

**Department of Education**  
**Formula Programs**

A.R.S. § 15-231

	FY 2009 ACTUAL	FY 2010 ESTIMATE	FY 2011 APPROVED
<b>OPERATING BUDGET</b>			
<i>Full Time Equivalent Positions</i>	29.0	26.0	24.0 <sup>1/</sup>
Personal Services	1,221,900	1,073,100	1,027,200
Employee Related Expenditures	369,200	322,000	311,700
Professional and Outside Services	260,200	20,000	20,000
Travel - In State	13,500	1,500	1,500
Other Operating Expenditures	210,000	324,200	324,200
Equipment	22,000	0	0
<b>OPERATING SUBTOTAL</b>	<b>2,096,800</b>	<b>1,740,800</b>	<b>1,684,600</b>
<b>SPECIAL LINE ITEMS</b>			
Basic State Aid	3,240,669,800	2,690,803,800	3,045,375,700 <sup>2/3/4/5/6/</sup>
Additional State Aid	295,940,800	423,642,700	419,264,000
Special Education Fund	34,884,000	35,242,100	35,242,100
Other State Aid to Districts	818,100	983,900	983,900
<b>PROGRAM TOTAL</b>	<b>3,574,409,500</b>	<b>3,152,413,300</b>	<b>3,502,550,300<sup>7/8/</sup></b>
<b>FUND SOURCES</b>			
General Fund	3,529,188,800	3,105,937,800	3,456,074,800
<u>Other Appropriated Funds</u>			
Permanent State School Fund	45,220,700	46,475,500	46,475,500
SUBTOTAL - Other Appropriated Funds	45,220,700	46,475,500	46,475,500
<b>SUBTOTAL - Appropriated Funds</b>	<b>3,574,409,500</b>	<b>3,152,413,300</b>	<b>3,502,550,300</b>
Other Non-Appropriated Funds	491,340,600	413,955,700	421,059,500
Federal Funds	0	472,114,000	92,800,000
<b>TOTAL - ALL SOURCES</b>	<b>4,065,750,100</b>	<b>4,038,483,000</b>	<b>4,016,409,800</b>

- <sup>1/</sup> Includes 1 GF FTE Position funded from Special Line Items in FY 2011.
- <sup>2/</sup> Includes K-12 rollover appropriations of \$602,627,700 and \$886,200 from Laws 2009, 3<sup>rd</sup> Special Session, Chapter 12 and \$350,000,000 from Laws 2010, 7<sup>th</sup> Special Session, Chapter 1, for a total combined FY 2011 rollover appropriation of \$953,513,900. Laws 2010, 7<sup>th</sup> Special Session, Chapter 1, appropriates \$952,627,700 in FY 2012 to reflect the deferral of FY 2011 payments. The latter amount is \$(886,200) less than the FY 2011 total because it does not include continued funding for interest.
- <sup>3/</sup> 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 \$46,475,500 in expendable income derived from the Permanent State School Fund and from state trust lands pursuant to A.R.S. § 37-521B for FY 2011. (General Appropriation Act footnote)
- <sup>4/</sup> The portion of the above appropriation for basic state aid for charter school additional assistance pursuant to A.R.S. § 15-185B4 includes a \$10,000,000 reduction. (General Appropriation Act footnote)
- <sup>5/</sup> 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)
- <sup>6/</sup> 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)
- <sup>7/</sup> See agency summary for agencywide lump sum reductions.
- <sup>8/</sup> 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 homeowner’s school property taxes.

**Operating Budget**

The budget includes \$1,684,600 and 23 FTE Positions from the General Fund for the operating budget in FY 2011. These amounts fund the following adjustments:

**Statewide Adjustments**

The budget includes a decrease of \$(56,200) from the General Fund in FY 2011 for statewide adjustments. (Please see the General Provisions section.)

**Basic State Aid**

The budget includes \$3,045,375,700 for Basic State Aid in FY 2011. This amount consists of:

	<b>FY 2011</b>
General Fund	\$2,998,900,200
Permanent State School Fund	46,475,500

FY 2011 adjustments are described in the “Major Changes to Basic State Aid” section below.

