

State Funding for School Construction

The State Program of School Construction Assistance

The state provides assistance to school districts for constructing new school buildings and remodeling existing ones. The state assistance is provided as a match for local capital revenues. “The state assistance program is based on two principles: (a) state and local school districts share the responsibility for the provision of school facilities, and (b) there is an equalization of burden among school districts to provide school facilities regardless of the wealth of the districts.” (OPR, January 2001.) State matching assistance for school construction is not part of the state’s obligation for the funding of basic education.

To be eligible for state aid for school construction, a school district must:

1. Demonstrate need, as expressed by unhoused pupils, usually from projected enrollment growth. In addition, a district can document a need for modernization assistance based on facility condition if the facility is at least 20 years old, or at least 30 years old for buildings completed after Jan. 1, 1993, *and*
2. Have already secured sufficient local funding to cover its share of the project’s cost. This requirement is usually met by securing voter approval of a bond levy.

How the School Construction Assistance Program Works

Once a school district has received approval for state matching funding, the amount of aid to which it is entitled is based on a determination of (1) matchable costs, and (2) the state share of those matchable costs.

(1) Matchable costs. The state will not provide a match for all costs incurred by a district in building or modernizing school facilities, but only for those costs eligible according to provisions of state law. A formula set in rule establishes maximum *matchable area per student*, varying by grade level and other factors. High school facilities are deemed to require more square feet per student, for example, than elementary school facilities. State assistance is also based on a *maximum area cost allowance (ACA)*; that is, the state will only match construction costs up to a certain number of dollars per square foot. OSPI calculates the maximum area cost allowance based on certain industry standards, and projects those costs into the future.

Not all the square footage in a planned school project is eligible for state matching assistance. Eligible area is limited to instructional space, and excludes athletic facilities, auditoriums and other facilities whose primary use is non-instructional.

School districts have expressed concerns that the state’s maximum area cost allowance is not sufficient to cover their costs of construction, and that this gap between what the state will pay and the costs the districts incur have caused them to have to pay for more of the actual costs of new and modernized facilities from local levies. Over time, this has contributed to a decline in the state’s share of statewide expenditures for school construction.

The Legislature responded to those complaints during the prior two biennia by substantially increasing state funding for matchable costs. The 2003-05 capital budget funded new area cost allowance standards adopted by the State Board of Education, adding \$32.5 million to the amount

the state would have spent for the same projects had the old standards been in place. The 2005-07 budget went much further, increasing both the area cost allowance and the matchable area per student, at a cost of \$64.9 million.

For most of the history of the program, the state matched costs for modernization projects at 90 percent of area cost allowance rather than the 100 percent of ACA it funded for new construction. The 2005-07 capital budget initiated a policy of funding modernization projects at 100 percent of ACA, treating new construction and modernization the same. The reasoning for the policy is that as the large number of new facilities built 20-30 years ago to accommodate rising enrollments age, a larger share of future projects will be modernization of existing schools rather than construction of new ones.

(2) State share. Once matchable costs are determined, the amount of state aid provided is determined by a matching ratio based on the relative wealth of the district. The formula, set in RCW 28A.525.166, “establishes a relationship between the adjusted assessed valuation per pupil in the individual district and the statewide adjusted assessed valuation per pupil, thus in effect measuring the district’s wealth per pupil.” (OSPI, *Organization and Financing of Schools*, 2004). The wealthier the district – that is, the greater its ability to generate a local match through local levies – the smaller the state share of matchable project costs. The formula provides assistance for projects from a hypothetical maximum of 100 percent for the property-poorest districts to a minimum 20 percent for the most property-rich.

The basic formula for determining state matching funds for a school construction project is therefore the matchable cost of the project times the percentage of state assistance. The formula is designed to provide the average district with 50 percent state aid. In practice the state share is on average considerably less, based on how much districts actually spend -- a product both of local choices in project design and the cost environment in which they go out to bid.

If state funding is insufficient to meet all approved requests, projects are funded in rank order through a priority system set in rule. The system ranks both growth-related projects, such as new buildings and additions needed to expand capacity, and condition-related projects such as modernization or replacement of existing facilities, on a scale of values measuring need, with more weight given to growth-related projects than condition-related ones. The state has had sufficient funds for school construction that it has not had to utilize the priority system since the early 1990s.

Sources of State Funding for School Construction

An amendment to the Washington Constitution in 1967 created a dedicated account, the Common School Construction Fund, to finance the state share of school construction through the sale of timber harvested on state trust lands. For about the next twenty years the Common School Construction Fund supported the entire cost of the state’s share of school construction. Beginning in the late-1980s, restrictions on the cutting of timber on state lands and other circumstances caused resources to the Common School Construction Fund to fall far short of need. The state has had to supplement timber revenue with other means of funding since that time. Alternative sources of revenue the state has utilized for school construction since 1989-91 include:

- Cash from the state general fund;
- General obligation bonds;
- The Education Savings Account, which allows some unspent General Fund appropriations to be expended for school construction instead of reverting to the General Fund;

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- The Education Construction Fund established by I-601 and amended by I-728, which is funded by the state lottery;
- The Trust Land Transfer program, which transfers unharvestable school trust lands to other public agencies while reimbursing the school trust for the value of the land and timber.

