

Department of Education
Formula Programs

A.R.S. § 15-231

	FY 2005 Actual	FY 2006 Estimate	FY 2007 Approved
OPERATING BUDGET			
<i>Full Time Equivalent Positions</i>	21.0	29.0	29.0 ^{1/}
Personal Services	666,800	1,422,400	1,490,900
Employee Related Expenditures	102,700	391,400	427,200
Professional and Outside Services	20,200	19,200	19,200
Travel - In State	1,300	62,000	62,000
Other Operating Expenditures	163,400	134,100	134,100
Equipment	33,000	0	0
OPERATING SUBTOTAL	987,400	2,029,100	2,133,400
SPECIAL LINE ITEMS			
Basic State Aid	2,766,603,400	3,164,559,400 ^{2/}	3,610,551,600 ^{3/-10/}
Additional State Aid	279,818,000	294,126,200	324,224,300
Special Education Fund	31,093,900	33,130,500	35,235,500
Other State Aid to Districts	3,978,900	951,500	983,900
Hayden-Winkelman School District	0	0	1,865,400 ^{11/}
Ch. 343 School District Budget; Debts	0	318,100	0
PROGRAM TOTAL	3,082,481,600	3,495,114,800	3,974,994,100^{12/}
FUND SOURCES			
General Fund	3,032,757,500	3,444,501,700	3,927,908,000
<u>Other Appropriated Funds</u>			
Permanent State School Fund	46,509,100	50,295,000	45,220,700
School Improvement Revenue Bond Debt Service Fund	3,215,000	318,100	1,865,400
SUBTOTAL - Other Appropriated Funds	49,724,100	50,613,100	47,086,100
SUBTOTAL - Appropriated Funds	3,082,481,600	3,495,114,800	3,974,994,100
Other Non-Appropriated Funds	396,732,200	516,189,000	511,501,600
TOTAL - ALL SOURCES	3,479,213,800	4,011,303,800	4,486,495,700

1/ Includes 1 FTE Position funded from Special Line Items in FY 2007.

2/ Includes a \$191,293,800 appropriation from Laws 2004, Chapter 278 to fund a deferred ("K-12 rollover") payment from FY 2005 plus \$191,000,000 appropriated in FY 2006 from Laws 2006, Chapter 353 to pay off the rollover.

3/ Includes a \$191,293,800 appropriation from Laws 2005, Chapter 329 to fund the deferred rollover payment from FY 2006.

4/ Laws 2006, Chapter 4 appropriation of \$14,300,000.

5/ Laws 2006, Chapter 353 appropriation of \$215,200,000.

6/ Laws 2006, Chapter 353 appropriation of \$100,000,000.

7/ Laws 2006, Chapter 353 appropriation of \$118,050,000.

8/ The above appropriation provides basic state support to school districts for maintenance and operations funding as provided by A.R.S. § 15-973, and includes an estimated \$45,220,700 in expendable income derived from the Permanent State School Fund and from state trust lands pursuant to A.R.S. § 37-521B for FY 2007. (General Appropriation Act footnote)

9/ Receipts derived from the Permanent State School Fund and any other non-state General Fund revenue source that is dedicated to fund Basic State Aid will be expended, whenever possible, before expenditure of state General Fund monies. (General Appropriation Act footnote)

10/ Except as required by A.R.S. § 37-521, all monies received during the fiscal year from national forests, interest collected on deferred payments on the purchase of state lands, the income from the investment of permanent funds as prescribed by the Enabling Act and the Constitution of Arizona and all monies received by the Superintendent of Public Instruction from whatever source, except monies received pursuant to A.R.S. § 15-237 and 15-531, when paid into the State Treasury are appropriated for apportionment to the various counties in accordance with law. An expenditure shall not be made except as specifically authorized above. (General Appropriation Act footnote)

11/ Laws 2006, Chapter 353 appropriation of \$1,865,400.

12/ General Appropriation Act funds are appropriated as Operating Lump Sum with Special Line Items by Program.

COST CENTER DESCRIPTION — This program funds the agency’s School Finance Unit, which processes formula funding payments to schools and monitors school district and charter school compliance with school budgeting laws. It also funds the formula programs themselves, the largest of which are Basic State Aid and Additional State Aid. Basic State Aid provides the state’s share of equalization assistance to school districts and charter schools based on a funding formula set in statute. Additional State Aid funds the “Homeowner’s Rebate” program, through which the state pays a portion of each homeowners’ school property taxes.

