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CASE 5: CAMPAIGN FOR FISCAL EQUITY VS. NEW YORK[1]

Introduction

In June 2003, the New York State Court of Appeals, which is the highest court in the State, ruled that the system for funding the New York City schools violated the State's constitutional requirement to provide all children with a "sound basic education." It is now the spring of 2006, and this case, called *Campaign for Fiscal Equity vs. New York (CFE)*, is still tied up in court. Teachers, school administrators, parents, and educational interest groups are becoming increasingly frustrated with the situation, and a broad coalition, the School Aid Reform Coalition (SARC), with representatives for each of these groups, has convened a conference in Albany to explore possible solutions, both for New York City and for other troubled districts in the state. As an expert in education finance, you have been asked to participate in this conference.

Historical Background

A concise synopsis of the *CFE* case is provided on the website maintained by the Campaign for Fiscal Equity (CFE), which is a non-profit organization founded in 1993 to seek reform in New York State's education finance system.[2]

[1] This case was written by Professor John Yinger solely for the purposes of class discussion. Although it draws on the actual facts of the *CFE* lawsuit, this case is not intended to be an analysis of that suit. Unlike the other organizations in the case, SARC is not a real organization.

[2] This material is taken from the entry on New York at www.accessednetwork.org. The main website for the Campaign for fiscal equity is www.cfequity.org.

In 1978, a group of property-poor school districts, joined by the five large urban New York districts, filed Levittown v. Nyquist , to challenge the state's education finance system. In its 1982 decision, 439 N.E.2d 359, the Court of Appeals– New York State 's highest court–ruled that while substantial inequities in funding did exist, the state constitution does not require equal funding for education. However, the court also held that the state constitution guarantees students the right to the opportunity for a "sound basic education."

This right was at the center of the CFE v. State case filed in 1993 and asserting that New York State was failing in its constitutional duty to provide the opportunity for a sound basic education to hundreds of thousands of its schoolchildren. In a landmark 1995 decision, the Court of Appeals distinguished its Levittown ruling and remanded the case for trial. After a seven-month trial, Justice Leland DeGrasse rendered his decision, 719 N.Y.S.2d 475, on January 10, 2001 in favor of plaintiffs and ordered the State to ensure that all public schools provide the opportunity for a sound basic education to their students. This decision also ordered a costing-out study as the threshold task in developing a new school funding system.

- In June 2002, the intermediate-level appeals court overturned the trial-court ruling and claimed that an eighth-grade education was all the New York State Constitution required. Plaintiffs appealed, and the Court of Appeals issued its decision (CFE II) in favor of plaintiffs on June 26, 2003. The court considered school funding court rulings in other states during oral argument and its court order in favor of plaintiffs gave the State until July 30, 2004 to:
  determine the cost of providing a sound basic education
- fund those costs in each school, and establish an “accountability” system to ensure that the reforms actually provide the opportunity for
- a sound basic education.

When the July 30, 2004 deadline passed without state action, the remand judge appointed a panel of three special masters to hold hearings on the matter and make recommendations to the court. On November 30, 2004, the panel issued its Report and Recommendations and, in sum, urged the court to order the state to enact legislation within 90 days that would:

- provide an additional $5.63 billion for annual operating aid, phased in over a four-year period;
- undertake a new cost study every four years to determine the cost of a sound basic education;
- provide an additional $9.2 billion for building, renovating, and leasing facilities, phased in over a five-year period; and

- undertake a facilities study every five years, in accordance with the methodology used by CFE in its facilities analysis to develop the BRICKS Plan.

These recommendations were limited by the CFE II decision to New York City, but the panel concurred with all parties in their agreement that the state should enact a statewide remedy. In March 2005, the trial court confirmed the special masters' report and recommendations and ordered the state to comply within 90 days. The state appealed.

This appeal was heard in the fall of 2005 by the appellate division of the New York Supreme Court, which is not the highest court in the state. This court has not yet ruled, however, and it is not clear when they will. Regardless of the way this court rules, the case will undoubtedly be appealed to the Court of Appeals by one side or the other. A court solution to the *CFE* case therefore appears unlikely to be in place in time for the 2006-2007 school year.

Elected officials do not, of course, have to wait for the court to come up with a remedy. Hence, there is growing pressure on the state legislature to get to work on a plan right away and not to wait for the appeals process to play itself out. More and more voters and interest groups are saying that the children in New York City and other poor districts should not have to wait another year to get the funding required by the New York State Constitution. That is why SARC has organized its conference.

