

MAINE STATE LEGISLATURE

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STATE OF MAINE
AUGUSTA, MAINE

AN ANALYSIS OF L.D. 1452

The School Funding Act of 1975

Prepared for the
Joint Standing Committee on Education

April 8, 1975

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OPTON TREE GROWTH

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PART I. Description of some major changes in the law

A. Changes in the uniform school tax, maintenance of effort and local leeway provisions

SUBJECT #1: Elimination of the tax pay-in feature for units using the 2.5 mill local leeway provision.

DESCRIPTION:

Under L.D. 1994, any town may, in addition to money raised for the maintenance of its programs, also tax itself another 2.5 mills. This tax effort, called "local leeway", is intended to provide funds for new programs and for the enrichment of existing programs. Under the present law, however, if a town, because of a high per pupil valuation, raises more than \$50 per pupil per mill, the difference must be paid to the State. Because of this pay-in provision, no high valuation community has used this leeway feature. The committee, following the Subsidy Commission, has recommended the pay-in of any amounts over \$50 per mill per student should be eliminated and any extra monies collected should be retained by the community.

SOME POSSIBLE
QUESTIONS AND
ANSWERS:

1. Isn't this elimination of local leeway a deviation from the philosophy of equal financial resources for the support of each Maine school child?

L.D. 1994 did not mandate absolute resource equality. Through both the maintenance of effort and the local leeway provisions, the law recognized that some local communities might be willing to tax themselves somewhat more than others for education.

2. Will this elimination of the pay-in feature of local leeway increase the costs of education?

No. Since high valuation towns have never used local leeway no loss of revenue will be produced by this change.

3. Will the elimination of the pay-in feature increase the future costs of education?

Because local leeway expenditures become part of future years' operating costs, the overall cost of education will increase in proportion to the increased use of the local leeway.

SUBJECT #2: 20% limit on the amount raised from the uniform school tax.

DESCRIPTION:

Under the present law, any town taxing itself for education at more than 2.5 mills below the uniform school (property) tax rate is permitted to "phase-in" to this rate in successive 2.5 mill annual increases. The intent of the law was to provide a gradual rise to the uniform school (property) tax rate for those towns who, because of high valuations, low number of students or both, were taxing themselves at a very low rate for education.

In the above absence of any change in the state valuation, this "phase-in" mechanism would have provided an adequate cushion against any sudden tax increases. The significant increase in the state valuation, however, compounded by the fact that the increase was concentrated in many of the communities requiring the "phase-in" procedure, seriously eroded any positive effects of the 2.5 mill "phase-in". Since the 2.5 mill increase was being applied to a valuation which in some towns had doubled, the intended effect of the phase-in was totally lost.

To adjust for the possibility of future increases in the state valuation, a limit of 20% has been placed on the amount by which school taxes from a community can increase in a single year. In addition, the 2.5 mill "phase-in" language is preserved.

The effect of this change will be to reduce the impact of sudden changes in the state valuation. Although towns will still be "phasing-up" to the uniform tax rate, this phase-in period may be somewhat longer than was originally conceived. Instead of 3-5 years, some towns may require 6-7 years to reach the uniform school (property) tax level. The fundamental intent of the law, however, is preserved, since all towns will, within a reasonable period, be taxing themselves at the same basic rate for education. The 20% limit will, however, provide immediate and meaningful property tax relief for those towns with rapidly increasing state valuations.

SOME POSSIBLE
QUESTIONS AND
ANSWERS:

1. If a 20% limit is enacted, then, many "pay-in" towns will have to pay-in less than was anticipated. Who will pay the difference?

The difference will be made up by a slight (roughly 1/2 mill) increase in the uniform school (property) tax rate as it is applied to all the other towns.

2. In a period of serious inflation, won't this 20% limit retard the movement upwards toward the uniform tax level by the pay-in towns?

Yes, but even a slightly higher tax rate when applied to greatly inflated real estate values already constitutes a significant increase in tax effort by these communities.

SUBJECT #3: How can a local unit's unique funding problems be accommodated within the general formula of the 1975 School Finance Act?

DESCRIPTION:

If a local unit's allocation, for reasons not related to sudden rising enrollments, is not sufficient to fund their existing educational programs the School Finance Act of 1975 provides 2 responses.

First, after a local unit has raised the local leeway, a second maintenance of effort is authorized so that the local unit can maintain its current year per pupil operating costs.

Second, the State Board of Education is given the authority to waive, in cases of "exceptional hardship", the uniform tax plus leeway limits for units that are unable to meet current financial obligations.