The \$3,045,375,700 total does not include \$86,280,500 in “additional school day” funding from Proposition 301 that will be allocated through Basic State Aid in FY 2011 because those monies are non-appropriated (See Table 1). It also excludes local property tax monies that will help fund K-12 formula costs for FY 2011, which also are non-appropriated.

The \$3,045,375,700 appropriated total includes a net General Fund increase of \$354,571,900 and no change from the Permanent State School Fund for FY 2011. Components of the General Fund increase 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) formula funding among school districts, enabling them all to spend approximately the same amount of formula 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 components: 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) pursuant to A.R.S. § 15-971B in order to determine the amount of funding that is assumed to come from QTR taxes under the formula. This amount, plus the district’s share of State Equalization Tax Rate (SETR) revenues pursuant to A.R.S. § 15-994, if any, are then subtracted from its equalization base. If the district’s combined QTR and SETR revenues exceed its equalization base, the district 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 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 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

**Table 1**

**FY 2011 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>ARRA</u> <sup>1/</sup>	<u>Total</u>
Basic State Aid from FY 2010	2,644,328,300 <sup>2/</sup>	46,475,500	86,280,500	2,239,763,500 <sup>3/</sup>	472,114,000	5,488,961,800
Changes for FY 2011:						
Base Adjustment – Rollover	350,000,000					350,000,000
Base Adjustment – ARRA	472,114,000				(472,114,000)	0
Base Adjustment – Cash Balances	(116,109,300)					(116,109,300)
Enrollment Growth @ 0.9%	52,000,000					52,000,000
1.2% Inflation	5,385,900					5,385,900
Net Assessed Valuation Growth	89,839,400			(89,839,400)		0
Truth in Taxation	(150,239,100)			150,239,100		0
No Early Kindergarten Repeaters	(6,200,000)					(6,200,000)
Full-Day Kindergarten	(218,298,300)					(218,298,300)
Soft Capital <sup>4/</sup>	(21,120,700)					(21,120,700)
Charter Additional Assistance	(10,000,000)					(10,000,000)
ARRA offset	(92,800,000)				92,800,000	0
<b>Total - Cost after Formula Changes</b>	<b>2,998,900,200<sup>5/</sup></b>	<b>46,475,500<sup>5/</sup></b>	<b>86,280,500</b>	<b>2,300,163,200</b>	<b>92,800,000</b>	<b>5,524,619,400</b>

1/ Federal "State Fiscal Stabilization Fund" (SFSF) monies from the American Recovery and Reinvestment Act of 2009 (ARRA).  
 2/ Reflects adjustments from Laws 2009, 4<sup>th</sup> Special Session, Chapter 1 and a \$350,000,000 rollover increase from Laws 2010, 7<sup>th</sup> Special Session, Chapter 1.  
 3/ Includes \$243,439,100 from the State Equalization Tax Rate (SETR). Roughly \$400,000,000 of the \$2.2 billion is funded by the state through the Homeowner's Rebate.  
 4/ This reduction is in addition to the \$(144,000,000) reduction from Laws 2009, 4<sup>th</sup> Special Session, Chapter 2, which is continued for FY 2011.  
 5/ Represents appropriated Basic State Aid funds. Proposition 301 monies for Basic State Aid are not appropriated.

is determined under the same formula prescribed for traditional public schools, which is in A.R.S. § 15-943. Additional Assistance funding amounts are established in A.R.S. § 15-185B4 and for FY 2011 equal \$1,607.50 per pupil for Grades K-8 and \$1,873.52 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**

The narrative below describes major changes to Basic State Aid funding for FY 2011 relative to the Basic State Aid appropriation for FY 2010 of \$3,045,375,700.

