



Legislative Research Commission

Understanding How Tax Provisions Interact With the SEEK Formula

Research Report No. 354

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Understanding How Tax Provisions Interact With the SEEK Formula

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Foreword

In December 2006, the Education Assessment and Accountability Review Subcommittee approved a research agenda for the Office of Education Accountability that included *Understanding How Tax Provisions Interact With the SEEK Formula*. The purpose of the report is to provide the General Assembly with a greater understanding of the interrelationships among tax provisions and the Support Education Excellence in Kentucky funding formula.

Office of Education Accountability staff would like to acknowledge the assistance of many individuals whose cooperation and expertise contributed to this report. The Division of Data Management was instrumental in providing volumes of historic tax rate data. Susan Goins, retired from the Department of Education's Division of School Finance, provided historical knowledge of the events that occurred in the early 1990s as well as her technical expertise in answering staff's many questions.

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Summary

This report reviews the property tax rate options available under statutes governing how school districts may raise local revenue to support their public school system. These statutes are KRS 160.470, which implements 1979 House Bill 44; and KRS 157.440, which implements 1990 House Bill 940, the education reform measure. Local boards of education are also authorized to levy permissive taxes under KRS 160.593. The impact of local property assessments on school district revenues and decisions made by local boards of education under the various tax provisions, in combination with funding provided through the Support Education Excellence in Kentucky (SEEK) formula, is also examined. The purpose of the overview is to provide the General Assembly with a greater understanding of the interrelationships among these tax provisions and SEEK.

Chapter 1 introduces the issues that are presented in this report and summarizes the major provisions of the Kentucky Education Reform Act.

Chapter 2 describes the process by which school districts set tax rates to support public education and provides an analysis of the rates historically levied by local boards of education. The chapter also provides an explanation of how the value of property is assessed and describes major changes in the evaluation of property from fiscal year 1997 to fiscal year 2008.

Chapter 3 discusses the process by which districts receive state education funding through the SEEK calculation. The chapter provides definitions and formulas for the components within the SEEK calculation.

Chapter 4 illustrates how local property assessment conditions and levied tax rate activity in a district are accounted for in the SEEK formula. The chapter, in particular, demonstrates how the formula accounts for local revenue and adjusts—upward or downward—the amount of districts' total state education funding.

Chapter 5 summarizes the policy implications of the previous sections. The chapter highlights the major issues involving taxing provisions and SEEK funding mechanisms—including interactions between taxes and SEEK—that impact the level of funding received by local school districts.

Chapter 1

Understanding How Tax Provisions Interact With the SEEK Formula

Background

This report reviews the property tax rate options available under KRS 160.470 and KRS 157.440. These statutes govern how school districts may raise local revenue to support their public school systems. Local boards of education are also authorized to levy permissive taxes under KRS 160.593.

This report reviews the property tax rate options available under statutes governing how school districts may raise local revenue to support their public school systems. These statutes are KRS 160.470 and KRS 157.440. KRS 160.470 implements House Bill 44, which was passed in the Extraordinary Session of 1979. KRS 157.440 implements House Bill 940, the 1990 education reform measure. Local boards of education are also authorized to levy permissive taxes under KRS 160.593. The impact of local property assessments on school district revenues and decisions made by local boards of education under the various tax provisions, in combination with funding provided through the Support Education Excellence in Kentucky (SEEK) formula, will also be examined. The purpose of the overview is to provide the General Assembly with a greater understanding of the interrelationships among these tax provisions and SEEK.

In the early years of Kentucky's education reform, some districts chose to increase their local tax effort under the provisions of 1990 House Bill 940 by raising property taxes. House Bill 44, from 1979, has allowed districts to maintain the higher property revenues.

Also reviewed in this report will be the impact of local decisions about when taxes were added or increased and how the timing of those decisions influenced local and state funding. In the early years of the education reform, some districts chose to increase their local tax effort under the provisions of HB 940 by raising property taxes. House Bill 44 has allowed districts to maintain the higher property revenues through its authorization of annual increases in tax revenues of up to 4 percent.

While a majority of school districts' state revenue comes from the Support Education Excellence in Kentucky (SEEK) funding formula established as part of the Kentucky Education Reform Act (KERA), most of school districts' local revenue comes from local taxes.

While a majority of school districts' state revenue comes from the SEEK funding formula established as part of the Kentucky Education Reform Act (KERA) of 1990, most of the school districts' local revenue comes from local taxes. Under KRS 160.470(9)(a), school districts are required to levy a minimum equivalent tax of 30 cents per \$100 of assessed property to participate in the SEEK program. SEEK funding is distributed on a per-pupil basis, and this basic funding level is known as the guaranteed base. Districts receive additional funds, or add-ons, for specially identified populations of students such as at-risk and exceptional students and for transportation. The SEEK guaranteed base plus any add-ons comprises the adjusted SEEK base.

School districts may increase their local tax effort above the minimum 30 cents up to 15 percent of the revenue generated through the adjusted SEEK base. This additional amount of locally raised tax revenue is known as Tier I funding. The state equalizes Tier I revenue at 150 percent of the statewide average per-pupil property tax assessment.

In addition, school districts may increase their local tax effort beyond Tier I up to 30 percent of the revenue generated through the adjusted SEEK base plus Tier I. These funds, known as Tier II funding, are subject to voter referendum and are not equalized by the state. Table 1.1 summarizes school district tax levels in support of education. As indicated in the table, districts also are required to levy a 5-cent tax per \$100 of assessed property to participate in the state program that supports school facility funding.

Table 1.1
School District Tax Levels in Support of Education

Local Tax Levels	Description
30 cents per \$100 of assessed property	Tax required to participate in SEEK
5 cents per \$100 of assessed property	Tax required to participate in FSPK
Tier I: 15 percent of SEEK base plus add-ons for specially identified populations of students, such as at-risk and exceptional students, and for transportation	Tier I is authorized but not required. It is equalized by the state at 150 percent of the statewide average per-pupil property tax assessment.
Tier II: 30 percent of SEEK base plus add-ons plus Tier I	Tier II is authorized but not required. It is not equalized.

Notes: SEEK is the Support Education Excellence in Kentucky program. FSPK is the Facilities Support Program of Kentucky. The SEEK base is the guaranteed amount of per-pupil funding established by the General Assembly for each biennium.

Source: Staff compilation.

The tax efforts made by school districts, including the required equivalent tax of 30 cents and the amounts levied for Tier I and Tier II, can be made through any combination of property taxes, motor vehicle taxes, and permissive taxes.

The tax efforts made by school districts, including the required equivalent tax of 30 cents and the amounts levied for Tier I and Tier II, can be made through any combination of property taxes, motor vehicle taxes, and permissive taxes. Since school districts' local tax effort consists of various types of taxes, the rates at which these revenue sources are taxed can vary across districts.

The pre-KERA provisions of 1979 HB 44 provide three possible levies: the Compensating Tax Rate; Subsection (1) Tax Rate; and 4 Percent Increase Tax Rate. A fourth option, the Tier I Property Tax Rate, is provided for under 1990 HB 940, the KERA authorization legislation. These tax options will be discussed in detail in Chapter 2.

The following are additional issues first identified in the Office of Education Accountability's *2005 School Finance Report* and discussed in more detail in this report (Commonwealth Legislative Office, 2005 22-23). These are factors affecting the distribution of education resources among school districts in Kentucky. The factors impact districts differently, allowing some to raise additional local revenue, while limiting the ability of others to do so.

Permissive taxes are levied under KRS 160.593 and generate substantially more revenue in some school districts than in others.

- Permissive taxes are levied under KRS 160.593 and consist of utility taxes, occupational taxes, and excise taxes. Prior to KERA, 93 districts levied a utility tax and 6 districts levied an occupational tax. In FY 1991, 57 districts adopted a utility tax and 2 districts adopted an occupational tax, for a total of 150 districts levying a utility tax and 8 districts levying an occupational tax. By adding these taxes, districts were able to increase their local tax effort without raising, or significantly raising, their property taxes in order to qualify for Tier I equalization. By FY 2007, 157 districts had levied a utility tax, and 8 districts continued to levy an occupational tax. (No district has levied an excise tax.) These taxes generate substantially more revenue in some school districts than in others.

In theory, under KERA, changes in local wealth should have no effect on total funds available to school districts. As districts collect more in local taxes, their state funds would be offset by an equal amount. However, as the following two bullet points illustrate, there are factors that depend upon local conditions and can result in varying impacts on district funds.

Holding all other variables constant in the SEEK formula, as total local property assessments increase, school districts with property tax rates above their maximum Tier I equivalent rates collect more in local taxes than is offset by decreases in state SEEK funds. In contrast, school districts with property tax rates lower than their maximum Tier I equivalent rates will not collect more in local taxes than the offset of their state SEEK funds.

- Holding all other variables constant in the SEEK formula, as the total local property assessments increase, districts' state SEEK funds are reduced. School districts with property tax rates above their maximum Tier I equivalent rates collect more in local property taxes than is offset by decreases in state SEEK funds. In contrast, school districts with property tax rates lower than their maximum Tier I equivalent rates will not collect more in local taxes than is offset by a reduction in their state SEEK funds. These unintended consequences may be mitigated or worsened by the mix of taxes the districts levy. For example, some districts increase local effort to qualify for Tier I funding by adding permissive taxes rather than by increasing their property tax rates. Permissive tax collections may or may not offset this net impact on revenue.

House Bill 44 limits the increase in property assessment tax receipts from one year to the next to 4 percent.

- House Bill 44 limits the increase in property assessment tax receipts from one year to the next to 4 percent. Per KRS 160.470 (3c), the 4 percent limitation applies to existing, real property only, which excludes new property. Districts' state SEEK calculations are based on their property assessments, rather than on revenue generated. In other words, the SEEK calculation does not factor in HB 44's limitation on local revenue generated from growth in districts' assessments from existing real estate property. Consequently, when school districts' *property assessments* from existing real estate property grow by more than 4 percent per year, but their *property tax collections* are limited to 4 percent growth, districts' state SEEK funds will decrease by more than the districts are allowed to collect in local taxes from this property.

There are also other factors that influence how much total revenue districts actually receive. For example, permissive taxes, new property, and motor vehicle taxes levied by districts may help to curb the impact of SEEK's use of property assessments rather than actual revenue collected. Since some districts impose permissive taxes and others do not, and the revenue generated from these taxes varies widely across districts, this offsetting mechanism is not uniform across the state.

Organization of the Report

Chapter 2 details the process by which school districts set tax rates to support public education and provides an analysis of the rates historically levied by local boards of education. Chapter 2 also presents an explanation of how the value of property is assessed and describes major changes in the evaluation of property from FY 1997 to FY 2008.

Chapter 3 discusses the process by which districts receive state education funding through the SEEK calculation. The chapter provides definitions and formulas for the components within the SEEK calculation.

Chapter 4 illustrates how local property assessment conditions and levied tax rate activity in a district are accounted for in the SEEK formula. The chapter, in particular, demonstrates how the formula accounts for local revenue and adjusts—upward or downward—the amount of districts' total state education funding.

Chapter 5 summarizes the policy implications of the previous sections. The chapter highlights the major issues involving taxing provisions and SEEK funding mechanisms—including interactions between taxes and SEEK—that impact the level of funding received by local school districts.

Chapter 2

School Taxes

Introduction

Chapter 2 details the process by which local boards of education set property tax rates to support education. Major changes in the evaluation of property from fiscal year 1997 to fiscal year 2008 are described. Also, an estimate of revenue foregone is provided.

Chapter 2 describes the process by which local boards of education set property tax rates to support education. This chapter discusses the major changes in the evaluation of property from FY 1997 to FY 2008. The chapter also provides an estimate of revenue foregone when school districts elected to levy tax rates lower than the maximum rates not subject to recall as certified to them by the Kentucky Department of Education (KDE).

Each year, KDE calculates four different property tax rates for each school district, pursuant to statutory and regulatory provisions governing the taxing authority of local boards of education. Local boards review these calculations and select the rate that will be used to collect school taxes. These property tax rates correspond to the pre-education reform provisions of 1979 HB 44, as well as to HB 940, the Kentucky Education Reform Act of 1990. KDE informs each school district of its options under the four tax rates by a process known as tax rate certification. Each local board of education considers the options available and selects its tax rate. The following analysis provides information on the various tax levies districts may impose and details the impact on district funding under the four tax rates. The process being described is KDE's interpretation and implementation of the tax statutes and regulations for fiscal years 1991 through 2007.

Authority To Levy Taxes To Support Education

Local boards of education are the "tax levying authority" for public schools under KRS 160.455.

Local boards of education are the "tax levying authority" for public schools under KRS 160.455. They are authorized to levy taxes on real estate property, personal property, and motor vehicles. A local board of education is also authorized to levy permissive taxes under KRS 160.593, which consist of utility taxes, occupational taxes, and excise taxes. Table 2.1 describes the nature of and statutory authority for these taxes. Taxing under all of these statutes is discretionary and can be used in any combination.

Table 2.1
Tax-levying Authority of Local Boards of Education

Type of Tax	Description	Statutory Authority
Real Estate	Land, buildings, and improvements thereon, including real property of public service corporations	KRS 160.470
Personal Property	Equipment or inventory used in the operation of a business, including personal property of public service corporations	KRS 160.470
Motor Vehicle	Motor vehicles and recreational boats owned by residents within the school district; if a boat is permanently docked in another school district, then the tax would be applicable in the other school district.	KRS 160.470
Permissive Taxes		KRS 160.593
Utility	A utility gross receipts license tax not to exceed 3 percent of the gross receipts derived from the sale of communications services; electric power; water; and natural, artificial, and mixed gas	KRS 160.613
Occupational	An occupational license tax, not to exceed 0.5% or 0.75% for counties with 300,000 or more residents, on salaries or wages of individuals for work done in a county and on the net profits of all businesses, professions, or occupations from activities conducted in a county	KRS 160.605
Excise	An excise tax not to exceed 20 percent on a county resident's state individual income tax liability	KRS 160.621

Sources: Commonwealth. Dept. of Ed. *Financial Management Manual* 4-7; Barlow. Nov. 7, 2007.

Determining the Value of Property in School Districts

The Kentucky Department of Revenue and the local property valuation administrators are responsible for reporting the assessed value of property subject to taxation by local boards of education. The certified property assessments are used in the SEEK calculation to reflect the district's local wealth.

The Kentucky Department of Revenue and the local property valuation administrators are responsible for reporting the assessed value of property subject to taxation by local boards of education. Each July, the Kentucky Department of Revenue begins certifying property assessments to KDE. The property assessment contains property valuations for real estate, personal property, public service real estate and personal property, and motor vehicles. The certified property assessments are used in the SEEK calculation to reflect the district's local wealth. KDE uses the property assessments and prior-year tax collections from districts' annual financial reports to calculate and certify four tax rates for real estate and personal property for each district to consider. These include three rates calculated under HB 44 as implemented in

KRS 160.470 and one rate under HB 940 as implemented in KRS 157.440.

Tables 2.2 and 2.3 contain an example of a tax rate certification that a school district receives from the Kentucky Department of Education (KDE).

This section of the report describes in detail the process of certification and selection of tax rates. Tables 2.2 and 2.3 contain an example of a tax rate certification that a school district receives from KDE. Throughout the tables, there are references to Appendix A, which contains the specific calculations that support each of the items on the tax rate certification.

Table 2.2
House Bill 44 Tax Rates

Kentucky Department of Education Real Estate and Personal Property Tax Calculation Report 1				
District 000 Sample County - School Year: 2006-2007				
The property tax rates shown below are calculated under the provisions of KRS 160.470 (House Bill 44). The hearing and recall requirements footnoted apply unless the rates are less than those allowed under KRS 157.440 (House Bill 940) shown on Report 2.				
CLASS OF PROPERTY - REAL ESTATE, TANGIBLE PERSONALTY, PUBLIC SERVICE COMPANIES, AND DISTILLED SPIRITS				
Item A		<u>Compensating*</u>	<u>Subsection (1)**</u>	<u>4% Increase***</u>
General Fund	Rate	38.7	48.3	40.2
Real Estate	Revenue	\$1,772,360.64	\$2,212,015.99	\$1,841,056.79
KRS 160.470		(See Appendix A, Table A.1) [†]	(See Table A.2) [†]	(See Table A.3) [†]
General Fund	Rate	44.3	48.3	44.3
Personal Property	Revenue	\$242,722.81	\$264,639.09	\$242,722.81
KRS 160.473			(See Appendix A, Table A.4) [†]	
Item D				
Maximum Tax Rate for Motor Vehicles: 56.3 (See Appendix A, Table A.5) [†]				
*No hearing required - no recall. KRS 160.470(2)				
**Hearing required if this rate exceeds the compensating rate; subject to recall if exceeds 4 percent. KRS 160.470(1)				
***Hearing, no recall. KRS 160.470(7)				
6.0 cents of the total property rate shown above is required to produce the 5-cent equivalent tax necessary for participation in the SFCC and FSPK programs. (See Appendix A, Table A. 6) [†]				
Note: 0.2 cents may be added to the above property rates to recover prior-year losses due to exonerations. KRS 134.590 (See Appendix A, A.7) [†]				

Notes: [†]References to appendices do not appear in the tax calculation document received by school districts. They are added here to refer readers to the appendices in this report that explain how these rates are derived. SFCC is the School Facilities Construction Commission. FSPK is the Facilities Support Program of Kentucky.

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

Table 2.3
House Bill 940 Tax Rate

Kentucky Department of Education Real Estate and Personal Property Tax Calculation Report 2			
District 000 Sample County - School Year: 2006-2007			
The property tax rates shown below are calculated under the provisions of KRS 157.440 (House Bill 940). These may be levied without hearing or recall. The equivalent rate shown is the maximum Tier I equivalent, or the 1989-90 equivalent, whichever is higher, plus the 5-cent growth district levy, equalized growth levy, and recallable nickel levy, if applicable.			
CLASS OF PROPERTY - REAL ESTATE, TANGIBLE PERSONALTY, PUBLIC SERVICE COMPANIES, AND DISTILLED SPIRITS			
Required Tax Rate for 45.70-Cent Equivalent Revenue* (See Appendix A, Table A.8) [†]			
Item E			
General Fund	Rate	30.4	
Real Estate	Revenue	\$1,392,241.95	
			(See Appendix A, Table A.8) [†]
General Fund	Rate	30.4	
Personal Property	Revenue	\$166,563.73	
Prior Year Motor Vehicle Tax Levy: 56.3			
Item E above may be used in place of Item A General Fund Tax Rate and Revenue Certification. If a higher motor vehicle rate is used, this property tax rate must be recalculated.			
*No hearing required - no recall. KRS 157.440(1)(a)			
6.0 cents of the total property rate shown above is required to produce the 5-cent equivalent tax necessary for participation in the SFCC and FSPK programs. (See Appendix A, Table A. 6) [†]			
Note: 0.2 cents may be added to the above property rates to recover prior-year losses due to exonerations. KRS 134.590 (See Appendix A, A.7) [†]			

Notes: [†]References to appendices do not appear in the tax calculation document received by school districts. They are added here to refer readers to the appendices in this report that explain how these rates are derived. SFCC is the School Facilities Construction Commission. FSPK is the Facilities Support Program of Kentucky.