SOME POSSIBLE
QUESTIONS AND
ANSWERS:

1. How are the two maintenance of efforts and local leeway computed.

Assume that in the base year of 1973-74 your local unit's per pupil expenditure was \$800. In addition, assume that in 1975 your per pupil expenditures have risen to \$900. Finally, assume that the State average per pupil costs have only reached \$650. How is the necessary \$250 made up by the town?

A. Base year 1973-74		
per pupil expenditures		
(PPE)		\$800
Hypothetical State average		
per pupil cost (PPC)		-\$650
Difference		\$150; 1/2 of which the State
		will pay, the other 1/2
		of which the town must
		raise by local taxation
		through its <u>first</u> main-
		tenance of effort.
		Thus,
B. Hypothetical State		
per pupil average cost		\$650
1/2 of difference between		
base year PPE and current		
State PPC		+\$ 75

D. State PPC	\$650	
1/2 difference between base year PPE and State PPA, paid by State	\$ 75	
1st maintenance of effort (locally paid)	\$ 75	
Maximum local leeway (shared state/local costs)	\$125	
2nd maintenance of effort (locally paid)	\$100	
	<u>\$1025</u>	Total amount which can be raised for 1975 operating costs and new programs.

B. Items in the computation.

SUBJECT #1: Debt service and bus purchases.

DESCRIPTION:

Presently, 50% of the total costs of debt service and bus purchases is funded by the uniform school (property) tax and the other half is supported from state tax sources. The Education Subsidy Commission (its Recommendation #1) would have removed the costs of these 2 items from any support by the uniform school (property) tax. Under this recommendation, the local share of debt service and bus purchases would have been funded by any municipality incurring the costs. The state's share would have been provided on a sliding scale of 0% to 90% of the total costs, depending on the per pupil valuation of the municipality. The sliding scale was intended to ensure that towns with low valuations and significant enrollments are provided with more state aid than other towns with high valuations and low enrollments.

The Subsidy Commission recommended this change in the funding of debt service and bus purchases for 3 main reasons:

1. The local share of the costs would be more visible to local voters in each municipality. Under the present law, if a municipality initiates a project, the actual costs of that project to the town are buried in the total costs of all such projects across the state. Although these total costs are funded in part by the town's uniform school (property) tax effort, the costs of the individual project to the town are not sorted out of the total. As a result the illusion that the state is paying "100%" of the costs of debt service and bus purchases has been generated. This recommendation was intended to dispel the illusion.
2. Removal of these 2 items from the uniform school (property) tax would reduce the mill rate nearly 1.5 mills and this lowering of the mill rate would bring immediate relief to the "pay-in" communities who had experienced the largest increases in property tax levels.
3. Finally, the recommendation was intended to slow the increase in the number of requests for construction and bus purchases. In part because of the illusion of "100%" state funding, the requests for construction and buses have increased. By making the local unit's share of costs more visible, this recommendation was intended to somewhat dampen the rising demand.

Each of the Subsidy Commission's reasons for its recommendations is sound. The Education Committee, however, has not accepted the recommendation. Instead, the present method has been retained with some major new controls.

REASONS FOR
NOT ACCEPTING
RECOMMENDATION:

The Education Committee has recommended no change in the present method of funding debt service and bus purchases for the following reasons:

1. Although the change suggested by the Subsidy Commission might slow requests, the requests discouraged by the change would probably be from the units most in need of and least able to pay for construction and buses. The result, then, might be that the units with greater needs would continue to have these needs unfulfilled.
2. Any town incurring costs under these two items would have to tax itself beyond the uniform school (property) tax rate. This additional taxation would reintroduce the same inequities in tax efforts that the present law avoids.
3. If the financing of debt service and bus purchases was changed, a decision would be necessary about which units should qualify for "grandfathering" protection under the present law. Almost any unit or group of units excluded from such provisions would strongly object if a local need for construction or buses existed.

THE EDUCATION
COMMITTEE'S
APPROACH:

The problems generated by the "100%" illusion and the accompanying increase in construction requests are undeniable. Rather than changing the present funding method, however, 3 other changes are recommended which directly address these problems.

1. An article specifying the state cost of any capital outlay project is made a requirement in the annual warrant of each municipality. This change will identify the costs of these items to local voters.
2. A law has already been enacted giving the Commissioner of Educational and Cultural Services the authority to limit the bus leasing and purchases of any unit.
3. A dollar limit for debt service is established by the legislature, to be reviewed annually, as part of the School Finance Act of 1975. The level for 1975-76 is \$35 million. This figure contrasts with the actual \$50 million levels of the last two years.