**Base Adjustment - Rollover**

The budget includes an increase of \$350,000,000 from the General Fund in FY 2011 to fund an additional deferred Basic State Aid payment from FY 2010. The General Appropriation Act for FY 2011 (Laws 2010, 7<sup>th</sup> Special Session, Chapter 1) deferred until July 1, 2010, but no later than August 29, 2010, \$350,000,000 in Basic State Aid and Additional State Aid funding that otherwise would have been distributed by the department to school districts during FY 2010. This deferral was in addition to \$602,627,700 that was already deferred from FY 2010 by Laws 2009, 3<sup>rd</sup> Special Session, Chapter 12. Chapter 12 advance appropriated \$602,627,700 plus \$886,200 for related interest costs in FY 2011 in order to fund that deferral. That amount plus the additional \$350,000,000 FY 2011 appropriation from Laws 2010, 7<sup>th</sup> Special Session, Chapter 1 provides a total of \$952,627,700 in

deferred FY 2010 funding in FY 2011 (\$953,513,900 with interest).

Chapter 1 continues the \$952,627,700 rollover in FY 2011 by deferring \$952,627,700 of FY 2011 state aid payments until FY 2012. As a result, the 12 monthly payments that school districts will receive in FY 2011 will consist of 3 deferred payments from FY 2010 and 9 (rather than 12) "current year" payments for FY 2011. Chapter 1 advance appropriates \$952,627,700 in FY 2012 in order to fund the \$952,627,700 deferred obligation from FY 2011 in FY 2012, but does not continue the \$886,200 in prior year interest funding.

As a result of existing rollovers, the base budget for Basic State Aid going into FY 2012 will include a total deferred obligation of \$952,627,700. That obligation will not be paid off until a 13<sup>th</sup> payment of \$272,627,700 (for the original FY 2008 rollover), 14<sup>th</sup> payment of \$330,000,000 (for the additional FY 2009 rollover) and 15<sup>th</sup> payment of \$350,000,000 (for the additional FY 2010 rollover) are provided in future years in addition to 12 "regular" payments made for the budget year.

On a related note, the K-12 Education BRB for FY 2011 continues to require school districts to include in the revenue estimates that they use for computing their tax rates the rollover monies that they will receive for FY 2011 in July or August 2011.

**Base Adjustment - ARRA**

The budget includes an increase of \$472,114,000 from the General Fund in FY 2011 in order to restore a one-time

funding reduction authorized by Laws 2009, 3<sup>rd</sup> Special Session, Chapter 11. Chapter 11 (Section 14) reduced General Fund funding for Basic State Aid by \$(472,114,000) on a one-time basis in FY 2010 due to the availability of State Fiscal Stabilization Fund (SFSF) monies from the American Recovery and Reinvestment Act of 2009 (ARRA). Partially offsetting this \$472,114,000 increase is a new \$(92,800,000) ARRA-related reduction for FY 2011 that is discussed separately below.

### Base Adjustment - Cash Balances

The budget includes a decrease of \$(116,109,300) from the General Fund in FY 2011 in order to remove one-time funding that was used in FY 2010 in order to reimburse school districts for the portion of the FY 2009 “cash balances rollover” not covered by school district cash balances. The cash balances rollover was required by Laws 2009, Chapters 5 and 6. Chapter 5 reduced K-12 formula funding by \$(300,000,000) for FY 2009 and Chapter 6 required school districts to cover a formula-determined portion of that amount with their own cash balances. Chapter 6 required the state to reimburse school districts during FY 2010 for the portion of the \$(300,000,000) reduction not covered by school district cash balances and that amount was later determined to be \$116,109,300 (including related interest costs). The FY 2010 budget (as amended by Laws 2009, 4<sup>th</sup> Special Session, Chapter 1) included \$116,109,300 in one-time funding for this issue. This policy issue eliminates that funding for FY 2011.

The FY 2010 budget also included an increase of \$300,000,000 in order to restore the \$(300,000,000) amount removed from the Basic State Aid funding base for FY 2009 because of the cash balances rollover. That \$300,000,000 amount remains in the Basic State Aid funding base for FY 2011.

### Enrollment Growth

The budget includes an increase of \$52,000,000 from the General Fund in FY 2011 for enrollment growth. This assumes that the statewide Average Daily Membership count for school districts and charter schools combined will increase by 9,300 students (0.9%) in FY 2011 (see Table 2).

