NEPC

NATIONAL EDUCATION POLICY CENTER

REVIEW OF *UNDERSTANDING ILLINOIS' BROKEN EDUCATION FUNDING SYSTEM*

Reviewed By

Amy Ellen Schwartz and Sarah A. Cordes

New York University

November 2013

Summary of Review

An October Illinois Policy Institute report argues that Illinois' education finance system is fundamentally flawed because it systematically favors a few specific areas within the state—namely Cook and the Collar Counties. It contends that state funding is inequitable because the formula for state aid uses capped property values in these counties and allows for exclusion of property wealth growth in certain areas. The report also points to the state's current method for allocating poverty grant aid, which tends to flow to the same set of districts. Based on these critiques, the report concludes that the Illinois education finance system should be turned over to parents, but it never explains what this means. In the end, the report does not present any convincing evidence that the current distribution of state aid is inequitable by any standard. It also does not present any evidence that parents would do a better job of allocating resources for student success, any evidence that student performance is harmed by the current finance system, or a clear policy prescription to "fix" the problem. Thus, the report's usefulness for evaluating the current education finance system in Illinois is limited.

Kevin Welner

Project Director

William Mathis

Managing Director

Erik Gunn

Managing Editor

National Education Policy Center

School of Education, University of Colorado
Boulder, CO 80309-0249
Telephone: (802) 383-0058

Email: NEPC@colorado.edu
http://nepc.colorado.edu

Publishing Director: Alex Molnar

GREAT LAKES CENTER
FOR EDUCATION RESEARCH & PRACTICE

This is one of a series of Think Twice think tank reviews made possible in part by funding from the Great Lakes Center for Education Research and Practice. It is also available at http://greatlakescenter.org.

Review of *Understanding Illinois' Broken Education Funding System*

Amy Ellen Schwartz and Sarah A. Cordes
New York University

I. Introduction

A recent report from the Illinois Policy Institute (IPI) argues that the state's school finance system is broken, favoring a few districts—Chicago, Cook County and the Collar Counties—at the expense of districts elsewhere in the state.[1] The authors' proposed solution is to turn spending decisions over to parents, who would then have the ability to individually determine where their education dollars are spent.

The report cites three main policies as contributing to this inequitable distribution of funds. The first is the Property Tax Extension Limitation Law (PTELL), which limits the annual growth in property tax bills in certain districts throughout the state. The second is the exclusion of property located in Tax Increment Finance (TIF) zones from the computation of district property values for the purposes of state aid calculations. Third is the change to a broader, more inclusive definition of "low-income" for the calculation of poverty grant aid. Each of these is explained below.

The report makes a legitimate claim that TIF financing carries consequences for school finance and, indeed, the exclusion of this property from state aid calculations is likely to affect the distribution of state aid. Similarly, limits on the growth of property tax bills from PTELL are likely to affect the amount and distribution of aid. Finally, the amount of state aid devoted to students in poverty has grown in recent years. That said, IPI does not provide any specific policy recommendations for how to reform the system or any empirical evidence that the current distribution of aid is inequitable.

II. Findings and Conclusions of the Report

The report sets the stage by documenting the growth in per student funding in Illinois since the passage of the Property Tax Extension Limitation Law (PTELL) in the mid-1990s. Particularly striking is the 148 percent increase in per pupil funding over the past 20 years. That said, only about 25 percent of education revenues come from state sources, compared to the national average of 44 percent from state revenues, ranking Illinois 50th in the share of education funding provided in 2010.[2]

The centerpiece of the report is a critique of the formula grant program and the poverty grant program by which Illinois' allocates General State Aid (GSA). In Illinois, the formula is designed to provide a minimum level of education spending—the Foundation Level—for each pupil in the state. Districts with property wealth below the level at which a 2.3% tax rate yields the Foundation Level of spending are provided aid from the state to make up the difference. Thus, the amount of state aid depends critically upon the district's measured property values.

The poverty grant program distributes funds to districts based on the number and concentration of low-income students. The concentration is calculated by the Department of Human Services as the district's 3-year "low-income" average divided by average daily attendance. State aid allocations increase with the school district concentration of poverty, that is, those districts with higher concentrations of poor students receive more dollars per pupil in poverty aid. Thus, the amount of state aid also depends critically upon the poverty counts.

