



# RURAL KIDS COUNT REPORT

## ADDRESSING RURAL SCHOOL EQUITY

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Minnesota's school funding formula is based on adequacy and equity in funding. MREA analyzed school funding for districts in rural areas compared to those in urban areas in Minnesota to assess how the funding is meeting the needs of all students.

#### KEY FINDING >>

Minnesota's rural schools of all sizes trail behind the state's urban schools in per student funding.

Minnesota's 280 non-metro school districts educate about 394,000 students daily, representing about 45 percent of the state's students.

The equity gap widens for the state's smaller school districts due to the intrinsic inefficiencies due to smaller class sizes and the cost of providing secondary electives to a smaller group of students. This widening gap starts with schools with about 1,500 students and magnifies significantly for schools with fewer than 750 students. Minnesota has 131 school district that have 750 or fewer students. These districts serve a combined 53,000 students, the equivalent of one of the largest districts in the state.

### KEY FINDINGS

- **Wide metro-rural divide in school funding per pupil.**  
>> The 15 school districts in the central cities and inner ring suburbs receive nearly \$1,400 more per pupil than the average of the state's other four tiers.
- **Two funding sources account for one of the largest gaps.**  
>> Nearly 40 percent of rural school districts in Minnesota receive \$724 or less per Adjusted Pupil Unit (APU) from of Local Optional Revenue (LOR) and Operating Referendum. That's nearly half the state average of \$1,303 per APU.

### KEY STRATEGIES

In this report, MREA identifies what's driving the funding divide and what can be done to ensure all students in Minnesota receive support – no matter where they live and attend school. MREA offers key strategies for state leaders to consider and shares the impact of each.

- >> Foundation And Incentive Revenue (FAIR)
- >> Enhanced Local Optional Revenue (E-LOR)
- >> Increased Tier III Equalization
- >> Fairer State Share for Facilities: Ag2School and Restored Debt Service Equalization



## WHERE'S THE GAP?

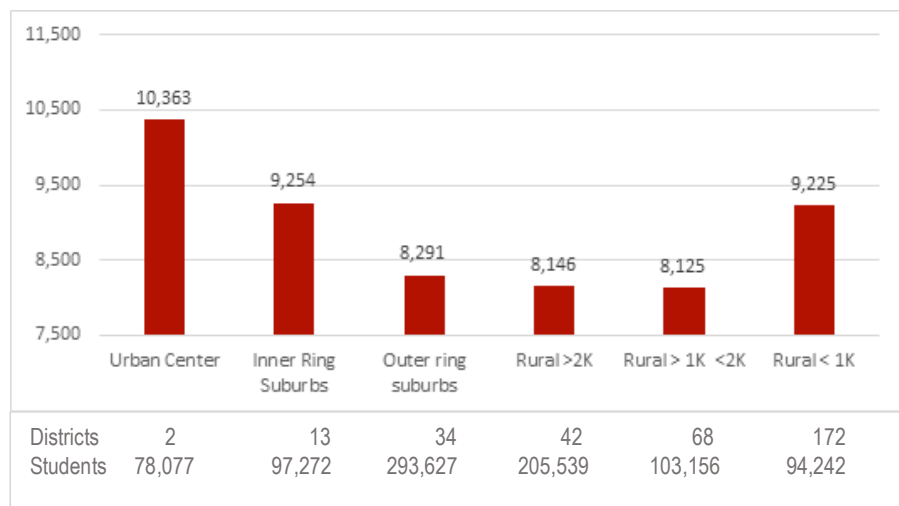
MREA's analysis of school funding in Minnesota found inequity based on the location and wealth of the school district:

- **Location:** Metro school districts receive more funding than those in Greater Minnesota. (Figure 1)
- **Wealth:** School districts with greater property wealth and higher household incomes, generally in the metro, receive significantly more operating referendum revenue than rural districts. (Figure 2)