For FY 2006 and prior years, the operating budget for the School Finance Unit was funded through the former General Services Administration cost center and Basic State Aid and other formula programs were funded through the former Assistance to Schools cost center. All “non-formula” programs formerly funded through “Assistance to Schools” now are funded through the “Non-Formula Programs” cost center. These changes are being made in FY 2007 due to the agency’s transition to “program budgeting.” Funding totals in the table above have been adjusted for all years for comparability with the agency’s new budget structure.

Operating Budget

The budget provides \$2,133,400 from the General Fund for the operating budget in FY 2007. This amount includes an increase of \$104,300 from the General Fund for statewide adjustments. (Please see the Statewide Adjustments section at the end of this Appropriations Report for details.)

Special Line Items/Statutory Formula Programs

BASIC STATE AID

Basic State Aid Entitlement

The budget provides \$3,610,551,600 for Basic State Aid in FY 2007. This amount consists of:

	FY 2007
General Fund	\$3,565,330,900
Permanent State School Fund	45,220,700

These totals do not include \$86,280,500 in “additional school day” funding from Proposition 301 that would be allocated through Basic State Aid in FY 2007 because those monies are non-appropriated. The recommended Basic State Aid total includes \$191,293,800 in “rollover” funding that has already been appropriated for FY 2007 by the Education Budget Reconciliation Bill for FY 2006 (Laws 2005, Chapter 329). Those monies therefore do not appear in the General Appropriation Act for FY 2007.

The budgeted \$3,610,551,600 total includes a General Fund increase of \$451,066,500 and a Permanent State

Table 1

FY 2007 Basic State Aid Summary

	<u>General Fund</u>	<u>Permanent State School Fund</u>	<u>Prop 301 Sales Tax</u>	<u>Local Property Taxes</u>	<u>Total</u>
Basic State Aid from FY 2006	\$3,114,264,400 ^{1/}	\$50,295,000 ^{2/}	\$ 86,280,500	\$1,800,928,200	\$5,051,768,100
Changes for FY 2007:					
Base Adjustment – Caseload	18,581,900	(7,072,000)			11,509,900
Base Adjustment – Rollover Payoff	(191,000,000)				(191,000,000)
Enrollment Growth	165,822,700				165,822,700
2% Inflator	81,250,200				81,250,200
2.4% Additional Inflator	100,000,000				100,000,000
Kindergarten Group B Weight	118,050,000				118,050,000
English Learner Group B Weight	14,300,000				14,300,000
180 Day Transportation	5,500,000				5,500,000
Special Education Weights	5,000,000				5,000,000
Charter Additional Assistance	3,000,000				3,000,000
TAPBI	2,000,000				2,000,000
Joint Technology Districts	846,000				846,000
Dept of Juvenile Corrections	336,800				336,800
Net Assessed Valuation Growth	(154,529,700)			154,529,700	0
Truth in Taxation	68,706,300			(68,706,300)	0
County Equalization Tax Rate	215,200,000			(215,200,000)	0
Endowment Earnings	(1,997,700)	1,997,700			0
Total – Cost after Formula Changes	\$3,565,330,900 ^{2/}	\$45,220,700 ^{2/}	\$86,280,500	\$1,671,551,600	\$5,368,383,700

^{1/} Includes supplemental funding from Laws 2006, Chapter 316 and rollover payoff funding from Laws 2006, Chapter 353.

^{2/} Includes \$7,072,000 in one-time funding from Laws 2006, Chapter 316.

^{3/} Represents appropriated Basic State Aid Funds. Proposition 301 monies for Basic State Aid are not appropriated.

School Fund decrease of \$(5,074,300). Components of these recommended changes are described in detail after the overview of Arizona's K-12 equalization funding formula that appears below.

Formula Overview

K-12 Education funding in Arizona is based on a statutory formula enacted in 1980 and substantially modified in 1985. This formula "equalizes" maintenance and operation (M&O) funding among school districts, enabling them all to spend approximately the same amount of M&O money per pupil from state and local sources combined. A few districts with very strong local property tax bases are able to generate their entire formula funding entitlement from local property taxes alone. Most school districts, however, require "Basic State Aid" monies in order to receive full formula funding.

The equalization formula for school districts consists of 4 elements: the Base Support Level (BSL), Transportation Support Level (TSL), Capital Outlay Revenue Limit (CORL), and Soft Capital. All but the TSL are computed by multiplying a specific dollar amount by a school district's student count (adjusted for various weights). The TSL, however, is computed by multiplying a specific dollar amount by a district's pupil transportation route miles. BSL, TSL and CORL funds may be used for M&O or capital expenditures. Soft Capital funds may be used for capital items only. The sum of the 4 formula components equals what is referred to as a school district's "equalization base," which is its total funding entitlement under the K-12 equalization funding formula.