These three changes, unlike the recommendation of the Subsidy Commission, respond directly to the problems identified in the area of debt service and bus purchases without creating further problems.

SUBJECT #2: The removal of State operated schools from partial reliance on the uniform school (property) tax.

DESCRIPTION:

Prior to L.D. 1994, State supported schools -- Baxter, Stevens, Boys Training Center, Indian schools and Unorganized Territory Schools -- received no financing from a local unit. These schools were supported entirely from state tax sources. The present law was not intended to change that funding method. As the result of an Attorney General's opinion, however, the term "public schools" has been construed as including these formerly 100% state supported schools. The result is that part of their funding now comes from the uniform school (property) tax. The committee recommended defining "public schools" to exclude these State supported institutions. This change is consistent with the original intent of the law and will reduce the costs of education borne by the uniform school (property) tax.

SOME POSSIBLE
QUESTIONS AND
ANSWERS:

1. What difference does this change make in the computation of the total costs of education?

Removing these schools from partial reliance on the uniform property tax shifts the costs to General Fund revenue sources and thus lowers the property tax rate by roughly 1/4 of a mill, a reduction of \$6 million.

SUBJECT #3: Change in payment method for PL 874 (Federal) pupils.

DESCRIPTION:

Presently, pupils living on any property of the Federal Government are not considered as residents for the purposes of state aid to the local unit in which they are enrolled. The reason that they are not counted is that the Federal Government provides a per pupil payment to the local unit for each of these students. If the students were counted as "residents" by the state, the local unit would receive a per pupil payment from the state as well as the Federal Government for the same pupils.

Since the Federal per pupil payment is always lower than the state's payment, the state now pays the difference in order to ensure that the unit receives as much money as it would receive if the students were just regular resident pupils.

Within the last year the Federal law relating to these pupils has been changed. The law now allows monies received from the Federal government to be subtracted when the allocation to the local unit is computed. This change removes the only reason for not counting these pupils as "residents".

The change in the state law, then, provides that these pupils will be counted as residents and that Federal money received for them will be subtracted when the state figures its allocation to the unit.

Although this change is merely administrative, it will ease the uncertainty about allocation levels expressed by some of the affected areas. No additional money is committed because of the change. Rather, the same money is paid in a simpler way.

- C. Changes in methods of computing the state and local shares of education costs.

SUBJECT #1: Use known preceding year costs plus an inflation factor in computing the state and local share of education costs.

DESCRIPTION:

Under the present law the Department of Educational and Cultural Services estimates the costs of education for each year roughly 6 months prior to the beginning of that year. The uniform school (property) tax rate is then established by the Director of Property Taxation to return 1/2 of the total costs estimated.

The state share (50%) of education costs, however, is presently linked to the actual not to the estimated costs. If actual costs during the next year exceed the estimate, a deficit will be created which the state will be required to fund. Part of the existing deficit is due to such a gap between actual and estimated costs during the last year.

To eliminate this potential source of error and reduce the likelihood of any future deficits, 2 changes have been recommended. First, the costs of education are to be based on the last known costs plus an inflation factor. Under this system, the estimate, completed in 1975, for 1976 costs would be based on 1974 costs plus the inflation factor. The inflation factor is the average percentage change in costs during the preceding 2 years. Second, the state's obligation would be tied to this estimate, rather than to actual costs. With this change, the state's dollar obligation for the operating costs of local units will be known by both the state and local units in advance. The possibility of a deficit from costs exceeding the estimate is thus eliminated.

SUBJECT #2: Use known preceding calendar year enrollments, with adjustments for increases, in computing the State and local share of education costs.

DESCRIPTION:

There are two main problems with rapid fluctuations in enrollments. First, when there is a rapid increase in a local unit's enrollment, expenditure levels might be forced beyond the funds available from the uniform school property tax, maintenance of effort, and local leeway provisions of the law. Secondly, when there is a sudden decrease in the enrollment the present law provides for a decrease in allocation to the local unit. With contract commitments made and supplies purchased, the unit cannot immediately decrease its costs to reflect the decreasing enrollment. The local unit may, then, find itself with decreased funding for essentially unchanged school costs.

The School Finance Act of 1975 offers the following two solutions:

First, the State Board is authorized to adjust State aid to reflect rapidly increasing enrollments whenever a unit documents that it cannot meet its financial obligations within its allocation, supplemented by the amounts permitted through maintenance of effort and local leeway. This adjustment will be added to the already computed allocation for the unit.

