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The Basics of School Funding December 2023

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School Finance

How are Local School Districts Financed?

Three Primary Sources

- Local Taxation
- State Funding
- Federal Funding

Part I

How the State Raises Revenue for Schools

- The first part of the presentation will discuss pre-Proposal A, Proposal A, and post-Proposal A taxation rates and how the State finances the K-12 system in general.

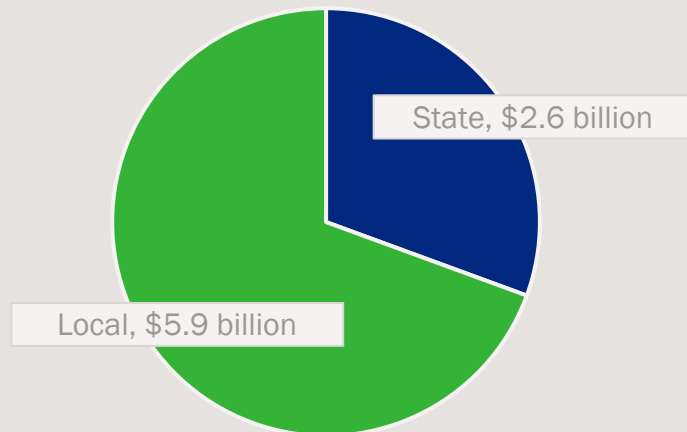


BEFORE Proposal A

Local Taxation Plays a Large Role

- Prior to Proposal A, schools were financed primarily through local property taxes. In fact, in 1993-94, home and business owners were paying on average 33 operational mills assessed on the State Equalized Value (50% of market value) of their properties. At that time, local taxation accounted for roughly 69% of the State/local split of school finance, with State funding making up the other 31%.

State/Local Funding Mix



The School Aid Fund at that time consisted of:

Sales Tax: 60% of proceeds at 4% rate;

Cigarette Tax: 2 cents of 25 cents/pack tax;

Lottery: Net Revenue;

Industrial and Commercial Facilities Tax: Paid to the SAF for properties of “in-formula” districts;

Commercial Forest Tax: same as above;

Liquor Excise Tax: Revenue from 4% excise tax.

What Spurred Proposal A?

Public Act 145 of 1993

- In July of 1993, the Legislature approved, and the Governor signed into law, P.A. 145 of 1993.
- This law exempted all real and personal property taxes for school operating purposes beginning in 1994.
- This law eliminated approximately 64% or \$6.4 billion of \$10.0 billion of total K-12 school funding beginning in FY 1994-95.
- The Legislature had approximately five months to create a new funding structure.

PROPOSAL A

How Did the Method of Financing Schools Change?

1. State School Aid Fund

- Sales Tax Increased from 4% to 6%, with 100% of the Revenue from the Additional 2% Dedicated to the School Aid Fund (SAF);
- Use Tax - All Revenue from the 2% Increase --SAF;
- State Education Tax Assessed on the Taxable Value of all Property at 6 mills;
- New Real Estate Transfer Tax - 0.75% applied to the selling price of the property;
- Cigarette Tax - increased from 25 to 75 cents per pack, with 63.4% of the increase dedicated to the School Aid Fund. (August 1, 2002, saw a 50-cent increase, 20 cents of which was dedicated to the SAF. This tax increased again on July 1, 2004, to \$2.00/pack; none of the 75-cent increase was dedicated to the School Aid Fund.)

School Aid Fund Earmarked Taxes and Lottery

May 2023 Senate Fiscal Agency Forecast

Fund Source	FY 2023-24 Estimate (in Millions)
Sales Tax	\$7,891.8
Use Tax	\$846.4
State Education Tax (6 mills)	\$2,753.0
Real Estate Transfer Tax	\$357.6
Income Tax	\$3,794.9
Lottery	\$1,241.4
Gaming Tax	\$447.4
Other	\$488.9
Total	\$17,821.4

PROPOSAL A

How Did the Method of Financing Schools Change?