After a school district's equalization base is determined, the net assessed property value (NAV) of the district is multiplied by the statutory "Qualifying Tax Rate" (QTR) in order to determine the amount of funding that is assumed to come from local sources under the formula. If this amount exceeds the district's equalization base, it is not entitled to Basic State Aid. If, however, its "local share" funding does not exceed its equalization base, the district receives Basic State Aid funding to make up the difference. The actual local tax rate for schools may be lower than the QTR, or higher if the district is allowed to budget for items outside of its "Revenue Control Limit" (RCL) under A.R.S. § 15-910. It also may be higher if the district participates in a Career Ladder program pursuant to A.R.S. § 15-918, or in an Optional Performance Incentive Program pursuant to A.R.S. § 15-919.

Basic State Aid is also provided to charter schools, which are schools that (unlike school districts) do not have geographic boundaries, operate under terms specified in a "charter," and are sponsored by an entity such as the State Board for Charter Schools. The equalization funding formula for charter schools is somewhat different than that of school districts in that it does not include separate funding for CORL, Soft Capital or Transportation.

Instead, the charter school funding formula consists only of BSL funding plus "Additional Assistance." BSL funding for charter schools is determined under the same computational formula prescribed for traditional public schools (A.R.S. § 15-943). Additional Assistance funding amounts are established in statute (A.R.S. § 15-185.B4) and for FY 2007 will equal \$1,387.25 per pupil for Grades K-8 and \$1,616.81 per pupil for Grades 9-12. Charter schools receive all of their equalization funding through Basic State Aid, since they do not have authority to generate funding through local property taxes.

Major Changes to Basic State Aid

Base Adjustment - Caseload

The budget provides \$11,509,900 for caseload base adjustment for FY 2007 (*see Table 1*). This amount consists of:

General Fund	\$18,581,900
Permanent State School Fund	(7,072,000)

The \$11,509,900 net adjustment is due to higher than expected ADM growth in FY 2005 and FY 2006. This higher growth permanently increases the base number of students being funded, which increases "starting point" costs for Basic State Aid for FY 2007.

The \$(7,072,000) Permanent State School Fund base adjustment for FY 2007 is due to the elimination of carry forward and other one-time monies available from the fund for FY 2006 only.

Base Adjustment – Rollover Payoff

The budget provides a decrease of \$(191,000,000) from the General Fund in FY 2007 to reflect the pay off of the K-12 "rollover" in FY 2006 (*see Table 1*). Laws 2006, Chapter 353, the K-12 Budget Reconciliation Bill, appropriated \$191,000,000 in FY 2006 to pay off the K-12 Rollover. These monies remain available until June 30, 2007.

In FY 2003, \$191,000,000 of the final June monthly payment to school districts was deferred, or "rolled-over" to July 1 of the following fiscal year to help resolve a state budget shortfall. In each subsequent year, the school districts continued to receive a deferred payment of \$191,000,000 on July 1 while having their regular June payment reduced by \$191,000,000. For example, Laws 2005, Chapter 329 (the K-12 Education Budget Reconciliation Bill for FY 2006) appropriated \$191,293,800 (including interest) for FY 2007 to recognize the state's obligation from having reduced the June 2005 payment by that same amount.

To pay off the K-12 rollover, school districts would need to receive an extra \$191,000,000 in any one year. The rollover is eliminated when all funding to school districts is aligned with the fiscal year and there are no deferred payments. Under this Chapter 353 appropriation, school

districts will receive their full Basic State Aid funding in FY 2006.

Enrollment Growth

The budget provides an increase of \$165,822,700 from the General Fund for enrollment growth for FY 2007. This total consists of approximately \$141,447,500 for ADM growth in school districts and \$24,375,200 for ADM growth in State Board-sponsored charter schools. These estimates are based on ADM projections shown in *Table 2*.

Table 2 shows a currently projected total statewide ADM count in FY 2007 of 1,035,154 for school districts and charter schools combined. This would be an increase of 32,590 ADM pupils (3.25%) above the current estimate for FY 2006. The 3.25% estimate is the midpoint between the current JLBC Staff estimate of 3.3% and a 3.2% estimate from the University of Arizona Economic and Business Research Center (EBR).

The approved \$165,822,700 increase for Enrollment Growth reflects a continued funding of the Rapid Decline formula in A.R.S. § 15-942 at 50% of the full formula cost for FY 2007, pursuant to Section 19 of the K-12 Budget Reconciliation Bill for FY 2007.

estimated at 2.8% for calendar year 2005), whichever is less. A.R.S. § 901.01 prohibits the Legislature from ever setting a base level that is lower than the FY 2002 base level (\$2,687.32).