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

House Bill 44 Tax Rates

House Bill 44 rates are solely dependent on property valuation and provide the following possible levies to school districts: the Compensating Tax Rate, Subsection (1) Tax Rate, and 4 Percent Increase Tax Rate.

House Bill 44 provides for the calculation of three tax rates. Unlike the HB 940 rate, which takes into account the mix of taxes levied by a district (real estate, personal property, motor vehicle, and permissive), the HB 44 rates are solely dependent on property valuation and provide the following possible levies to school

districts: the Compensating Tax Rate, Subsection (1) Tax Rate, and 4 Percent Increase Tax Rate. Each rate is calculated for real estate and personal property. The following definitions and descriptions of each of the rates are based on KDE's *Financial Management Manual* (4-5).

The Compensating Tax Rate is the rate that when applied to the current year's property assessment, excluding new property, produces an amount of revenue equal to that produced in the preceding year.

Compensating Tax Rate. The Compensating Tax Rate is the rate that when applied to the current year's property assessment, excluding new property, produces an amount of revenue equal to that produced in the preceding year. This rate may be levied without a public hearing and is not subject to the recall provisions of KRS 160.470(8)(a). As shown in Appendix A, Table A.1, there are two compensating tax rate calculations. The Compensating Tax Rate I calculation is based on real estate property, while the Compensating Tax Rate II calculation is based on both real estate and personal property. The higher rate produced by these two calculations is certified to the district.

The Subsection (1) Tax Rate, which refers to subsection (1) of KRS 160.470, is the rate that produces no more revenue than the previous year's maximum rate.

Subsection (1) Tax Rate. The Subsection (1) Tax Rate, which refers to subsection (1) of KRS 160.470, is the rate that produces no more revenue than the previous year's maximum rate. This rate is subject to the hearing and recall provisions in KRS 160.470(7)(8). As shown in Appendix A, Table A.2, the calculation is based on prior-year maximum revenue from both real estate and personal property. A school district may exceed the Subsection (1) Tax Rate with the approval of a majority of the qualified voters but may not levy a tax rate that would generate revenue in excess of the district's Tier II cap, which is equal to 30 percent of the adjusted SEEK base plus Tier I. The Tier II cap is discussed later in this chapter.

The 4 Percent Increase Tax Rate is the rate that produces 4 percent over the amount of revenue generated by the Compensating Tax Rate.

4 Percent Increase Tax Rate. The 4 Percent Increase Tax Rate is the rate that produces 4 percent over the amount of revenue generated by the Compensating Tax Rate. Prior to recent legislative actions, districts could not levy the 4 Percent Increase Tax Rate if it exceeded the Subsection (1) Tax Rate; however, KRS 160.470 (10) now removes this limitation.¹ The 4 Percent Increase Tax Rate is subject to the hearing provisions in KRS 160.470(7). As shown in Appendix A, Table A.3, the calculation is based on real estate property only.

¹In 2003, the General Assembly removed this limitation through budget language. In 2005, the General Assembly permanently removed this limitation as part of the tax modernization plan in HB 272.

Personal Property Tax Rates

To calculate a district's personal property tax rates, the Compensating, Subsection (1), and the 4 Percent Increase Tax Rates are separately applied to each district's current year real estate and personal property assessments. The resulting revenues are then compared to the previous year's revenue to determine the percentage increases in revenues for the current year. These calculations are shown in detail in Appendix A, Table A.4.

When the percent increase in personal property is higher than the percent increase in real estate property, the same tax rates are certified for both real estate and personal property. However, when the percent increase in real estate property is higher than personal property, KRS 160.473 allows an alternative rate to be calculated for personal property that will produce the same percent increase as that of real estate property, not to exceed the prior-year personal property rate.

The personal property tax rates certified to the district depend upon which is growing faster, the district's real estate assessment or personal property assessment. When the percent increase in personal property is higher than the percent increase in real estate property, the same tax rates are certified for both real estate and personal property. However, when the percent increase in real estate property is higher than that for personal property, an alternative rate is calculated under KRS 160.473. This will produce the same percent increase as that of real estate property, not to exceed the prior-year personal property rate. Appendix A, Table A.4 illustrates how this mechanism impacts district tax rates. If the rates calculated under the provisions of KRS 160.473 result in lower rates, then KDE has historically certified the original, higher rates calculated under the three options of KRS 160.470—the Compensating, Subsection (1), and the 4 Percent Increase Tax Rates—as a district's personal property rates.

House Bill 940 Tax Rate

Tier I Property Tax Rate

In addition to the provisions set out in HB 44, the enactment of KERA led to a fourth tax rate that districts are authorized to levy—the Tier I Property Tax Rate. Often referred to as the HB 940 Tax Rate, this tax rate is dependent on the mix of taxes levied by a district, including real estate, personal property, motor vehicle, and permissive.

In addition to the provisions set out in HB 44, the enactment of KERA led to a fourth tax rate that districts are authorized to levy—the Tier I Property Tax Rate. Often referred to as the HB 940 Tax Rate, this tax rate is dependent on the mix of taxes levied by a district (real estate, personal property, motor vehicle, and permissive). This rate results in tax revenue that qualifies districts for maximum Tier I equalization. As discussed in Chapter 1, a district that levies taxes up to its maximum Tier I level (and thus qualifies for state equalization) is levying the required 30 cents per \$100 of assessed property as well as additional taxes that result in revenue equivalent to 15 percent of its adjusted SEEK base funding. The HB 940 Tax Rate is not subject to hearing or recall provisions of KRS 160.470(7)(8).

The maximum Tier I equivalent must first be calculated and compared to the levied equivalent rate each district imposed in FY 1990. For those districts whose FY 1990 levied equivalent rates are higher, this statute allows them to continue levying local taxes at their FY 1990 level.

As shown in Appendix A, Table A.8, the maximum Tier I equivalent must first be calculated and compared to the levied equivalent rate each district imposed in FY 1990.² If applicable, the growth nickels and recallable nickel are added to the higher of the maximum Tier I equivalent and the FY 1990 levied equivalent rate. The growth and recallable nickels are 5-cent equivalent taxes authorized by the General Assembly to support school facilities. They are detailed in OEA's *A Review of the School Facilities Construction Commission* and are described briefly later in this chapter (Commonwealth. Legislative. Office. *A Review* 7). The higher of the FY 1990 levied equivalent rate and the maximum Tier I equivalent, plus applicable nickels, is used to calculate the Tier I Property Tax Rate.

For those districts whose FY 1990 levied equivalent rates are higher, this statute allows them to continue levying local taxes at their FY 1990 level. These districts are considered to be grandfathered. Forty districts have been grandfathered for all 17 years.

To calculate the Tier I Property Tax Rate, KDE must incorporate the base SEEK funding that districts are expected to receive, average daily attendance adjusted for growth in the number of students during the first 2 months of the school year, and the Tier I equalization level set by the General Assembly. At the time the tax rates are being calculated, this information is tentative and comes from the SEEK Forecast calculation. Chapter 3 provides a detailed discussion of the SEEK calculation.

The Tier I Property Tax Rate is certified for both real estate and personal property and is the same rate for both properties.

The Tier I Property Tax Rate is certified for both real estate and personal property and is the same rate for both properties. As shown in Appendix A, Table A.8, the district's prior-year collection rate on all properties taxed, including real estate, personal property, motor vehicle, and permissive taxes, impacts the rate. Tax collections are reported by school districts to KDE on annual financial reports, which are due to KDE in July. Motor vehicle and permissive tax revenue are subtracted from the maximum levied revenue to arrive at the maximum revenue required from property tax. This number is divided by the prior-

² As is discussed later in this chapter, the levied equivalent rate is a district's total tax revenue divided by its total assessment, which includes property and motor vehicles. This calculation accounts for the fact that districts levy various types of property and permissive taxes and the rates at which these revenue sources are taxed can vary across districts. The levied equivalent rate allows districts' tax rates to be compared.

year property assessment to arrive at the Maximum Tier I Property Tax Rate allowable under HB 940.

Table 2.4 summarizes the property tax rate options that a school district has in setting its tax rates.

Table 2.4
Property Tax Rate Options

Tax Rate	Description of Tax Rate	Subject to Hearing and Recall Provisions
House Bill 44 (KRS 160.470)		
Compensating Tax Rate	The Compensating Tax Rate is the rate that when applied to the current year's property assessment, excluding new property, produces an amount of revenue equal to that produced in the preceding year.	No Hearing
Subsection (1) Tax Rate	The Subsection (1) Tax Rate, which refers to subsection (1) of KRS 160.470, restricts local school boards to a tax rate that will produce no more revenue than the previous year's maximum rate.	Hearing and Recall
4 Percent Increase Tax Rate	The 4 Percent Increase Tax Rate is the rate that will produce 4 percent over the amount of revenue produced by the Compensating Tax Rate.	Hearing
House Bill 940 (KRS 157.440)		
Tier I Property Tax Rate	The Tier I Property Tax Rate is dependent on the mix of taxes levied by a district, including real estate, personal property, motor vehicle, and permissive taxes.	No Hearing

Source: Commonwealth, Dept. of Ed. *Financial Management Manual* 4-5.

Additional Tax Rates

The following additional taxes are levied by local boards of education regardless if levying taxes under HB 44 or HB 940: Motor Vehicle Tax Rate, Five-cent Equivalent Tax Rate, Growth Nickel, Equalized Growth Nickel, Recallable Nickel, and Exoneration Recovery Rate.

The following additional taxes are levied by local boards of education regardless of whether they are levying taxes under HB 44 or HB 940.

Motor Vehicle Tax Rate. A district's maximum tax rate for motor vehicles is certified under HB 44. The maximum tax rate is determined by comparing the district's prior-year motor vehicle tax rate to its current-year maximum Tier I equivalent rate. As shown in Appendix A, Table A.5, the higher of these two rates becomes the amount of the district's current-year maximum motor vehicle rate. The motor vehicle rate certified under HB 940 is the district's prior-year motor vehicle rate.

Nickel Taxes. Through the years, the General Assembly has passed legislation both in budget and statutory language permitting districts to levy taxes to support school facilities. Appendix B contains a summary of local and state funding sources available to school districts for capital construction, including the various nickels discussed in this chapter.

Five-cent Equivalent Tax Rate. In addition to the 30-cent equivalent tax required for SEEK participation, districts must levy a 5-cent equivalent tax to participate in the School Facilities Construction Commission (SFCC) and the Facilities Support Program of Kentucky (FSPK) programs. All districts have levied this tax. The local assessment, which includes property and motor vehicle assessments, is multiplied by 5 cents per \$100 of assessed valuation, and the amount calculated must be committed to the district building fund.³ This amount is equalized at 150 percent of the statewide average per-pupil assessment. Appendix A, Table A.6 demonstrates the calculation for determining the 5-cent equivalent tax rate.

The 5-cent equivalent tax rate is reflected within the certified real estate and personal property tax rates rather than being reflected as a separate, additional tax. The exception to this is when a district is levying a growth nickel, equalized growth nickel, or recallable nickel (described below) for the first time. In the first year that any of these nickels are imposed, the 5-cent equivalent is added to the current-year's tax rates certified by the Department of Education.

Growth Nickel. To accommodate districts with growing numbers of students, school districts meeting the criteria in KRS 157.621 can levy an additional nickel for building fund needs.⁴ Tax revenue from this source is not equalized by the state. Districts must hold a public hearing prior to levying the growth nickel. Currently 33 districts levy the growth nickel. The General Assembly enacted the growth nickel authorization in 1994. At the time, the FSPK

³The actual tax rate that districts levy to produce the 5-cent equivalent tax is greater than 5 cents because the calculation takes into consideration that the tax is only applied to real estate and personal property, not to motor vehicles, and also adjusts for the fact that districts will collect less than 100 percent of the tax. Regardless of the amount collected from the tax, districts are required to transfer the exact amount produced by 5 cents per \$100 of assessed value of property and motor vehicles to the building fund.

⁴The growth criteria in KRS 157.621 includes the following: growth of at least 150 students and 3 percent overall growth in the last 5 years; debt service of at least 80 percent of capital outlay, and local and state Facilities Support Program of Kentucky; current enrollment greater than available classroom space; and certified district facility plan.

program was not fully funded, and the legislation included a sunset provision for the growth nickel once full funding of FSPK was restored. Although FSPK has been fully funded since FY 1996, the General Assembly has continued to allow for the growth nickel through budget language.

Equalized Growth Nickel. Through budget language in 2003 and 2005, the General Assembly provided those districts that continued to meet the growth criteria the option to levy a second growth nickel. This nickel is referred to as the equalized growth nickel because the General Assembly has provided an additional equalization funding for those districts that have levied both the original nickel and second growth nickel. By FY 2006, 22 districts levied the second growth nickel; however, the General Assembly did not continue the second growth nickel provision in the 2006 budget.

Recallable Nickel. Through budget language in 2003, 2005, and 2006, the General Assembly allowed all districts the opportunity to levy a nickel for building needs that was subject to public petitions for recall. By FY 2007, 13 districts levied the recallable nickel. The General Assembly has provided retroactive equalization for 9 of the 13 districts that levied the recallable nickel. The remaining four districts that levied the recallable nickel were only guaranteed funding for 1 year, in FY 2008, through funding provided by the Urgent Needs Advisory Committee, an entity established in the 2006 budget enacted by the General Assembly.

Exoneration Recovery Rate. Beginning with the FY 1994 tax rate certifications, KRS 134.590 permitted districts to recover prior-year losses due to exonerations or issuance of refunds due to errors in assessments. This additional tax rate may be added to a district's real estate and personal property tax rate. As shown in Appendix A, Table A.7, the Exoneration Recovery Rates I and II are calculated in the same way as the Compensating Tax Rates I and II but are based on assessments increased by the amount of the exonerated assessment.

Tier II Property Tax Rate

Although the tax rate certifications do not reflect the Tier II Tax Rate as a tax option, HB 940 does provide for a second tier, which is essentially a cap on local effort.

Another tax option exists for school districts to consider. The Tier II Tax Rate allows local boards of education to increase revenue—subject to voter referendum—up to 30 percent of revenue generated through the adjusted SEEK base (guaranteed base plus add-ons) plus Tier I. Although the tax rate certifications do not

reflect the Tier II Tax Rate as a tax option, HB 940 does provide for this second tier, which is essentially a cap on local effort. Similar to Tier I, if a district's FY 1990 levied equivalent rate exceeded the maximum Tier II equivalent rate, the district would not be required to levy a lower equivalent in succeeding years. Tier II funds are not equalized by the state. Table A.9 in Appendix A illustrates the Tier II calculation.

District Selection of Tax Rates

Upon receipt of the tax rate certification from KDE, local boards of education must decide which rates they wish to adopt.

Upon receipt of the tax rate certification from KDE, local boards of education must decide which rates they wish to adopt. There are a number of issues districts must consider when selecting tax rates. These include local sentiment and politics related to increasing taxes, whether current tax collections are sufficient to support education needs, and the question of whether to seek a rate that is subject to voter approval. Also, since the certified rates are maximums, districts may consider levying rates lower than the certified rates.

A board is not required to be consistent from year to year in the tax provisions it selects. If a district's Tier I Tax Rate under HB 940 exceeds the tax rates under HB 44, the board may levy the higher rate under HB 940, and this rate is not subject to a hearing or voter recall. A local board of education may levy a rate that exceeds the Subsection (1) Tax Rate under HB 44 by going to the voters but is nonetheless capped at its Tier II Tax Rate under HB 940. For these reasons, HB 44 and HB 940 are referred to as intertwining tax laws.

Within 30 days of receiving the tax rate certification from KDE, which generally occurs in July or August, local boards of education must adopt the rates they wish to levy for the current year and submit the Tax Rate Levied Form to KDE.

Within 30 days of receiving the tax rate certification from KDE, which generally occurs in July or August, local boards of education must adopt the rates they wish to levy for the current year and submit a Tax Rate Levied Form to KDE as notification of the rates adopted. If the adopted rates are subject to hearing and recall, the rates will not be final until that process is complete. KDE submits the tax rates to the Kentucky Board of Education for approval.

Rates Historically Levied by Local Boards of Education

Historical data indicating the type of rates levied by local boards of education for fiscal years 1993 through 2007 is shown in Table 2.5.

Historical data indicating the types of rates levied by local boards of education for fiscal years 1993 through 2007 are shown in Table 2.5. The tally excludes the growth and recallable nickels for

the purpose of categorizing the rates. FY 1991 and FY 1992 are excluded because the methods by which KDE certified tax rates to districts differed from procedures that were followed in later years.⁵

In order to analyze district taxing efforts, the rates levied were categorized according to the tax rate authority selected by school districts.

In order to analyze district taxing efforts, the rates levied were categorized according to the tax rate authority selected by school districts. Since the certified rates are maximums and districts may select the certified rate or a lower rate, the process of categorizing districts' tax rate selections required some rules. This methodology is described in Appendix C.

The number of times districts have levied the Compensating Tax Rate, Subsection (1) Tax Rate, 4 Percent Increase Tax Rate, and House Bill 940 Tax Rate is shown in Panel 1 of Table 2.5.

The number of times districts have levied the Compensating Tax Rate, Subsection (1) Tax Rate, 4 Percent Increase Tax Rate, and House Bill 940 Tax Rate is shown in Panel 1 of Table 2.5. The number of districts levying the Compensating Tax Rate has stayed steady over the years, the number levying the House Bill 940 Tax Rate has dropped off, and the number levying the 4 Percent Increase Tax Rate has increased substantially.

Since the rates certified to districts are maximums, some districts have chosen to levy below the maximum rates certified to them. The number of times districts levied below each of the four possible tax rates, the number of times districts have exceeded the Subsection (1) Tax Rate, and the number of times information was not available is shown in Panel 2 of Table 2.5. The number of districts levying below the various categories has dropped. Two districts exceeded the Subsection (1) Tax Rate by successfully going to the voters and asking for tax increases three times over the years.

⁵For FY 1991, the first year of education reform, each district completed a letter of intent notifying KDE of the level at which it wanted to levy within Tier I. For most districts, the department only certified the HB 940 tax rate for the first 2 years of reform. The department certified HB 44 rates for just a limited number of districts when those rates exceeded the HB 940 Tax Rate. Beginning in FY 1993, KDE certified tax rates under both HB 44 and HB 940.

Table 2.5
Tax Rate Categories for FY 1993-FY 2007

Panel 1

Fiscal Year	Compensating Tax Rate (No Hearing)	Subsection (1) Tax Rate (Hearing and Recall)	4 Percent Increase Tax Rate (Hearing)	HB 940 Tax Rate (No Hearing)	Total From Panel 2	Total by Year
1993	44	27	33	26	46	176
1994	31	21	38	38	48	176
1995	29	10	49	48	40	176
1996	38	11	52	40	35	176
1997	44	17	60	24	31	176
1998	51	13	61	24	27	176
1999	47	17	57	25	30	176
2000	41	14	63	32	26	176
2001	53	16	66	21	20	176
2002	44	22	75	21	14	176
2003	47	25	68	15	21	176
2004	44	3	87	17	25	176
2005	54	28	63	10	21	176
2006	39	2	99	12	24	176
2007	42	3	110	6	14	175
All Years	648	229	981	359	422	2,639
Percent of all rates	24.6%	8.7%	37.2%	13.6%	16.0%	100%

Panel 2

Fiscal Year	Below Compensating Tax Rate	Below Subsection (1) Tax Rate	Below 4 Percent Increase Tax Rate	Below HB 940 Tax Rate	Above Subsection (1) Tax Rate	No Information
1993	5	13	16	12	-	-
1994	5	10	11	22	-	-
1995	7	3	12	17	1	-
1996	6	4	14	11	-	-
1997	10	2	13	6	-	-
1998	4	2	13	7	-	1
1999	5	4	15	5	-	1
2000	6	4	10	6	-	-
2001	2	1	12	4	-	1
2002	3	4	5	-	1	1
2003	5	2	11	3	-	-
2004	3	3	18	1	-	-
2005	2	3	15	-	1	-
2006	3	5	13	3	-	-
2007	4	2	7	1	-	-
All Years	70	62	185	98	3	4

Notes: Four districts' tax rate certifications were missing from the files, one from each of the following fiscal years: 1998, 1999, 2001, and 2002. There were 175 districts in FY 2007. Growth nickels, equalized growth nickels, and recallable nickels were excluded in categorizing the rates.