The IPI report levels three critiques of school finance in Illinois: (1) the property tax extension law limit gives some districts unfair funding advantages, (2) when districts establish a tax increment financing zone, the state shares the burden (3) the more inclusive definition of poverty leads to higher poverty grant awards and does not account for districts' ability to pay.

Critique 1: The Property Tax Exemption Law Limit (PTELL) Gives Some Districts Unfair Funding Advantages

The PTELL was designed with two purposes in mind: first, to limit the growth in property tax bills in districts where property values and assessments are increasing faster than the rate of inflation, and second to provide property owners with protection from tax bills that increase due to the rapidly increasing market value of their property. This limit has been in effect for the "collar" counties[3] since 1991 and for Cook County since 1995. Other districts in the state can hold a referendum to become PTELL districts, and all districts subject to the limit can hold referenda to override the limit.[4] When calculating education aid in these districts, the state uses capped property tax values, rather than the actual property values.

According to the Institute, PTELL provides "subsidies" to certain districts because these capped property values are used in the calculation of the formula grant, rather than the (somewhat higher) *actual* property values the districts.[5] Further, the report argues that this policy disproportionately benefits Chicago and Cook counties, which receive larger "embedded subsidies" than other districts, at the expense of downstate counties.

Critique 2: When Districts Establish a TIF Zone, the State Shares the Burden

Tax increment finance zones (TIFs), are established by local governments to encourage economic growth in geographically circumscribed areas through improvements in infrastructure (or other public investments). The debt incurred to finance improvements is repaid through the tax revenues generated by the increases in property values occurring within the zone. Thus, revenue increases generated in TIF zones cannot be used to finance any other local public goods, such as education, until the debt has been repaid and the TIF zone has been terminated.

Because the increase in property values for properties located in TIF zones is excluded from state aid calculations, they are allocated down higher levels of general state aid. Furthermore, the additional funds tend to flow to a small number of districts - specifically, districts located in Cook County and the collar counties.

Critique 3: More Expansive Definition of Poverty Leads to Higher Poverty Grant Awards and Does Not Account for Districts' Ability to Pay

Finally, the report describes how changes in the way poor children are counted result in larger poverty grants for these same districts. Beginning in FY 2004, children living in households with income below 200 percent of the federal poverty line ($46,100 for a family of four) are counted as low-income. Prior to this, only those students with household incomes below 100 percent of the poverty line ($22,811 for a family of four) were counted. This change led to a dramatic increase in the number of students classified as "low-income" across the state, which the report implies was particularly dramatic in Cook and the collar counties. In addition to qualms about the overall increase in the count of low-income students, the report criticizes the structure of the poverty grant formula, which gives districts increasingly more funding per pupil as the poverty concentration increases and is "not distributed based on the demonstrable need of individual districts."

Recommendations

From this, the report argues that these general state aid "subsidies" need to be discontinued and the financial power for the education system needs to be turned over to the parents. It cites alternative schemes in Wisconsin and Indiana, but does not provide a concrete policy recommendation as to what this finance system should look like.

III. The Report's Rationale for Its Findings and Conclusions

Critique 1: Proper Tax Extension Law Limit (PTELL) Gives Some Districts Unfair Funding Advantages

The report argues that because PTELL districts are treated as having lower amounts of taxable property wealth than they truly have, the tax limitation provides these districts with an unfair advantage. This, the report argues, means that the state aid formula does not accurately portray PTELL districts' ability to pay.

Critique 2: When Districts Establish a TIF Zone, the State Ends up Sharing the Costs

Since the general state aid formula excludes the increase in property wealth in TIF districts, they get more aid than they would have if TIF gains were included. Thus, non-TIF districts subsidize TIF districts through higher levels of state aid.

Critique 3: The More Expansive Definition of Poverty Leads to Higher Poverty Grant Awards and Does Not Account for Districts' Ability to Pay

The report argues that the growth in the amount spent on the poverty grant (from $0.29 billion in FY 2000 to $1.77 billion in FY 2013) and growth in the poverty grant as a share of state aid to districts (from 10 to 37 percent) is due entirely to the change in the definition of low income in 2004. It also notes that Cook and the Collar counties experienced the most growth in their poverty grants during this time.

