THE NEGATIVE FACTOR AND PUBLIC SCHOOL FINANCE

By Josh Abram

The "negative factor" is a provision in state law that reduces the amount of total program funding and state aid provided to K-12 school districts. This issue brief discusses how the negative factor is applied in the School Finance Act (SFA), gives a short history of school finance leading to the creation of the negative factor, and provides a summary of the recent legal challenge to the negative factor.
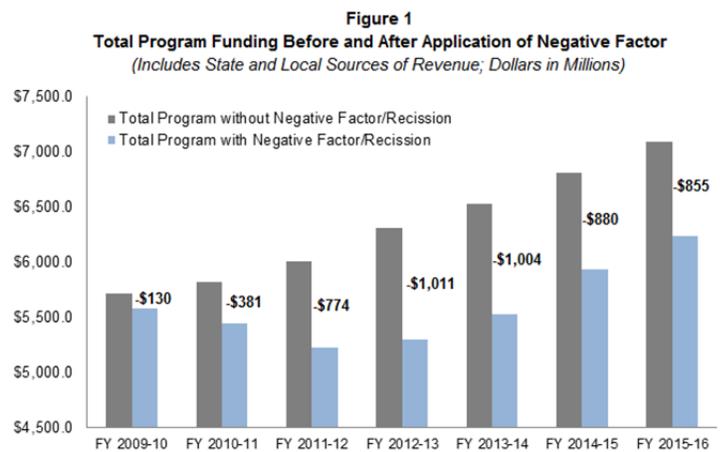
School finance in Colorado. The SFA is the statutory mechanism through which school districts receive state and local funding for operating purposes. For FY 2015-16, the act authorizes about $6.2 billion in total program funding to school districts. The SFA calculation begins with a base per-pupil amount of funding that is uniform for all school districts. This base amount is then adjusted to account for district-specific differences such as size, cost of living, and the relative size of a district's at-risk student population. The district's per-pupil funding amount is multiplied by the district's funded pupil count to calculate a total program amount.

Once this total program amount is calculated, local property and specific ownership taxes are used to fund as much as possible of this amount, and the state backfills or "equalizes" the difference. In this way, the law uses state money to financially support schools in districts where local revenue sources are insufficient to fully fund total program.

Constitutional increases in per-pupil funding. In 2000, voters passed a constitutional amendment that requires the base per-pupil funding amount to increase yearly by at least the rate of inflation plus 1 percent through 2011, and increase yearly by inflation thereafter (Amendment 23). The state constitution therefore requires that base per-pupil funding increase yearly.

The economic downturn beginning in 2007 reduced state operating revenue from income taxes and the state sales tax. As a result, the General Assembly faced budget shortages across all functions of government. Although the constitution requires annual increases in base per-pupil funding, the constitution also requires a balanced budget. For this reason, paying for the annual increase in base per-pupil funding can be challenging for the state legislature.

How much is funding reduced by the negative factor? Since it was first introduced, the cost of the negative factor has grown from an original recission of $130 million, to its present value in FY 2015-16 of about $855 million. Figure 1 shows the cost of the negative factor in each of the last seven fiscal years. The cost is the difference between total program with inclusion of the negative factor and total program without the negative factor.

Figure 1
Total Program Funding Before and After Application of Negative Factor
(Includes State and Local Sources of Revenue; Dollars in Millions)

Source: Colorado Department of Education and Legislative Council Staff.

How does the negative factor work? The negative factor reduces each district's total program funding by a specified percentage determined by a targeted funding level chosen by the General Assembly. The negative factor imposes this reduction by reducing the amount state aid received by each district. In some school districts, the negative factor reduces state aid by a relatively smaller percentage than in other districts, because those districts receive a higher percentage of funding from state versus local sources. In districts that receive a relatively small amount of state aid, the negative factor can eliminate 100 percent of the state aid to that district. A small number of districts fund their schools exclusively from local sources. These districts are therefore unable to rescind the full amount of the negative factor, and instead are required to make up the difference through other mechanisms to the degree possible. In this way, the law aims to spread the financial impacts of the negative factor across all school districts.

Local revenue can partially offset the negative factor in districts that have authorized mill levy overrides. In addition to funding from the SFA, state law allows each local school district to seek voter approval to increase property tax rates and collect and spend additional local revenue dedicated exclusively for the district's public schools. Referred to as "mill levy overrides," some districts are able to backfill a portion of lost state revenue from the negative factor by collecting additional property taxes for schools.

In FY 2014-15, 115 school districts received voter approval for mill levy overrides. In total, these districts collected about $826 million in override property tax revenue that year.[1]

Legal interpretation. In 2003, the Office of Legislative Legal Services (OLLS) issued a legal opinion addressing the constitutional requirement for increased public school funding, concluding that the constitution requires that base per-pupil funding increase annually, but does not require that total program funding for schools increase. Essentially, the OLLS interpretation finds that the constitution requires *only* that the base per-pupil funding amount increase. So long as this amount is increased as the first step in the SFA calculation, the General Assembly is not required to increase the *total* amount of funding for schools. Accordingly, the state constitution does not limit the General Assembly's authority to determine the total amount of school funding, so long as the base per-pupil amount is adjusted upward each year by at least inflation.

Based on this legal opinion, the legislature amended the SFA in 2010 to create the negative factor, originally labeled the "budget stabilization factor." The factor is a percentage reduction in each school district's total program funding that is calculated *after* the base per-pupil funding amount is increased and other district-specific adjustments are calculated. The negative factor enables the state to ensure that revenue is sufficient to pay the state's share of total program funding for K-12 public schools, as well as the other expenses of state government. From FY 2001-02 through FY 2008-09, the legislature increased the amount of base per-pupil funding by at least the amount required by the constitution; however, due to application of the negative factor, the state's appropriation for school districts beginning in FY 2009-10 has been less than what would have otherwise been appropriated to fund the state's share of total program under the SFA.

Legal challenges to the negative factor. In June 2014, a group of parents, education advocacy organizations, and school districts filed suit against the state claiming that the negative factor is unconstitutional. Plaintiffs argued that when voters approved Amendment 23 in 2000, the clear intent of the amendment was to increase total program funding annually, regardless of other state needs. By reducing total funding, plaintiffs argued that the negative factor de facto reduces base per-pupil funding, which is required to increase annually. The state countered that the legislature has fully complied with Amendment 23 by increasing the base per-pupil funding amount, and that a plain language reading of the amendment requires only this annual increase to the statewide base amount, *but does not require an increase in the total program funding for K-12 public schools.*

In November 2014, the trial courts denied a motion to dismiss the lawsuit and allowed the case to proceed. In January 2015, the state appealed, asking the Colorado Supreme Court to dismiss the case. In September 2015, that court voted 4 to 3 to uphold the state's use of the negative factor, agreeing that the legislature's annual increases to the base per-pupil spending amount meet the constitutional requirements of Amendment 23[2].

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[1] Data on school district mill levy overrides are available from the Colorado Department of Education website:
http://www.cde.state.co.us/cdefinance/sfmilllevy

[2] *Dwyer v. State,* 15SA22 (Colo. 2015).