The approved 2% increase would have resulted in a base level of \$3,061.02 per pupil for FY 2007, but this is further increased to \$3,133.53 by an additional inflation adjustment described below. The 2% increase in transportation route mile funding will provide \$1.77 or \$2.19 per route mile for FY 2007, depending on average per pupil route miles for a district (A.R.S. § 15-945.A5). The 2% inflation adjustment also applies to special education vouchers, as described in the “Special Education Fund” narrative below. The total approved amount for the 2% inflation adjustment for Basic State Aid and special education vouchers combined for FY 2007 is \$81,912,800.

Additional Base Level Increase

The budget provides an increase of \$100,000,000 from the General Fund in FY 2007 for an additional Base Level increase. This funding, as noted above, provides an additional 2.4% “base level” increase for FY 2007, resulting in a “base level” of \$3,133.53 for the year. The K-12 Education Budget Reconciliation Bill requires the \$100,000,000 amount to be used for salary and benefit increases for non-administrative school personnel.

Charter School Additional Assistance

The budget provides an increase of \$3,000,000 from the General Fund in FY 2007 for an additional funding increase for charter school “Additional Assistance.” This amount is in addition to the increase provided as part of the “2% Inflation Adjustment” policy issue described above and results in a total 4.3% increase in charter school “Additional Assistance” funding per pupil for FY 2007.

Kindergarten Weight

The budget provides an increase of \$118,050,000 from the General Fund in FY 2007 to establish a new Kindergarten “Group B” funding weight in A.R.S. § 15-943(2b). This amount includes \$80,000,000 in new funding and \$38,050,000 transferred from the now-eliminated Full-Day Kindergarten (FDK) Special Line Item. The K-12 Education Budget Reconciliation Bill sets the new Kindergarten weight at 0.835 for FY 2007 and 1.352 for FY 2008 and beyond, which would require an additional estimated \$80,000,000 increase for FY 2008.

The K-12 Budget Reconciliation Bill also modifies existing statutory language regarding Kindergarten instruction to 1) require each school district Kindergarten program to include a half-day option that provides academically meaningful instruction, 2) delete language requiring the Legislature to develop a plan to provide statewide FDK by FY 2010, 3) require school districts and charter schools to provide any capital monies needed to implement FDK and 4) delete language pertaining to the establishment and administration of state and local level

Table 2
Average Daily Membership (ADM)
Students by Academic Year

	Districts (including Charters) *	State Charters	Total	Change	% Change
2004	860,496	73,238	933,734	27,372	3.0%
2005	888,874	82,111	970,985	37,251	4.0%
2006 est	917,678	84,886	1,002,564	31,579	3.25%
2007 est	946,024	89,130	1,035,154	32,590	3.25%

* Includes 1,473 charter school ADM for FY 2004, 1,495 for FY 2005 and 1,495 (estimated) for FY 2006 and FY 2007.

2% Inflation Adjustment

The budget provides an increase of \$81,250,200 from the General Fund in FY 2007 for a 2% inflation adjustment. This includes a 2% increase in the “base level” in A.R.S. § 15-901.B2, the charter school “Additional Assistance” funding levels in A.R.S. § 15-185.B4, and transportation funding levels per route mile in A.R.S. § 15-945.A5. (See *Table 1*.) (See “Charter School Additional Assistance” narrative below for a description of an additional inflation adjustment for that program for FY 2007.) (See also the “180-Day Transportation” narrative below for a description of additional increased formula funding for transportation for FY 2007.)

A.R.S. § 901.01 (established by Proposition 301) requires the Legislature to increase the base level or other components of the Revenue Control Limit (RCL) by 2% each year through FY 2006. After FY 2006 it requires the base level or other components of the RCL to be increased by 2% or by the change in the GDP price deflator (currently

FDK Funds and regarding a Department of Education review of FDK academic literature.

English Learner Weight

Laws 2006, Chapter 4 includes an increase of \$14,300,000 from the General Fund in FY 2007 to increase the English Learner “Group B” funding weight in A.R.S. § 15-943(2b). This funding is appropriated by Laws 2006, Chapter 4 (the “Flores bill”), which increased the English Learner “Group B” weight from 0.140 in FY 2006 to 0.115 in FY 2007. That weight increase and associated funding, however, are appropriated on the condition that the United States District court for the district of Arizona in the case Flores v. State of Arizona issues an order that Chapter 4 “addresses the order in the case,” at least on an interim basis. On April 25, 2006, a United States District Judge issued an order that Chapter 4 did not satisfy prior court orders in this case, but the April 25th order is now under appeal. A final determination therefore has not yet been made regarding whether the department can allocate the funding appropriated for this issue.