Source: Staff analysis of tax data obtained from the Kentucky Department of Education.

The tax rates local districts selected during the past 15 years, and the impact of those taxing decisions on local revenue, should be considered within the context of differences that exist under HB 44 and HB 940.

The tax rates local districts selected during the past 15 years and the impact of those taxing decisions on local revenue should be considered within the context of differences that exist under HB 44 and HB 940. As shown in Panel 1 of Table 2.5, districts selected tax rates a total of 2,639 times between FY 1993 and FY 2007. The 4 Percent Increase Tax Rate accounted for 37.2 percent of all rates. Districts levied the Compensating Tax Rate 24.6 percent of the time and levied the HB 940 Tax Rate 13.6 percent of the time. The Subsection (1) Tax Rate accounted for 8.7 percent of all rates selected. In addition, in 16 percent of the cases, districts selected rates below the maximum allowed for the four tax rate categories, districts levied a rate above the Subsection (1) Tax Rate by going to the voters, or the information was not available. The following analysis, based on Panel 1 of Table 2.5, summarizes the major conclusions about the rates districts levied over this time period.

As noted earlier, only the Subsection (1) Tax Rate is subject to hearing and recall provisions. Districts levied the Subsection (1) Tax Rate 229 times (or 8.7 percent of the time) from 1993 to 2007. This rate is generally higher than the other rates, although for a few districts whose assessments are stagnant or are declining, the Subsection (1) Tax Rate can be lower than the Compensating and 4 Percent Increase Tax Rates. Prior to recently enacted legislation, some districts whose 4 Percent Increase Tax Rates were higher than their Subsection (1) Tax Rates had their rates capped at the Subsection (1) Tax Rate. In 2003, the General Assembly removed this limitation through budget language. In 2005, the General Assembly permanently removed this limitation as part of the tax modernization plan in HB 272.

When districts levy the Subsection (1) Tax Rate, this action is subject to a recall only when this rate is higher than the 4 Percent Increase Tax Rate. If the Subsection (1) Tax Rate is equal to or lower than the 4 Percent Increase Tax Rate, both are subject to only the hearing requirement. Of the 229 times the Subsection (1) Tax Rate was levied, in only 9 instances was the Subsection (1) Tax Rate higher than the 4 Percent Increase Tax Rate. This is evidence of the fact that very few districts have levied a rate subject to recall over the past 15 years. The Subsection (1) Tax Rate levied by districts was less than the Compensating Tax Rate 79 times and less than the HB 940 Tax Rate 6 times. For the latter, districts were not capped at the Subsection (1) Tax Rate but chose to levy below what they could have levied under HB 940.

Of the 359 times districts have levied the HB 940 Tax Rate (or 13.6 percent of the rates levied), this rate exceeded the 4 Percent

Increase Tax Rate 198 times, was less than the 4 Percent Increase Tax Rate 147 times, and was exactly the same as the 4 Percent Increase Tax Rate 14 times.

Of the 981 times districts have levied the 4 Percent Increase Tax Rate, which accounted for 37.2 percent of all rates levied, this rate was less than the HB 940 Tax Rate 66 times. In 69 instances, the 4 Percent Increase Tax Rate exceeded the Subsection (1) Tax Rate, indicating that districts took advantage of the fact that the General Assembly has removed the provision that prohibited districts from levying the 4 Percent Increase Tax Rate if it was higher than the Subsection (1) Tax Rate.

In summary, the historical overview of the tax provisions districts have selected demonstrates that few districts have chosen tax rates that are subject to voter recall. In addition, in a substantial number of instances, districts have opted to levy tax rates lower than the maximum rate certified to them.

Levied Equivalent Rate

Districts' local tax effort consists of various types of taxes. The rates at which these revenue sources are taxed can vary. KDE converts the districts' local tax efforts to a standardized tax rate called a levied equivalent rate.

As noted earlier, often the districts' local tax effort consists of various types of taxes, and the rates at which these revenue sources are taxed can vary. KDE converts the districts' local tax efforts to a standardized tax rate called a levied equivalent rate. The levied equivalent rate is a district's total tax revenue divided by its total assessment, which includes property and motor vehicles. The supporting calculation for the levied equivalent rate is shown in Appendix A, Table A.10.

Upon receipt of the Tax Rate Levied Form submitted by each district, KDE calculates each district's levied equivalent rate.

Upon receipt of the Tax Rate Levied Form submitted by each district, KDE enters the current year's tax rates into the tax program to calculate each district's levied equivalent rate. The levied equivalent rate for the base year (which is the odd year before the biennium) and the current year's levied equivalent rate are used in the SEEK calculation to determine a district's level of participation in Tier I.

Assessment Changes

In 1990, new statutory provisions were enacted under KRS 132.690 and KRS 160.460(3) that required a review every 4 years of all the property in the Commonwealth, required all properties to be assessed at 100 percent of fair market value, and imposed rigid performance standards for local property valuation administrators.

In 1990 and 1991, the Department of Revenue performed emergency certifications for 25 counties, delaying some districts' property certifications. It took until FY 2006 for the last county to get back on the required certification schedule (Crawford).

Table 2.6 shows the percent change in the assessment value of each type of property that school districts taxed from FY 1991 through FY 2007.

Each year, the Department of Revenue certifies property assessments to KDE but because of the timing these certifications, the assessments for some types of property are estimated. Table 2.6 shows the percent change in the assessment value of each type of property that school districts taxed from FY 1991 through FY 2007. Some estimates are based on prior-year actual valuations and others are forecasted. On the following year's property certifications issued by the Department of Revenue, the estimated data is replaced with the actual assessments upon which districts collected taxes.⁶

The percent changes in Table 2.6 are calculated using the prior-year actual and the current-year estimate. KDE calculates districts' SEEK amounts based on the current-year certification, which contain estimates.

The percent changes in Table 2.6 are calculated using the prior-year actual and the current-year estimate since these are the valuations used to calculate districts' tax rates. However, KDE calculates districts' SEEK amounts based on the current-year certification, which contain estimates. No adjustment is made in SEEK to reflect the difference between the estimated assessments and actual assessments. However, the impact of this adjustment would be minimal according to staff calculations.

⁶ Unmined coal assessments are included within real estate property. It does not appear that the Department of Revenue replaces the estimate with actual numbers but carries the estimate forward to the following year. This results in districts' tax rates being calculated on unmined coal assessment data that is 2 years old.

Table 2.6
Assessment Change Over the Years, FY 1991-FY 2007

Fiscal Year	Real Estate Property % Change	Personal Property % Change	Public Service Real Estate % Change	Public Service Personal % Change	Distilled Spirits % Change	Motor Vehicle % Change	Total Assessment % Change
1991	9.8%	3.7%	1.3%	0.8%	2.2%	7.4%	8.1%
1992	5.4%	2.5%	2.0%	2.9%	5.0%	-0.7%	4.2%
1993	6.3%	-1.3%	-0.2%	6.7%	1.5%	2.7%	4.9%
1994	5.3%	-2.6%	2.4%	11.2%	0.9%	7.9%	5.0%
1995	9.2%	1.5%	0.5%	2.1%	2.9%	19.1%	9.0%
1996	5.7%	9.6%	2.4%	-2.8%	2.0%	14.8%	6.7%
1997	7.7%	10.1%	1.7%	-1.6%	-0.3%	-0.1%	6.2%
1998	6.4%	2.5%	1.1%	-3.1%	3.6%	4.1%	5.1%
1999	7.0%	8.6%	-0.1%	0.7%	-2.0%	-9.8%	4.6%
2000	7.5%	1.7%	-0.6%	-0.7%	5.8%	8.4%	6.5%
2001	7.8%	6.0%	5.5%	6.4%	-19.2%	12.5%	7.9%
2002	7.7%	-2.5%	0.7%	0.9%	12.2%	3.3%	5.8%
2003	5.8%	-1.8%	-0.9%	-0.2%	6.8%	-1.3%	4.0%
2004	5.8%	3.2%	-0.3%	-1.1%	4.6%	4.2%	5.0%
2005	5.8%	0.4%	-0.2%	-1.6%	-18.6%	-1.8%	4.1%
2006	6.7%	4.2%	-1.4%	-0.5%	0.0%	9.0%	6.3%
2007	7.3%	5.1%	-16.4%	-21.3%	0.0%	5.2%	5.2%

Source: Staff calculation using tax data obtained from the Kentucky Department of Education.

Over the years, several changes have been made in how property evaluations are determined; Table 2.7 presents the more notable changes in assessment policy. A few of these methodological changes have impacted the overall valuation of property in the state, as shown in Table 2.6. For example, motor vehicle assessments decreased in fiscal years 1997 and 1999, reflecting the change in how motor vehicle valuations were determined. Rather than using retail value, the mid-point between retail and trade-in value was used in FY 1997. Then, the trade-in value was used in FY 1999, resulting in a 9.8 percent decrease in motor vehicle assessments across the state. In FY 2007, public service real estate and personal property assessments decreased, reflecting statutory changes that removed public service company franchise values from certified assessments. Although the types of property have experienced decreases in assessed value over the years, the total assessment has consistently experienced increases in value.

Table 2.7
Changes in Assessment Evaluations, FY 1997-FY 2008

Fiscal Year	Explanation of Changes in Assessment
1997	Change in motor vehicle assessments; prior years used National Automobile Dealers Association (NADA) average retail value as of January 1; change used mid-point between average retail and trade-in value
1999	Change in motor vehicle assessments to NADA January 1 trade-in value Unmined coal was included on the property assessment and included in tax rate calculation in FY 1999 for the first time, but the Kentucky Department of Education (KDE) received judicial permission to exclude these amounts in the Support Education Excellence in Kentucky (SEEK) calculation for the first year to allow districts time to adjust for the reduction in SEEK funds.
2000	Districts could tax or exempt certain personal property (aircraft, watercraft, and inventory in transit). Assessments from this personal property are not in KDE's tax system in FY 2000 because the Department of Revenue excluded amounts until KDE found out if districts were taxing or exempting this property. Assessments were adjusted in the SEEK database.
2001	Inventory in transit was taxed at 80% of assessed value. This began phasing out taxing inventory in transit for school purposes.
2002	Inventory in transit was taxed at 50% of assessed value.
2003	Inventory in transit was no longer taxable by school districts.
2006	House Bill 272 provided for extension of utility gross receipts license tax to direct broadcast satellite and wireless cable services as an option if the school district also imposes the tax on cable services.
2007	House Bill 272 eliminated public service company's franchise value from certified assessments and replaced it with a hold harmless provision, effective January 1, 2006. The Department of Revenue distributes hold harmless monies to districts monthly.
2008	Per court case of <i>Commonwealth of Kentucky, Finance and Administration Cabinet v. Jim Beam Brands, Co.</i> , No. 2006-CA-002176, distilled spirits' inventory is now exempt from school taxation due to the settlement of litigation regarding the classification of inventory (i.e., merchants' inventory, goods in process, in transit inventory).

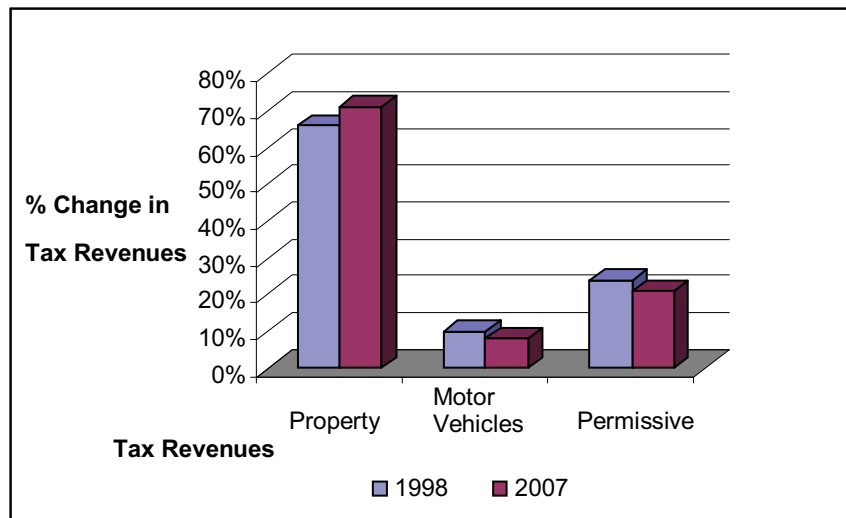
Sources: Commonwealth. Dept. of Revenue; Barlow. Sept. 19, 2007; Livers; Rice.

Changing Revenue Mix for School Districts

The amount of revenue generated by the mix of taxes collected by school districts shifted slightly from FY 1998 to FY 2007, as shown in Figure 2.A.

As previously explained in this chapter, the local revenue collected by districts is accumulated through a mix of taxes. The amount of revenue generated by the mix of taxes collected by school districts shifted slightly from FY 1998 to FY 2007, as shown in Figure 2.A.⁷ For example in FY 1998, property tax made up 66 percent of the tax revenue collected by school districts, while motor vehicle tax made up 10 percent and permissive tax made up 24 percent. In FY 2007, property tax made up 71 percent, while motor vehicle tax made up 8 percent and permissive tax made up 21 percent. The decrease in motor vehicle revenue can be attributed to the changes in valuation methods noted above in Table 2.7. The increase in tax revenue from property can be attributed to the increases in real estate values as a result of stricter state requirements regarding property valuation.

Figure 2.A
Local Tax Revenues Supporting Education



Source: Staff calculation of tax revenue data obtained from the Kentucky Department of Education.

⁷FY 1998 was selected for this comparison because it was the first year all districts were utilizing MUNIS, the statewide financial accounting system.

Revenue Forgone

Districts do not always levy the maximum tax rate not subject to recall. As illustrated in Table 2.8, districts have forgone an average of \$8.5 million in revenue a year, or approximately \$30 per pupil, from FY 1993 through FY 2007, in the districts that did not levy the maximum rate not subject to recall.

Districts do not always levy the maximum tax rate not subject to recall. As noted earlier in this chapter, local education leaders must weigh a variety of factors when setting tax rates. The decision to set or keep rates below the maximum levy not subject to recall reflects, among other things, the history of rate levels in the district and local sentiments regarding tax rates.

As discussed earlier, of the four possible tax provisions districts may use to levy taxes, only the Subsection (1) Tax Rate, which limits districts to no more revenue than the previous year's maximum rate, is subject to hearing and recall. Also, prior to recent legislative actions, districts could not levy the 4 Percent Increase Tax Rate if it exceeded the Subsection (1) Tax Rate. Furthermore, due to the intertwining of tax laws, the HB 940 rate could possibly be higher than the Subsection (1) Tax Rate. Staff compared these rates to determine the maximum rate not subject to recall and then compared this rate to each district's actual tax levy.⁸ Also included in the analysis was an examination of untaxed exoneration revenue.⁹

As illustrated in Table 2.8, from FY 1993 through FY 2007, districts have forgone an average of \$8.5 million in revenue a year, or approximately \$30 per pupil, in those districts that did not levy the maximum rate not subject to recall. Of this amount, from FY 1994 through FY 2007, the average exoneration amount forgone was \$1.3 million, or approximately \$7 per pupil in those districts that didn't levy the maximum exoneration amount.

⁸ To determine the maximum rate not subject to recall, the Subsection (1) Tax Rate was compared to the 4 Percent Increase Tax Rate. The lower rate was selected and compared to the HB 940 Tax Rate. The higher of the two rates was selected as the maximum rate not subject to recall. For fiscal years 2004, 2006, and 2007, the Subsection (1) Tax Rate cap was removed through budget language and statute, so the 4 Percent Increase Tax Rate was selected and compared to the HB 940 Tax Rate.

⁹ The exoneration rate was added to the maximum rate not subject to recall and compared to each district's actual rate. Exoneration rates were first included on the FY 1994 tax rate certifications in accordance with KRS 134.590.

Table 2.8
Revenue Forgone, FY 1993-FY 2007

Fiscal Year	Total Revenue Forgone	Per-pupil Revenue Forgone	Exoneration Revenue Forgone	Per-pupil Revenue Forgone
1993	15,894,226	58	-	-
1994	15,872,434	37	1,695,364	6
1995	10,338,293	32	993,057	4
1996	13,350,701	33	1,494,227	5
1997	8,706,531	27	1,576,431	6
1998	7,100,392	22	1,705,267	6
1999	7,861,964	25	1,113,216	6
2000	6,772,431	24	1,152,945	5
2001	7,356,312	27	1,218,171	7
2002	6,466,742	25	1,026,234	7
2003	5,800,703	28	1,426,713	11
2004	4,872,541	26	1,096,249	8
2005	5,330,177	23	1,172,910	7
2006	6,849,766	31	1,080,131	6
2007	5,619,585	29	1,054,466	7
Total	128,192,798		17,805,380	

Note: To calculate the per-pupil amounts, the revenue forgone amounts were divided by the average daily attendance adjusted for growth of only those districts that did not levy the maximum rate.

Source: Staff calculation using tax data obtained from the Kentucky Department of Education.

The process by which districts receive state education funding through the SEEK calculation is described in Chapter 3. In addition to accounting for the number and types of students in each district and for transportation costs, the SEEK formula incorporates the levied equivalent tax rates and property assessment data discussed in this chapter.

Chapter 3

Support Education Excellence in Kentucky

Introduction

Chapter 3 describes the process by which districts receive state education funding through the SEEK calculation.

Chapter 3 describes the process by which districts receive state education funding through the SEEK calculation. In addition to accounting for the number and types of students in each district and for transportation costs, the SEEK formula utilizes the tax rates and property assessments discussed in Chapter 2 to determine the amount districts will receive in state funding. District property assessments and levied tax rates determine the amount of local revenue districts receive.

This chapter provides a synopsis of the SEEK process, including definitions and formulas for the components within the SEEK calculation.

This chapter provides a synopsis of the SEEK process, including definitions and formulas for the components within the SEEK calculation. In order to discuss this process in detail, the property assessment data, tax rates, and funding of a sample school district are provided in the tables below. Table 3.1 contains an example of a SEEK calculation that a school district receives from the Kentucky Department of Education. References have been added to Table 3.1 that link to other tables within this chapter that provide additional detail and supporting calculations.

There have been very few changes to the SEEK formula since it was first implemented, and these have had minimal impact on state funding.