Disparities

The student performance disparities at the heart of the *CFE* case are very large; because New York City makes up such a large share of the state's student population, however, these disparities are often underestimated. An article in *The New York Times,* for example, provided misleading information on about the disparities on the State's 2004 fourth- and eighth-grade English language arts tests.[3] According to this article, 49.5 percent of the City's fourth graders passed this test compared to 62.2 percent of fourth graders in the state as a whole. These numbers are correct but misleading, because the City contains about 40 percent of the students in the state and the State figure reflects the low performance of the City's students. A better comparison would be between the passing rate in the City (49.5 percent) and the passing rate in the rest of the State (70.7 percent). The eight-grade scores are presented in the same way. New York City's passing rate (35.6

[3] Elissa Gootman, "How City Students Fared on the State English Exam." *The New York Times*, June 6, 2004.

percent) is farther below the passing rate in the rest of the state (54.9 percent) than below average passing rate for the state as a whole, including New York City (47.2 percent).

New York City is not, of course, the only district with a relatively low student performance. In an article published right before the *CFE* decision was announced, Professors William Duncombe and John Yinger, from The Maxwell School at Syracuse University, and Professor Anna Lukemeyer of the University of Nevada at Las Vegas (henceforth D/L/Y) published an article on education finance in New York State.[4] This article developed a district-level index of student performance in 2000 based on the passing rates for fourth- and eighth-grade math and English exams and for high school Regents exams in the same subjects. The Regents exam scores were given twice as much weight because they are required for high school graduation. This index has a maximum value of 200, which would indicate that all students passed all tests.

Results for this index are presented in Figure 1. This figure shows that student performance in New York City, Yonkers, and the upstate big three districts (Buffalo, Rochester, and Syracuse) falls far below the performance in all other types of districts. The city-suburban comparisons in this figure are particularly striking. Both New York City and the upstate big three have index values that fall more than 60 points below the average value in their suburbs.

Finally, the funding disparity on which the *CFE* case is based also is notable. For many years, New York City received less aid per pupil than the average district in the state, despite its high required wages and high concentration of disadvantaged students. In recent years, New York City's share of state aid has crept up to be approximately equal to its share of the state's student population.

The funding disparities in New York State generally were highlighted in a recent report by The Education Trust.[5] The report found that the 2005 funding gap between the lowest-poverty districts and the highest-poverty districts was $2,236 in New York State, which was the highest gap in the nation. This gap was $907 in the nation as a whole.

Analytical Issues

[4] William Duncombe, Anna Lukemeyer, and John Yinger, "Financing an Adequate Education: The Case of New York." Available at http://nces.ed.gov/pubsearch/pubsinfo.asp?pubid=2003403.

[5] The Education Trust. 2006. "The Education Gap, 2005." Available at http://www2.edtrust.org/NR/rdonlyres/31D276EF-72E1-458A-8C71-E3D262A4C91E/0/FundingGap2005.pdf.

The *CFE* decision in June 2003 clearly stated that the New York Constitution requires an adequate education in every district. It does not require an equal education and it does not require steps to "recapture" funds from or otherwise bring down the educational performance of the state's best school districts. As a result, most of the parties to this case, including the Governor's Office, the New York State Education Department, and the Campaign for Fiscal Equity, agree that the appropriate response to this decision is to pass a new foundation aid program. After all, a foundation aid program is specifically designed to ensure a minimum performance in every district.

To implement a foundation aid program, public officials must address five questions: (1) What level of educational performance is "adequate" (and how much does it cost to get it)? (2) How should the spending required to reach adequacy (the foundation spending level) be adjusted for educational costs? (3) Should a minimum property tax rate be imposed on all districts? (4) What is an equitable way to spread the burden for the program across different groups in the state? (5) How can the state minimize the school district inefficiency that might accompany a large aid increase?

Several parties have contributed to the debate on these analytical issues. The New York Commission on Education Reform (the Zarb Commission), appointed by Governor George E. Pataki, commissioned a report from Standard and Poor's (S&P), which addresses some of these issues. CFE hired the consulting firm, American Institutes for Research/Management Analysis and Planning (AIR/MAP). The New York State Department of Education (NYSED) prepared an analysis of these issues, and several scholars, including D/L/Y, have written on the subject. All of these contributions are referred to in the following discussion.[6]

What level of educational performance (and spending) is adequate?