On a related note, Laws 2009, Chapter 95 removed a cap on the number of school districts and charter schools that can participate in the Arizona Online Instruction (AOI) program (formerly called the “Technology Assisted Project-Based Instruction” program, or “TAPBI”). Prior to this change, only 7 school districts and 7 charter schools were allowed to participate in the program. This change could result in an increase in AOI sites starting in FY 2011. The cost of such potential growth is unknown, however, because it will depend on the proportion of new AOI students who would have been in public schools anyway in FY 2011, which likewise is unknown. In

addition, Chapter 95 reduced the amount of Base Support Level (BSL) funding that AOI students received starting in FY 2010. (Full-time AOI students now receive 95% and part-time students 85% of the BSL amounts received by non-AOI students, versus 100% for all AOI students previously.) As a result, any growth in AOI participation in FY 2011 that is attributable to existing public school students would reduce rather than increase state costs.

Table 2

Districts (including Charters) <sup>1/</sup>	Average Daily Membership (ADM) Students by Academic Year				
	State Charters	Total	Change	% Change	
2007	936,497	87,904	1,024,401	26,180	2.6%
2008	951,685	93,100	1,044,785	20,384	2.0%
2009	944,940	98,415	1,043,355	(1,430)	(0.1)%
2010 <sup>2/</sup>	937,620	108,185	1,045,805	2,450	0.2%
2011 <sup>2/</sup>	938,806	116,299	1,055,105	9,300	0.9%

<sup>1/</sup> Assumes an estimated 603 ADM from district sponsored charter schools for FY 2010 and FY 2011 versus 682, 568 and 603 ADM (actuals), respectively, for FY 2007, FY 2008 and FY 2009.

<sup>2/</sup> Estimated.

<sup>3/</sup> Assumes a reduction of (1,000) ADM for a new prohibition on “early Kindergarten repeaters” and (2,250) ADM reduction for a new cap on ADM for most pupils at 1.0. Otherwise estimated growth rate would be 0.5%.

### 1.2% Inflation Adjustment

The budget includes an increase of \$5,385,900 from the General Fund in FY 2011 for a 1.2% inflation increase in the transportation funding levels prescribed in A.R.S. § 15-945A5 and the charter school “Additional Assistance” amounts prescribed in A.R.S. § 15-185B, as authorized by the K-12 Education Budget Reconciliation Bill (BRB) (Laws 2010, 7<sup>th</sup> Special Session, Chapter 8). This will provide \$1.91 or \$2.35 per route mile in FY 2011 (depending on average per pupil route miles for a district pursuant to A.R.S. § 15-945A5) and will fund charter school additional assistance at \$1,607.50 per pupil for Kindergarten through grade 8 and \$1,873.52 per pupil for high school students. It does not include a 1.2% increase in the “base level” prescribed in A.R.S. § 15-901B2, which remains in FY 2011 at the FY 2010 level of \$3,267.72. Funding a 1.2% increase in the base level would have cost an additional \$61,392,900, for a total inflation adjustment of \$66,778,800.

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% or by the change in the GDP price deflator for the prior calendar year, whichever is less. The FY 2011 adjustment is estimated at 1.2%, since the calendar year 2009 GDP price deflator is currently projected to be 1.2%. A.R.S. § 15-901.01 prohibits the Legislature from setting a base level that is lower than the FY 2002 base level of \$2,687.32.

### Net Assessed Value Growth

The budget includes an increase of \$89,839,400 from the General Fund in FY 2011 due to a projected decline in Net Assessed Value (NAV) for taxable properties. The estimated \$89,839,400 increase assumes that the combined Net Assessed Value (NAV) of all properties statewide will decline by (4.6)% for FY 2011. Decreases in statewide NAV decrease “local share” funding for Basic State Aid because the K-12 “Qualifying Tax Rate” (QTR) and State Equalization Tax Rate (SETR) generate less local funding when property values decline. This increases the amount of K-12 equalization formula funding that must be provided by the state General Fund.