Secondly, in order to soften the blow of sudden decreases in a local unit's enrollments, the costs of education will no longer be based on the current number of students but rather on pupil counts conducted in April and October of the preceding calendar year. This will allow local units one full school year to adjust to the lower level of funding which may accompany decreased enrollments.

SOME POSSIBLE
QUESTIONS AND
ANSWERS:

1. Does this method of handling enrollment changes entail any additional costs as compared with the present practice of using current year enrollment figures?

Yes. Without the year for adjustment, programs would have to be cut or personnel released in order to stay within the uniform school tax limits. Thus, the artificially high costs of operation for that exempt school year will be reflected in the computation of the next year's State cost of education.

SUBJECT #3: Review of total education costs by the Governor and the Legislature.

DESCRIPTION:

Presently, the Commissioner of Educational and Cultural Services computes a figure for the total costs of education. This figure is certified to the State Director of Property Taxation who establishes the mill rate of the uniform school (property) tax, by simply dividing the figure for the total costs of education by the amount of the most recent state valuation. The law directs that the state and local shares should each be 50% of the total costs. Although the law is explicit, leaving no administrative flexibility in the actual computing of the mill rate, the Governor and the Legislature are not now involved in any part of the process of establishing costs.

The Education Committee has recommended, therefore, that 2 steps should be added to the process. First, the Commissioner of Educational and Cultural Services will communicate his estimate of total education costs to the Budget Office and the Governor. The Governor may review and revise this estimate and, then, send it to the Legislature. The Legislature must review and approve the final figure for the total costs before the mill rate is established by the Director of Property Taxation.

SUBJECT #4: Uniform school year and consistency between tax assessment and subsidy distribution year.

DESCRIPTION:

- (a) Presently, the tax assessment and subsidy distribution years overlap by 6 months. Because of this overlap, monies are raised in excess of local needs for distribution purposes. The result is that some local units find themselves with money which they must raise but cannot spend. This excess money should not be confused with the overcollection feature of the law which requires that certain money in excess of local needs should be sent to the state for redistribution.

The pointless raising of this extra money, an inadvertant by-product of the overlapping of the tax assessment and subsidy distribution years, can be eliminated by changing the language in the tax statutes so that the 2 years coincide. Following the recommendation of the Subsidy Commission, the Education Committee has recommended this change. This change is consistent with intent of the law and eliminates a potential and needless hardship for some communities.

- (b) A second problem relates to the absence of any uniform school budget year. Presently, some local budgets are adopted before the state uniform property tax is established. In addition, new programs may be approved by voters who see only part of the full year's total costs of the programs. Finally, voters now must approve budgets before any changes in State aid for education are established. Each of these problems can be eliminated through the adoption of a school budget year which coincides with the State's fiscal year.

D. The Property Tax Circuit Breaker

SUBJECT: The committee's recommendations to the Committee on Taxation that property tax relief should be accomplished through a property tax "circuit breaker".

DESCRIPTION:

The School Finance Act of 1975 offers property tax relief to some high valuation towns through the 20% limitation on the yearly increase in the amount raised by the uniform school (property) tax. In addition, the committee has suggested a vehicle for additional direct property tax relief by formally requesting that the Taxation Committee develop a property tax circuit breaker system.

SOME POSSIBLE
QUESTIONS AND
ANSWERS:

1. What exactly is a property tax circuit breaker?

Maine currently administers such a circuit breaker for all its citizens over 62 years of age. Under the Elderly Household Tax and Rent Refund Act property tax refunds, limited to \$400, are made by the State when a person's property tax, or 25% of a person's rent, exceeds 21% of household income over \$3,000. To be eligible a person must earn less than \$4,500 if single or less than \$5,000 if married. The average yearly refund this year will be approximately \$225. The name "circuit breaker" is derived from the fact that tax refunds are not made until the amount of tax exceeds -"breaks the circuit"- a certain per cent of a person's income.

2. How is a circuit breaker approach superior to reducing the uniform school (property) tax by simply raising the State income tax?

Circuit breakers accurately and directly provide property tax relief to only those persons most in need. While an income tax increase would make it possible for communities to lower their property taxes, there is no guarantee that the mill rate would actually be lowered.

3. What are the disadvantages of a circuit breaker?

Circuit breakers are administratively complex and increased accuracy in determining who is truly eligible for relief is achieved only with even greater administrative effort.