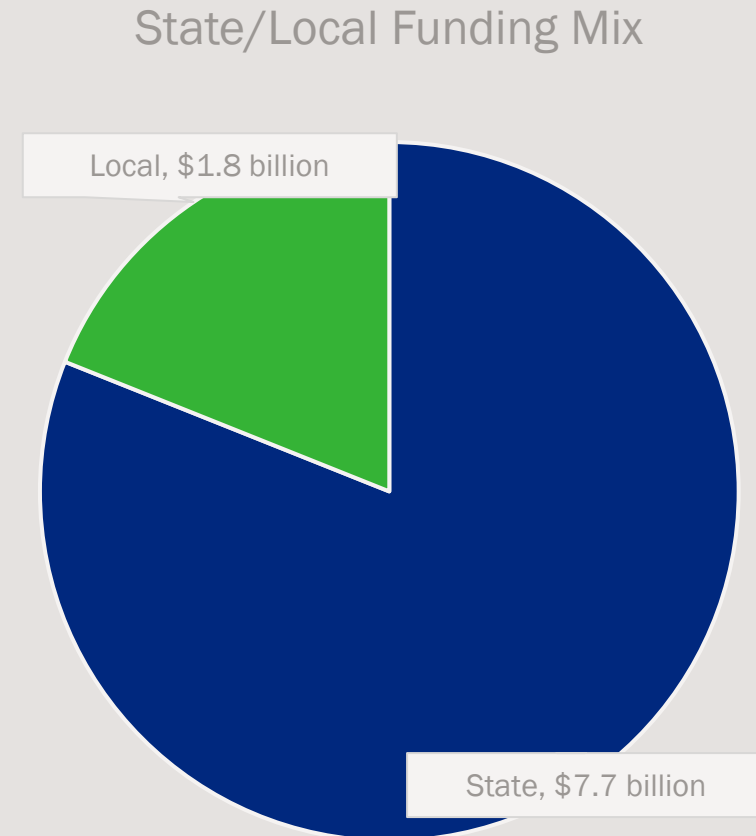
2. Local Taxation

- In general, local taxation for operations (not including debt/capital or sinking fund) is capped at 18 mills levied on the taxable value of non-homestead property, with no operational mills levied on homesteads (there is an exception for “hold-harmless” districts);
 - Homesteads: Taxpayer’s primary residence, including noncommercial agricultural property.
 - Non-homesteads: All other property such as business, rental property, vacation homes, and commercial agriculture.
- Also, taxable value increases are capped at the lesser of the rate of inflation or 5%. State equalized value (SEV) continues to grow uncapped, and taxable value=SEV when a property transfers ownership.

AFTER Proposal A

How Did Local Taxation Change?

- After the passage of Proposal A in March 1994 by the voters of Michigan (69% Yes, 31% No), average operational mills decreased to 6 mills levied on homeowners by the State for the State Education Tax (SET), and 24 mills for non-homesteads (6 mills for the SET, 18 mills levied by schools). This reduction in property taxes, and increase in State revenues for schools, changed the State/local funding mix to approximate an 80%/20% split.