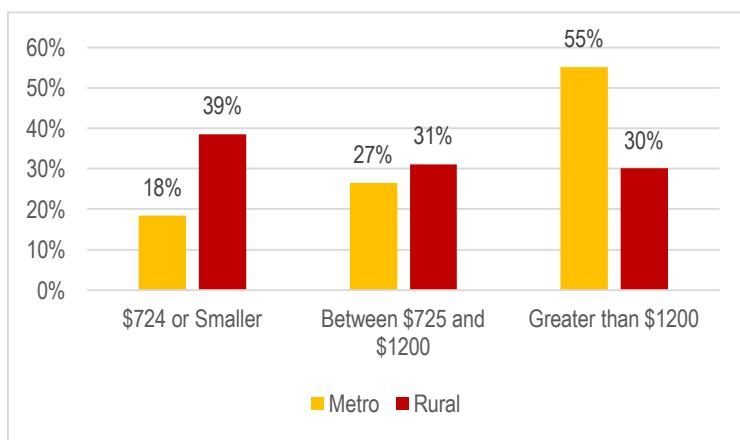
**Figure 1. TOTAL GENERAL FUND REVENUE BY MDE TIERS**

### KEY FINDING >>

The 15 school districts in the central cities and inner ring suburbs receive nearly \$1,400 more per pupil than the average of the other four tiers, a 16% difference.



**Figure 2. LOR AND OPERATING REFERENDUM REVENUES PER APU (by MDE school district regions)**



One of the largest metro-rural gaps is in the total dollars received from Local Optional Revenue (LOR) and Operating Referendum. While the average revenue of these two sources is \$1,303 per Adjusted Pupil Unit (APU), nearly 40 percent of rural districts receive \$724 or less revenue per APU. Ninety public school districts receive \$724 — the revenue school boards can enact for their students — while 55 percent of metro districts have voter approval and board approval for greater than \$1,200 per APU.



## ADDRESSING THE GAP

### STRATEGY 1 >> Foundation And Incentive Revenue (FAIR)

Where students attend a public school currently matters in Minnesota. Rural schools receive far less funding per pupil than their metro area counterparts. Yet the standards and expectations are the same. Minnesota wants all students to succeed. A new Foundation And Incentive Revenue (FAIR) can help achieve that. [Learn more and view impact by school district at MREAVoice.org/FAIR](https://mreavoice.org/FAIR)

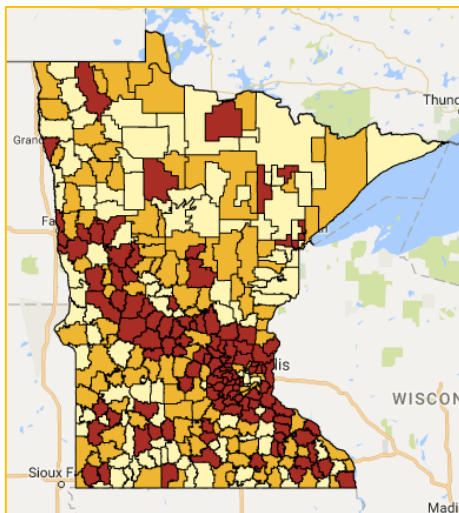
**HOW IT WORKS:** Every school district starts with \$200,000. This is then multiplied by the ratio of the district's three-year rolling average of 8<sup>th</sup> grade MCA reading and math scores divided by the state's three-year average. The result is a median revenue of \$184,000 per district, and a median of \$190 per ADM.

The three-year average provides a balance between stability due to student differences in smaller classes and the ability of schools to positively affect student achievement.