4. How might a property tax circuit breaker be funded?

While there are many avenues by which State revenues might be increased -- increased cigarette taxes, liquor taxes, corporate income taxes, a new business inventory tax -- the most likely means of raising the necessary money would seem to be the raising of the State's personal income tax.

5. If a property tax circuit breaker means a rise in the State's personal income tax, why didn't the committee take the more simple approach to property tax relief and endorse the Education Subsidy Commission's recommendation to increase the State's share of education costs to 55% in 1977 and 60% in 1978 and pay for the increase through the personal income tax?

First, simply raising the personal income tax does not guarantee property tax relief to those most in need. The circuit breaker approach does.

Second, the cost in 1977 for the State to assume 55% of the burden of education might be approximately \$14 million; in 1978, with the State carrying 60% of the burden, the cost might be \$30 million. A circuit breaker approach might¹ be much less expensive. For example, if the benefits currently received through the elderly property tax circuit breaker were extended to all Maine homeowners or renters over 18 the cost might be no more than \$20 million². Further, a circuit breaker could be devised that, with lower benefits, could cost even less than \$20 million.

¹ Estimates of a circuit breaker's costs are not precise. The present elderly circuit breaker offers a relatively generous refund and yet is administratively uncomplicated. A different program might result in greatly increased applications, thereby making the estimates included here too low.

² At this price an individual with a taxable income of \$10,000 per year might expect to pay an additional \$76 per year in State income taxes.

PART II. Controls on education expenditures contained in the School Finance Act of 1975

The School Finance Act of 1975 responds in the following ways to the major reasons for the existing deficit in education expenditures:

1. An article in the town warrant must specify the state and local share of any major capital outlay (debt service) thus clarifying the local unit's perception of their financial commitment in such projects;
2. A legislative ceiling will be established each year for the authorization of major capital outlay (last year's outlays were approximately 50,000,000).
3. In a separate Act the legislature has restricted bus purchases by allowing the Commissioner of Education to approve all future bus purchases and leasing.
4. Instead of calculating the total education costs on the basis of estimates of the next year's expenses and numbers of students, as is the current practice, the costs will now be limited to a local unit's last known expenditures, plus an inflationary factor which adjusts for increasing or decreasing costs, and the last known numbers of students, thereby reducing the possibility of a faulty estimate.
5. Because of the above changes the amount of money a local unit can appropriate for education is limited to the uniform school tax, the maintenance of effort and local leeway. The Commissioner will have authority to offer flexible relief in certain cases.
6. Finally, with both the Executive Department and the Legislature now having the opportunity to review and, if necessary, revise the total costs of education, the taxpayer is protected against soaring costs without proper representation.

PART III. A short key to L.D. 1453

Major recommendations and their location in L.D. 1453

1. Overcollection of the local leeway for high valuation units which use this feature is eliminated: Sec. 33.
2. A limitation of 20% is placed on the increase that any community is required by the State tax assessment to bear annually on school costs: Sec. 41.
3. A second locally funded maintenance of effort is provided to give a more flexible ceiling to local units: Sec. 33, subsection 13; Sec. 17, sub-§ 7-D; Sec. 27, ¶B.
4. The State Board is given flexibility to waive leeway limits when a local unit is not able in any way to meet current financial obligations: Sec. 33.
5. Legislative ceilings are placed on authorizations of all school construction: Sec. 21, sub-§11.
6. Minor capital outlay is included in operating costs and a limit is placed on it: Sec. 21, sub-§§ 12,13; and Sec. 2 through 13.
7. State operated schools are removed from consideration in establishing the uniform property tax: Sec. 15, sub-§1.
8. Methods of computing projected costs and the distribution of aid are based on known previous figures: Sec. 15, sub-§§ 2 and 3; Sec. 30.
9. Both the Executive Department and the Legislature will have an opportunity to review and/or revise total State education costs: Sec. 38.
10. A unit which gains pupils over the last year will have to allocation adjusted for the increase: Sec. 29.
11. A unit which loses students will be reimbursed on last year's enrollment, giving it one year to adjust to decreased funding: Sec. 15, sub-§§2 and 3; Sec. 23, sub-§1, ¶¶ A and B; Sec. 31.
12. P.L. 874 funds for federally impacted areas are brought into conformity with federal law: Sec. 15, sub-§1; Sec. 28.
13. Uniform school budget year: Sec. 34.
14. Consistency between tax assessment and subsidy distribution year: Sec. 38.