As demand for school construction assistance has risen rapidly and timber revenues have been flat or even in decline, the share of school construction grants from the state's constitutionally dedicated funding source has fallen precipitously. In the 1989-91 biennium, timber trust revenue made up 53 percent of all state resources for school construction assistance. In the 2007-09 biennium, only about 19 percent of state capital funding will come from timber trust revenue. At the same time, state general obligation bonds are assuming a much larger role in meeting the need for assistance for K-12 building projects. The amount of state bonds needed to support school construction is expected to increase sharply in the coming years.

Recent Developments in School Construction Funding

The 2005-07 capital budget included by far the largest amount of state funding for K-12 construction in the state's history. The budget provided \$641 million in school assistance grants, an increase of \$239 million (60 percent) over 2003-05, and \$159 million higher than proposed by the governor. Funding was increased from 2005-07 maintenance level by \$156 million (36 percent) through three major enhancements to the funding formula:

- (1) Increase the area cost allowance -- \$39.3 million
- (2) Increase the matchable area per student -- \$25.6 million
- (3) Fund modernization at 100% of ACA -- \$91.3 million

In addition to the large increase in matching assistance grants, the 2005-07 budget provided about \$34 million in support for other capital programs in K-12:

- \$14.6 million for vocational skills centers;
- \$6.5 million to help school districts comply with "green building" standards set in 2005 legislation;
- \$4.5 million for digital mapping to improve school security;
- \$3.0 million for a new program of grants for emergency school repairs.

The 2007-09 capital budget provided \$880 million for school construction assistance grants, \$110 million of it from state bonds. (The bonds were reduced in the 2008 supplemental for revised assumptions about eligible projects.) This was an increase of \$238 million from the already elevated funding level of 2005-07. Another \$75 million in bonds was appropriated for vocational skills centers, including three new skills centers serving the Skagit Valley, the Yakima Valley, and the Snohomish-Island County region. The small repair grant program was continued at \$4 million, and \$6.2 million was set aside to complete the mapping of all public elementary and middle schools.

The 2008 supplemental budget utilized a new bond authorization to further expand the capacity of vocational skills centers around the state. **HB 3330** authorized \$100 million in state general obligation bonds, backed by investment income in the Common School Construction Account, to finance school construction assistance grants and capital improvements related to skills centers.

The supplemental budget appropriated \$16 million from this authorization in the current biennium for skills centers, including studies of the feasibility of satellite or branch campus programs for underserved areas.

Joint Legislative Task Force on School Construction Funding

School district concerns about the adequacy and efficiency of the present state program of school construction assistance, and legislative concerns about how the state will meet the large anticipated increase in the demand for that assistance with current resources, led to the creation in the 2007-09 capital budget act of a Joint Legislative Task Force on School Construction Funding. The task force, made up of legislators and school district representatives, was directed to examine the following:

- (1) The statutory provisions regarding the funding of school construction projects
- (2) Eligibility requirements and distribution formulas for the state's school construction assistance grant program;
- (3) Flexibility needed in the system to address diverse district and geographic needs, including the construction needs unique to high-growth areas and the needs of school districts that have experienced consecutive school bond levy failures.
- (4) Potential revenue sources and alternative funding mechanisms for school construction.

The task force was to report its findings and recommendations to the Legislature by December 1, 2007. Certain incremental recommendations identified during the 2007 interim were funded in the 2008 supplemental capital budget, including development of a K-12 facility condition and inventory system pilot program by JLARC, to give the Legislature a better handle on the potential need for new and renovated school facilities, and development of regional school construction technical assistance program.

The task force fell far short, however, of the mandate in the budget act, the scope of the proviso exceeding the capacity of the members to comply with it in the time allotted. The 2008 supplemental capital budget act, EHB 2765, amended the proviso in the original capital budget act – after the fact – to provide for a preliminary report by December 2007 and a final report by January 2009.

Among the issues the task force is seeking to address in the 2008 biennium are:

- (1) Is the state's current program of matching assistance fundamentally sound, or should it be replaced with a different kind of system entirely?
- (2) Should the area cost allowance be further enhanced? Should the funding formula be modified to better recognize inflation in construction costs?
- (3) Should there be further enhancements in matchable square footage, particularly for specialized space such as science labs?
- (4) How can the current assistance formula be made more transparent in terms of underlying funding assumptions, and more understandable to the public?
- (5) What can be done to provide more timely facility assistance to fast-growing school districts?
- (6) Should state capital funding for public schools be better linked to changes in operating funding, especially as basic education requirements are re-examined by the Basic Education Finance Task Force?
- (7) What can be done to provide appropriate help to districts with low property wealth that are unable to qualify for a state matching assistance because they cannot pass local levies?