IV. The Report's Use of Research Literature

While the report cites a number of government-generated statistics, it is quite thin on relevant literature. For example, it fails to cite any of the extant literature on the effects of school finance on inter-district equity or student achievement.[6] Further, in order to make concrete recommendations about a more appropriate state aid system, the report should describe more efficient and equitable systems and also describe how Illinois compares to other states in terms of standard equity statistics.[7]

Additionally, the report includes no reference to the extensive research literature documenting the higher cost of educating poor students, nor any reference to the research exploring the weights used in categorical funding formulas in other states. Rather than addressing the wide literature on vertical equity, the authors simply claim that poverty grants were instituted because the "state believes low-income students require more resources to educate."[8]

Finally, the report details the drawbacks of TIF districts but neglects to discuss any of the reasons localities might create a TIF zone. In particular, it neglects to cite any of the extant literature on the effects of TIFs on economic development, property values, and spillovers into surrounding districts, etc., much of which finds, at most, modest changes in property values in TIF zones, casting doubt on the report's claim that the exclusions have dramatic effects on state aid distribution.[9]

V. Review of the Report's Methods

The methods used in this paper are entirely descriptive and focused on distributions, and trends in state spending. One major issue is that many of the graphics report distributions for a single year rather than showing how these distributions have changed over time. A cross-sectional analysis such as this provides no evidence about whether—or to what extent—policies such as PTELL and TIF exclusions have led to a fundamental *change* in the distribution of funds. Without any "pre-post" comparison data it is impossible to determine whether the distribution of spending is a function of actual property wealth, changes in demographics across the state, or the policies themselves. Thus, the report provides no direct evidence about its causal claims.

VI. Review of the Validity of the Findings and Conclusions

The conclusions do not flow from evidence.

Even taking all of the evidence at face value, none of it supports the report's conclusion that the education finance system in Illinois should be turned over to parents. No evidence presented in this report suggests that parents would do a better job of allocating resources for student success, nor is there any description of what exactly the authors intend. What "turning power over to the parents" actually means in terms of policy and logistics is not described. Do the authors propose to use a system of statewide weighted student funding where funding "follows" the student to whatever public school he or she attends, as proposed by the Fordham Institute?[10] Most proposals to "fund the child" rely upon weights that give additional funding for special education, poverty, English language learners and other cost factors. If so, what weights do they imagine using in that formula? Presumably the poverty weights would be smaller than those currently used in the poverty grant aid. How much smaller? Also, given that students will likely travel limited distances to school, how will the fundamentally change the distribution of poverty aid? Perhaps they have a voucher system in mind. Whatever the underlying preferences of the *authors*, no evidence is presented that Illinois *voters* prefer an alternative system, much less weighted student funding or vouchers in particular.

More generally, the IPI report provides no evidence of any real "flaws" in the current funding system, nor any evidence on trends in student performance or school finance equity or other indicators of problems in the education sector statewide.

The report provides no evidence from the research literature in support of its critiques of the PTELL, TIFs, and poverty measures.

Critique 1: The Property Tax Exemption Law Limit (PTELL) Gives Some Districts Unfair Funding Advantages

The PTELL property value exclusion does affect the distribution of state aid and some districts do, in fact, receive larger amounts of state aid than they would absent this law. Whether this means state aid is unfair, however, is unclear and the report provides no specific criteria for evaluating fairness.

Low tax bases mean that Downstate counties receive substantial state aid funding and in fact, receive significantly more such funding per pupil than either Cook or Collar counties. The only exception to this, as presented by the report, is the Chicago public school district, which receives only $400 per student more general state aid funding than Downstate districts. Thus, the report fails to demonstrate that Downstate districts are "harmed" by the property tax limitations.

At the same time, the report ignores any differences in state income and sales taxes paid by residents of PTELL and non-PTELL districts. Whether taxpayers in a district are net "winners" or "losers" in public education finance depends upon their income and sales taxes as well as property taxes and state aid. Since much of the state revenues derive from residents of Cook and the Collar counties, an equally (or more) compelling case might be made for larger aid payments to these districts in the interest of fairness.

Critique 2: When Districts Establish a TIF Zone, the State Ends up Sharing the Costs

The report's claims about TIF zones are not without merit. Excluding gains in property values in these zones undoubtedly translates into more aid in a given year. That said, at least some of the gains in property values are due to the TIFs, which were explicitly created with the intention of *increasing* property values. Thus, while districts with TIF zones receive more aid from the state than they would if the TIF exclusion were eliminated, the state may be providing little or no more aid than it would have in the absence of these zones.