**Figure 3. IMPACT OF FAIR ON GAP BY TIER**

Tier (Region)	Region Description	FAIR Avg. (Per APU)	Closing the Gap
1	Urban Center	\$4	
2	Inner Ring Suburbs	\$27	0.7%
3	Outer ring suburbs	\$28	1.1%
4	Rural > 2,000	\$49	1.4%
5	Rural 1,001-1,999	\$136	2.4%
6	Rural < 1,000	\$317	4.0%

**Figure 4. FAIR FUNDING BY DISTRICT**



- Below 8<sup>th</sup> Grade Proficiency
- Near Median 8<sup>th</sup> Grade Proficiency
- Above 8<sup>th</sup> Grade Proficiency

**WHAT'S THE COST:** FAIR costs about \$60 million per year, but only a dozen rural districts receive less than \$60 per pupil, or 1 percent on per pupil funding. All other 150+ rural districts receive more up to a maximum of \$1,000 per APU.

**WHAT'S THE IMPACT:** FAIR addresses the equity needs of small schools and closes the adequacy funding gap for all tiers, as shown in Figure 3. In addition to delivering more equitable funding to school districts across the state, FAIR also rewards school districts for student achievement, as illustrated on the next page.



## ADDRESSING THE GAP

### STRATEGY 1 >> FAIR: A Student Achievement Bonus

In addition to narrowing the funding gap between rural and metro schools, FAIR aims to reward schools that are closing the achievement gap and getting better results for students in Minnesota.

**WEALTH & ACHIEVEMENT:** A MREA analysis shows a clear relationship between wealth and achievement when state's districts are split in thirds by FRE percentages and MCA 8<sup>th</sup> grade proficiency. The lowest FRE schools align with the highest MCA scores while the highest third of FRE schools have the lowest MCA scores. Schools that are in the middle for FRE tend to be in the middle of MCA scores.

#### DEFYING THE PATTERN >>

Six rural districts with the highest FRE percentages achieved the highest 8<sup>th</sup> grade MCA proficiency.



Another 63 rural districts' MCA scores are in the next highest third than expected given their FRE percentage, as shown in the chart below. **These districts defying the pattern represent 25 percent of rural districts.**

**Figure 5. 8TH GRADE MCA SCORES AND FREE AND REDUCED LUNCH (FRE)**

	Rural School Districts	Percent Rural Districts	Metro School Districts	Percent Metro Districts	State Total	State Percentages
<b>Significantly Above Expectations</b>	6	2%	0	0%	6	2%
<b>Above Expectations</b>	63	23%	6	10%	69	21%
<b>Meeting Expectations</b>	141	52%	50	85%	191	58%
<b>Below Expectations</b>	54	20%	1	2%	55	17%
<b>Significantly Below Expectations</b>	9	3%	2	3%	11	3%
<b>Total</b>	273	100%	59	100%	332	100%



## ADDRESSING THE GAP

### STRATEGY 2 >> Enhanced Local Optional Revenue (E-LOR)

**HOW IT WORKS:** Enhanced Local Optional Revenue (E-LOR) would increase the equalization factors and LOR by \$226 to \$650 per Adjusted Pupil Unit (APU) over a three-year period without any referendum subtraction. When equalization is increased proportionately, the first year (Pay '18, FY '19) net statewide levies can remain level—no increase. Levy increases in FY '20 and '21 could be moderated with an increase in the equalization factors in FY '21, as modeled in Figure 7.

**WHAT'S THE COST:** E-LOR would require an estimated \$59.5 million investment in this biennium and an estimated \$75 million in the 20-21 biennium, based on FY '18 Referendum Market Value (RMV) and RPU. This analysis is an estimate and does not factor in growth in RMV, RPU, nor future voter-approved operating referendums.

**WHAT'S THE IMPACT:** E-LOR with sufficient equalization to make the statewide impact neutral in Pay '18, FY '19 would reduce LOR and Operating Referendum property taxes in 246 districts, representing 74 percent of Minnesota's school districts, while increasing revenue in all districts. E-LOR closes the adequacy gap because \$226 is 31 percent of \$724, but only 17 percent of the average \$1,303, and it is not linked to other formulas. The estimated results can be seen in Figures 6 and 7.