180-Day Transportation

Laws 2006, Chapter 353 includes \$5,500,000 from the General Fund in FY 2007 to fund the Basic State Aid transportation formula in A.R.S. § 15-945 on a 180-day basis versus 175 days under current law. The \$5,500,000 appropriation and associated statutory change are authorized in the K-12 Budget Reconciliation Bill. That law also prohibits a school district from increasing its Transportation Revenue Control Limit (TRCL) if its TRCL currently is more than 120% of its Transportation Support Level (TSL). The TSL is the amount of transportation funding that a school district is entitled to under the Basic State Aid transportation funding formula in A.R.S. § 15-945, whereas the TRCL is an alternative amount computed pursuant to A.R.S. § 15-946. A school district may levy property taxes to make up the difference if its TRCL is higher than its TSL, subject to the new “120 percent” restriction.

Special Education Weights

The budget provides an increase of \$5,000,000 from the General Fund in FY 2007 to fund increases in 3 special education “Group B” weights established in A.R.S. § 15 943(2b) (see Table 3). The first 2 weights shown in Table 3 are increased to levels recommended in the most recent (December 2005) special education cost study conducted pursuant to A.R.S. § 15-236. The third is only partially increased toward its recommended level of 5.702 in order to fit the 3 weight changes within the \$5,000,000 appropriation for this issue. The weights selected for increases are the ones that were furthest from their recommended levels in FY 2005. The December 2005 cost study indicated that special education “Group B” costs collectively were underfunded by approximately \$5,000,000 that year, but under the assumption that “over funded” weights would be reduced and 4 new preschool weights would be created. The \$5,000,000 appropriation for this

issue therefore provides a net increase equivalent to that recommended in the December 2005 cost study, but without decreasing any existing weights or establishing new preschool weights.

Special Education Category	Group B Weight	
	FY 2006	FY 2007
• Multiple Disabilities – Severe Sensory Impairment	6.531	7.947
• Orthopedic Impairment – Self Contained	5.576	6.773
• Emotional Disabilities – Private Placement	4.647	4.822

TAPBI

The budget provides an increase of \$2,000,000 from the General Fund in FY 2007 for enrollment growth in the Technology Assisted Project Based Instruction (TAPBI) program. The approved \$165,822,700 increase for Enrollment Growth described above does not include a specific adjustment for enrollment growth in the Technology Assisted Project Based Instruction program authorized by A.R.S. § 15-808. Laws 2005, Chapter 323 expanded the program by allowing sites to double their enrollment each year and by allowing up to 20% of pupils who are “accepted each academic school year” to be pupils who were not in public schools in the prior year, which increases Basic State Aid costs. The JLBC Staff estimates that this expansion will increase Basic State Aid costs by an additional \$2,000,000 in FY 2007.

Joint Technological Education Districts

The budget provides an increase of \$846,000 from the General Fund in FY 2007 to fund increased “double the QTR” costs under a cap on state aid to Joint Technological Education Districts (JTEDs) for FY 2007. Laws 2006, Chapter 341 (the “JTED bill”) caps state aid to an individual JTED for FY 2007 at its FY 2006 level or “double its Qualifying Tax Rate (QTR)” funding for FY 2007, whichever is greater (plus, in both cases, the amount of County Equalization Tax Rate (CETR) funding that they received in FY 2006 in order to offset suspension of that tax for FY 2007) (see “County Equalization Tax Rate” discussion below for further discussion on that topic). (Note: The K-12 Education BRB also included this provision, but without the required CETR language, so its language for this issue was notwithstanding in Chapter 341.) Of the 10 existing JTEDs, only West-MEC is expected to receive state aid under the “double the QTR” option for FY 2007 and its costs for that option (which also existed for FY 2006) are expected to increase by an estimated \$846,000 in FY 2007.

On a related note, the K-12 Education Budget Reconciliation Bill caps a JTEDs property tax rate for FY 2007 at the FY 2005 level and prohibits the formation or joining of additional JTEDs in FY 2007, except in Pima County. (See the Additional Legislation section below for

information on other JTED-related statutory changes in Laws 2006, Chapter 341.)

Department of Juvenile Corrections

The budget provides an increase of \$336,800 from the General Fund in FY 2007 for Basic State Aid for the Department of Juvenile Corrections (DJC). The approved increase provides DJC with \$2,638,300 in total Basic State Aid funding for FY 2007. This amount assumes that DJC will experience 4.7% enrollment growth for FY 2007 based on currently available data. DJC receives Basic State Aid funding each year pursuant to A.R.S. § 15-1371.