Appendix D contains notable changes in the SEEK formula and the valuation of property assessments over the years. There have been very few changes to the SEEK formula since it was first implemented in 1990, and these have had minimal impact on state funding. As discussed in Chapter 2, changes in the valuations of property assessments have had a more substantial impact on local and state funding.

Table 3.1
SEEK Calculation

Support Education Excellence in Kentucky Final Calculation 2006-2007 School Year District: 000 Sample County				
			Refer to <u>Report Table</u>	
		2005-2006 End-of-Year ADA	2,426.2	3.3
		Growth	0.0	3.3
		2005-2006 ADA Plus Growth	2,426.2	3.3
Assessment	\$603,402,051	Levied Equivalent Rate	53.6	3.15
Per Pupil Assessment	\$248,703	Maximum Tier I Rate	47.1	3.15
		91-92 State Per-pupil Funding	\$2,915.83	3.18
SEEK Calculation		Per Pupil	Total	
Guaranteed Base		3,508.00	8,511,110	3.3
At-Risk		311.66	756,149	3.4
Home & Hospital		10.53	25,560	3.5
Exceptional Child		788.50	1,913,053	3.7
Transportation		405.46	983,718	3.9
LEP		<u>.76</u>	<u>1,842</u>	3.10
Adjusted SEEK Base		5,024.91	12,191,432	3.11
Less 30 Cent Local Effort		<u>746.00</u>	<u>1,810,206</u>	3.12
Calculated State Portion		4,278.80	10,381,226	3.12
State Tier I		467.99	1,135,436	3.15
Hold Harmless		0.00	0	3.18
Adjustment to Appropriation		<u>0.00</u>	<u>0</u>	3.19
Total State SEEK		4,746.79	11,516,662	
Prior-year Adjustment		<u>0.00</u>	<u>0</u>	3.19
Total State Funds		<u>4,746.79</u>	<u>11,516,662</u>	3.19
Less Capital Outlay			242,620	3.20
Net General Fund SEEK			11,274,042	
FSPK				
Local			301,701	3.21
State			471,044	3.21
Original Growth Nickel				
Local			0	
State			0	
Equalized Growth Nickel				
Local			0	
Recallable Nickel				
Local			0	
State			0	
Equalized Facility Funding Nickel				
Local			0	
State			0	

Table 3.1 continued
SEEK Calculation

Support Education Excellence in Kentucky Final Calculation 2006-2007 School Year District: 000 Sample County		
		Refer to <u>Report Table</u>
Base Year Levied Equivalent Rate	53.6	3.15
Current Year Levied Equivalent Rate	54.7	3.15
Assessment	\$603,402,051	3.12
Prior Year End-of-Year ADA	2,426.2	3.3
Prior Year 8-Month Average Free Lunch	1437.0	3.4
Prior Year December 1 Child Count		3.7
Low Incidence (Severe: Weight 2.35)	99.00	
Moderate Incidence (Moderate: Weight 1.17)	249.00	
High Incidence (Speech: Weight 0.24)	89.00	
Prior Year Home & Hospital	7.5	3.5
Base Year Debt Service	\$789,249	3.21
Current Year Second Month Growth Factor Percentage	-2.8	3.3
LEP	7	3.10
Transportation (Unprorated)	\$1,210,129	3.9

Note: References to report tables do not appear in the SEEK calculation received by school districts. They are added here to refer readers to the tables in this chapter that contain the supporting calculations.

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education.

SEEK Process and Formula

KDE's Division of Data Management is responsible for the SEEK calculation.

KDE's Division of Data Management is responsible for the SEEK calculation. KDE sends school districts the following three SEEK calculations for each fiscal year.

SEEK Forecast. The first calculation, the SEEK Forecast, is sent to districts in December or January, prior to the fiscal year the calculation covers. All data in this calculation are estimated by KDE and reviewed by districts. Districts use the SEEK Forecast to establish their draft and tentative budgets, which are due on January 31 and May 30, respectively.

SEEK Tentative. The second calculation, the SEEK Tentative, is usually sent to districts in August or September for use in districts' working budgets, which are due to the department on September 30. For this calculation, many items previously estimated are replaced with actual data.

SEEK Final. The third calculation is the SEEK Final. According to a provision included in the 2005 and 2006 enacted budgets, districts must receive this calculation by March 1. The SEEK Final informs districts of the amount of state funds they will receive through the formula for the fiscal year. All estimated data have been replaced with actual data for this calculation. Districts report the amounts from the SEEK Final on their annual financial reports, which are due to KDE on July 25. Table 3.1 provides an example of the SEEK Final calculation.

Guaranteed Base Funding

A guaranteed base amount of per-pupil funding is established by the General Assembly for each budget cycle.

A guaranteed base amount of per-pupil funding is established by the General Assembly for each budget cycle. The amounts funded by the General Assembly from FY 1991 through FY 2007 are presented in Table 3.2. Also reflected is the 1991 guaranteed base in inflation-adjusted terms for subsequent years. This reflects how much per-pupil funding would have been appropriated—in inflation-adjusted terms—if no increases had been made to the guaranteed base. As Table 3.2 shows, the guaranteed base has sometimes been below and sometimes above inflation, but in all years, the base appropriation has been very close to the 1991 funding adjusted for inflation. In other words, in real dollar terms, no substantial increases or decreases have occurred in base funding for SEEK.

Table 3.2
Guaranteed Base for FY 1991-FY 2007

Fiscal Year	Guaranteed Base	Percent Increase	FY 1991 Guaranteed Base Adjusted for Inflation
1991	\$2,305		\$2,305
1992	\$2,420	5.0%	\$2,379
1993	\$2,420	0.0%	\$2,453
1994	\$2,495	3.1%	\$2,517
1995	\$2,517	0.9%	\$2,589
1996	\$2,593	3.0%	\$2,659
1997	\$2,673	3.1%	\$2,735
1998	\$2,756	3.1%	\$2,784
1999	\$2,839	3.0%	\$2,832
2000	\$2,924	3.0%	\$2,914
2001	\$3,046	4.2%	\$3,014
2002	\$3,066	0.7%	\$3,067
2003	\$3,081	0.5%	\$3,134
2004	\$3,191	3.6%	\$3,203
2005	\$3,240	1.5%	\$3,299
2006	\$3,445	6.3%	\$3,425
2007	\$3,508	1.8%	\$3,514

Sources: SEEK Final calculations obtained from the Kentucky Department of Education; U.S. Bureau of Labor Statistics.

The guaranteed base funding is determined by multiplying the per-pupil funding level set by the General Assembly by the prior year end-of-year average daily attendance adjusted for growth experienced in the current year.

As shown in Table 3.3, the guaranteed base funding for each district is determined by multiplying the per-pupil funding level set by the General Assembly by the prior year end-of-year average daily attendance (ADA) adjusted for growth experienced in the current year.¹ An adjustment is made for increases in students served if the first 2 months' ADA in the current year is greater than the first 2 months' ADA in the prior year. The growth ADA is added to the prior year end-of-year ADA to arrive at the total ADA funded in SEEK.² If a district has experienced a decline in average daily attendance compared to the previous year, SEEK funding is not reduced. KRS 157.360(9) and (10) provide for additional adjustments to be made to ADA for those districts experiencing

¹ADA is defined under KRS 157.320(1) as "the aggregate days attended by pupils in a public school, adjusted for weather-related low attendance days if applicable, divided by the actual number of days the school is in session, after the five (5) days with the lowest attendance have been deducted." ADA is reported on the Superintendent's Annual Attendance Report and is due to the department by June 30.

²If an increase exists when comparing a district's first 2 months' ADA of the current year to the prior year, the percent increase is multiplied by the prior year end-of-year ADA to produce the growth ADA. The first 2 months' ADA for the current and prior year is reported on the second month growth factor report. This report is submitted by districts to KDE 10 days after the last day of the second month, but no later than November 1 of the current school year.

extreme decline in ADA. These adjustments result in modest increases in ADA for purposes of calculating SEEK funding.

Table 3.3
Guaranteed Base Funding Calculation

First 2 Months' ADA - Current Year	2,402.01
Less: First 2 Months' ADA - Prior Year	<u>2,471.86</u>
Equals: Change in ADA	-69.85
Divided by: First 2 Months' ADA - Prior Year	<u>2,471.86</u>
Equals: Percent Change in ADA	-2.83
Multiplied by: Prior Year End-of-Year ADA	<u>2,426.20</u>
Equals: Growth ADA (zero if negative)	0
Prior Year End-of-Year ADA	2,426.20
Plus: Growth ADA	<u>0</u>
Equals: Funded ADA	2,426.20
Funded ADA	2,426.20
Times: Guaranteed Base	<u>3,508</u>
Equals: Guaranteed Base Dollars	8,511,110

Sources: Staff adaptation of a selected district's FY 2007 SEEK Final calculation and SEEK example obtained from the Kentucky Department of Education.

Add-ons: Adjustments to the SEEK Guaranteed Base

Each district's guaranteed base funding level is adjusted by factors that are commonly called SEEK add-ons and reflect the increased costs associated with educating at-risk, exceptional, and limited English proficiency students and with providing home and hospital instruction and transportation.

The at-risk funding is based on the number of students in the district who are approved for the free-lunch program.

At-risk Funding. The at-risk funding is based on the number of students in the district who are approved for the free-lunch program. As shown in Table 3.4, the weight applied to at-risk students is 15 percent (that is, the prior year 8-month average of approved free-lunch applications is multiplied by 15 percent of the guaranteed base). The free-lunch application data are provided by the Division of Nutrition and Health Services.

Table 3.4
At-risk Add-on Calculation

Guaranteed Base	3,508
Times: At-risk Weight Factor	0.15
Times: Prior Year 8-Month Average Free-Lunch Applications	<u>1,437.0</u>
Equals: At-risk Add-on Dollars	756,149

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education and its *Financial Management Manual*.

Home and hospital funding is based on the number of students receiving instruction in the home or in a hospital under the provisions of KRS 157.270.

Home and Hospital Funding. Home and hospital funding is based on the number of students receiving instruction in the home or in a hospital under the provisions of KRS 157.270. The home and hospital ADA is reported on the Superintendent's Annual Attendance Report provided by all school districts. As illustrated in Table 3.5, the prior year home and hospital ADA is multiplied by the guaranteed base less \$100, the amount of the capital outlay allotment.

Table 3.5
Home and Hospital Add-on Calculation

Guaranteed Base less \$100 for Capital Outlay	3,408
Times: Prior Year Home and Hospital ADA	<u>7.5</u>
Equals: Home and Hospital Add-on Dollars	25,560

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education and its *Financial Management Manual*.

The exceptional child funding is based on the number and types of exceptional children as defined in KRS 157.200.

Exceptional Child Funding. The exceptional child funding is based on the number and types of exceptional children as defined in KRS 157.200. The weights and categories of exceptionality are identified in Table 3.6. The weights are multiplied by the guaranteed base and applied to the prior year December 1 child count provided by KDE's Division of Exceptional Children Services by category of exceptionality as shown in Table 3.7.

Table 3.6
Exceptional Child Weights and Categories

Category	Weight	Category Description
Low Incidence Disabilities	2.35	Functional mental disability, hearing impairment, emotional-behavioral disability, visual impairment, multiple disabilities, deaf-blind, autism, and traumatic brain injury.
Moderate Incidence Disabilities	1.17	Mild mental disability, orthopedic impairment or physically disabled, other health impaired, specific learning disabilities, and developmental delay.
High Incidence Disability	0.24	Communication disorders of speech or language.

Source: Commonwealth. Dept. of Ed. *Financial Management Manual*.

Table 3.7
Exceptional Child Add-on Calculation

Guaranteed Base	3,508
Times: Low Incidence Weight Factor	2.35
Times: Low Incidence Child Count	99
Equals: Low Incidence Add-on Dollars	816,136
Guaranteed Base	3,508
Times: Moderate Incidence Weight Factor	1.17
Times: Moderate Incidence Child Count	249
Equals: Moderate Incidence Add-on Dollars	1,021,986
Guaranteed Base	3,508
Times: High Incidence Weight Factor	0.24
Times: High Incidence Child Count	89
Equals: High Incidence Add-on Dollars	74,931
Low Incidence Dollars	816,136
Plus: Moderate Incidence Dollars	1,021,986
Plus: High Incidence Dollars	74,931
Equals: Total Exceptional Child Add-on Dollars	1,913,053

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education and its *Financial Management Manual*.

Transportation funding for school districts is calculated under the provisions of KRS 157.370 and is based on the prior-year number of transported students and the average per-pupil transportation cost at the district's pupil-density level.

Transportation Funding. Transportation funding for school districts is calculated under the provisions of KRS 157.370. A district's funding is based on the number of students transported in the prior year and the average per-pupil transportation cost at the district's pupil density level. Districts are grouped according to pupil density; county and independent districts are treated separately. The formula is based on the premise that as a district's student population density increases, the cost to transport each child decreases. An adjustment is made for growth in the number of transported students in the current year. The transportation funding calculation is performed by KDE's Division of Data

Management and Division of District Operations. The General Assembly has appropriated \$211,953,500 a year for transportation for fiscal years 2005, 2006, and 2007. As illustrated in Table 3.8, when appropriations do not cover the cost generated by the transportation formula, the appropriations are divided by the cost to arrive at the level funded by the General Assembly

**Table 3.8
Transportation Funding Levels**

Fiscal Year	Transportation Appropriation	Transportation Cost Through Transportation Formula	% Funded
2005	211,953,500	221,438,986	95.7%
2006	211,953,500	241,340,163	87.8%
2007	211,953,500	260,737,863	81.3%

Sources: Biennial Budgets and SEEK Final calculations for respective years.

Because transportation was not fully funded in FY 2007, the amount generated by the transportation calculation is multiplied by the level funded by the General Assembly to arrive at a district's funded transportation amount as shown in Table 3.9.

**Table 3.9
Transportation Add-on Calculation**

Transportation Calculation	
(Prior Year Transportation Cost Adjusted for Growth)	1,210,129
Times: Level Funded by General Assembly (not rounded)	81.3%
Equals: Transportation Add-on Dollars	983,718

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education and its *Financial Management Manual*.

Funding to address the added costs of serving students with limited English proficiency has been provided by the General Assembly through budget language in 2005 and 2006.

Limited English Proficiency Funding. Funding to address the added costs of serving students with limited English proficiency has been provided by the General Assembly through budget language in 2005 and 2006. The prior-year child count for limited English proficiency is provided by the Division of Curriculum Development. For FY 2006 and FY 2007, the weight for students with limited English proficiency has been 7.5 percent (that is, the prior-year child count for limited English proficiency is multiplied by 7.5 percent of the guaranteed base) as shown in Table 3.10.

Table 3.10
Limited English Proficiency Add-on Calculation

Guaranteed Base	3,508
Times: LEP Weight Factor	0.075
Times: Prior Year LEP Child Count	7
Equals: LEP Add-on Dollars	<u>1,842</u>

Note: LEP is limited English proficiency.

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education.

Adjusted SEEK Base Funding

Table 3.11 shows the impact on SEEK funding of the add-ons for various types of students and for transportation. The table reflects the funding of a selected district and is intended as an example of the information calculated for and provided to each district.

Table 3.11
Adjusted SEEK Base Funding

Guaranteed Base	8,511,110
Plus: At-risk	756,149
Plus: Home and Hospital	25,560
Plus: Exceptional Child	1,913,053
Plus: Transportation	983,718
Plus: LEP	<u>1,842</u>
Equals: Adjusted SEEK Base Funding	12,191,432

Note: LEP is limited English proficiency.

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education.

Required Local Effort and Calculated State Funding

The Kentucky Education Reform Act mandates that each district must levy a minimum equivalent tax rate of 30 cents per \$100 in assessed value of property and motor vehicles in the district in order to receive SEEK funding.

KRS 160.470 (9)(a) mandates that each district must levy a minimum equivalent tax rate of 30 cents per \$100 in assessed value of property and motor vehicles in the district in order to receive SEEK funding. This locally generated tax revenue is referred to as "required local effort." As shown in Table 3.12, the adjusted SEEK base funding is reduced by the amount of the minimum local effort, and what remains is the calculated state portion of SEEK.

Table 3.12
Required Local Effort and Calculated State Portion

Property Assessment	512,765,028
Plus: Motor Vehicle Assessment	<u>90,637,023</u>
Equals: Total Assessment	603,402,051
Times: Required Local Effort	<u>0.0030</u>
Equals: Required Local Effort Dollars	1,810,206
Adjusted SEEK Base Funding	12,191,432
Less: Required Local Effort	<u>1,810,206</u>
Equals: Calculated State Portion	10,381,226

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education.

Tier I Funding

Through "Tier I," school boards may increase revenue above the minimum required local effort, up to 15 percent of the revenue generated through the adjusted SEEK base funding. The state equalizes the local revenue districts raise in Tier I at 150 percent of the statewide average per-pupil assessment.

Through a level of funding that is called "Tier I," school boards may increase revenue above the minimum required local effort, up to 15 percent of the revenue generated through the adjusted SEEK base funding. As noted in Chapter 1, funds received through the guaranteed base plus any add-ons comprise the adjusted SEEK base. The state equalizes the local revenue districts raise in Tier I at the level of 150 percent of the statewide average per-pupil assessment. This is referred to as the equalization level. The General Assembly sets the equalization level for each biennium through budget language. The equalization levels for FY 1991 through FY 2007 are presented in Table 3.13.

Through Tier I equalization, the state guarantees districts whose property wealth—defined as per-pupil assessment—is at or below the equalization level that their additional local levy will produce the same total revenue per pupil. As illustrated in Table 3.14, the state contributes more to the less-wealthy district than it does to the wealthier district due to the percent each district contributes locally. Districts whose per-pupil assessments exceed the equalization level do not receive state Tier I equalization funding since their entire Tier I dollars are provided through revenue generated by their local tax effort.

In Table 3.14, the additional revenue raised through Tier I is provided for the purpose of understanding equalization; however, Table 3.15 contains an example of the entire Tier I calculation.

Table 3.13
Equalization Levels for FY 1991-FY 2007

Fiscal Year	Equalization Level
1991	\$225,000
1992	\$225,000
1993	\$280,000
1994	\$280,000
1995	\$295,000
1996	\$295,000
1997	\$365,000
1998	\$365,000
1999	\$410,000
2000	\$410,000
2001	\$470,000
2002	\$470,000
2003	\$545,000
2004	\$545,000
2005	\$587,000
2006	\$587,000
2007	\$637,000

Source: Kentucky Department of Education.

Table 3.14
Illustration of Equalization

	District A Property-poor District	District B Property-rich District
Percent of Local Tier I		
Per-pupil Assessment	248,703	412,167
Divided by: Equalization Level	637,000	637,000
Equals: Percent of Local Tier I	39%	65%
(A) Additional Revenue Raised Through Tier I	1,862,676	1,862,676
Times: Percent of Local Tier I (calculated above)	39%	65%
(B) Equals: Local Tier I Dollars	727,242	1,205,234
(C) State Tier I Dollars (A) - (B)	1,135,434	657,442

Sources: Staff adaptation of a selected district's FY 2007 SEEK Final calculation and SEEK example obtained from the Kentucky Department of Education.