AFTER Proposal A

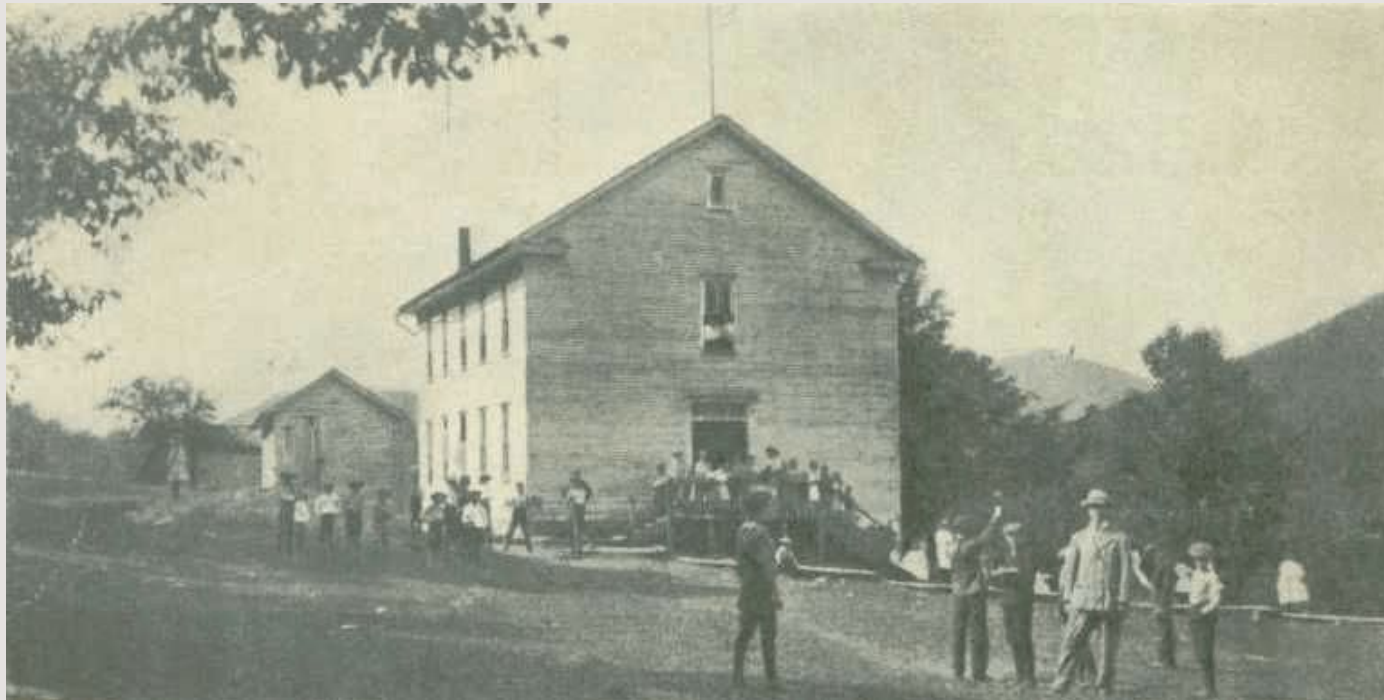
Local Taxation Can and Does Still Occur

- School district voters still must approve the mills assessed on non-homesteads and are required to renew these mills over time. School districts also may ask voters for approval to levy mills for debt (i.e., capital outlay to build or renovate facilities), sinking funds (i.e., purchase of land for future building projects), and to enhance funding for operations on an Intermediate School District-wide basis only (up to 3 “enhancement” mills).
- (Six of 56 ISDs are levying an enhancement millage for operations: Monroe at 0.9866 mill, Kalamazoo and Midland at 1.5 mills each, Muskegon at 1.0 mill, Kent at 0.9 mill, and Wayne at 2.0 mills.)

Part II

Funding at the School District Level

- Now that we've covered how State funding of schools has changed with Proposal A, we will turn to a discussion of funding at the district level.



Financing for Schools

Before Proposal A: Guaranteed Mill Amount

- Prior to Proposal A, schools received local property tax revenue as determined by voters, plus State aid. If districts were “in-formula”, they received State funds so that they were guaranteed a dollar amount for each mill levied. There were 381 “in-formula” and 177 “out-of-formula” districts. Districts also received categorical aid for specific expenditures, such as School Readiness and Special Education.

Financing for Schools

After Proposal A: the Foundation Allowance Concept

- After Proposal A, school funding was tied to each pupil counted in a district's membership. Districts receive a foundation allowance, which is a per-pupil funding amount initially determined in 1994-95 based on what the district was receiving on a per-pupil basis in 1993-94. A minimum level of funding was established (\$4,200), a target level (the "basic") was determined (\$5,000), and a "cutoff" point for State Aid was set (\$6,500), with dollars above that point raised from local mills.