Net Assessed Valuation (NAV) Growth

The budget provides a decrease of \$(154,529,700) from the General Fund in FY 2007 due to growth in statewide property values. The approved \$(154,529,700) decrease assumes that the combined Net Assessed Value (NAV) of all properties statewide will grow by 9.9% for FY 2007. Growth in statewide NAV increases “local share” funding for Basic State Aid because the K-12 “Qualifying Tax Rate” (QTR) generates more local funding when property values rise. This reduces the amount of K-12 equalization formula funding that must be provided by the state General Fund.

The estimated \$(154,529,700) savings for NAV growth does not include offsets for higher “Truth in Taxation” and Additional State Aid costs that occur when statewide NAV values increase. Those increases partially offset state savings due to NAV growth and are discussed separately below.

“Truth in Taxation”

The budget provides an increase of \$68,706,300 from the General Fund in FY 2007 for “Truth in Taxation” (TNT) pursuant to A.R.S. § 41-1276, which requires a lowering of the K-12 QTR each year in order to offset growth in local property values. This increases Basic State Aid costs because it reduces the amount of “local share” monies that are generated by the QTR and the state must make up the difference.

As of April 24, 2006, the JLBC reported that FY 2007 QTR would be \$1.74 or \$3.48 (depending upon the type of district and rounded to the nearest penny) per \$100 of NAV (see Table 4).

Table 4			
Estimated TNT Tax Rates			
Tax Rate	FY 2006	FY 2007	
Qualifying Tax Rate (QTR)			
• High School districts and elementary districts located within a high school district	\$1.8090	\$1.7394	
• Unified districts and elementary districts not located within a high school district	\$3.6180	\$3.4788	

County Equalization Tax Rate Suspension

The budget provides an increase of \$215,200,000 from the General Fund in FY 2007 to replace “local share” monies

foregone in FY 2007 due to a 3-year suspension of the County Equalization Tax Rate (CETR) instituted by Laws 2005, Chapter 353. For FY 2007, the CETR would generate an estimated \$215,200,000 to help fund Basic State Aid and related programs that year. Since the Basic State Aid formula backfills with state funding whatever the QTR and CETR do not fund, the \$215,200,000 appropriation for this issue is required in order to maintain total K-12 equalization formula funding at the pre-CETR suspension level.

Endowment Earnings

The budget includes a decrease of \$(1,997,700) from the General Fund and an increase of \$1,997,700 from the Permanent State School Fund for K-12 Endowment Earnings in FY 2007. This reduces the portion of K-12 Endowment Earnings earmarked for School Facilities Board revenue bond debt service from \$29,040,000 in FY 2006 to \$27,042,300 in FY 2007 based on the actual funding requirement for that program and increases the amount available to help fund Basic State Aid from \$43,223,000 in FY 2006 to \$45,220,700 in FY 2007. This results in a net General Fund savings of \$(1,997,700) in FY 2007.

For FY 2007, the JLBC Staff currently estimates that expendable K-12 endowment earnings will equal \$101,913,000, which would be a \$6,530,300 increase above the current \$95,382,700 JLBC Staff estimate for FY 2006. None of this increase would be available to help fund Basic State Aid or debt service on State School Trust Revenue Bonds, however, because A.R.S. § 37-521, as amended by Proposition 301, dedicates all growth in expendable endowment earnings above the FY 2001 level \$(72,263,000) to the Proposition 301 Classroom Site Fund. (See the “Summary of Funds” for additional information regarding the Proposition 301 Classroom Site Fund.)

Endowment Earnings consist of interest on securities held in the Permanent State School Fund, receipts from leases of state lands and “lease-purchase” interest paid to the State Land Department by buyers of state trust land who finance those purchases through the State Land Department. “Principal” on those purchases is not considered expendable and is instead deposited into the Permanent State School Fund for investment by the State Treasurer.

**ADDITIONAL STATE AID
 (“Homeowner’s Rebate” and “1% Cap”)**

Additional State Aid

The budget provides \$324,224,300 from the General Fund for Additional State Aid in FY 2007.

Additional State Aid is authorized by A.R.S. § 15-972, which requires the state to pay 35% of each homeowner’s school district primary property taxes, up to a maximum of \$500 per parcel. The program also pays for any portion of a homeowner’s primary property taxes for all taxing jurisdictions combined (not just schools) that exceeds 1%

of the full cash value of their home. This second feature is referred to as the “1% cap” and is required by Article IX, Section 18 of the State Constitution, which limits Class 3 primary property taxes to no more than 1% of a home’s full cash value. All Class 3 properties are eligible for both “homeowner’s rebate” and “1% cap” funding.

