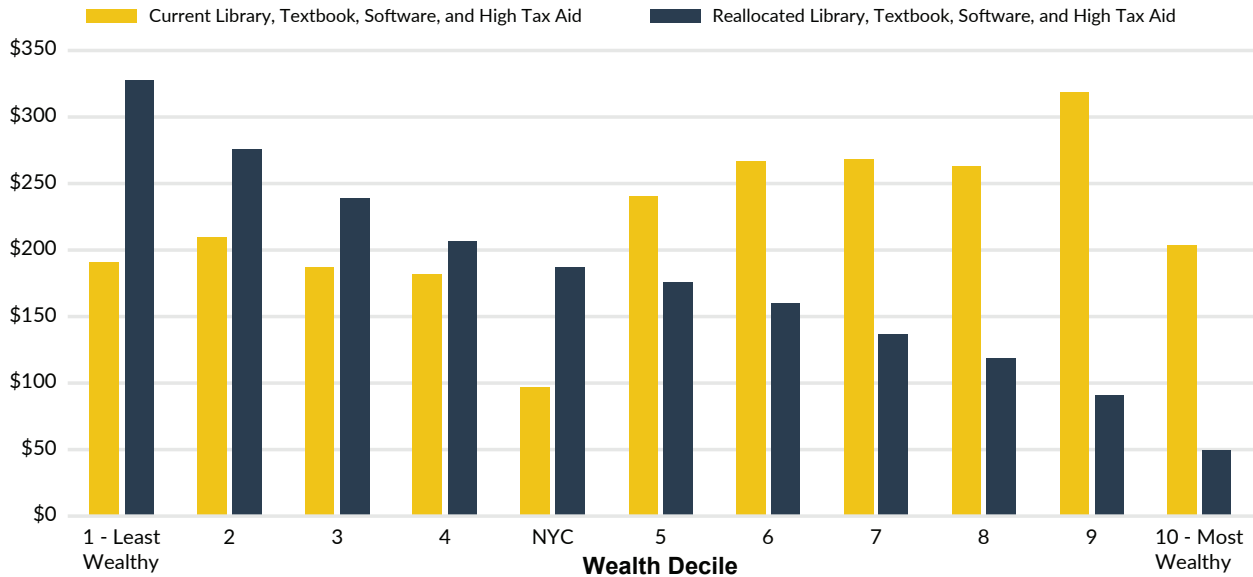
Notes: Library, Textbook, and Software Aid are currently allocated on a flat dollar-per-student basis. High Tax Aid was originally intended to encourage districts to increase their local revenue effort, but district allocations have been frozen since the 2013-2014 school year.

Source: CBC staff analysis of New York State Education Department, Fiscal Analysis & Research Unit, "FY 2025 Enacted Budget School Aid Files" (received via email on April 22, 2024.)

## Impact of Shifting to Need-Based Allocation of School Tax Relief (STAR) Program Funds

The STAR program is school aid by another name. STAR partially shifts the burden of education funding from locally raised property tax revenue to the State, by either providing homeowners an exemption (a reduction in their school tax bill paid, which the State reimburses the school district for) or a credit (a check directly from the State to offset a portion of the homeowner's school tax bill). The school district is kept whole, as the reduction in local taxes collected is reimbursed by the State. In essence, the school district either receives the funding as property taxes or as a state reimbursement—the method is immaterial to the school district since it receives the funds either way.

Because the value of STAR in a district is a function of that district's property values and tax rate, high-tax jurisdictions, especially those with high property values, benefit the most from STAR. For example, in the 2024-25 school year, we estimate districts in the bottom three wealth deciles receive $501 million in STAR aid while districts in the top three wealth deciles receive approximately $942 million.

As eligibility is limited to homeowners and based on the value of the residence, the distribution of STAR benefits favors higher wealth districts. If the $3.3 billion of annual STAR funding were reallocated proportional to district's share of Foundation Aid, aid to districts in the bottom three wealth deciles would double to $1 billion while the funds flowing to the top three deciles would be cut by two-thirds, substantially redistributing aid. On a per-student basis, districts in the lowest

wealth decile would receive an average of $1,674 more per student than they currently receive from STAR (220 percent), while the allocation to districts in the top decile would decrease by $1,157 (76 percent). (See Figure 2.)