**Figure 6.** E-LOR EFFECT ON CLOSING THE ADEQUACY GAP  
Total General Revenue Over 3 Years

Tiers	Region Description	E-LOR	Closing the Gap
1	Urban Center	\$226	
2	Inner Ring Suburbs	\$226	0.4%
3	Outer ring suburbs	\$226	0.8%
4	Rural > 2,000	\$226	0.9%
5	Rural 1,001-1,999	\$226	0.9%
6	Rural < 1,000	\$226	0.4%

**Figure 7.** E-LOR ANNUAL EFFECTS (Estimate based on 100 percent participation)

Fiscal Year	LOR Increase	LOR	RMV/RPU	Equalization Factor			Annual Revenue Increase	Annual State Aid Increase	Annual Levy Change
				Tier 1	Tier 2	Tier 3			
2018		424	419,652	880,000	510,000	290,000			
2019	75	499	438,677	980,000	590,000	325,000	66,040,710	66,109,079	-68,368
2020	75	574	438,677	980,000	600,000	325,000	65,496,976	18,891,461	46,605,515
2021	76	650	438,667	1,100,000	610,000	330,000	66,370,269	36,206,345	20,163,923



## ADDRESSING THE GAP

### STRATEGY 3 >> Increased Tier III Equalization

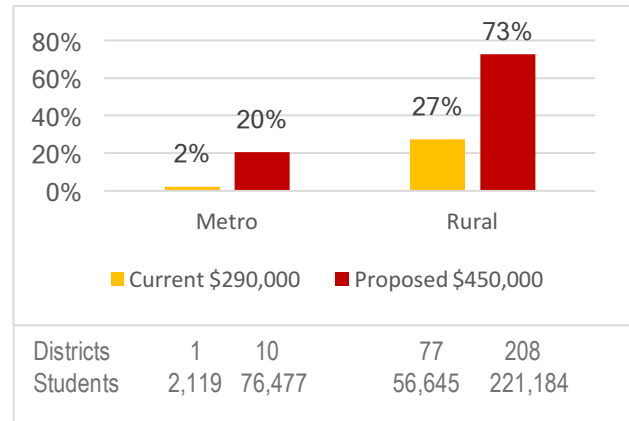
#### HOW IT WORKS:

**Increased equalization** for rural and property poor school districts would be most effective with a significant increase to the Tier III equalization factor to \$450,000 RMV/RPU.

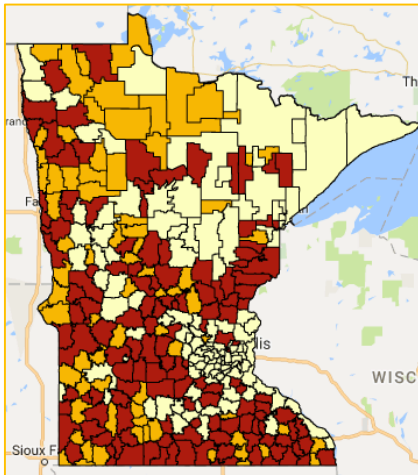
**A community option** for districts below 1,000 APU would be to remove their referendum cap, not just for those receiving sparsity aid.

**WHAT'S THE COST:** Increased Tier III Equalization would cost an estimated \$3 million for the 2018-19 biennium for existing referendums.

**Figure 8. DISTRICTS ELIGIBLE FOR INCREASED TIER III EQUALIZATION**



**Figure 9. CHANGE IN FUNDING BY SCHOOL DISTRICT**



#### WHAT'S THE IMPACT:

**Increased equalization** would make an estimated 153 more rural districts eligible for Tier III aid for referendum amounts over \$760 per pupil, due to lower referendum market values per pupil. In districts under 1,000 students where a referendum can make the difference between having a district remain open and viable or consolidate or close, an additional 90 districts would be eligible for Tier III aid for a total of 136 districts, or 79 percent of the 172 districts.

**The Community Option** would double the number of school districts without a per-pupil cap from 91 receiving sparsity aid to all 172 below 1,000 APU.