The approved amount includes no funding change for continuing a 1 year “soft cap” on school district desegregation expenditures pursuant to Section 18 of the K-12 Education Budget Reconciliation Bill. That bill prohibits a school district from increasing its desegregation expenditures other than for enrollment growth and inflation. The soft cap was initially established for 1-year (FY 2005) by Laws 1994, Chapter 278. It affects Homeowner’s Rebate costs because desegregation expenditures are funded with primary property taxes and those taxes qualify for Homeowner’s Rebate and 1% cap funding.

Base Adjustment

The budget provides a decrease of \$(3,087,000) from the General Fund in FY 2007 for a base adjustment for the program. This is reflected in the approved amount because the actual cost of the program for FY 2006 was \$(3,087,000) less than the program’s FY 2006 appropriation. This allows the budget base for the program to be reduced by \$(3,087,000) for FY 2007.

Net Assessed Value Growth

The budget provides an increase of \$17,268,700 from the General Fund in FY 2007 for Net Assessed Value (NAV) growth. This assumes that statewide NAV in FY 2007 will grow by 9.9% for all classes of property combined, 11% for Class III only (owner occupied homes) and 4% for existing property. It also assumes that average school district tax rates will decrease by 4%.

Business Property Tax

The budget provides an increase of \$12,829,400 from the General Fund in FY 2007 to fund higher homeowner rebate costs that will occur in FY 2007 because of a reduction in the assessment ratio for business property in FY 2007 pursuant to Laws 2005, Chapter 302. That law will reduce the assessment ratio for Class I properties (commercial and industrial) from 25% in FY 2006 to 24.5% in FY 2007 (and ultimately to 20% by FY 2015). It also will increase the Homeowner’s Rebate from 35% of a homeowner’s primary property taxes for schools in FY 2006 to 36% in FY 2007 (and 40% by FY 2010). Chapter 302 also will increase the current Homeowner’s Rebate cap from \$500 per home in FY 2006 to \$520 in FY 2007 (and \$600 by FY 2010). The higher (36%) Homeowner’s Rebate percentage and higher (\$520) Homeowner’s Rebate cap for FY 2007 will increase the cost of the Homeowner’s Rebate by an estimated \$12,829,400 for FY 2007. Chapter 302 did not advance appropriate monies to pay for future increases in Homeowner’s Rebate costs under the bill, so the estimated FY 2007 cost is included in the approved budget.

OTHER STATUTORY FORMULA PROGRAMS

Special Education Fund

The budget provides \$35,235,500 and 1 FTE Position from the General Fund for special education vouchers in FY 2007. The approved amount includes an increase of \$3,200 from the General Fund for statewide adjustments. The approved amount also includes the other following changes:

Enrollment Growth

The budget provides an increase of \$1,439,200 from the General Fund in FY 2007 for estimated 3.2% overall growth in the number of pupils requiring special education vouchers.

2% Inflation Adjustment

The budget provides an increase of \$662,600 from the General Fund in FY 2007 in order to fund a 4.4% increase in the “base level” for special education vouchers. The funding formula for special education vouchers uses the same “base level” as the Basic State Aid program and that base level is increasing by 4.4% for FY 2007 as described in the Basic State Aid narrative above.

The Special Education Fund provides funding for special education costs of students from 1) Arizona State Schools for the Deaf and the Blind, 2) Arizona State Hospital (ASH), or 3) developmentally disabled programs operated by DES [A.R.S. § 15-1202]. It also funds costs of residential education for students who require a private residential special education placement, or who are placed in a residential education facility by a state placing agency (Department of Juvenile Corrections, DES, DHS, or the Administrative Office of the Courts) [A.R.S. § 15-1182].

Other State Aid to Districts

The budget provides \$983,900 from the General Fund for Other State Aid to Districts in FY 2007. The approved amount also includes the other following changes:

Base Increase

The budget provides an increase of \$583,100 from the General Fund in FY 2007 in order to increase base funding for the program to the level required by the department for FY 2006. The approved amount includes \$852,100 (an increase of \$582,100) for Certificates of Educational Convenience and \$100,500 (an increase of \$1,000) for Assistance to School Districts for Children of State Employees (ASDCSE).

Enrollment Growth

The budget provides an increase of \$31,400 from the General Fund in FY 2007 for projected 3.3% enrollment growth. The net \$31,400 increase includes \$28,100 for Certificates of Educational Convenience and \$3,300 for the ASDCSE program.

Certificates of Educational Convenience allow students to attend school in a district other than the one they live in if they are placed there by an authorized state or federal agency. This includes placement into a 1) rehabilitative or corrective institution, 2) foster home or child care agency or institution which is licensed and supervised by the Department of Economic Security (DES) or the Department of Health Services (DHS), or 3) residential facility operated or supported by DES or DHS [A.R.S. § 15-825]. CEC's also provide supplemental special education funding for school districts that provide special education services to out-of-district children.