The projected (4.6)% NAV growth rate for FY 2011 assumes a (7.3)% decline for “existing properties” (properties other than new construction) and 2.7% growth due to new construction. The projected (4.6)% decline is lower than might be expected given dramatic decreases in statewide home prices in the recent months, but reflects the fact that 1) homes account for only about half of the statewide property tax base, and 2) caps on NAV growth for homes in the State Constitution partially deferred the impact of past housing price increases. Regarding the latter issue, the State Constitution caps annual NAV growth for homes at 10%, or at 25% of the difference between a home’s primary and secondary NAV, whichever is less. This has spread out over a period of years the NAV impact of the rapid increase in home prices that occurred in Arizona prior to calendar year 2007. FY 2011 NAVs will be based on property values from January 2009.

The estimated \$89,839,400 amount does not include offsets for lower “Truth in Taxation” and Additional State Aid costs that occur when statewide NAV values decline. Those declines partially offset state costs due to NAV decreases and are discussed separately below.

### Truth in Taxation

The budget includes a decrease of \$(150,239,100) from the General Fund in FY 2011 for Truth in Taxation (TNT) pursuant to A.R.S. § 41-1276. That law requires a change in the K-12 QTR and SETR each year in order to offset changes in local property values. In most years, TNT requires decreases in the QTR and SETR in order to offset increases in statewide property values. For FY 2011, however, statewide property values are expected to decrease, which will require increases in the QTR and SETR under TNT. This will decrease Basic State Aid costs because it will increase the amount of “local share” monies generated by the QTR and SETR and this increase will offset state costs on a dollar for dollar basis.

As of February 16, 2010, the JLBC reported that the FY 2011 QTR will be \$1.48 or \$2.96 (depending on the type of district and rounded to the nearest penny) and that the SETR will be \$0.36 per \$100 of NAV (*see Table 3*).

Table 3

Estimated TNT Tax Rates			
Tax Rate		FY 2010	FY 2011
Qualifying Tax Rate (QTR)			
• High School districts and elementary districts located within a high school district		\$1.3726	\$1.4797
• Unified districts and elementary districts not located within a high school district		\$2.7452	\$2.9594
• State Equalization Tax Rate (SETR)		\$0.3306	\$0.3564

### No Early Kindergarten Repeaters

The budget includes a decrease of \$(6,200,000) from the General Fund in FY 2011 for the estimated second year impact of a prohibition on state funding for “early Kindergarten repeaters” from Laws 2009, 3<sup>rd</sup> Special Session, Chapter 2. Chapter 2 amended A.R.S. § 15-821 in order to prohibit Basic State Aid funding in the second year of Kindergarten for Kindergarten repeaters who turned 5 years old after September 1<sup>st</sup> of the year that they initially enter Kindergarten. This change does not affect school districts with declining enrollments until FY 2011, since they are funded based on their prior year rather than current year ADM counts. The estimated FY 2011 reduction for such school districts is \$(6,200,000).

### Full-Day Kindergarten

The budget includes a decrease of \$(218,298,300) from the General Fund in FY 2011 for savings associated with returning to half-day only Kindergarten funding in FY 2011. Prior to FY 2007, the Basic State Aid formula funded Kindergarteners on a half-day basis. For FY 2007 through FY 2010, however, a Kindergarten “Group B” funding weight established by Laws 2006, Chapter 353 provided add-on monies in order to fund Kindergartners on a full time basis. The K-12 Education BRB permanently eliminates the Kindergarten Group B weight starting in FY 2011, which restores half-day only funding for Kindergarten. Monies generated by the Kindergarten Group B weight for FY 2007 through FY 2010 were not restricted for a specific purpose, but generally were used by schools to fund voluntary Full-Day Kindergarten pursuant to A.R.S. § 15-901.02.

On a related note, the K-12 Education BRB for FY 2011 allows a school district to charge tuition for Full-Day Kindergarten in FY 2011 if it decides not to provide free Full-Day Kindergarten for that fiscal year.