Table 3.15
Tier I Calculation

Base Year Levied Equivalent Rate (odd year before biennium)	0.00536
Current Year Levied Equivalent Rate	0.00547
Compare Base Year Levied Equivalent Rate to Current Year Levied Equivalent Rate. Select the lower rate and compare to the Maximum Tier I Equivalent Rate calculated as follows:	
Maximum Tier I Equivalent Calculation:	
Full Adjusted SEEK Base Funding ^a	12,417,843
Times: Maximum Tier I Participation	<u>0.15</u>
Equals: Maximum Tier I Revenue	1,862,676
Divided by: Estimated ADA with Growth	<u>2,426.20</u>
Equals: Maximum Tier I Revenue Per Pupil	768
Divided by: Higher of State Equalization Level (637,000) or Per-pupil Assessment (248,703)	<u>637,000</u>
Equals: Tier I Equivalent Rate	0.00121
Plus: Required 30 cents Local Effort	0.00300
Plus: Required 5 cents FSPK	<u>0.00050</u>
Equals: Maximum Tier I Equivalent Rate ^b	0.00471
Since the lower rate selected above exceeds the Maximum Tier I Equivalent Rate, the district receives Maximum Tier I funding, which is calculated as follows:	
Full Adjusted SEEK Base Funding ^a	12,417,843
Times: Maximum Tier I Participation	<u>0.15</u>
Equals: Maximum Tier I Revenue	1,862,676
Times: Percent of Local Tier I (not rounded)	
Per-pupil Assessment	248,703
Divided by: Equalization Level	637,000
Equals: Local Tier I Dollars	<u>727,241</u>
Maximum Tier I Revenue	1,862,676
Less: Local Tier I Dollars	<u>727,241</u>
Equals: State Tier I Dollars ^c	1,135,436

^aThe Tier I calculation is determined by assuming full funding for all add-ons is included in the adjusted SEEK base. Therefore, any components not fully funded by the General Assembly must be included in full prior to the calculation being made. As previously explained, transportation is not fully funded in this example and thus, the district's full transportation costs must be reflected in order to calculate Tier I.

^bThe maximum Tier I equivalent rate calculated in this table does not match the maximum Tier I equivalent rate calculated in Appendix A, Table A.8 because at the time the rate is calculated for tax rate purposes, estimated data is used for the full adjusted SEEK base funding and ADA with growth. However, this rate is calculated for SEEK purposes at a later date when actual data has become available.

^cRounding issue: $1,862,676.45 - 727,240.70 = 1,135,435.75$.

Sources: Staff adaptation of a selected district's FY 2007 SEEK Final calculation and SEEK example obtained from the Kentucky Department of Education.

Tier II Funding

Through “Tier II,” local school boards are permitted to increase revenue—subject to voter referendum—up to 30 percent of revenue generated through the adjusted SEEK base plus Tier I. These funds are not equalized by the state.

The final level of SEEK funding is known as “Tier II” funding. Through Tier II, local school boards are permitted to increase revenue—subject to voter referendum—up to 30 percent of the revenue generated through the adjusted SEEK base plus Tier I. These funds are not equalized by the state. As shown in Table 3.16, the maximum Tier II revenue for each district is determined by multiplying the district’s full adjusted SEEK base by 34.5 percent.³

Table 3.16
Maximum Tier II Revenue Calculation

Full Adjusted SEEK Base Funding ^a	12,417,843
Times: Maximum Tier II Participation	0.345
Equals: Maximum Tier II Revenue	4,284,156

^aThe maximum Tier II revenue calculated in this chapter does not match the maximum Tier II revenue calculated in Appendix A, Table A.9 because at the time the rate is calculated for tax rate purposes, estimated data is used for the full adjusted SEEK base funding; however, this rate is calculated for SEEK purposes at a later date when actual data has become available.

Sources: Staff adaptation of a selected district’s FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education; 702 KAR 3:275 Section 6.

Tier II was intended to serve as a cap on the amount of local revenue districts are permitted to raise in support of education to ensure that the amount of education funding for all students would be equitable. However, grandfathering and the provisions of HB 44 have allowed districts to exceed the Tier II cap.

Tier II was intended to serve as a cap on the amount of local revenue districts are permitted to raise in support of education. The intent of the cap was to ensure that the amount of education funding for all students would be equitable. However, grandfathering and the provisions of HB 44 have resulted in a number of districts exceeding Tier II. For the earliest years of education reform, only one district exceeded Tier II. However, by 2007, nine districts benefited from a combination of the grandfather provision and HB 44’s authority to raise revenue by 4 percent and were able to raise local revenue in excess of the Tier II cap. As shown in Table 3.17, districts generate Tier II revenue from local sources when their current-year levied equivalent rates exceed their maximum Tier I rates.

³ The 34.5 percent figure is derived as follows: 1.0 (the guaranteed SEEK base and add-ons) plus 0.15 (Tier I) multiplied by 0.30 (Tier II).

Table 3.17
Levied Tier II Revenue Calculation

Levied Equivalent Rate	0.00547
Less: Maximum Tier I Equivalent Rate	<u>0.00471</u>
Equals: Levied Tier II Equivalent Rate	0.00076
Times: Total Assessment	<u>603,402,051</u>
Equals: Levied Tier II Revenue	461,461

Sources: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education; 702 KAR 3:270 Section 2.

Hold Harmless Funding

Hold harmless is a provision provided in budget language that guarantees a school district will not receive less state SEEK funding per pupil than it did in FY 1992. A district could receive less overall funding than it did in FY 1992 if its enrollment declined.

Hold harmless is a provision provided in budget language that guarantees a school district will not receive less state SEEK funding per pupil than it did in FY 1992. Under this provision, 1992 per-pupil funding levels are maintained without regard to the local wealth of the school district. However, a district could receive less overall funding than it did in FY 1992 if its funded ADA has declined. As shown in Table 3.18, this sample district did not receive any additional funds through the hold harmless provision.

Table 3.18
Hold Harmless Calculation

FY 1992 Per-pupil State Funding	2,915.83
Times: Funded ADA	<u>2,426.2</u>
Equals: Hold Harmless Funding	7,074,387
Less: Current Year Calculated State Portion	10,381,226
Less: Current Year State Tier I Dollars	<u>1,135,436</u>
Equals: Hold Harmless Amount (if positive)	0

Sources: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education and its *Financial Management Manual*.

Adjustment to Appropriation

Adjustment to appropriation is a necessary adjustment when the funding levels appropriated by the General Assembly do not cover the cost generated by the formula.

Adjustment to appropriation is a necessary adjustment when the funding levels appropriated by the General Assembly do not cover the cost generated by the formula. For example, in FY 2006, there was an adjustment to appropriations of \$5.3 million. As shown in Table 3.19, there is no adjustment to appropriation in this example.

Prior-year Adjustment

When incorrect data are used in a district's SEEK calculation or corrections must be made for other reasons, the subsequent year's SEEK calculation will include a prior-year adjustment.

When incorrect data are used in a district's SEEK calculation or corrections must be made for other reasons, the subsequent year's SEEK calculation will include a prior-year adjustment. For example, in the past when a district's assessment was delayed by the Department of Revenue in performing an emergency assessment, an estimated assessment was used in the formula in the final calculation. When the actual assessment data became available, an adjustment was made in the following year to reflect the appropriate funding level for the previous year based on the actual assessment. As shown in Table 3.19, there is no prior-year adjustment in this example.

Total State Funds

As shown in Table 3.19, Tier I dollars and hold harmless funding are added, any adjustment to appropriation is subtracted, and any prior-year adjustments are added or subtracted from the calculated state portion to arrive at total state funds.

Table 3.19
Total State Funds Calculation

Calculated State Portion	10,381,226
Plus: State Tier I Dollars	1,135,436
Plus: Hold Harmless Amount	0
Less: Adjustment to Appropriation	0
Plus/Less: Prior Year Adjustment	0
Equals: Total State Funds	11,516,662

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education.

Capital Outlay Funds

Districts are provided capital outlay funds in the SEEK base for building needs. The capital outlay allotment has been set at \$100 per pupil since 1954.

Districts are provided capital outlay funds in the SEEK base for building needs. Recent budget language has permitted districts to use capital outlay funds for maintenance and property insurance upon approval of the commissioner of education. The capital outlay allotment has been set at \$100 per pupil since 1954. Districts' capital outlay funding is determined by multiplying \$100 times the funded ADA as shown in Table 3.20.⁴

⁴The attendance measure used in capital outlay funding is known as "funded ADA." This means the prior year end-of-year ADA plus any growth in ADA during the first 2 months of the current year compared to the first 2 months of the previous year. Capital outlay dollars are subtracted from total state funds to arrive at net general fund SEEK since districts are required to code these amounts to a restrictive fund within the school districts' accounting system.

Table 3.20
Capital Outlay Calculation

Funded ADA	2,426.20
Times: \$100 allotment	<u>100.00</u>
Equals: Capital Outlay Dollars	242,620

Source: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education.

State Equalization

In order to participate in the School Facilities Construction Commission program and the Facilities Support Program of Kentucky, districts are required to levy a 5-cent equivalent tax earmarked for school facilities. This levy is equalized by the state when the locally generated funds are committed to debt service.

In order to participate in the School Facilities Construction Commission program and the Facilities Support Program of Kentucky, districts are required to levy a 5-cent equivalent tax earmarked for school facilities. The revenue generated by this tax is equalized by the state when the locally generated funds are committed to debt service. Table 3.21 contains the calculation for eligibility and state equalization.

Table 3.21
State Equalization Calculation

State Equalization Eligibility Calculation:	
Assessment	603,402,051
Times: Required Tax for Facilities	<u>0.0005</u>
Equals: Amount Generated by Local FSPK	301,701
Less: Base Year Debt Service	<u>789,249</u>
Equals: Debt Service Needed for Equalization	-487,548
(If positive, bonds must be sold by October 1 of the odd numbered year to qualify for equalization the following biennium.)	
State Equalization Calculation:	
Equalization Level	637,000
Times: Required Tax for Facilities	0.0005
Times: Funded ADA	<u>2,426.2</u>
Equals: Maximum FSPK Funding	772,745
Less: Amount Generated by Local FSPK	<u>301,701</u>
Equals: State Equalization	471,044

Note: FSPK is Facilities Support Program of Kentucky.

Sources: Staff adaptation of a selected district's FY 2007 SEEK Final calculation obtained from the Kentucky Department of Education and its *Financial Management Manual*.

As discussed in Chapter 2, through recent budget language, districts have received equalization funding in addition to that just described through the following means: levying both the first and second growth nickels, levying the recallable nickel, qualifying for equalized facility funding by committing a 10-cent equivalent tax for building purposes, or having debt service equal to at least a 10-cent equivalent tax. The equalization for these 5-cent equivalent taxes is calculated in the same manner as shown in Table 3.21.

Chapter 4

Local and State Funding Analyses

Introduction

Chapter 4 builds on the previously provided descriptions of district tax rate procedures and SEEK formula calculations. This background information is used in the chapter to illustrate the interrelationships between SEEK and the school district tax structure. The purpose of this section of the report is to describe how the SEEK formula accounts for local property assessments and levied tax rate activity in a district and to demonstrate how the formula accounts for local revenue and adjusts—upward or downward—the amount of districts’ total state education funding. There are several mechanisms at work in the interaction between SEEK and tax policy, and they impact districts differently depending upon local conditions in the district. This chapter analyzes these interactions and illustrates how they can result in funding variations across districts.

Maximum Tier I Funding

Increasing numbers of districts have qualified for maximum Tier I funding through the SEEK formula over the years, as shown in Table 4.1.

Chapter 3 described the level of funding that is called “Tier I,” through which school boards may increase revenue above the minimum required local effort, up to 15 percent of the revenue generated through the adjusted SEEK base funding. As shown in Table 4.1, increasing numbers of districts have qualified for maximum Tier I funding through the SEEK formula over the years. The percentage of districts qualifying for maximum Tier I funding in FY 1993 was 70 percent. In FY 2007, 93 percent qualified. As Table 3.15 illustrated in Chapter 3, districts qualify for maximum Tier I funding if the lower of the base-year levied equivalent rate or the current-year levied equivalent rate meets or exceeds the maximum Tier I rate.

KDE calculated maximum Tier I funding slightly differently in the first 2 years of education reform. Districts qualified for maximum Tier I funding in FY 1991 if they levied the rate they indicated to KDE on a letter of intent. Since many districts took advantage of the incentive to raise their local tax effort and receive state equalization, the state appropriations did not cover the amount needed to fully fund state Tier I the first year.

For FY 1992, the calculation was changed again. In order to qualify for maximum Tier I funding, the lower of the current-year levied equivalent or the prior-year levied equivalent rate had to meet or exceed the maximum Tier I rate. In FY 1992, the guaranteed base increased from \$2,305 to \$2,420, and this raised the Tier I equivalent by about 1 cent. This, in turn, resulted in higher property rates being certified to districts under HB 940 than had been certified to them in FY 1991. Since many districts had increased taxes in FY 1991, they did not want to raise taxes again in FY 1992 and consequently, they did not qualify for maximum Tier I funding in the second year. As Table 4.1 shows, only 40 districts qualified for maximum Tier I equalization in FY 1992.

Historically, the amount of the guaranteed base increases in the second year of each biennium, while the equalization level remains the same. This results in higher property rates being certified to districts under HB 940.

Historically, the amount of the guaranteed base increases in the second year of each biennium, while the equalization level remains the same. This results in higher property rates being certified to districts under HB 940. Districts have generally chosen not to raise taxes and have not qualified for maximum Tier I funding in the second year of the biennium. This explains the slight decrease in the number of districts qualifying for full Tier I funding every other year (Goins).

Table 4.1
Tier I Funding for FY 1991-FY 2007

Fiscal Year	# of Districts Qualifying Maximum Tier I Funding	% of Qualifying Districts
1991	163	93%
1992	40	23%
1993	123	70%
1994	113	64%
1995	142	81%
1996	129	73%
1997	158	90%
1998	156	89%
1999	162	92%
2000	161	91%
2001	166	94%
2002	162	92%
2003	170	97%
2004	170	97%
2005	173	98%
2006	168	95%
2007*	163	93%

Notes: There was a total of 176 districts for all fiscal years except 2007. For FY 2007, there were 175 districts. *The number of districts qualifying for maximum Tier I funding in FY 2007 is less than the last few years because estimates for the adjusted SEEK base used by KDE in the tax program were too low. This resulted in maximum Tier I equivalent rates that were also too low, and these factors led to lower property rates under House Bill 940. Based on the tax rate calculations, it appears that 11 of the 12 districts that did not qualify for maximum Tier I funding in FY 2007 had levied at the level needed to qualify according to the estimated data. However, when the actual adjusted SEEK base was calculated in the SEEK Final calculation, it was much higher than the estimated adjusted SEEK base, resulting in higher Tier I equivalents. These districts' local effort no longer qualified them for maximum Tier I funding.

Source: Staff calculation using SEEK Final calculations obtained from the Kentucky Department of Education.

Maximum Tier II Funding

Until FY 1998, only one district's levied equivalent rate exceeded its maximum Tier II equivalent rate. That district's higher equivalent rate had been grandfathered through HB 940 provisions.

Through Tier II, local school boards are permitted to increase revenue—subject to voter referendum—up to 30 percent of the revenue generated through the adjusted SEEK base plus Tier I. These funds are not equalized by the state. Until FY 1998, only one district's levied equivalent rate exceeded its maximum Tier II equivalent rate, and that district's higher equivalent rate had been grandfathered through HB 940 provisions. However, by FY 2007, nine districts' levied equivalent rates exceeded their maximum Tier

II equivalent rates. As will be discussed below, the maximum Tier I and Tier II equivalent rates have been shrinking over time. In addition, under HB 44, districts have been able to increase tax revenue on existing real property by 4 percent a year. The combination of these factors has allowed some districts to exceed the Tier II cap specified in HB 940.

While many districts are reaching maximum Tier I and Tier II by increasing their local effort, some are reaching these funding levels not through their local effort but because the amounts of the Tier I and Tier II equivalents have been decreasing over the years.

While many districts are reaching maximum Tier I and Tier II by increasing their local effort, some are reaching these funding levels not through their local effort but because the amounts of the Tier I and Tier II equivalents have been decreasing over the years. As Table 4.2 illustrates, Tier I has been decreasing because larger increases have been made in the state equalization level than have been made in the guaranteed base. And in turn, the maximum Tier I equivalent becomes a part of the maximum Tier II equivalent. District wealth is also a factor in the decreasing Tier II equivalent. Large increases in the assessments of property and motor vehicles cause the maximum Tier II equivalent rate to decrease. Tables A.8 and A.9 in Appendix A detail the calculations for the maximum Tier I and Tier II equivalent rates.

Table 4.2
Shrinking Tier I Equivalent

Fiscal Year	Guaranteed Base	% Increase	Equalization Level	% Increase	Tier I Equivalent
1991	\$2,305		\$225,000		19.4
1992	\$2,420	5.0%	\$225,000		20.6
1993	\$2,420	0.0%	\$280,000	24%	17.5
1994	\$2,495	3.1%	\$280,000		17.3
1995	\$2,517	0.9%	\$295,000	5%	16.5
1996	\$2,593	3.0%	\$295,000		17.2
1997	\$2,673	3.1%	\$365,000	24%	14.4
1998	\$2,756	3.1%	\$365,000		15.0
1999	\$2,839	3.0%	\$410,000	12%	13.7
2000	\$2,924	3.0%	\$410,000		14.2
2001	\$3,046	4.2%	\$470,000	15%	13.0
2002	\$3,066	0.7%	\$470,000		13.2
2003	\$3,081	0.5%	\$545,000	16%	11.5
2004	\$3,191	3.6%	\$545,000		12.0
2005	\$3,240	1.5%	\$587,000	8%	11.4
2006	\$3,445	6.3%	\$587,000		11.1
2007	\$3,508	1.8%	\$637,000	9%	11.5

Source: Staff compilation of SEEK and tax data obtained from the Kentucky Department of Education.

Growth in Existing Real Estate Assessments Exceeding 4 Percent

House Bill 44 limits the increase in tax revenue from one year to the next to 4 percent.

In theory, under the Kentucky Education Reform Act, changes in local wealth that result from increases or decreases in property assessments should have no effect on total funds available to support education. When property assessments increase and districts collect more in local taxes, their state funds would be offset by an equal amount. However, HB 44 limits the increase in tax revenue from one year to the next to 4 percent. This means when property assessment values increase at a rate that would result in tax receipts of more than 4 percent over the previous year's revenue, tax rates must be reduced to bring tax revenues down to no more than 4 percent above the previous year. Per KRS 160.470 (3c), the 4 percent limitation applies to existing real property only, which excludes new property. Table 4.3 shows the number of districts for which increases in the assessed value of their existing real property exceeded 4 percent from FY 1991 through FY 2007.

There is an important disparity between the 4 percent limitation found in HB 44 and the method by which districts' SEEK funding is calculated. Districts' state SEEK calculations are based on their property assessments rather than on the actual revenue generated by the assessments. Permissive taxes, new property, and motor vehicle taxes, which are not subject to the HB 44 limitation, may offset the impact of the conflict between the 4 percent limit on revenue and the SEEK calculation's use of assessment rather than revenue.