The report's use of rhetoric in some ways masks the validity of its claims. For example, Table 10 is titled "Chicago hides nearly $30,000 in property value per student," which could more accurately be said, "Chicago allowed to exempt nearly $30,000 in property value per student." While the former is phrased in a way to ignite strong opinions, the latter is more likely to be read and believed by an objective audience.

A final shortcoming regarding the TIF exemption is that the report fails to present any evidence that the resulting distribution of state aid is inequitable by any standard. By providing a more comprehensive and objective presentation, the report's claims would be much more convincing and the points that the report makes would, ultimately, be strengthened.

Critique 3: More Expansive Definition of Poverty Leads to Higher Poverty Grant Awards and Does Not Account for Districts' Ability to Pay

Although it is clear that using the more inclusive threshold for household poverty will allocate more to some districts than they would have received with the more conservative definition, the magnitude and significance of the difference is unclear. If the "near poor" (included in the new measure) are concentrated in districts also serving high shares of the poor (counted in both the new and old), the change in poverty counts may have little effect on the overall distribution of poverty aid. The more inclusive definition of low-income may increase the level of funding, but have little effect on the relative share of aid received by each district.

Further, increases in poverty aid do not necessarily result from changing the definition of low-income, as state policymakers could enact offsetting changes in the aid programs to maintain the overall budget allocation.

IPI presents an incomplete view of the changing poverty grants, by focusing attention on the percentage change in poverty grants, rather than the absolute levels of funding. Thus, some of the large percentage growth in aid the report highlights reflects low initial aid more than large dollar increases in aid. In fact, in terms of absolute growth in aid, downstate districts are second only to Chicago.

Finally, the report's claim that the *poverty* grant should account for each district's ability to pay conflicts with both standard practice and empirical evidence.[11] While states generally distribute most state aid through programs that explicitly account for district ability to pay, state aid programs that expressly direct revenues based upon the representation of poor children are also almost universal. Such aid is provided in part because of the widely recognized higher cost of educating poor students and, in part, because districts with high shares of poor students may be disadvantaged in their ability to raise sufficient funds to offset this additional cost. Illinois' poverty grant program is not unusual in this regard.

VII. Usefulness of the Report for Guidance of Policy and Practice

While this report provides some good background on Illinois' General State Aid system and raises some legitimate concerns about the use of tax increment financing, its usefulness for evaluating education finance in Illinois is limited.

Most importantly, the empirical support for the report's critiques of the current system is weak and there is little in the way of concrete, specific policy objectives or proposals. Despite voicing concerns about the current distribution of state aid, it does not provide any clear and useful information about what the distribution of state aid should look like (according to some clear criteria) or what it *would* look like if the current policies were changed. Is the objection presented in the report to the level of funding or to the distribution? These are different concerns, with different solutions. While the report leads with the claim that that money is not being spent in a way that is "best" for the students, it never details what "best" for the student means. Without any explicit criterion, it is impossible to evaluate. In the end, the policy conclusions do not follow from the evidence presented. The report seems to argue that the distribution of funds across the state is unfair and from this conclude that the finance system should be turned over to parents. There is, however, no specific plan for what this might look like or evidence to back up the claim that parents would do a better job in determining how money should be spent.

Notes and References

1 Dabrowski, T., Dwyer, J., & Klingner, J. (2013). *Understanding Illinois' Broken Education Funding System: A Primer*. Chicago: Illinois Policy Institute. Retrieved October 9, 2013, from http://illinoispolicy.org/wp-content/files_mf/1380814767Ed_finance_1.pdf.

2 Snyder, T.D. & Dillow, S.A. (2012). *Digest of Education Statistics 2011* (NCES 2012-011). Washington, DC: National Center for Education Statistics, Institute of Education Sciences, U.S. Department of Education;

Corcoran, S.P., Cordes, S.A., & Schwartz, A.E. (Forthcoming). State education expenditures. In M. Rubin & Katherine Willoughby (eds.),*Sustaining the States: The Fiscal Viabiltiy of American State Governments*.

3 The Collar counties consist of DuPage, Kane, Lake, McHenry, and Will counties.

4 Illinois Department of Revenue (2013).Property tax extension limitation law. Springfield, IL: Author. Retrieved November 20, 2013, from http://tax.illinois.gov/localgovernment/PropertyTax/ptell.htm.