### Soft Capital Reduction

The budget includes a decrease of \$(21,120,700) from the General Fund in FY 2011 for Soft Capital funding authorized by A.R.S. § 15-962. This decrease is in addition to a \$(144,000,000) session law reduction continued from FY 2010 (from Laws 2009, 3<sup>rd</sup> Special Session, Chapter 12). In total, Soft Capital funding will be \$(165,120,700) below the formula requirement.

The \$(165,120,700) reduction is authorized by the K-12 Education BRB for FY 2011, which continues to exempt school districts with fewer than 600 K-8 pupils from 50% of the K-8 Soft Capital reductions and districts with fewer

than 600 high school pupils from 50% of the high school Soft Capital reductions that they otherwise would experience for FY 2011. The K-12 Education BRB also continues to permit school districts to use Soft Capital funding for FY 2011 for any operating or capital expenditure. The \$(165,120,700) Soft Capital reduction leaves an estimated \$48,745,000 in Soft Capital funding available to school districts for FY 2011.

#### **Charter School Additional Assistance**

The budget includes a decrease of \$(10,000,000) from the General Fund in FY 2011 for charter school Additional Assistance funding authorized by A.R.S. § 15-185B4. This change is authorized by the K-12 Education BRB for and is separate from the 1.2% increase in charter school Additional Assistance per pupil funding that is discussed in the “1.2% Inflation Adjustment” narrative above.

#### **ARRA**

The budget includes a decrease of \$(92,800,000) from the General Fund in FY 2011 due to the assumed availability of \$92,800,000 in federal ARRA monies to help fund K-12 formula costs in FY 2011. The General Appropriation Act for FY 2011 stipulates that if the state receives federal assistance from the federal education stabilization fund established by ARRA, the FY 2011 Basic State Aid and Additional State Aid General Fund appropriation is reduced by \$(92,800,000). The General Appropriation Act further stipulates that:

- 1) It is the intent of the Legislature that in FY 2011 \$92,800,000 in federal education stabilization fund monies will be disbursed to school districts and not-for-profit charter schools to offset the \$(92,800,000) reduction in state funding.
- 2) As soon as possible after the effective date of the act, ADE shall reduce scheduled Basic State Aid and Additional State Aid payments to school districts for FY 2011 by \$(92,800,000).
- 3) The federal “backfill monies” shall not impact the Revenue Control Limit (RCL) of any school district.
- 4) The reduction does not affect for-profit charter schools, which are ineligible for federal “backfill” monies.
- 5) The sum of Basic State Aid, Additional State Aid, and federal “backfill” monies that school districts and non-for-profit charter schools receive for FY 2011 shall not exceed the amount of funding that they are entitled to receive under the Basic State Aid and Additional State Aid funding formulas for FY 2011, or the amount that they would receive under the state’s application for federal education stabilization fund monies.

This adjustment is in addition to the “Base Adjustment – ARRA” policy issue discussed separately above.

#### **Endowment Earnings**

The budget includes no change from the Permanent State School Fund in FY 2011 for endowment earnings funding for Basic State Aid. This is due to no estimated change in debt service costs for FY 2011 for State School Trust Revenue Bonds and Qualified Zone Academy Bonds (QZABs) that were issued by the School Facilities Board (SFB) in prior years in order to fund deficiencies correction in public schools. Debt service costs on those bonds is funded with monies from the Permanent State School Fund pursuant to A.R.S. § 37-521B1. The SFB projects that combined debt service costs for State School Trust Revenue Bonds and QZABs will again equal \$25,787,500 in FY 2011 (unchanged from FY 2010). This would leave the amount of land trust monies available to fund Basic State Aid in FY 2011 at \$46,475,500 (unchanged).