There is an important disparity between the 4 percent limitation found in HB 44 and the method by which districts' SEEK funding is calculated. Districts' state SEEK calculations are based on their property assessments rather than on the actual revenue generated from the assessments. In other words, the SEEK calculation does not factor in House Bill 44's 4 percent limitation on local revenue generated from growth in districts' assessments from existing real estate property. Consequently, when school districts' property assessments from existing real estate property grow by more than 4 percent per year but their property tax collections are limited to 4 percent growth, districts' state SEEK funds will decrease by more than they are allowed to collect in local taxes from this property. The number of districts that has been impacted by this is shown in Table 4.3. However, other factors also contribute to the amount of total revenue districts are able to collect. Permissive taxes, new property, and motor vehicle taxes, which are not subject to the HB 44 limitation, may offset the impact of the conflict between the 4 percent limit on revenue and the SEEK calculation's use of assessment rather than revenue.

Table 4.3
Growth in Districts' Existing Real Property
Assessment Above 4 Percent
FY 1991-FY 2007

Fiscal Year	# of Districts Existing Real Estate Property Assessment Growth is Greater than 4%
1991	108
1992	72
1993	62
1994	62
1995	96
1996	60
1997	73
1998	57
1999	63
2000	75
2001	69
2002	54
2003	51
2004	51
2005	42
2006	53
2007	65

Source: Staff compilation of tax data obtained from the Kentucky Department of Education.

In March 2006, KDE received a report by a consulting group hired by the department to analyze specific questions related to SEEK that had been raised by superintendents and district finance officers.

In March 2006, KDE received a report by the consulting group Augenblick, Palaich and Associates, Inc. (APA), which the department had hired to analyze specific questions related to SEEK that had been raised by superintendents and district finance officers. One of the issues APA was asked to address concerned the method used in the SEEK formula to measure and account for district wealth. APA concluded that “since the vast majority of tax wealth in the state is derived from property values, using this tax base as the primary determinant of overall district wealth is logical for SEEK’s purposes” (Augenblick 40). To address anomalies in the way SEEK interacts with HB 44, APA suggested that the state consider altering SEEK so that it views districts’ wealth in terms of their *accessible* property value. In other words, if a district’s property wealth increased beyond 4 percent in a given year because of increases in the assessed value of real property, APA recommended that the SEEK calculation incorporate the assumption that the district’s wealth has grown only by HB 44’s limit of 4 percent. This recommendation has become known as the “accessible assessment” recommendation.

Since APA did not specifically distinguish between the types of property that districts levy taxes on, for purposes of the analysis below, staff has defined accessible assessment as follows.

- Prior-year real estate multiplied by 1.04 (to allow for a 4 percent increase); plus
- Current-year new property; plus
- Current-year personal property; plus
- Current-year motor vehicles

Table 4.4 presents the estimated impact of adopting the consultant's suggestion.

Table 4.4 presents the estimated impact of adopting the APA suggestion. Specifically, the analysis calculates the difference between the state funding districts received from FY 1998 through FY 2007 and the funding that would have been received (including nickel equalizations) based on the proposed definition of accessible assessment.¹ As noted earlier, under the current SEEK formula, when school districts' property assessments grow by more than 4 percent per year but their property tax collections are limited to 4 percent growth, districts' state SEEK funds will generally decrease by more than they are allowed to collect in local taxes.

In the simulation illustrated in Table 4.4, the accessible assessment definition was used if it generated a lower assessment for districts. If a higher assessment was generated, the certified assessment was used, and these districts would not have received additional state funds through SEEK. Over the 10-year period, districts would have received a yearly average of \$4.76 million in additional state funds. The additional revenue ranges from \$2.2 million to \$6.8 million a year.

¹ Assessments from the tax database system, which reflect the values certified by the Department of Revenue, were used rather than the assessments from the SEEK Final calculations for this comparison. Depending on the year, there are various differences between the two assessments. For example, an estimated assessment may have been used for SEEK purposes if the assessment was not timely certified; however, the tax database would reflect the values of the certified assessment.

Table 4.4
State Revenue Difference Between Accessible
Assessment and Certified Assessment

Fiscal Year	Additional State Funding Required Using Accessible Assessment
1998	2,254,488
1999	4,337,641
2000	5,400,292
2001	6,298,171
2002	6,817,177
2003	4,077,070
2004	3,497,104
2005	2,813,982
2006	5,292,679
2007	6,873,843

Note: Assessments from the tax database system, which reflect the values certified by the Department of Revenue, were used rather than the assessments from the SEEK Final calculations for comparison to the accessible assessment. Depending on the year, there are various differences between the two assessments. For example, unmined coal was used to calculate tax rates in FY 1999 but was not used in SEEK until FY 2000. Adjustments for taxing status of aircraft, watercraft, and inventory in transit and estimated assessments are additional reasons why the two assessments may not match.

Source: Staff simulation using assessment data obtained from the Kentucky Department of Education.

Real Estate Rates Greater or Less Than Maximum Tier I

Revenue is impacted in ways that vary across districts depending on whether districts' property tax rates are above or below their maximum Tier I equivalent rates.

The interaction between the SEEK formula's use of property assessments and HB 44's limit on real property tax increases, described earlier, illustrates one incongruity in the way districts' education funds are derived. In this section, another issue is analyzed: revenue is impacted in ways that vary across districts depending on whether districts' property tax rates are above or below their maximum Tier I equivalent rates.

Holding all other variables constant in the SEEK formula, as total local property assessments increase, districts' state SEEK funds are reduced. School districts with tax rates above their maximum Tier I equivalent rates collect more in local taxes than they lose through a decrease in their state SEEK funds. In contrast, school districts with property tax rates lower than their maximum Tier I equivalent rates do not collect more in local taxes than the reduction in their

state SEEK funds. These unintended consequences may be mitigated or worsened by the mix of taxes the districts levy. For example, some districts increase local effort to qualify for Tier I funding by adding a permissive tax rather than increasing their property tax rate. The permissive tax may or may not offset this net impact on revenue.

Staff estimated the impact of the assessment change on district revenue and examined variations in the impact depending on whether districts' tax rates were above or below maximum Tier I equivalent rates. This analysis is presented in Table 4.5.

Staff estimated the impact of the assessment change on district revenue and examined variations in the impact depending on whether districts' tax rates were above or below maximum Tier I equivalent rates. This analysis is presented in Table 4.5. The estimation compares two SEEK calculations: the current-year SEEK revenue, which uses current-year property assessment data; and the same SEEK calculation using prior-year property assessment data. Thus, the analysis holds constant all other components of the SEEK formula and isolates the impact of changes in property assessments from one year to the next.² The analysis also calculates the difference between local tax revenues to illustrate the increase in local funds from year to year as the assessment of local property values increases. Tax receipts include collections from property tax, motor vehicle tax, and permissive tax. Finally, in order to assess the overall impact of decreases in state funding brought about by increases in local revenue, Table 4.5 shows the net revenue to districts. The net revenue shows whether districts collected more or less in local revenue than their SEEK funds were reduced when growth in property assessments is accounted for.

The analysis in Table 4.5 is presented in two parts. Panel 1 includes those districts whose real estate rates were less than their maximum Tier I equivalent rates. Panel 2 includes districts whose real estate rates were greater than their maximum Tier I equivalent rates. As the table shows, districts in Panel 2 whose rates were greater than their maximum Tier I equivalent rates consistently experienced a positive net funding amount. In other words, they collected more in local tax revenues than they lost through reductions to SEEK state funds. Turning to districts in Panel 1 whose rates were less than their maximum Tier I equivalent rates, in some years net funding was negative, reflecting the fact that these districts lost more in state funds than was offset by increases in local revenue. Although in other years net funding was positive, the overall per-pupil revenue of districts in Panel 1 was substantially less than net revenue for districts in Panel 2. Thus, it

² Nickel equalizations were included in the analysis. While there are other ways to conduct this analysis, the results are consistent with those presented here.

appears that permissive taxes did not always offset the net impact on revenue.

Table 4.5
Illustration of Assessment Impact When Districts' Real Estate Rates Are Greater or Less Than Maximum Tier I Equivalent Rates

Panel 1: Districts With Real Estate Tax Rates Less Than Maximum Tier I Equivalent Rates

Fiscal Year	Assessment Impact on State SEEK Funding	Increase in Local Tax Revenue	Net State and Local Funding	Per-pupil Net State and Local Funding	# of Districts With Real Estate Rates Less Than Maximum Tier I Equivalent Rates
1999	(13,496,230)	25,521,439	12,025,209	37	120
2000	(26,525,936)	17,173,314	(9,352,622)	(29)	122
2001	(25,629,162)	27,838,951	2,209,789	7	118
2002	(18,958,863)	15,251,857	(3,707,006)	(13)	115
2003	(14,792,609)	22,790,337	7,997,728	28	111
2004	(13,276,979)	24,587,969	11,310,990	45	100
2005	(14,294,366)	20,091,725	5,797,359	23	97
2006	(22,895,054)	21,825,363	(1,069,691)	(4)	97
2007	(14,283,655)	21,176,795	6,893,140	32	88

Panel 2: Districts With Real Estate Tax Rates Greater Than Maximum Tier I Equivalent Rates

Fiscal Year	Assessment Impact on State SEEK Funding	Increase in Local Tax Revenue	Net State and Local Funding	Per-pupil Net State and Local Funding	# of Districts With Real Estate Rates Greater Than Maximum Tier I Equivalent Rates
1999	(14,047,121)	51,416,139	37,369,018	151	56
2000	(25,724,670)	28,261,051	2,536,381	10	54
2001	(27,309,680)	52,357,460	25,047,780	100	58
2002	(22,555,597)	32,979,820	10,424,223	38	61
2003	(13,933,090)	46,946,757	33,013,667	117	65
2004	(28,139,194)	66,013,806	37,874,612	117	76
2005	(23,030,625)	65,835,319	42,804,694	130	79
2006	(40,662,228)	71,380,161	30,717,933	92	79
2007	(41,372,726)	90,274,635	48,901,909	133	87

Notes: This analysis presents the difference between two SEEK calculations: the current-year SEEK revenue, which uses current-year property assessment data, and the same SEEK calculation using prior-year property assessment data.

Source: Staff simulation using SEEK Final calculations and annual financial reports obtained from the Kentucky Department of Education.

Impact on Local, State, and Combined Local and State Funds

The analysis that follows examines the varying levels of local revenue, state revenue, and combined local and state revenue, by placing districts into groups according to specific local characteristics.

The previous sections describe instances in which district revenue is impacted by a number of factors, such as changes in property assessments, whether districts' property taxes are above or below maximum Tier I equivalent rates, and interactions between the SEEK formula and HB 44. The analysis demonstrates that these factors can affect districts differently depending on local district characteristics. The analysis that follows examines the varying levels of local revenue (Table 4.6), state revenue (Table 4.7), and combined local and state revenue (Table 4.8), by placing districts into groups according to specific local characteristics. Table 4.9 shows per-pupil property assessments by district categories, as described below. Table 4.10 summarizes the local, state, and combined local and state revenue and district property assessment wealth by district category.

It is important to note that there are many different factors to consider in grouping districts. Staff selected the groups presented here based on the items covered in this report. Local revenue reviewed in this analysis includes tax collections from property tax, motor vehicle tax, and permissive tax. State revenue includes SEEK and the various state equalization payments. Revenue disparities discussed below are based on the following district groupings; data are analyzed for FY 1998 through FY 2007, and revenues for the groups are compared to the state average for these years.³

Grandfathered Districts

For those districts whose FY 1990 levied equivalent rates are higher than the current year's maximum Tier I equivalent rate, the KERA Grandfather provision allows them to continue levying local taxes at their FY 1990 level.

For those districts whose FY 1990 levied equivalent rates are higher than the current year's maximum Tier I equivalent rate, the KERA Grandfather provision allows them to continue levying local taxes at their FY 1990 level. Forty districts were grandfathered all 17 years. These were the districts selected for this group. As Table 4.6 illustrates, this group's local revenue is much higher than the state average, while Table 4.7 shows that the state revenue for these districts is below the state average. However, the combined local and state revenue of the grandfathered districts, shown in Table 4.8, reflects net revenue much higher than the state average. This group tends to be wealthier than the state average because this group's per-pupil assessment is substantially higher than the state average per-pupil assessment as shown in Table 4.9.

³FY 1998 was selected for this comparison because it was the first year all districts were utilizing MUNIS, the statewide financial accounting system.

First and Second Growth Nickels

Districts experiencing growth in the number of students served per KRS 157.621 can levy a 5-cent equivalent tax—known as a growth nickel—for building fund needs. In 2003 and 2005 budget language, legislators authorized a second growth nickel for districts continuing to meet the criteria in KRS 157.621 plus state equalization of the first growth nickel.

Districts experiencing growth in the number of students served in accordance with KRS 157.621 can levy a 5-cent equivalent tax—known as a growth nickel—for building-fund needs. In 2003 and 2005 budget language, legislators authorized a second growth nickel for districts continuing to meet the criteria in KRS 157.621 plus state equalization of the first growth nickel. Twenty-two districts have levied both growth nickels and are included in this group. As shown in Table 4.6, this group’s local revenue was close to the state average until FY 2004 when the second growth nickel became available. For FY 2004 and following years, the group’s local revenue exceeded the state average. This group’s state revenue and combined local and state revenue are slightly below the state average as shown in Tables 4.7 and 4.8. This group tends to be wealthier than the state average because its per-pupil assessment, shown in Table 4.9, is substantially higher than the state average per-pupil assessment.

Real Estate Assessment Increases Greater Than 4 Percent

There are 43 districts whose existing real property assessments grew by more than 4 percent at least five times from FY 1998 to FY 2007.

There are 43 districts whose existing real property assessments grew by more than 4 percent at least five times from FY 1998 to FY 2007. Some of these districts experienced property assessment growth greater than 4 percent in all 10 years. New property was excluded for this calculation since the 4 percent provision of HB 44 excludes new property. This group’s local revenue exceeds the state average as shown in Table 4.6, and their state revenue is less than the state average as shown in Table 4.7. The combined local and state revenue for this group of districts is higher than the state average as shown in Table 4.8. As Table 4.9 shows, this group tends to be wealthier than the state average because its per-pupil assessment is substantially higher than the state average per-pupil assessment.

Met Maximum Tier I With Property Combination

In FY 1991, 99 out of 163 districts that qualified for maximum Tier I funding did so by increasing property taxes in combination with other taxes.

In FY 1991, 99 out of 163 districts that qualified for maximum Tier I funding did so by increasing property taxes in combination with other taxes. Districts did this in several ways. For example, some districts added a permissive tax in addition to increasing property and motor vehicle taxes; others added a permissive tax in addition to increasing property taxes; and other districts chose to increase property and motor vehicle taxes. This group’s local revenue is less than the state average as shown in Table 4.6, and as Table 4.7 illustrates, its state revenue is more than the state

average. The combined local and state revenue of this group is lower than the state average as shown in Table 4.8. This group tends to be less wealthy than the state average as reflected by the per-pupil assessments in Table 4.9; its assessments are substantially lower than the state average per-pupil assessment.

Met Maximum Tier I Without Increasing Property Taxes

In FY 1991, 15 out of 163 districts that qualified for maximum Tier I funding did not increase property taxes to reach this funding level.

In FY 1991, 15 out of 163 districts that qualified for maximum Tier I funding did not increase property taxes to reach this funding level. Instead, some districts added a permissive tax in addition to increasing motor vehicle taxes; others added a permissive tax only or increased motor vehicle taxes only. This group's local revenue is less than the state average as shown in Table 4.6, and its state revenue is more than the state average, as shown in Table 4.7. Combined local and state revenue, shown in Table 4.8, is lower than the state average. This group tends to be less wealthy than the state average; its per-pupil assessments in Table 4.9 are substantially lower than the state average.

Met Maximum Tier I by Increasing Property Taxes

In FY 1991, 40 out of 163 districts that qualified for maximum Tier I funding did so by increasing property taxes.

In FY 1991, 40 out of 163 districts that qualified for maximum Tier I funding did so by increasing property taxes. This group's local revenue is more than the state average as shown in Table 4.6, and its state revenue is less than the state average as shown in Table 4.7. Overall, this group has combined local and state revenue that is higher than the state average as shown in Table 4.8. Per-pupil assessments in Table 4.9 illustrate that this group tends to be wealthier than the state average.⁴

Real Estate Rate Exceeds Maximum Tier I Rate

Forty-eight districts' real estate rates exceeded their maximum Tier I rate each year for 10 years, from fiscal years 1998 through 2007.

Forty-eight districts' real estate rates exceeded their maximum Tier I rate each year for 10 years, from fiscal years 1998 through 2007. This group's local revenue is more than the state average as shown in Table 4.6, its state revenue is less than the state average as shown in Table 4.7, and the combined local and state revenue is higher than the state average as shown in Table 4.8. This group tends to be wealthier than the state average because its per-pupil assessment is higher than the state average per-pupil assessment as shown in Table 4.9.

⁴The remaining nine districts that qualified for maximum Tier I funding did so because higher rates were grandfathered and, thus, these districts did not have to increase their local effort to reach Tier I.

Real Estate Rate Does Not Exceed Maximum Tier I Rate

Eighty-three districts' real estate rates did not exceed their maximum Tier I rate in any year for 10 years, from fiscal years 1998 through 2007.

Eighty-three districts' real estate rates did not exceed their maximum Tier I rates in any year for 10 years, from fiscal years 1998 through 2007. This group's local revenue is less than the state average as shown in Table 4.6, and its state revenue is more than the state average as shown in Table 4.7. The combined local and state revenue is lower than the state average as shown in Table 4.8. The per-pupil property assessments shown in Table 4.9 demonstrate that this group tends to be less wealthy than the state average.

Unmined Coal

Twenty-nine districts have unmined coal assessments exceeding \$300,000 each year. Unmined coal assessments tend to swing widely depending on the stage of the coal when it is assessed.

Although not previously discussed, unmined coal tax is a source of revenue for approximately 38 districts. Unmined coal revenue has been a topic of interest to the General Assembly. Twenty-nine districts have unmined coal assessments exceeding \$300,000 each year.⁵ Unmined coal assessments tend to swing widely depending on the stage of the coal when it is assessed. This group's local revenue is less than the state average as shown in Table 4.6, and its state revenue is more than the state average as shown in Table 4.7. Considered together, this group's local and state revenue is lower than the state average as shown in Table 4.8. This group tends to be less wealthy than the state average because its per-pupil assessment is substantially lower than the state average per-pupil assessment as shown in Table 4.9.

⁵In order to study the revenue impact for this group of districts, those districts with unmined coal assessments less than \$300,000 were excluded.

Table 4.6
Per-pupil Local Revenue, FY 1998-FY 2007

Group Type	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.
Grandfathered	2,701	2,900	3,048	3,302	3,419	3,581	3,713	3,943	4,217	4,478
1st and 2nd Growth Nickels	1,592	1,727	1,840	1,985	2,059	2,152	2,510	2,618	2,747	2,882
Real Estate Increases Greater Than 4 Percent	2,092	2,277	2,372	2,568	2,665	2,789	2,966	3,147	3,334	3,545
Met Maximum Tier I With Property Combination	1,192	1,320	1,369	1,480	1,548	1,633	1,798	1,901	1,992	2,126
Met Maximum Tier I Without Property	1,070	1,157	1,239	1,332	1,383	1,461	1,561	1,649	1,728	1,782
Met Maximum Tier I With Property	2,451	2,622	2,761	2,992	3,101	3,249	3,382	3,583	3,821	4,058
Real Estate Rate Greater Than Maximum Tier I	2,406	2,628	2,743	2,980	3,082	3,234	3,419	3,626	3,829	4,065
Real Estate Rate Less Than Maximum Tier I	954	1,035	1,081	1,158	1,205	1,273	1,370	1,449	1,530	1,617
Unmined Coal	948	1,094	1,058	1,123	1,175	1,253	1,313	1,393	1,462	1,605
State Average	1,590	1,729	1,813	1,961	2,045	2,155	2,309	2,443	2,582	2,749

Source: Staff compilation of property tax, motor vehicle tax, and permissive tax collections from annual financial reports obtained from the Kentucky Department of Education.