State/Local Funding of Foundation Allowance

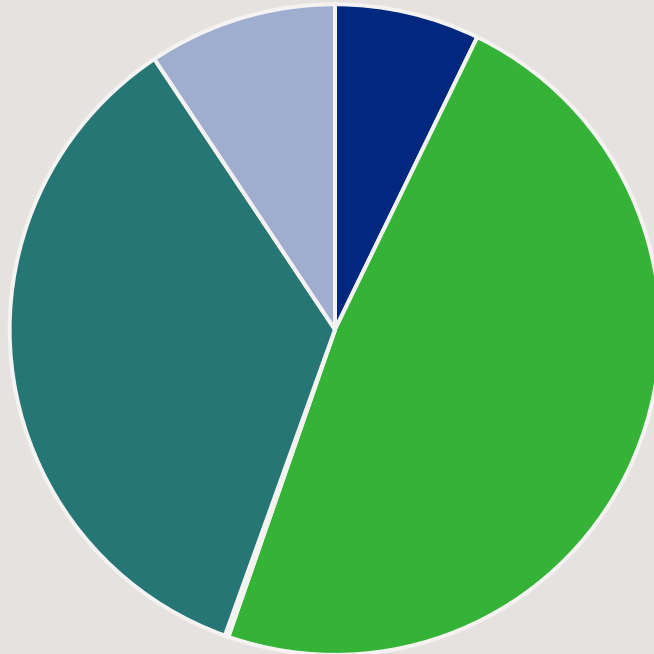
- Each district must levy 18 mills on non-homesteads.
- Local revenue from 18 mills is calculated at the State level on a per-pupil basis.
- State deducts the per-pupil local revenue from the lesser of the foundation allowance or hold-harmless “guaranteed” per-pupil amount.
- Districts above the hold-harmless cap are allowed by law to levy additional mills (with voter approval) to achieve their prescribed foundation allowance.

	Munising Public Schools
1994-95 Foundation	\$4,200
1994 Non-homestead T.V.	\$45,545,273
1994-95 Pupils	1,107.34
18 Mills (Per-Pupil Basis)	\$740
State Aid (Per-Pupil Basis)	\$3,460
Hold-Harmless Millage Rev. If Nec.	\$0
	Central Lake Schools
1994-95 Foundation	\$5,961
1994 Non-homestead T.V.	\$62,930,152
1994-95 Pupils	504.4
18 Mills (Per-Pupil Basis)	\$3,715
State Aid (Per-Pupil Basis)	\$2,246
Hold-Harmless Millage Rev. If Nec.	\$0
	New Buffalo Schools
1994-95 Foundation	\$8,527
1994 Non-homestead T.V.	\$203,811,384
1994-95 Pupils	651.24
18 Mills (Per-Pupil Basis)	\$5,633
State Aid (Per-Pupil Basis)	\$867
Hold-Harmless Millage Rev. If Nec.	\$2,527
Hold-Harmless Mills Levied	12

1994-95 Foundation Allowances

Five Groupings of Districts' Per-Pupil Funding

Numbers of Districts by 1994-95
Foundation Allowance Grouping



■ Minimum ■ Min to Basic ■ Basic ■ Basic to H.H. ■ Above H.H. Cap

Minimum	\$4,200	40
Min to Basic	\$4,200-\$5,000	267
Basic	\$5,000	1
Basic to H.H.	\$5,000-\$6,500	195
Above H.H. Cap	Above \$6,500	52

Dollar Increases in the Basic (Target) Foundation Grant

- The amount of available State funding allowance determines the increase in the basic foundation allowance. (The basic foundation allowance was renamed to “target foundation allowance” in FY 2019-20.)
- Between ‘95 and ‘00, districts at the minimum foundation got twice the dollar increase of the basic foundation grant, to partially close the funding gap. Between ‘01 and ‘07, all districts received the same dollar increase per pupil. The “2x” formula was reinstated in FY 2007-08 and the basic was increased to the hold harmless/”State max” level of funding.
- In FY 2021-22, the minimum foundation allowance was raised to a level equal to the target foundation allowance. Beginning in FY 2022-23, references to the minimum foundation allowance were removed.

