

Basic Aid

Income Research Paper



CBO Mentor Project
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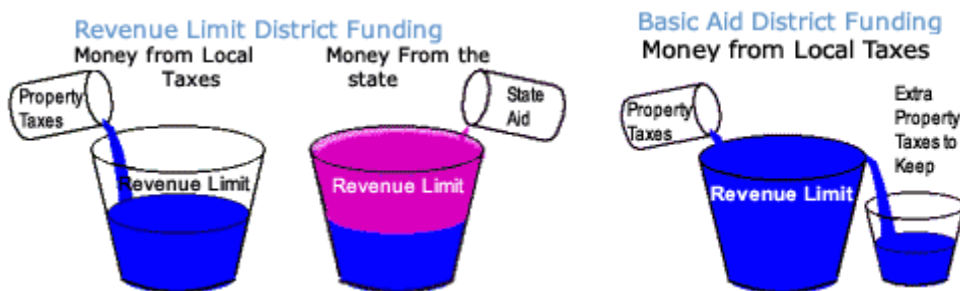
Executive Summary

Property taxes in the state of California have been the subject of controversy for as long as the state has assessed taxes. Before Proposition 13 passed in 1978, property taxes could increase dramatically from year to year based on the assessed value of the home. Since the passage of Proposition 13, a couple of things have happened. The property tax rate was set at a 1% cap. This means that the amount in property taxes paid by a homeowner is based on 1% of the assessed value of your home. The assessed value of homes can increase based on the Consumer Price Index (CPI) by no more than 2% per year. If a transfer of ownership takes place or improvements are made, the property is subject to a reassessment at the current market value. The newly assessed value will then increase on a yearly basis not to exceed 2% per year.

Public school districts receive most of their funding from local property taxes. State and federal sources, as well as a variety of other local revenues make up the rest. The amount of general purpose funding a school district receives per student (using ADA—Average Daily Attendance) is called its "revenue limit." It is a combination of local property taxes and state taxes. Each of the nearly 1,000 school districts in California has its own revenue limit, based on its type (elementary, high, or unified), size (small or large), historical spending patterns, and a multitude of other variables which, together, make for a complicated and lengthy formula.

State and local property taxes are combined to make up a district's revenue limit funding. A simple analogy can help illustrate this. Imagine a bucket. Each district has a different-sized bucket, representing its individualized revenue limit. Revenues raised through local property taxes are dumped into the district's bucket, and if the bucket is not filled all the way, the state tops it off with state tax revenues.

If the bucket is completely filled by local property tax revenues, the state has no need to "top off" the bucket. If the bucket overflows with local property taxes, the district gets to keep the overage. Districts whose buckets are filled by local property taxes are called "basic aid" or "excess revenue" districts.



The role of the CBO is critical in a basic aid district. The CBO will need to accurately project property tax revenues, and constantly monitor these revenues in relation to tax estimates given by County Auditors. The following report will explain how differences in estimates vs. actual receipts have affected one particular district in California, as well as advise a CBO of other adverse affects of this unique model of funding.

How does a District become Basic Aid?

Based on local property tax revenues, each year there have been approximately 60 to 80 "basic aid" districts out of a total of almost 1,000 districts. Because local property tax revenues and enrollments fluctuate from year to year, some districts are basic aid one year but not the next. At the time of the second principal apportionment (which is made in June), the California Department of Education officially certifies which districts are basic aid for the school year that is ending.

In general, there are three characteristics that can lead to a school district being basic aid. A school district can be basic aid as a result of having a very low revenue limit calculation and, thus, it is easy for property tax income to exceed the low state revenue limit threshold. A district can be basic aid as a result of a decline in enrollment and moderate growth in district property tax income. Or, a district can be basic aid as a consequence of high property values. The Vallecito Union School District is basic aid due to both a decline in enrollment, and property tax values that have increased significantly in recent years.