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

#### **Continuation of Prior Year Session Law**

The budget includes no change from the General Fund in FY 2011 for the following session law changes from FY 2010, which are continued for FY 2011 by the K-12 Education BRB:

- Joint Technological Education Districts – Fund JTEDs at a percentage that would provide them with approximately \$70,000,000 in Basic State Aid funding statewide for FY 2011 and continue to “hold harmless” a JTED if the adjustment factor otherwise would cause it to receive less state aid in FY 2011 than in FY 2010, apart from reductions due to changes in student counts, property values or other technical factors.
- Career Ladder - Establish a maximum base level increase of 5.0%, rather than the 5.5% increase authorized in permanent law, and limit the program to teachers who participated in it during the prior fiscal year.
- Early Graduation Scholarship Program – Suspend new funding for the program, but allow current participants to continue to receive scholarships to the extent permitted by existing fund balances.
- Actual Utility Costs – Notwithstanding and do not fund the “Actual Utility Cost” (formerly “Excess Utilities”) formula authorized in A.R.S. § 15-910.04 and suspend related reporting requirements currently prescribed in A.R.S. § 15-910.03.

### ***Additional State Aid***

The budget includes \$419,264,000 from the General Fund for Additional State Aid in FY 2011. This amount funds the following adjustments:

#### **Net Assessed Value Growth**

The budget includes a decrease of \$(4,378,700) from the General Fund in FY 2011 for changes in the Net Assessed Value (NAV) of taxable properties statewide for FY 2011. These changes are expected to reduce Homeowner's Rebate costs by \$(4,378,700) because negative NAV growth for FY 2011 will reduce the amount of local property taxes paid by homeowners in FY 2011, which, in turn, will reduce the cost of subsidizing those taxes through the Homeowner's Rebate in FY 2011. The estimated \$(4,378,700) savings amount assumes that statewide NAV in FY 2011 will experience a net decrease by (4.6)% for all classes of property combined (7.3% decline for existing property and 2.7% increase for new construction). It also assumes a (10.6)% decline for Class III properties (owner occupied homes, both new and existing) and that average school district tax rates will increase by 4.0%.

The \$(4,378,700) estimate also includes costs associated with a reduction in the assessment ratio for business property in FY 2011 pursuant to Laws 2005, Chapter 302, as amended by Laws 2007, Chapter 258. Chapter 258 reduces the assessment ratio for Class I properties (commercial and industrial) from 22% in FY 2010 to 21% in FY 2011 (and ultimately to 20% by FY 2012). It also increases the Homeowner's Rebate from 39% of a homeowner's primary property taxes for schools in FY 2010 to 40% in FY 2011. In addition, Chapter 258 increases the current Homeowner's Rebate cap from \$580 per home in FY 2010 to \$600 for FY 2011. Chapters 302 and 258 did not advance appropriate monies to pay for future increases in Homeowner's Rebate costs resulting from their implementation. The (4.6)% NAV growth rate assumed for FY 2011, however, reflects all anticipated NAV changes for the year, including the effects of Chapters 301 and 258.

On a related note, the K-12 Budget Reconciliation Bill for FY 2011 limits the Homeowner's Rebate to the K-12 QTR or to a district's actual primary property tax rate, whichever is lower, starting in FY 2012. This change will eliminate Homeowner's Rebate funding for primary property taxes paid for items such as desegregation programs (A.R.S. § 15-910G), Career Ladder (A.R.S. § 15-918.05) and Transportation Revenue Control Limit (TRCL) (A.R.S. § 15-946) costs that exceed a district's Transportation Support Level (TSL) (A.R.S. § 15-945). The estimated FY 2012 savings for this issue is \$70,500,000.

*Background* – Additional State Aid is authorized by A.R.S. § 15-972, which for FY 2011 will require the state to pay

40% of each homeowner's school district primary property taxes, up to a maximum of \$600 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 III properties are eligible for both "homeowner's rebate" and "1% cap" funding.

### ***Special Education Fund***

The budget includes \$35,242,100 and 1 FTE Position from the General Fund for the Special Education Fund Special Line Item in FY 2011. These amounts are unchanged from FY 2010. An adjustment for enrollment growth is not included for the program in FY 2011, as caseloads for special education vouchers currently are expected to remain unchanged for FY 2011.

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, Department of Economic Security (DES), Department of Health Services (DHS), or the Administrative Office of the Courts) [A.R.S. § 15-1182].

### ***Other State Aid to Districts***

The budget includes \$983,900 from the General Fund for Other State Aid to Districts in FY 2011. This amount is unchanged from FY 2010.