#### Current and MREA Proposed Tier III Operating Referendum Aid Eligibility

- 0.00 to 290,000.00 School Districts currently eligible for Tier III Aid: RMV/RPU < \$290,000
- 290,000.01 to 450,000.00 School Districts proposed to be eligible for Tier III Aid: RMV/RPU < \$450,000
- 450,000.01 to 1,590,000.00 Other MN School Districts: RMV/RPU > \$450,000



## ADDRESSING THE GAP

### STRATEGY 4 >> Fairer State Share for Facilities

Local taxpayers contribute 97-100 percent to build and remodel educational facilities. The state contributes at most 3 percent through Debt Service Equalization (DSE), which supports only 44 school districts and leaves the remaining 288 districts 100 percent dependent on local tax support for their facilities. The state share of debt service declined from 11.3 percent in 1995 to 3.1 percent in 2015. In many of the state's rural districts, an unfair portion has been placed on farmers with one-third of the districts having half of their net tax property wealth in ag land. About 20 percent of districts have at least three-fourths in ag land.

#### HOW IT WORKS:

**Ag2School** would offset this with a 40 percent credit on the taxes paid on farmland for school bonds.

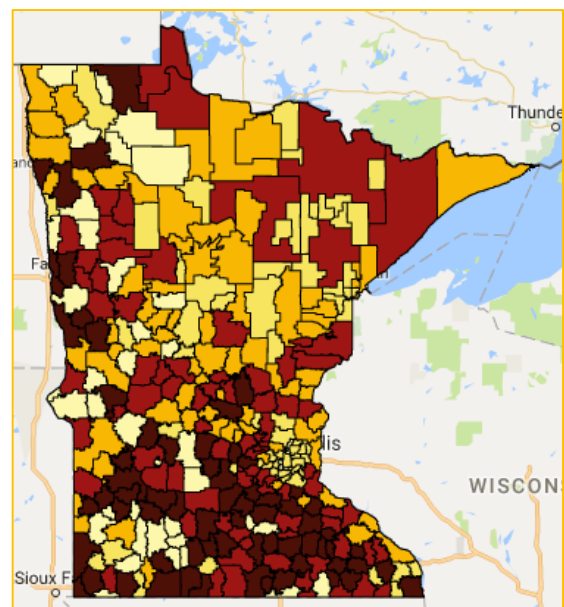
**Restored Debt Service Equalization (DSE)** would reduce the threshold from 15 percent of Adjusted Net Tax Capacity (ANTC) to 12.5 percent. The equalization system would be replaced with one tier at 100 percent of average modified ANTC/APU. MREA estimates it to be \$7,720 for FY '20. This is recommended by the School Facilities Working Group, but with 50 percent ag land values used for equalization purposes (as is done with LTfM).

#### WHAT'S THE COST:

**Ag2School** would provide an estimated \$40 million in tax relief for farmers in 2018.

**Restored DSE** would provide \$49.6 million in tax relief.

**Figure 10. AG2SCHOOL IMPACT BY SCHOOL DISTRICT**



**Ag2School 40% Ag Credit Tax Aggregate Ag and Timber Tax Relief per School District**

0.00 to 0.01	Zero due to no bonded school debt or no Ag or Timber land
0.02 to 34,999.99	Less than \$35,000
35,000.00 to 99,999.99	Between \$35,000 and \$100,000
100,000.00 to 224,999.99	Between \$100,000 and \$225,000
225,000.00 to 699,999.99	Greater than \$225,000

#### WHAT'S THE IMPACT:

**Ag2School** would help create a Fairer State Share for farmers in 284 school districts and help address the state's school facility fallout.

**Restored DSE** would provide tax relief immediately in 109 districts across Minnesota. Taxpayers in another 74 school districts would be eligible for state aid should voters approve a school bond that exceeds the threshold for state aid. This would restore DSE to 9.4 percent of all voter approved school debt payments.