Vallecito Union School District is located in Calaveras County, situated in the beautiful Sierra Foothills. Most of the area consists of mountains, canyons, and heavily forested groves. The area is rich in history from the discovery of gold, through the period of the lumber industry, and is now a key recreational and retirement community. The District is comprised of two K-5 schools and one 6-8 middle school. The District also has a Home School Academy located on the Albert Michelson Elementary School campus in Murphys, and a Community Day School located on the Hazel Fischer School campus in Arnold. Avery Middle School is located in Avery.



This is Gold Country



The District became "basic aid" during the 2005-2006 fiscal year when its property tax revenues exceeded the revenue limit calculation by a mere \$1,827.17. Although final taxes have not been posted for the 2006-2007 tax year, the latest estimate from the County Auditor Controller appears to be accurate and therefore the District expects to receive \$456,101 in excess taxes over the revenue limit calculation.

	2005-06	Projected 2006-07
Prior year base revenue limit	\$4,799.28	\$5,001.28
Cost of Living Adjustment	\$202.00	\$295.00
Equalization aid	0	\$12.96
Revenue limit before deficit	\$5,001.28	\$5,309.24
Deficit	\$(42.81)	0
Current year funded revenue limit	\$4,958.47	\$5,309.24
Revenue limit ADA	901.16	874.96
Calculated revenue limit	\$4,468,374.83	\$4,645,372.63
Total gross taxes before charter deduction	\$4,502,413	\$5,136,474
Subtract charter tax	\$(32,166)	\$(35,000)
Total net local taxes	\$4,470,247	\$5,101,474
Taxes received more/(less) than revenue limit funding	\$1,872.17	\$456,101

While the current year taxes are coming in according to the estimate that was given by the Auditor in November 2006, there have been prior years where the estimate was significantly different than what the District actually ended up receiving at year end. This being said, it is very important that property tax revenues are budgeted conservatively.

Each year in November, the Auditor-Controller prepares and provides to the County Office of Education, an estimate of revenues for the fiscal year per Ed. Code 41760.2. This J29-B & J29-C is the first look at what a district might receive in tax receipts for the year. Since the district's budget has already been adopted with an educated guess of what local revenues will be, this document is the most important piece of information that a CBO in a basic aid district has been waiting for. With the term "estimate" clearly written upon the document, it is vitally important the information is used as such. Property taxes are based on the assessed value of land, structures, timber, etc. as of a lien date of January 1st each year. Basic aid districts do not receive supplemental taxes that are assessed for change in ownership, or new construction added to an existing structure, and therefore they only receive lien date taxes. Therefore, one would assume that the "estimate" should be fairly accurate. However, that might not necessarily be the case.

Systems/Methodology of Projecting Tax Revenue

During 2005-06, the County Auditor's initial tax estimates for Vallecito Union School District showed an approximate 10% increase over 2004-05. At the end of the 2005-06 fiscal year, the local taxes received were only a 5% increase due to various issues, including an error made by the auditor's office. Using the initial 10% estimate in 2005-06 could have been disastrous if the entire 10% had been spent by the District.

The following compares the initial tax estimates from the auditor's office to the amount the district received at year-end.

Fiscal Year	Auditor's Estimate for Fiscal Year	Auditor's Actual Tax Disbursement at end of Fiscal Year	Difference between the Estimate and the Actual Disbursement	Percent Change from the Estimate to the Actual
2001-02	\$3,707,534	\$3,931,513	+\$223,979	+6.04%
2002-03	\$4,087,973	\$4,274,287	+\$186,314	+4.56%
2003-04	\$4,554,561	\$4,404,856	\$(149,705)	(3.29)%
2004-05	\$4,567,782	\$4,289,753	\$(278,029)	(6.09)%
2005-06	\$4,821,751	\$4,502,413	\$(319,338)	(6.62)%
2006-07	\$5,140,242	Unknown	Unknown	Unknown

Breaking out the 2005-06 year even further, the tax estimates received from the auditor's office were as follows:

1st apportionment P1 estimate in November 2005: \$4,821,751
 2nd apportionment P2 estimate in April 2006: \$4,681,180

The actual amount received in August 2006 was \$4,502,413. Thus, even between the second apportionment in April and the final in August, the amount decreased by \$178,767. This exemplifies how difficult it is to estimate taxes in a current year. The P2 estimate would probably be used to estimate taxes for 2006-07, as it should include 90% of total collections for any given year. In this case, if the district used the P2 estimate for purposes of budgeting for the next fiscal year, the tax revenue would be overestimated.