Table 4.7
Per-pupil State Revenue, FY 1998-FY 2007

Group Type	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.
Grandfathered	2,631	2,703	2,723	2,779	2,727	2,802	2,865	2,892	3,100	3,127
1st and 2nd Growth Nickels	2,839	2,939	2,950	3,091	3,072	3,213	3,290	3,399	3,584	3,672
Real Estate Increases Greater Than 4 Percent	2,856	2,946	2,965	3,065	3,018	3,108	3,175	3,238	3,434	3,485
Met Maximum Tier I With Property Combination	3,259	3,391	3,432	3,623	3,607	3,759	3,859	3,951	4,148	4,242
Met Maximum Tier I Without Property	3,330	3,463	3,501	3,714	3,746	3,924	4,020	4,129	4,371	4,463
Met Maximum Tier I With Property	2,722	2,807	2,823	2,900	2,850	2,935	3,006	3,057	3,270	3,311
Real Estate Rate Greater Than Maximum Tier I	2,687	2,761	2,772	2,849	2,812	2,901	2,956	3,003	3,193	3,235
Real Estate Rate Less Than Maximum Tier I	3,493	3,644	3,704	3,918	3,908	4,067	4,183	4,274	4,482	4,583
Unmined Coal	3,618	3,766	3,826	4,077	4,086	4,243	4,373	4,493	4,708	4,816
State Average	3,104	3,222	3,255	3,409	3,382	3,511	3,599	3,676	3,883	3,960

Source: Staff compilation of SEEK Final calculations and state equalization payments obtained from the Kentucky Department of Education.

Table 4.8
Per-pupil Local and State Revenue, FY 1998-FY 2007

Group Type	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.	Per-pupil Rev.
Grandfathered	5,332	5,603	5,771	6,080	6,145	6,383	6,578	6,835	7,318	7,605
1st and 2nd Growth Nickels	4,431	4,666	4,790	5,076	5,132	5,365	5,800	6,016	6,330	6,555
Real Estate Increases Greater Than 4 Percent	4,948	5,223	5,336	5,633	5,682	5,897	6,141	6,384	6,769	7,030
Met Maximum Tier I With Property Combination	4,451	4,712	4,800	5,103	5,155	5,392	5,656	5,852	6,140	6,369
Met Maximum Tier I Without Property	4,401	4,620	4,740	5,046	5,129	5,385	5,581	5,777	6,099	6,245
Met Maximum Tier I With Property	5,173	5,429	5,584	5,892	5,950	6,184	6,388	6,640	7,091	7,370
Real Estate Rate Greater Than Maximum Tier I	5,092	5,389	5,515	5,829	5,894	6,136	6,376	6,629	7,022	7,301
Real Estate Rate Less Than Maximum Tier I	4,448	4,679	4,784	5,076	5,113	5,340	5,553	5,723	6,012	6,200
Unmined Coal	4,566	4,859	4,884	5,201	5,261	5,496	5,685	5,886	6,170	6,421
State Average	4,694	4,950	5,068	5,369	5,426	5,666	5,908	6,119	6,465	6,709

Source: Staff compilation of SEEK Final calculations, state equalization payments, and annual financial report data obtained from the Kentucky Department of Education.

Table 4.9
Per-pupil Property Assessments, FY 1998-FY 2007

Group Type	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment	Per-pupil Assessment
Grandfathered	361,760	377,767	405,633	443,836	470,187	483,156	505,316	523,033	552,361	581,871
1st and 2nd Growth Nickels	289,603	308,248	334,514	359,869	374,922	381,913	404,742	418,592	440,042	456,773
Real Estate Greater Than 4 Percent	314,448	330,016	357,651	390,322	414,047	425,214	448,817	464,892	490,583	513,752
Met Maximum Tier I With Property Combination	220,611	232,826	254,355	273,831	289,315	297,698	314,370	327,006	347,959	362,314
Met Maximum Tier I Without Property	203,137	211,991	227,135	245,287	253,696	263,808	274,306	284,419	298,718	308,734
Met Maximum Tier I With Property	342,522	356,341	384,879	420,167	445,844	457,726	479,011	494,046	520,794	546,770
Real Estate Rate Greater Than Maximum Tier I	345,173	363,255	393,314	429,158	452,943	463,813	488,285	505,192	533,365	558,896
Real Estate Rate Less Than Maximum Tier I	183,804	191,881	207,934	223,503	236,363	245,920	256,680	268,679	285,868	298,072
Unmined Coal	167,700	175,758	196,103	208,256	219,692	230,467	238,113	246,902	269,358	280,112
State Average	256,770	269,377	292,502	316,769	335,418	346,153	363,528	377,318	399,511	417,747

Source: Staff compilation of SEEK Final calculations obtained from the Kentucky Department of Education.

Table 4.10
Summary of Tables 4.6-4.9

Group Type	Local Revenue > State Average	Local Revenue < State Average	State Revenue > State Average	State Revenue < State Average	State & Local Combined Revenue > State Average	State & Local Combined Revenue < State Average	Per-pupil Assessment > State Average	Per-pupil Assessment < State Average
Grandfathered	X			X	X		X	
1st and 2nd Growth Nickels	X			X		X	X	
Real Estate Greater Than 4 Percent	X			X	X		X	
Met Maximum Tier I With Property Combination		X	X			X		X
Met Maximum Tier I Without Property		X	X			X		X
Met Maximum Tier I With Property	X			X	X		X	
Real Estate Rate Greater Than Maximum Tier I	X			X	X		X	
Real Estate Rate Less Than Maximum Tier I		X	X			X		X
Unmined Coal		X	X			X		X

Notes: > symbol denotes greater than. < symbol denotes less than. These comparisons are made in general terms for each group type.

Source: Staff summary of Tables 4.6, 4.7, 4.8, and 4.9.

Chapter 5

Summary and Conclusions

Major Issues in Tax and SEEK Provisions Impacting District Revenue

Chapter 5 summarizes the policy implications of the impact of interrelationships between taxes and SEEK.

Chapter 5 summarizes the policy implications of the impact of interrelationships between taxes and Support Education Excellence in Kentucky.

The tax processes and SEEK formula calculations described in Chapters 2 and 3 incorporate KDE's interpretation and implementation of the SEEK and tax statutes and regulations referenced in this report for fiscal years 1991 through 2007. The incongruities within the funding system that have been discussed here were components of the funding system implemented by the 1990 Kentucky Education Reform Act. Indeed, it is likely that KERA could not have won passage without some of these very components. For example, as discussed earlier, districts were allowed to continue levying local taxes at their FY 1990 level through the grandfather provision and were not required to lower their tax rates.

Tier II Cap

The grandfather provision, the shrinking of maximum Tier I and Tier II, and the provisions of HB 44 have allowed districts to exceed the Tier II cap.

Tier II was intended to serve as a cap on the amount of local revenue districts are permitted to raise in support of education. This cap was to ensure that the amount of education funding for all students would be equitable. However, grandfathering and the provisions of HB 44 have resulted in a number of districts exceeding Tier II. For the earliest years of education reform, only one district exceeded Tier II. However, by 2007, nine districts benefited from a combination of the grandfather provision and HB 44's authority to raise revenue by 4 percent and were able to raise local revenue in excess of the Tier II cap. At the same time, the shrinking maximum Tier I and Tier II equivalent rates have also allowed districts to exceed the Tier II cap.

As discussed in Chapter 4, the maximum Tier I equivalent rate has decreased over time because larger increases have been made in the state equalization level than have been made in the guaranteed base. The maximum Tier I equivalent is used to calculate the Tier I Property Tax Rate under HB 940. When the maximum Tier I

equivalent rate decreases, the Tier I Property Tax Rate also decreases. The property tax rate certified to districts under HB 940 was an attractive option in the early years of the reform. However, because the HB 940 tax rate has decreased in the later years of reform, most districts have turned to tax rates certified under HB 44. This is evident from Table 2.5 in Chapter 2, which shows the number of districts levying the various tax rate categories from fiscal years 1993 through 2007.

Tax rates certified to districts under HB 940 were higher in the early years of education reform than they are now. Once districts adopted the higher levies certified under HB 940, their subsequent adoption of HB 44 provisions has allowed them to maintain these higher levies.

District revenues have also been impacted by the intertwining of HB 940 and HB 44. In addition to the fact that tax rates certified to districts under HB 940 were higher in the early years of the reform than they are now, in the 1990s, HB 940 rates were also higher than HB 44 rates. Once districts adopted the higher levies certified under HB 940, their subsequent adoption of HB 44 provisions has allowed them to maintain these higher levies. This has occurred because while the HB 940 rate has been decreasing, HB 44's Compensating Tax Rate has permitted districts to levy tax rates that generate the same revenue from one year to the next. The 4 Percent Increase Tax Rate also has resulted in increases in tax revenue over time. In summary, the number of districts levying the HB 940 rate has steadily decreased, adoption of the HB 44 Compensating Tax Rate has remained consistent over the years, and the number levying the 4 Percent Increase Tax Rate has substantially increased.

As the maximum Tier II equivalent rate decreases, more districts are able to meet or exceed the Tier II cap without having to go to the voters for approval.

An increasing number of districts are levying tax rates that generate revenues beyond Tier I (15 percent of the adjusted SEEK base) and into Tier II (up to 30 percent of the adjusted SEEK base plus Tier I). As the Tier I equivalent rate decreases, the amount of local effort needed to exceed Tier I is also reduced. This has resulted in moving many districts' tax revenue into the Tier II level. In addition, as the maximum Tier II equivalent rate decreases, more districts are able to meet or exceed the Tier II cap without having to go to the voters for approval.

Mix of Taxes Levied by Districts

Under KERA, districts were given flexibility in how they increased their local tax effort. This decision has had consequences that were unanticipated at the time.

Under KERA, districts were given flexibility in how they increased their local tax effort. The Tier I Property Tax Rate provided for under HB 940 is dependent on the mix of taxes districts levy, which include real estate property, personal property, motor vehicle, and permissive taxes. Given the option to increase local tax effort through a mix of taxes, some districts added a permissive tax rather than increasing their property rates. This decision has had consequences that were unanticipated at the time.

Holding all other variables constant in the SEEK formula, as total local property assessments increase, districts' state SEEK funds are reduced. School districts with property tax rates above their maximum Tier I equivalent rates collect more in local taxes than their state SEEK funds decrease. In contrast, school districts with property tax rates lower than their maximum Tier I equivalent rates do not collect more in local taxes than the offset of their state SEEK funds. These unintended consequences may be mitigated or worsened by the mix of taxes the districts levy.

Growth in Existing Real Estate Assessments Exceeding 4 Percent

In theory, under KERA, changes in local wealth as evidenced by increases or decreases in property assessments should have no effect on total funds available to support education. When property assessments increase and districts collect more in local taxes, their state funds would be offset by an equal amount. However, HB 44 limits the increase in tax revenue from one year to the next to 4 percent.

In theory, under KERA, changes in local wealth as evidenced by increases or decreases in property assessments should have no effect on total funds available to support education. When property assessments increase and districts collect more in local taxes, their state funds would be offset by an equal amount. However, House Bill 44 limits the increase in tax revenue from one year to the next to 4 percent. This means when property assessment values increase at a rate that would result in tax receipts of more than 4 percent over the previous year's revenue, tax rates must be reduced to bring tax revenues down to no more than 4 percent above the previous year. Per KRS 160.470 (3c), the 4 percent limitation applies to existing real property only, which excludes new property. However, as this report has discussed, the SEEK formula incorporates property assessments rather than actual tax receipts and ignores House Bill 44's limitation on local revenue generated from growth in districts' assessments from existing real estate property.

With the adoption of KERA, it was anticipated that the HB 44 limits on revenue growth would no longer play a prevalent role in local school finance. However, as this report has demonstrated, shortly following the enactment of education reform, HB 44 tax rates became the most attractive option.

With the adoption of KERA, it was anticipated that the HB 44 limits on revenue growth would no longer play a prevalent role in local school finance. House Bill 940 allows districts to raise tax rates without limits on revenue and is not subject to hearing and recall provisions. However, as this report has demonstrated, shortly following the enactment of education reform, the tax rates under HB 44 provided the most attractive options for school districts because the rates were higher than the rate under HB 940. This has had both a positive and negative impact on local school revenue. House Bill 44 has allowed districts to continue levying tax rates at and above HB 940 levels. However, districts' increasing use of HB 44 also has meant that more districts are impacted by the fact that SEEK adjusts districts' state funding downward based on growth in property assessments despite the fact that districts are

limited to a 4 percent increase on revenue generated by the assessments.

Conclusion

The purpose of this report is to provide members of the General Assembly with a greater understanding of important elements of school finance in Kentucky. However, policy makers may use the issues highlighted here to identify areas where unintended consequences have emerged that affect districts in varying ways.

The purpose of this report is to provide members of the General Assembly with a greater understanding of important elements of school finance in Kentucky. The intent has been to provide a summary of how districts raise local revenue for education and the ways in which the SEEK program incorporates local effort and distributes state funding. For this reason, the report does not offer recommendations regarding adjustments to current policy. However, policy makers may use the issues highlighted here to identify areas where unintended consequences have emerged that affect districts in varying ways.

As noted in the report, there have been very few changes to the SEEK formula since it was first implemented in FY 1990, although there have been numerous changes in property assessment evaluation. Studies commissioned by the General Assembly and KDE have noted issues that may warrant the attention of the General Assembly, and these have been summarized in the report.

As the focus of elementary and secondary education continues to evolve and as new legislative priorities emerge, this report can assist in providing a technical review of education funding in Kentucky.

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Appendix A

Examples of Tax Rate Calculations

Appendix A contains examples of the tax calculations described in Chapter 2.

Compensating Tax Rate

The Compensating Tax Rate is the rate that when applied to the current year's property assessment, excluding new property, produces an amount of revenue equal to that produced in the preceding year. This rate may be levied without hearing or recall.

Table A.1
Compensating Tax Rate Calculation

Compensating Tax Rate I Calculation:	
Prior-year Real Estate Rate	0.00398
Times: Prior-year Real Estate Property Assessment	<u>430,326,731</u>
Equals: Prior-year Revenue From Real Estate Property	1,712,700.39
Divided by: Current-year Real Estate Property Assessment, Excluding New Property	<u>451,346,132</u>
Equals: Compensating Tax Rate I (rounded to next higher one-tenth cent)	0.0038
Compensating Tax Rate II Calculation:	
Prior-year Real Estate Rate	0.00398
Times: Prior-year Real Estate Property Assessment	<u>430,326,731</u>
Equals: Prior-year Revenue From Real Estate Property	1,712,700.39
Prior-year Personal Property Rate	0.00443
Times: Prior-year Personal Property Assessment	<u>61,301,899</u>
Equals: Prior-year Revenue From Personal Property	271,567.41
Prior-year Revenue From Real Estate Property	1,712,700.39
Plus: Prior-year Revenue From Personal Property	<u>271,567.41</u>
Equals: Total Prior-year Revenue	1,984,267.80
Divided by: Current-year Total Valuation of Property	<u>512,765,028</u>
Equals: Compensating Tax Rate II (rounded to next higher one-tenth cent)	0.00387
The Compensating Tax Rate certified to the district is the higher of the rate produced by the Compensating Tax Rate I calculation or the Compensating Tax Rate II calculation.	

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

Subsection (1) Tax Rate

The Subsection (1) Tax Rate, which refers to subsection (1) of KRS 160.470, is the rate that restricts local school boards to a tax rate that will produce no more revenue than the previous year's maximum rate. This rate is subject to the hearing and recall provisions in KRS 160.470(7)(8).

Table A.2
Subsection (1) Tax Rate Calculation

Prior-year Maximum Real Estate Tax Rate	0.00483
Times: Prior-year Real Estate Property Assessment	<u>430,326,731</u>
Equals: Prior-year Maximum Real Estate Revenue	2,078,478.11
Prior-year Maximum Personal Property Tax Rate	0.00483
Times: Prior-year Personal Property Assessment	<u>61,301,899</u>
Equals: Prior-year Maximum Personal Property Revenue	296,088.17
Prior-year Maximum Real Estate Revenue	2,078,478.11
Plus: Prior-year Maximum Personal Property Revenue	<u>296,088.17</u>
Equals: Prior-year Maximum Revenue	2,374,566.28
Divided by: Prior-year Total Valuation of Property, Excluding Homestead Exemptions	<u>491,403,230</u>
Equals: Subsection (1) Tax Rate (rounded to next lower one-tenth cent)	0.00483

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

4 Percent Increase Tax Rate

The 4 Percent Increase Tax Rate is the rate that will produce 4 percent over the amount of revenue produced by the Compensating Tax Rate. This rate is subject to the hearing provisions in KRS 160.470(7).

Table A.3
4 Percent Increase Tax Rate Calculation

Higher of Compensating Tax Rate I or II	0.00387
Times: Current-year Real Estate Property Assessment, Excluding New Property	<u>451,346,132</u>
Equals: Revenue From Existing Real Estate Property	1,746,709.53
Times: 4 Percent Increase	<u>1.04</u>
Equals: Revenue After 4 Percent Increase Applied to Existing Real Estate Property	1,816,577.91
Divided by: Current-year Real Estate Property Assessment, Excluding New Property	<u>451,346,132</u>
Equals: 4 Percent Increase Tax Rate (rounded to next lower one-tenth cent)	0.00402

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

Personal Property Tax Rates

Personal property tax rates are calculated under the Compensating Tax Rate, Subsection (1) Tax Rate, and 4 Percent Increase Tax Rate in accordance with KRS 160.470, KRS 160.473, and 702 KAR 3:275.