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- (8) What new or redirected revenue sources may be available to the state to increase resources for school construction?
- (9) Will the state need to resume use of the priority system for ranking eligible projects to be funded?

For the Legislature, the larger question looms of just what priority K-12 construction is going to have among the competing priorities for state capital resources. Based primarily on the “bow wave” of the 2005 enhancements (and assuming no further enrichment of the funding formula), the amount of state bonds needed to support school construction is expected to increase from \$110 million in 2007-09 to \$426 million in 2009-11, rising thereafter. With bond capacity under the state’s 9 percent debt limit currently projected to be *less* in the next biennium than in the current one, where will the state find the money to meet the anticipated demand from school districts for assistance with facilities, and how will it affect its ability to meet more traditional priorities for state bonds such as higher education? Should the Legislature assess the rapid growth in state bond expenditures in recent biennia for purposes such as housing, local government infrastructure, economic development, grants to governments and nonprofits for social services, the arts and recreation, and local community projects, so as to reprioritize some current debt capacity to K-12?

For additional information see the Joint Legislative Task Force on School Construction Funding website at: <http://www.leg.wa.gov/Joint/Committees/K12SCF/>

Issues in School Construction Funding

The landmark increase in the current budget in funding state matching assistance for K-12 construction meets real and growing needs, and reverses a long trend toward a declining state share of overall school construction expenditures. It is not, however, without some risks. While the state has increased its commitment to school construction assistance, it has not identified additional revenues with which to support it. Future legislatures may face a gap between the demand for state funding for school construction and available resources for this purpose. Providing matching funds for school projects at higher unit costs, however warranted by need, may result in the state providing support for fewer projects in total if sufficient resources cannot be cobbled together from the available funding sources. This capital budget depends on \$139 million in general obligation bonds to achieve its funding total in K-12. An OPR analysis indicates that, holding all other funding sources constant, the amount of bonds for K-12 construction would need to rise to \$242 million in 2007-09 and \$324 million in 2009-11, to maintain the current funding policy. Those figures would go higher if the state lottery falls short of present forecasts, or the demand from school districts for matching assistance is greater than anticipated. It is difficult to know how districts’ behavior will be affected by the multiple enrichments of the state funding formula made this year.

It is of course up to the Legislature to decide what the state’s priorities are in the use of its bonding capacity, and it can choose to devote a much greater share of G.O. bonds to K-12 construction than before. It is not a choice without consequences for the rest of the budget, however, as there is a more-or-less fixed amount of bonds the state can issue at any time under the debt limit. More bonds for school construction unavoidably mean less for other parts of the budget.

At the same time as the Legislature greatly increased its commitment to school construction, however, it also increased its bond capacity by passing legislation in 2005, HB 2170 (C 486 L 05), which effectively raised the constitutional debt limit by including the real estate excise tax in the revenue base for the calculation of the limit. HB 2170 enabled the Legislature to make \$180

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million more in bond appropriations than had the debt limit not been altered. This followed on 2003 legislation raising the debt limit by including the state property tax levy in the limit calculation. The statutory 7 percent debt limit under which the state worked for so long in writing its capital budget has now been replaced, as a practical matter, by an 8.5 percent working debt limit intended to keep us safely under the 9 percent constitutional limit. So in that sense the Legislature *has* identified additional resources for school construction, if only in the form of additional bonding capacity. Nevertheless, a preliminary analysis indicates that it will be very challenging to meet likely spending demands – including for school construction – under the working debt limit in 2007-09.

The current budget may give rise to other issues for school construction funding, including:

- Will the emergency school repair program initiated in this biennium at \$3.0 million be a one-time or ongoing one? What policies and procedures are needed to ensure that it does not create incentives for districts to defer maintenance and preservation in the expectation that state aid may be available?
- Will the cost to school districts of conforming to “green building” standards be greater than current estimates, and the operational efficiencies from their use as much as expected? How will school districts respond to this legislation?
- How will school districts respond to the state’s adoption of a richer formula for matching assistance? Will more districts become available for assistance than currently assumed? Will some kinds of districts tend to benefit more than others?
- Should the Legislature continue to examine state funding assumptions for matchable costs to determine if they are based on the best data, and achieving the desired results?
- How can the state best forecast the need and demand for school construction assistance in future years, and plan capital budgets accordingly?
- What should be the state’s policy for the capital funding of skills centers?

Despite criticism in recent years that the state had faltered in its commitment, school construction has been and remains one of the strengths of Washington’s school finance system. The state funds a larger share of total school construction costs than most other states, in some of which school construction remains entirely a local function. In the 2005-07 capital budget the Legislature greatly enhanced funding for matching assistance to school districts for construction and modernization of facilities, addressing some of the largest concerns that districts have brought to prior legislatures. Meeting the demand for this funding, however, will be a challenge for future legislators, requiring hard decisions about resources and priorities in the capital budget.