Estimates are just that: estimates. Tax rolls change constantly based on assessed values in the tax assessment area. No two districts are the same. The estimate that the county auditor's office provides is the actual tax roll value at the time of the estimate, but if any subsequent changes occur, such as a large parcel being rezoned and reassessed, or perhaps a major wildfire occurring, the amount would change. The 2005-06 change was attributable to an error that may or may not recur. Regardless, since basic aid status is so new to the district, caution must be exercised.

The county auditor's estimate for 2006-07 is \$5,140,242, a projected increase of \$637,829, or 14.167%, over 2005-06. Based on the above information and variances, the CBO had budgeted tax revenue growth to come in at 50% of the original estimate. When final taxes are posted in August of 2007, the 2006-07 budget will need to be adjusted as well as the newly adopted 2007/08 and multi-year projections.

The CBO Leadership Role

- Do your homework! Go back five or more years and review the secured and unsecured tax roll estimates. Look at the variances and develop a methodology of projection. Talk to your County Assessor often. Ask him to advise you of significant reductions in value or increases in assessments. Get close up and friendly with your Board of Realtors. They can give you an idea of increases or decreases in home sale trends. Consult with your county office. Get their stamp of approval for your projections. Consider having FCMAT review your methodology and calculations for validity. It is well worth having some backing from an expert, as well as a strong tool to use in negotiations. Spending a little bit of money up front could save you a considerable amount should you make a mistake over-projecting tax revenue. Keep on good terms with your Auditor-Controller. Taxes should come in according to the schedule that you develop with your county, if they don't, take it as a red flag and get on the phone!

Tax apportionments are received taxes as follows:

20% November

35% December

40% April

5% June

- While at the bargaining table, remember that you cannot give salary increases based on the estimate of revenues. Budget for and negotiate increases conservatively. You may wish to hold off on negotiations until August each year, when you get your final taxes. This way you can bargain with money that you already have. You also may wish to incorporate a "settle-up" clause into your salary formula that addresses additional dollars received over your budgeted revenue be paid out in a one-time bonus. This will keep your salaries competitive with neighboring communities, as well as your budget in line.
- Remember, property tax revenues are unpredictable and nobody has a crystal ball. It is absolutely key, that you communicate your method of projections to all of the stake-holders (parents, students, teachers, support staff, program people, and of course the Board). All of these folks depend on schools to educate our future generation as well as employ our current workforce. A CBO will need to be prepared to explain basic aid funding to all of the stakeholders.

- You don't want to underestimate or overestimate taxes so significantly that you lose your credibility. You also don't want to just pull a number out of your....hat. Your Superintendent and Board need to believe in and depend on your estimates.
- If you are barely on the edge of basic aid, watch you enrollment closely. Know how many kids it will take to put you out of basic aid. Increase your reserves to allow for a little bit of cushion should you "fall out". If your expenses are maxed-out, and you suddenly get 100 new kids, make sure that you have enough money to hire 3 teachers. Communicate this with you stake holders as well so that it doesn't appear that you are holding money away from the bargaining table.
- Watch your cash flow very carefully. Remember, you don't receive monthly apportionments of state aid. You will most likely be in a negative cash flow situation from August to October because your first taxes of the year won't be received until November. Look to internal borrowing between funds or participate in the Tax Revenue Anticipation Note (TRAN) to fill up your shortfalls.

In conclusion, you can see that Basic Aid is a unique and dicey funding model. For the most part, if you budget and negotiate wisely, it will allow you extra money for special programs, and you may not have to lay off staff that you would have had you been revenue limit funded in a declining in enrollment district. It's a good thing to have your bucket runneth over.



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