Table A.4
Personal Property Tax Rates Calculation

	<u>Compensating</u>	<u>Subsection (1)</u>	<u>4 Percent</u>
Real Estate			
KRS 160.470 Rates	0.00387	0.00483	0.00402
Times: Current-year Assessment	<u>457,974,326</u>	<u>457,974,326</u>	<u>457,974,326</u>
Equals: Current-year Revenue	1,772,361	2,212,016	1,841,057
Less: Prior-year Revenue	<u>1,712,700</u>	<u>1,712,700</u>	<u>1,712,700</u>
Equals: Change in Revenue	59,660	499,316	128,356
Divided by: Prior-year Revenue	<u>1,712,700</u>	<u>1,712,700</u>	<u>1,712,700</u>
Equals: Percent Increase	3.483403%	29.153704%	7.494387%
	<u>Compensating</u>	<u>Subsection (1)</u>	<u>4 Percent</u>
Personal Property			
KRS 160.470 Rates	0.00387	0.00483	0.00402
Times: Current-year Assessment	<u>54,790,702</u>	<u>54,790,702</u>	<u>54,790,702</u>
Equals: Current-year Revenue	212,040	264,639	220,259
Less: Prior-year Revenue	<u>271,567</u>	<u>271,567</u>	<u>271,567</u>
Equals: Change in Revenue	-59,527	-6,928	-51,309
Divided by: Prior-year Revenue	<u>271,567</u>	<u>271,567</u>	<u>271,567</u>
Equals: Percent Increase	-21.9199326%	-2.5512337%	-18.8935734%
If the percent increase in real estate is greater than the percent increase in personal property, the following calculation is made in accordance with the provisions of KRS 160.473:			
	<u>Compensating</u>	<u>Subsection (1)</u>	<u>4 Percent</u>
Prior-year Personal Property Revenue	271,567	271,567	271,567
Times 100 % + Percent Increase in Real Estate	<u>103.483403%</u>	<u>129.153704%</u>	<u>107.494387%</u>
Equals: Personal Property Revenue	281,027.20	350,739.37	291,919.72
Divided by: Current-year Personal Property Assessment	<u>54,790,702</u>	<u>54,790,702</u>	<u>54,790,702</u>
Equals: KRS 160.473 Personal Property Rate With Real Estate Percent Applied	0.00513	0.00640	0.00533
Prior-year Rate	0.00443	0.00443	0.00443
KRS 160.470 Tax Rate	0.00387	0.00483	0.00402
Current-year Personal Property Rate	0.00443	0.00483	0.00443
Compare KRS 160.473 Tax Rate to the Prior-year Rate, select the lower rate. Compare result to the KRS 160.470 Tax Rate and select the higher rate to determine Current-year Personal Property Rate.			

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

Motor Vehicle Tax Rate

The Motor Vehicle Tax Rate may be raised to the maximum Tier I equivalent rate allowable under KRS 157.440(1)(a). If the Motor Vehicle Tax Rate is levied under KRS 132.487 and is higher than the rate allowed under KRS 157.440(1)(a), the rate does not have to be lowered.

Table A.5
Maximum Motor Vehicle Rate Calculation

Prior-year Motor Vehicle Rate	0.00563
Compared to: Maximum Tier I Equivalent Rate	<u>0.00457</u>
Take higher of two rates for the Maximum Motor Vehicle Rate	0.00563

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

Five-cent Equivalent Tax Rate

Districts are required to levy a 5-cent equivalent tax per \$100 of assessed valuation in order to participate in the School Facilities Construction Commission (SFCC) and the Facility Support Program of Kentucky (FSPK) programs.

Table A.6
Five-cent Equivalent Tax Rate Calculation

Current-year Property Assessment	512,765,028
Plus: Current-year Motor Vehicle Assessment	<u>90,637,023</u>
Equals: Current-year Total Assessment	603,402,051
Times: Required Nickel	<u>0.0005</u>
Equals: Amount Generated by Local FSPK	301,701
Divided by: Prior-year Property Collection Rate	0.988
Divided by: Current-year Property Assessment	<u>512,765,028</u>
Equals: 5-cent Equivalent Tax (round to next higher one-tenth)	.0006

Note: The actual tax rate that districts levy to produce the 5-cent equivalent tax is greater than 5 cents because the calculation takes into consideration that the tax is only applied to real estate and personal property, not to motor vehicles, and also adjusts for the fact that districts will collect less than 100 percent of the tax. Regardless of the amount collected from the tax, districts are required to transfer the exact amount produced by 5 cents per \$100 of assessed value of property and motor vehicles to the building fund.

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

Exoneration Recovery Rate

KRS 134.590 allows districts to recover prior-year losses due to exoneration or issuance of refunds.

Table A.7
Exoneration Recovery Rate Calculation

Exoneration Recovery Rate I Calculation:	
Prior-year Real Estate Property Assessment	430,326,731
Plus: Real Estate Exonerations Assessment	<u>1,965,830</u>
Equals: Prior-year Real Estate Property Assessment With Exonerations	432,292,560
Times: Prior-year Real Estate Rate	<u>0.00398</u>
Equals: Prior-year Revenue From Real Estate Property With Exonerations	1,720,524.39
Divided by: Current-year Real Estate Property Assessment, Excluding New Property	<u>451,346,132</u>
Equals: Exoneration Recovery Rate I (rounded to next higher one-tenth cent)	0.00382
Less: Compensating Tax Rate I	<u>0.0038</u>
Equals: Difference Between Exoneration Recovery Rate I and Compensating Tax Rate I	0.00002
Exoneration Recovery Rate II Calculation:	
Prior-year Revenue From Real Estate Property With Exonerations (See above calculation.)	1,720,524.39
Prior-year Personal Property Assessment	61,301,899
Plus: Personal Property Exonerations Assessment	<u>198,156</u>
Equals: Prior-year Real Estate Property Assessment With Exonerations	61,500,505
Times: Prior-year Personal Property Rate	<u>0.00443</u>
Equals: Prior-year Revenue From Personal Property With Exonerations	272,445.24
Prior-year Revenue From Real Estate Property With Exonerations	1,720,524.39
Plus: Prior-year Revenue From Personal Property With Exonerations	<u>272,445.24</u>
Equals: Prior-year Total Property Revenue With Exonerations	1,992,969.64
Divided by: Current-year Total Valuation of Property	<u>512,765,028</u>
Equals: Exoneration Recovery Rate II (rounded to next higher one-tenth cent)	0.00389
Less: Compensating Tax Rate II	<u>0.00387</u>
Equals: Difference Between Exoneration Recovery Rate II and Compensating Tax Rate II	0.00002
Compare the difference between the Exoneration Recovery Rate I and Compensating Tax Rate I to the difference between Exoneration Recovery Rate II and Compensating Tax Rate II. The higher difference is the amount the district may add to real estate and personal property tax rates to recover prior-year losses due to refunds and exoneration.	

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education.

Tier I Tax Rate

The Tier I property tax rate, provided for under 1990 House Bill 940, is dependent on the mix of taxes levied by a district (real estate, tangible, motor vehicle, and permissive). This tax rate qualifies districts for maximum Tier I equalization and can be levied without hearing and recall.

Table A.8
Tier I Tax Rate Calculation

Maximum Tier I Equivalent Calculation:	
Estimated Full Adjusted SEEK Base Funding	11,098,769
Times: Maximum Tier I Participation	<u>0.15</u>
Equals: Maximum Tier I Revenue	1,664,815
Divided by: Estimated ADA With Growth	<u>2,453.9</u>
Equals: Maximum Tier I Revenue Per Pupil	678
Divided by: Higher of State Equalization Level (637,000) or Per-pupil Assessment (245,895)	<u>637,000</u>
Equals: Tier I Equivalent Rate (rounded to next higher one-tenth cent)	0.00107
Plus: Required 30 Cents Local Effort	0.00300
Plus: Required 5 Cents FSPK	<u>0.00050</u>
Equals: Maximum Tier I Equivalent Rate	0.00457
Tier I Tax Rate Calculation:	
Higher of Maximum Tier I Equivalent Rate or FY 1990 Equivalent Tax plus growth nickel, equalized growth nickel, or recallable nickel, if applicable	0.00457
Times: Prior-year Total Assessment	<u>576,464,732</u>
Equals: Maximum Local Revenue	2,634,444
Divided by: Prior-year Collection Rate	<u>0.977</u>
Equals: Maximum Levied Revenue	2,696,462
Less: Prior-year Permissive Tax Revenue	740,209
Less: Prior-year Motor Vehicle Revenue at 96% Collection Rate	<u>458,522</u>
Equals: Maximum Levied Property Revenue	1,497,732
Divided by: Prior-year Property Assessment	<u>491,628,630</u>
Equals: Maximum Tier I Property Tax Rate (rounded to next lower one-tenth cent)	.00304

Notes: SEEK is the Support Education Excellence in Kentucky program. ADA is Average Daily Attendance. FSPK is the Facilities Support Program of Kentucky.

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education and its *Financial Management Manual*.

Tier II Tax Rate

The Tier II property tax rate, provided for under House Bill 940, is a second tier, which is essentially a cap on local effort. Tier II allows local school boards to increase revenue—subject to voter referendum—up to 30 percent of revenue generated through the adjusted SEEK base (guaranteed base plus add-ons) plus Tier I.

Table A.9
Tier II Tax Rate Calculation

Maximum Tier II Equivalent Calculation:	
Estimated Full Adjusted SEEK Base Funding	11,098,769
Times: Maximum Tier II Participation	<u>0.345</u>
Equals: Maximum Tier II Revenue	3,829,075
Divided by: Estimated ADA With Growth	<u>2,453.9</u>
Equals: Maximum Tier II Revenue Per Pupil	1,560
Divided by: Per-pupil Assessment (245,895)	<u>245,895</u>
Equals: Tier II Equivalent Rate	0.00635
Plus: Maximum Tier I Equivalent Rate	0.00457
Equals: Maximum Tier II Equivalent Rate (rounded to next higher one-tenth cent)	0.01092
Tier II Tax Rate Calculation:	
Maximum Tier II Equivalent Rate	0.01092
Times: Prior-year Total Assessment	<u>576,464,732</u>
Equals: Maximum Local Revenue	6,294,995
Divided by: Prior-year Collection Rate	<u>0.977</u>
Equals: Maximum Levied Revenue	6,443,188
Less: Prior-year Permissive Tax Revenue	740,209
Less: Prior-year Motor Vehicle Revenue at 96% Collection Rate	<u>458,522</u>
Equals: Maximum Levied Property Revenue	5,244,457
Divided by: Prior-year Property Assessment	<u>491,628,630</u>
Equals: Maximum Tier II Property Tax Rate (rounded to next lower one-tenth cent)	.01066

Notes: SEEK is the Support Education Excellence in Kentucky program. ADA is Average Daily Attendance. Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education and its *Financial Management Manual* and 702 KAR 3:275.

Levied Equivalent Rate

Because school districts' local tax effort consists of various types of taxes and because the rates at which these revenue sources are taxed can vary, the funding system uses a levied equivalent rate to convert districts' local tax efforts to a comparable basis. The levied equivalent rate, in simple terms, is a district's total tax revenue divided by its total assessment, which includes property and motor vehicles.

Table A.10
Levied Equivalent Rate Calculation

Current-year Levied Real Estate Property Tax Rate	.00404
Times: Prior-year Real Estate Property Assessment	<u>430,326,731</u>
Equals: Levied Real Estate Property Tax Revenue	1,738,520
Current-year Levied Personal Property Tax Rate	.00445
Times: Prior-year Personal Property Assessment	<u>61,301,899</u>
Equals: Levied Personal Property Tax Revenue	272,793
Current-year Levied Motor Vehicle Tax Rate	.00563
Times: Prior-year Motor Vehicle Assessment	<u>84,836,102</u>
Equals: Levied Motor Vehicle Tax Revenue	477,627
Levied Real Estate Property Tax Revenue (calculated above)	1,738,520
Plus: Levied Personal Property Tax Revenue (calculated above)	272,793
Plus: Levied Motor Vehicle Tax Revenue(calculated above)	477,627
Plus: Prior-year Permissive Tax Revenue	<u>740,209</u>
Equals: Total Local Taxes	3,229,149
Times: Prior-year Collection Rate	<u>0.977</u>
Equals: Total Levied Tax Revenue	3,154,879
Divided by: Prior-year Total Assessment	<u>576,464,732</u>
Equals: Levied Equivalent Rate	0.00547

Source: Staff adaptation of a selected district's FY 2007 tax rate certification obtained from the Kentucky Department of Education and its *Financial Management Manual*.

Appendix B

Summary of Capital Construction Funding Sources

The following is a summary of local and state funding sources available to school districts for capital construction, which include the various nickels discussed in Chapter 2.

Capital Outlay (1954) \$100 x Adjusted Average Daily Attendance Fund 310

FSPK (Facilities Support Program of Kentucky) (1990) Fund 320

- | | | | |
|----|-------------------------|--|----------|
| 1. | Local FSPK Nickel | Assessment x Nickel | Fund 320 |
| 2. | State Equalization FSPK | State equalizes up to 150% of statewide average per-pupil assessment | Fund 320 |

SFCC (School Facilities Construction Commission) (1985)

SFCC is established to provide equitable assistance in meeting local school districts’ facilities funding needs. SFCC uses the district statement of facility construction needs and local available revenue as certified by the Kentucky Board of Education to determine the rate of participation of each school district in any given biennium. The amount allocated to school districts is based on available state funding and the percentage of a district’s unmet facility needs to the total statewide needs. Participation in the SFCC program has certain requirements. Districts must have an unmet facility need as shown on its approved facilities plan, minus available local revenue. Districts must also show a local 5-cent equivalent tax revenue budgeted for facility debt service (#1 above), and all available local revenue as of June 30 must be transferred to a restricted account for school building construction on July 1 of each year.

Growth Nickel

- | | | |
|----|--|----------|
| 1. | First Growth Nickel (1994) (KRS 157.621) | Fund 320 |
| 2. | Second Growth Nickel (2003 and 2005) (budget language) | Fund 320 |

To qualify for first growth nickel, districts must meet growth criteria, classroom space needs, and finance needs. To qualify for the second growth nickel, districts must levy the first growth nickel and continue to meet growth criteria. The local amount raised by the first growth nickel is equalized by the state after district levies the second growth nickel.

Recallable Nickel (2003, 2005, 2006) (budget language) Fund 320

Districts can levy the recallable nickel, which is subject to a voter hearing with recall. The local amount raised by the recallable nickel has been equalized by the state in years following the levy of the tax.

Equalized Facility Funding (2005 and 2006) (budget language) Fund 320

Budget language allowed local school districts that have levied at least a 10-cent equivalent tax rate for building purposes or have debt service of at least a 10-cent equivalent tax rate as of February 24, 2005 to receive equalization from the state for 20 years, provided that the districts did not receive nickel equalization other than FSPK.

Urgent Need School Trust Fund (2003 and 2005)

For the past two budget cycles, the General Assembly has set up the Urgent Need School Trust, which is established in the Finance and Administration Cabinet for the purpose of assisting school districts that have urgent and critical construction needs. To qualify in fiscal years 2004 through 2006, a local district must have the project on its approved facility plan, must be a Category 5 school as of January 13, 2005, and must be a school with or including enrollment based on best practices outlined in the Kentucky School Facility Planning Manual.

Urgent Need School Trust Fund (2006)

The Urgent Need School Trust Fund was created in budget language to assist school districts that have urgent and critical construction needs. It is administered by the School Facilities Construction Commission. The General Assembly appropriated \$5 million to the Urgent Need School Trust Fund to be distributed after July 2007. Distribution possibilities included grants, loans, matching funds, offers of assistance to meet unmet need, or as equalization funds in situations where school districts have levied additional taxes for school construction purposes.

Appendix C

Methodology for Table 2.5

Appendix C describes the methodology used for analyzing districts' taxing efforts.

As discussed in Chapter 2, in order to analyze district taxing efforts, the rates levied were categorized according to the tax rate authority selected by school districts. Staff first identified if the tax rate levies exactly matched a rate under any of the four tax provision categories. If no match existed, staff subtracted the exoneration rate from the rate levied to assess whether the rate matched any of the four categories. If no direct match was found, staff identified the taxing category that most closely matched but did not exceed the rate levied.

When a levied rate matched more than one category, staff selected the least restrictive rate in terms of legal requirements. For example, if the Subsection (1) Tax Rate was the same as the Compensating Tax Rate, the Compensating Tax Rate was selected because the Subsection (1) Tax Rate is subject to hearing and recall. If the rate levied matched more than one category by itself and when factoring in the exoneration rate, staff selected the least restrictive rate. For example, if the rate levied matched the Subsection (1) Tax Rate exactly and matched the Compensating Tax Rate plus the exoneration rate, the Compensating Tax Rate was selected.

Appendix D

Notable Changes in SEEK and Assessments, FY 1991-FY 2008

This appendix contains notable changes in the Support Education in Kentucky (SEEK) calculation and the valuation of assessments over the years.

Fiscal Year	Explanation of Changes
1991	Formula-derived state funding was adjusted to ensure that relative to the prior year (FY 1990) no district received less than an 8 percent increase or more than a 25 percent increase in its total state SEEK dollars.
1992	Formula-derived state funding was adjusted to ensure that relative to the prior year (FY 1990) no district received less than a 5 percent increase or more than a 25 percent increase in its total state SEEK dollars.
1993	Hold harmless was implemented to ensure that each district received no less than its FY 1992 state SEEK dollar amount per pupil. A vocational education deduction of 30% was applied against the base funding for any pupil in average daily attendance (ADA) who spends a portion of his or her school day in a program at a state-operated career, technical education, or vocational facility.
1997	The home and hospital (H&H) calculation was changed. Previously, the prior-year guaranteed base less \$100 was multiplied by the second semester H&H ADA and added to the current-year guaranteed base less \$100 times the first semester H&H ADA. Now, the current-year guaranteed base less \$100 is multiplied by the prior-year H&H ADA. There was a change in motor vehicle assessments. Prior years used National Automobile Dealers Association (NADA) average retail value as of January 1. The change used the mid-point between average retail and trade-in value.
1999	Motor vehicle assessments changed again to use the NADA January 1 trade-in value. Unmined coal was included on the property assessment and included in tax rate calculation for the first time.
2000	Districts could tax or exempt certain personal property (aircraft, watercraft, and inventory in transit). Assessments from this personal property are not in the Kentucky Department of Education's (KDE) tax system in FY 2000 because the Department of Revenue excluded amounts until KDE found out if districts were taxing or exempting this property. Assessments were adjusted in the SEEK database. Unmined coal was included in the property assessment used for the SEEK calculation for the first time. Unmined coal was included in tax rate calculation in FY 1999, but KDE received judicial permission to exclude these amounts in the SEEK calculation for the first year to allow districts time to adjust for the reduction in SEEK funds.
2001	Inventory in transit was taxed at 80 percent of assessed value. This began phasing out taxing inventory in transit for school purposes. The vocational education deduction was reduced from 30 percent to 15 percent.

2002	Inventory in transit was taxed at 50 percent of assessed value. The vocational education deduction was discontinued in KRS 157.360(14).
2003	Inventory in transit was no longer taxable by school districts.
2006	House Bill 272 provided for extension of utility gross receipts license tax to direct broadcast satellite and wireless cable services as an option if the school district also imposes the tax on cable services. Funding was authorized for limited English proficiency students at a weight of 0.075 of the guaranteed base.
2007	House Bill 272 eliminated public service companies' franchise value from certified assessments and replaced it with a hold harmless provision, effective January 1, 2006. The Department of Revenue distributes hold harmless monies to districts monthly.
2008	Per the court case of <i>Commonwealth of Kentucky, Finance and Administration Cabinet v. Jim Beam Brands, Co.</i> , distilled spirits' inventory is now exempt from school taxation due to the settlement of litigation regarding the classification of inventory (i.e., merchants inventory, good in process, in transit inventory). Funding was increased for limit English proficiency students by adjusting the weight from 0.075 to 0.096 of the guaranteed base.

Sources: Commonwealth. Legislative. Program; *Commonwealth of Kentucky, Finance and Administration Cabinet v. Jim Beam Brands, Co.*, No. 2006-CA-002176; Barlow. Sept. 19, 2007; Livers; Rice; Commonwealth. Dept. of Revenue.