The ASDCSE program supplements Basic State Aid funding for school districts that educate pupils whose parents are employed and domiciled at certain state institutions located within the school district's boundaries, pursuant to A.R.S. § 15-976.

Hayden-Winkelman School District

The budget provides \$1,865,400 from the School Improvement Revenue Bond Debt Service Fund for the Hayden-Winkelman Unified School District in FY 2007 to redeem existing bonds. The school district currently has the highest overall property tax rate in the state and redeeming existing bonds will enable it to reduce that rate in the short term. The \$1,865,400 appropriation is in the K-12 Education BRB, which also includes the following related provisions: 1) requires the district to repay the \$1,865,400 amount in 3 annual installments at 4% interest starting on July 1, 2008 and ending on July 1, 2010; 2) prohibits the district from levying a primary property tax rate higher than \$11.89 minus any reductions required by Truth in Taxation; and 3) prohibits the district from increasing its secondary property tax rate through new budget overrides and bond issuances.

Ch. 343, School District Budget; Debts

The budget provides \$318,100 from the School Improvement Revenue Bond Debt Service Fund for the Colorado Unified School District in FY 2006 to pay existing warrants. Colorado City Unified is currently under receivership pursuant to A.R.S. § 15-103 and is experiencing cash flow problems because a large percentage of property tax payments to the district from local church-related property is delinquent. The receiver expects these delinquencies to be resolved in the coming months through either payment or foreclosure. Chapter 343 requires the Superintendent of Public Instruction to withhold a portion of the district's Basic State Aid entitlement in FY 2007 through FY 2011 in order to pay back the appropriated amount, which essentially is a temporary loan to the school district so it can pay its bills.

Also, due to budget errors, the school district received more state aid funding in FY 2005 than it was entitled to for that year and must return the difference to the department pursuant to A.R.S. § 15-915. That law typically requires such paybacks to occur over a 1 or 2

year period, but Chapter 343 allows the district to make the correction over a 5-year period.

Additional Legislation

K-12 Education Budget Reconciliation Bill

In addition to provisions described under, the K-12 Education Budget Reconciliation Bill for FY 2007 (Laws 2006, Chapter 353) includes the following provisions:

- 1) Amends statutory language requiring JLBC review of transfers into or out of formula programs to conform with revised line item names,
- 2) Requires all districts to report information on utility expenditures (currently only districts budgeting for Excess Utilities must report),
- 3) Allows a school district or charter school to make upward revision to its Average Daily Membership count for a year after the end of a fiscal year (currently they have up to 3 years),
- 4) Permits a school district to make corrections to its Teacher Experience Index (TEI) data between March 15 and April 15,
- 5) Permits the Prescott Unified School District to recalculate its TEI after April 15, 2006,
- 6) Allows school districts to have a shorter than 36-week school year using longer days,
- 7) Allows the Gila Bend Unified School District to correct budget errors over 5 year,
- 8) Expands school district planning and reporting requirements for excess utilities, and
- 9) Authorizes the department or Auditor General to conduct ADM audits of school districts and charter schools.

Joint Technological Education Districts

Laws 2006, Chapter 341 (the "JTED bill") makes the following statutory and session law changes that may affect state funding to JTEDs in the future:

- 1) Permits a JTED and charter school to share 1.25 ADM for an individual pupil (versus 1.0 ADM currently). The estimated cost FY 2007 cost for this provision is minimal because of a cap on JTED state aid for the year. Otherwise the estimated cost would have been \$3,000,000.
- 2) Precludes pupils in Grade 9 from being included in the ADM count of a JTED if enrolled in a career exploration course. Only a minimal savings is expected from this provision due to anticipated course reclassifications.
- 3) Allows the ADM of a pupil who is enrolled in a course that meets for at least 150 minutes per class period at a centralized campus owned and operated by a JTED to be 0.75 retroactive to August 1, 2005. This change will have no cost relative to current practice, but will result in a foregone savings of approximately \$2,300,000 relative to the December 2005 Auditor General report on JTEDs.

- 4) Requires each JTED to submit a course to be offered in school year 2007-2008 for approval to the department's Career and Technical Education Division by January 1, 2007. This provision will have no impact until FY 2008, as course approval is not required for FY 2007. The possible FY 2008 state savings will depend on the number of current JTED courses, if any, that will be disqualified from funding in FY 2008 under the new course requirements. If 10% of courses were disqualified that year, the savings would be roughly \$(6,500,000).

(See also the "Joint Technology Education Districts" narrative under Basic State Aid for additional information.)