This amount includes \$880,200 (unchanged) for Certificates of Educational Convenience and \$103,700 (unchanged) for Assistance to School Districts for Children of State Employees (ASDCSE).

Certificates of Educational Convenience (CEC's) 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 that is licensed and supervised by DES or 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.

#### **5<sup>th</sup> Special Session Reduction**

*Please see the agency summary for agencywide lump sum reductions.*

#### **Fund Transfers**

The budget includes transfers from this agency's funds to the General Fund. *(Please see the Fund Transfers section at the back of this report for more details.)*

#### **Additional Legislation**

##### **ADM Calculation**

Starting in FY 2012, Laws 2010, Chapter 318 redefines Average Daily Membership (ADM) as being the sum of student "membership" (enrollment minus withdrawals) for September 15, November 15, January 15 and March 15 of each school year divided by 4 (a 4-day average) instead of the 100-day average (for the first 100 days of the school year) that is defined under current law. As a result, schools will only need to report 4 days of "membership" data per year (rather than 100) starting in FY 2012.

Chapter 318 also eliminates "Average Daily Attendance" (ADA) calculations for public schools starting in FY 2012. ADA calculations historically have been used in order to adjust ADM counts downward for elementary and unified school districts with more than 6% average daily absences and for high school districts with more than 8.5% average daily absences. Chapter 318, however, requires school districts to continue to report student absence data to the department at least once every 60 days and requires the department and the Auditor General to include at least a 10% sample of daily attendance records as part of ADM audits beginning in FY 2012.

In addition, Chapter 318 requires the department to compute ADM for the current year no later than April 15 and inform school districts and charter schools of their final ADM counts no later than April 22. Chapter 318 requires any subsequent changes to ADM counts for a current year to be handled as corrections to state aid in the following fiscal year.

Chapter 318 will not have a fiscal impact for FY 2011 due to its delayed effective date. For FY 2012 and subsequent years, it is projected to be roughly cost neutral, with the state cost of foregoing penalties for excessive absences being approximately offset by savings associated with counting ADM later in each school year. (The new calculation includes data from March 15<sup>th</sup>, which is after

the 100<sup>th</sup> school day for most public schools. ADM counts typically decline as a school year progresses due to high school dropouts.)

##### **Budget Limits for School District Overrides**

Laws 2010, Chapter 179 stipulates that budget limits for school district overrides for FY 2011 shall not be affected by the elimination of the Kindergarten Group B funding weight in FY 2011 (*see "Full Day Kindergarten" narrative under Basic State Aid for more information*). Apart from this provision, school district override funding for FY 2011 would decrease because that funding is capped at a percentage of a district's Revenue Control Limit (RCL) and districts with Kindergartners will experience RCL reductions in FY 2011 due to elimination of the Kindergarten Group B weight. This provision is effective for FY 2011 only, so does not permanently hold school district overrides harmless from RCL declines due to the elimination of the Kindergarten Group B weight.

##### **Classroom Site Fund Budget Capacity for FY 2011**

Laws 2010, Chapter 306, stipulates that new spending authority ("budget capacity") from the Classroom Site Fund (CSF) for FY 2011 shall be \$120 per pupil. Apart from this provision, new budget capacity from the Classroom Site Fund (CSF) for FY 2011 would be \$25 per pupil due to a new adjustment required for CSF calculations starting in FY 2011 pursuant to A.R.S. § 15-977G1. Chapter 306 spreads out the impact of that new adjustment over more than 1 year.

##### **SAIS Replacement or Update**

Laws 2010, Chapter 334, requires the department to issue a request for proposal (RFP) by August 1, 2010 for evaluation of its current data system and to award a contract for that evaluation by October 1, 2010. Chapter 334 also requires the department to issue a RFP to replace or update the Student Accountability Information System (SAIS) and to bring it into compliance with the American Recovery and Reinvestment Act of 2009. Both RFP requirements are subject to the availability of funding from state, federal or other sources. Chapter 334 does not appropriate any state monies for these purposes.