5 This subsidies point is somewhat semantic. One could also view these as "tax expenditures" because the state government is in essence deducting the additional local revenues that could be realized from increases in property values above the rate of inflation.

6 See, for example:

Card, D., & Payne, A. A. (2002). School finance reform, the distribution of school spending, and the distribution of student test scores. *Journal of Public Economics*, *83*(1), 49-82;

Corcoran, S. P., & Evans, W. N. (2008). Equity, adequacy, and the evolving state role in education finance. In H.F. Ladd & E.B. Fiske (eds.), *Handbook of Research in Education Finance and Policy*, 332-356. New York: Routledge;

Downes, T. A. (1992). Evaluating the impact of school finance reform on the provision of public education: The California case. *National Tax Journal*, *45*, 405-405;

Murray, S. E., Evans, W. N., & Schwab, R. M. (1998).Education-finance reform and the distribution of education resources. *American Economic Review*, 789-812.

7 See: Berne, R. & Steifel, L. (1984). *The Measurement of Equity in School Finance: Conceptual, Methodological, and Empirical Dimensions*. Baltimore, MD: Johns Hopkins University Press.

8 See for example:

Baker, B., &Duncombe, W. (2004).Balancing district needs and student needs: The role of economies of scale adjustments and pupil need weights in school finance formulas. *Journal of Education Finance*, 195-221;

Duncombe, W. D., Lukemeyer, A., & Yinger, J. (2003). Financing an adequate education: A case study of New York. *Developments in School Finance 2001-2002*, 129-153. Washington, DC: National Center for Education Statistics, Institute of Education Sciences, U.S. Department of Education;

Duncombe, W., &Yinger, J. (2005). How much more does a disadvantaged student cost? *Economics of Education Review*, *24* (5), 513-532.

9 This literature finds that cities with TIFs grow more slowly than cities without and that there are heterogeneous effects on both industrial property values *within* TIF zones and property values in surrounding areas. These effects depend on the mixture of property located in the TIF zones such that those zones containing mostly industrial properties see a decrease in property values in the zone itself as well as in the surrounding districts, and zones containing both industrial and residential properties leading to increases in property values in surrounding districts.

See for example:

Dye, R. F., & Merriman, D. F. (2000). The effects of tax increment financing on economic development. *Journal of Urban Economics*, *47*(2), 306-328;

Weber, R., Bhatta, S. D., & Merriman, D. (2003). Does tax increment financing raise urban industrial property values?. *Urban Studies*, *40*(10), 2001-2021;

Weber, R., Bhatta, S. D., & Merriman, D. (2007). Spillovers from tax increment financing districts: Implications for housing price appreciation. *Regional Science and Urban Economics*, *37*(2), 259-281.

10 Thomas, B. (2009). *Fund the Child: Tackling Inequity and Antiquity in School Finance*: Thomas B. Fordham Institute. Retrieved November 11, 2013 from http://www.edexcellence.net/sites/default/files/publication/pdfs/FundtheChild062706_7.pdf.

11 Duncombe, W., Ruggiero, J., & Yinger, J. (1996). *Alternative Approaches to Measuring the Cost of Education*. Center for Policy Research, Maxwell School of Citizenship and Public Affairs, Syracuse University.

DOCUMENT REVIEWED:	**Understanding Illinois' Broken Education Funding System: A Primer**
AUTHORS:	Ted Dabrowski, Josh Dwyer, and John Klingner
PUBLISHER/THINK TANK:	Illinois Policy Institute
DOCUMENT RELEASE DATE:	October 3, 2013
REVIEW DATE:	November 21, 2013
REVIEWERS:	Amy Ellen Schwartz & Sarah A. Cordes, New York University
E-MAIL ADDRESSES:	amy.schwartz@nyu.edu Sarah.cordes@nyu.edu
PHONE NUMBERS:	(212)998-7405 (Schwartz) (703)307-6425 (Cordes)

SUGGESTED CITATION:

Schwartz, A. E. & Cordes, S.C. (2013). *Review of "Understanding Illinois' Broken Education Funding System: A Primer"* Boulder, CO: National Education Policy Center. Retrieved [date] from http://nepc.colorado.edu/thinktank/review-illinois-funding.