## OTHER STRATEGIES CONSIDERED

### Expanded Small Schools Revenue (ESSR)

**HOW IT WORKS:** Expanding Small School Revenue (ESSR) is an alternative to the Foundation And Incentive Revenue (FAIR). It would adjust the current SSR formula by starting the formula for school districts with fewer than 1,500 students and flattening the curve for school districts with fewer than 750 students.

**WHAT'S THE COST:** ESSR does have an advantage in investment costs. The annual projected annual investment cost is \$29.8 million for a biennial investment of \$56.6 million.

**WHAT'S THE IMPACT:** While ESSR achieves the goals of FAIR for the smallest of school districts, it does not close the adequacy gap for other tiers like FAIR, as shown in Figure 11.

**Figure 11. IMPACT OF ESSR ON GAP BY TIER**

Tiers	Region Description	Targeted SSR	Closing the Gap
1	Urban Center	\$0	
2	Inner Ring Suburbs	\$0	0.0%
3	Outer ring suburbs	\$1.23	0.0%
4	Rural > 2,000	\$0.83	0.0%
5	Rural 1,001-1,999	\$61.17	0.7%
6	Rural < 1,000	\$271.74	3.1%

### Fully Fund Special Education Cross Subsidy

**HOW IT WORKS:** The total 2018-19 special education cross subsidy is an estimated \$1.4 billion despite a formula driven biennial over biennial increase in special education funding of \$292 million, according to MDE. The majority of special education costs are in the metro region (Figure 12).

**WHAT'S THE COST:** For every dollar spent to reduce the special education cross subsidy, 64 cents go to the metro regions and 36 cents go to rural Minnesota. Rural districts have both lower per APU cross subsidies and fewer students, leading to less cross subsidy dollars.

**Figure 12. SPECIAL EDUCATION CROSS SUBSIDY BY MDE**

MDE Regions	Sped Cross Subsidy per APU	Total Annual Cross Subsidy
Metro Regions	\$883	\$453.8 million
Rural Regions	\$629	\$251.6 million

**WHAT'S THE IMPACT:** The Basic Formula needs to increase 2 percent per year just to maintain the same ratio of cross subsidy to formula at approximately 13.3 percent. If the '18 and '19 formula increase were to be 1 percent, the FY '19 cross subsidy jumps to 13.7 percent. Conversely an increase in the formula of 3 percent a year would reduce the cross subsidy to 13.2 percent. Increasing the Basic Formula both addresses the special education cross subsidy and rural school equity, because in rural districts more of the formula goes to the standard classroom due to lower cross subsidies.



## NEXT STEPS

### SUPPORTING ALL MINNESOTA STUDENTS

Ensuring all students receive a quality education across Minnesota can be made possible through a combined education funding and tax relief strategy. These strategies, when coupled with a sufficient increase in the formula to cover the operating costs of a high-quality education, will be a major step forward to addressing rural school equity.

These strategies address both the operating costs of schools and the needed facilities to educate youth. Only one of these strategies (FAIR) is straight state aid. All other parts require local community participation. This encourages close connections between schools and their communities.

#### RURAL KIDS COUNT — E-12 FUNDING —Equity for Rural Students

'18-19 Biennial  
Estimate (millions)

Foundation And Incentive Revenue (FAIR)	\$114.0
2.0% and 2.0% Formula Increase	\$371.0
<b>Total Estimated State Education Aid</b>	<b>\$485.0</b>

#### RURAL KIDS COUNT — TAX EQUITY —Equity for Rural Taxpayers & Families

'18-19 Biennial  
Estimate (millions)

Ag2School 40% Ag and Timber Credit	\$36.9
Enhanced Local Optional Revenue (E-LOR)	\$59.5
Restored Debt Service Equalization (DSE)	\$44.7
Increased Tier III Equalization	\$3.0
<b>Total Estimated Property Tax Equalization</b>	<b>\$144.1</b>