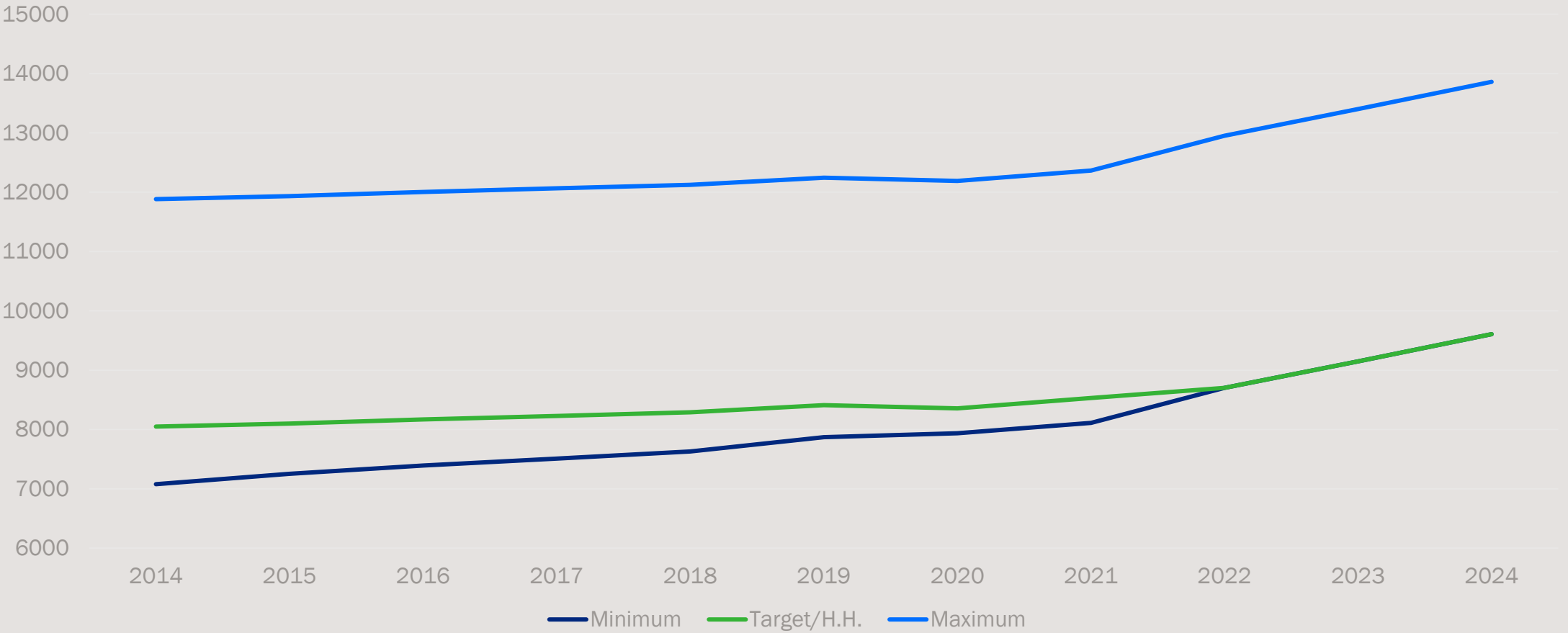
Dollar Increases in the Basic (Target) Foundation Grant

Fiscal Year	Dollar Increase	Fiscal Year	Dollar Increase
1994-95	n/a	2009-10	0
1995-96	153	2010-11	0
1996-97	155	2011-12	-470
1997-98	154	2012-13	0
1998-99	0	2013-14	30
1999-2000	238	2014-15	50
2000-01	300	2015-16	70
2001-02	300	2016-17	60
2002-03	200	2017-18	60
2003-04	0	2018-19	120
2004-05	0	2019-20	-55
2005-06	175	2020-21	175
2006-07	210	2021-22	171
2007-08	48	2022-23	450
2008-09	56	2023-24	458