Figure 2: School Tax Relief (STAR) Allocation Per Pupil Currently and Reallocated Proportional to Foundation Aid
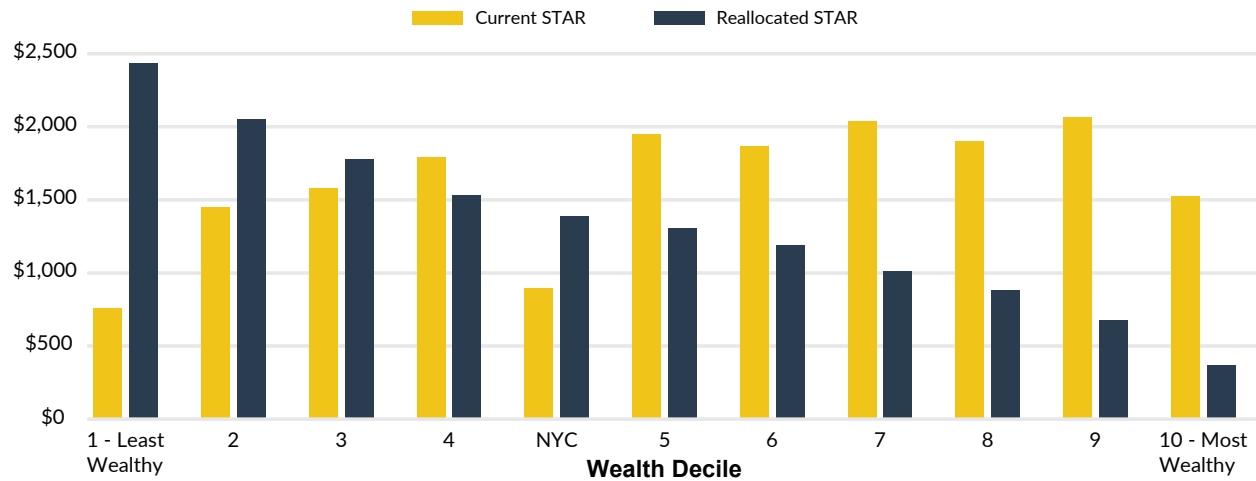
Notes: The School Tax Relief (STAR) Program reduces homeowner property taxes through a property tax exemption, in which case, the State reimburses the district for foregone revenue, or through a direct rebate.

Sources: CBC staff analysis of New York State Education Department, Fiscal Analysis & Research Unit "School District Fiscal Profiles" (last updated June 12, 2024), and "FY 2025 Enacted Budget School Aid Files" (received via email on April 22, 2024); and New York State Division of the Budget, *FY 2025 Enacted Budget Financial Plan* (May 2024).

Conclusion

The Rockefeller Institute study of the New York State school aid funding formulas is a tremendous opportunity to make long-needed changes to improve the distribution of State resources to school districts based on their needs and local capacity. We strongly urge the Rockefeller Institute and the State to expand the scope of this work to include State funding streams other than Foundation Aid. Expense-based aids and STAR are also flawed funding streams and combined represent more than one-third of overall State school aid.

Data Sources

School Aid Runs: New York State Education Department, Fiscal Analysis & Research Unit "FY 2025 Enacted Budget School Aid Files" (received via email on April 22, 2024).

School Aid Masterfiles: New York State Education Department, Fiscal Analysis & Research Unit "School District Fiscal Profiles" (last updated June 12, 2024), https://www.nysed.gov/fiscal-analysis-research/school-district-fiscal-profiles.

Endnotes

[1] CBC determines wealth deciles based on the average of a district's free and reduced-price lunch share and census poverty share, divided by the district's combined wealth ratio as determined by New York State Education Department (NYSED). The resulting figure is then indexed to the state average to determine a needs index.

[2] The first method multiplies district property wealth per enrolled resident students by a local tax factor, and the Income Wealth Index (IWI), and index of districts' relative adjusted gross income. The second method starts with the formula determined adjusted foundation amount, and multiplies it by the inverse of four Foundation Aid State Sharing Ratios (FASSR)—a combined wealth ratio of districts' relative property and income wealth, which is then further adjusted by district need.

[3] Matthew Chingos and Kristin Blagg, *Making Sense of State School Funding Policy* (Urban Institute, November 2017), https://apps.urban.org/features/funding-formulas/.

[4] Stevan Marcus and Patrick Orecki, *The Learning Ledger* (Citizens Budget Commission, September 2023), https://cbcny.org/research/learning-ledger.

[5] Aidable costs for Transportation Aid are those incurred in transporting students to and from school, or to approved shared district programs. Building Aid covers a portion of the cost of new building construction, additions and alterations, and lease and installment payments for building projects with both local approval and approval by the Facilities Planning Unit of the New York State Education Department (NYSED). The regional cost factor used to adjust Building Aid is different from the Foundation Aid regional adjustment. See New York State Education Department, Office of State Aid "2024-25 State Aid Handbook", https://stateaid.nysed.gov/publications/handbooks/handbook_2425.pdf.

[6] U.S. Census Bureau, "Annual Survey of School System Finances" (updated April 25, 2024),https://www.census.gov/programs-surveys/school-finances.html.

[7] There are 268 districts in bottom four deciles, which includes New York City, while there are 203 districts in the top three. Wealth deciles are based on the average of a district's free and reduced-price lunch share and Census poverty share, divided by the district's combined wealth ratio as determined by New York State Education Department (NYSED). The resulting figure is then indexed to the State average to determine a needs index.

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