Change in Foundation Allowance Over Time

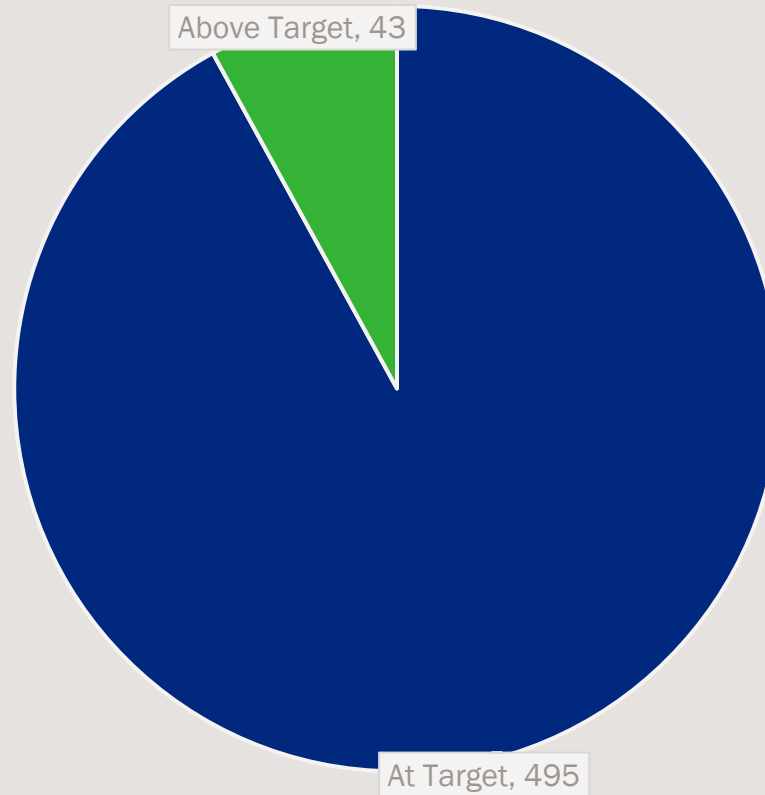
FY 2013-14 through FY 2023-24



2023-24 Foundation Allowances

Two Groupings of Local Districts' Per-Pupil Funding (excludes Charter Schools)

Numbers of Local Districts by 2023-24 Foundation Allowance Groupings



Charter Schools

- Charter Schools in Michigan are paid entirely with State funds. Charters do not have physical property boundaries and therefore do not levy mills for a local revenue collection. A charter school receives a foundation allowance equal to the \$9,608 for FY 2023-24. (Online-only “cyber” charter schools receive a foundation allowance of \$9,150 for FY 2023-24.)
- Charter Schools are not allowed to ask for debt millage in Michigan, and must finance capital projects out of operating revenues.
- As of FY 2022-23, there were 295 operating charter schools, with pupil memberships totaling more than 150,000, or 10% of the total students enrolled in Michigan schools on a full-time basis.

Part III Summary: How has School Finance Changed with Proposal A?

- First and foremost, Proposal A was designed to lower Property Taxes - we now have higher sales, use, and cigarette taxes, and a new real estate transfer tax to offset lower property taxes.
- Annual growth in local taxable value is capped at the lower of the rate of inflation, or 5%.
- Second, Proposal A raised the lowest per-pupil districts to a “basic” level of funding.
- Third, Proposal A tied funding to a per-pupil concept, rather than the Property Tax basis.

Part IV

Now and the Future: Some Recurring Questions in School Finance

- Districts above the Hold Harmless cap generally have not received inflationary increases and, though “wealthier” on a per-pupil basis, typically have smaller fund balances. Section 20j operational funding was vetoed in FY 2009-10, further exacerbating the issue. ‘Out-of-formula’ districts (those whose local revenue exceeds their foundation allowance) receive no State increases.
- Declining Enrollment districts: since funding is tied to pupils, what happens to a district with a shrinking pupil base? There is a minimum level of funding necessary to operate district and pupil counts are not known until October.
- Fiscal year of State doesn’t align with districts’ fiscal years, leading to cash flow borrowing costs. State begins paying in October, but school year begins in July.
- Inequities in taxable values of similar homes, dependent on when last sold (i.e., longer in same house, lower taxes). This is the so-called “pop-up” issue. Empty nesters sometimes now stay in the home.
- Probable future discussions - consolidation, class sizes, busing, sales tax stability, sinking fund uses.
- Continued use of School Aid Fund Revenue to Partially support Postsecondary Budgets (higher education and community colleges)? More than \$1.0 billion for FY 2023-24.
- MPSERS - Rate cap, assumed rates of return, new hybrid’s implementation.

Facts and Figures

- For enacted FY 2023-24, the total K- 12 budget is \$21.5 billion of which \$2.2 billion is Federal aid, and the remaining \$19.3 billion is State funding. (Local revenues are not included here.)
- Foundation Allowance payments make up roughly 50% of the K-12 budget. State MPSERS costs are 12%, Federal grants are 10%, State Special Education is 8%, At-Risk funding makes up 5%, Early Childhood makes up 2%, and other items account for the remainder of the budget.
- In 2023-24, there will be an estimated 1,243,100 FTEs in 538 Local School Districts and 150,500 FTEs in 285 Charter Schools.

FY 2023-24 Initial Gross Appropriations