According to the *CFE* decision, the state's obligation is to ensure that every district delivers "a meaningful high school education, one which prepares them to function productively as civic participants." Any

[6] The report prepared for CFE is J. G. Chambers, T. B. Parrish, J. D. Levin, J. R. Smith, J. W. Guthrie, and R. Seder, *The New York Adequacy Study: Determining the Cost of Providing All Children in New York an Adequate Education, Volume I—Final Report*, American Institutes for Research/Management Analysis and Planning, March 2004 (available at http://www.cfequity.org/FINALCOSTINGOUT3-27-04.pdf). The report prepared for the Zarb Commission is Standard and Poor's, *Resource Adequacy Study for the New York State Commission on Education Reform*, New York: Standard and Poor's School Evaluation Services, March 2004 (available at http://www.spses.com). The NYSED analysis is in New York State Department of Education, "Regent's 2004-2005 State Aid Proposal," Albany, NY: New York State Education Department, December 2003 (available at http://www.oms.nysed.gov/press/121103release.htm)

response to the court's mandate must decide what this means, that is, it must find a measure of student performance and set the minimum acceptable level.

One example is provided by the D/L/Y index described earlier. This index summarizes student performance in elementary, middle, and high schools and gives more weight to student performance on high school exams. The value of this index in the average district in the state is 160. One possible standard, therefore, would be to bring all districts up to the current state-wide average, that is, up this 160 value. As noted earlier, this standard is far above the current performance in the State's largest cities. Another possible standard would be an index value of 130, which could be reached with only about half as much change in the poor districts as a standard of 160.

This index does not, however, consider the problem of high school dropouts. This problem is relevant because a high passing rate on high school exams might reflect the tendency of a district to encourage (or at least not discourage) its lowest-performing students to leave school. This index also does not consider student performance in any subjects other than math and English. Alternative approaches could introduce adequacy standards for graduation rates and for passing rates on other tests, such as science and social studies.

The *CFE* decision does not simply set a (vague) standard, it also requires an education finance system "ensuring…that every school in New York City would have the resources necessary for providing the opportunity for a sound basic education." Indeed, the decision gives some interesting advice to elected officials by saying that "the funding level necessary to provide City students with the opportunity for a sound basic education is an ascertainable starting point." This statement simply recognizes that selecting a performance level is not sufficient, policy makers must also determine how much it costs to provide that level of performance. This step is often called "costing out."

Several methods of costing out have been proposed: the successful schools approach, the professional judgment approach, and the econometric approach.

The "successful schools approach" identifies districts that are meeting the standard and measures how much they are spending. In practice, this method usually trims off districts with relatively high wealth or a relatively high concentration of disadvantaged students.[7] This approach is appealing because it is simple to

[7] In some cases, the successful schools approach brings in additional information to adjust spending for high wages and/or the high costs of disadvantaged students. See below.

implement with widely available data and easy to explain: Simply find school districts meeting the standard and determine what they spend. As a result this approach has been used in states around the country, and it forms the basis of the cost estimates by S&P (and hence the Zarb Commission) and NYSED.

The second approach to estimating the cost of adequacy is to ask a panel of professional educators what resources they think are required for districts to achieve an adequacy standard. This is called the "professional judgment approach." Although it can be time-consuming and expensive to implement, this approach yields a wealth of details on the types and numbers of classrooms, teachers, other staff, and non-personnel resources that educators feel are necessary for a school to be successful. Because it draws on the expertise of educators and provides so much information, this approach has also been widely used and formed the basis of the costing-out study prepared by AIM/MAP for CFE.

The third approach is to estimate a "cost function" by applying statistical methods to data for a sample of school districts. A cost function relates data on actual spending in a district to student performance, resources prices, student needs, and other relevant characteristics of districts. This approach has been implemented by scholars for many states, and is the basis for the cost estimates prepared by D/L/Y.

For estimating the cost of adequacy in the average district, the cost function approach is quite similar to the successful schools approach. Both approaches determine the cost of adequacy by examining current spending in schools that meet the standard. As we will see, however, these two approaches can differ dramatically when it comes to adjusting for the cost impacts of disadvantaged students and high required wages.

Because it makes use of statistical methods, the cost function approach does not have the intuitive appeal of the other two. Indeed, some people reject it because of its technical complexity. Other people argue that the intuitive appeal of the other approaches may hide their approximate nature or even their errors. According to these people, the main criterion in selecting a method should be accuracy, not transparency.

Table 1 presents cost estimates (calculated by Professors Duncombe and Yinger, D&Y) for the average district in state based on these three approaches.[8] The columns refer to different performance standards. The first four columns are different values for the index created by D/L/Y. The last column is the performance standard used in the AIR/MAP report commissioned by CFE, which was to give every student the

[8] Amicus Curiae Brief of John Yinger and William Duncombe, Supreme Court of the State of New York, County of New York, Campaign for Fiscal Equity, Inc. (plaintiffs) v. The State of New York (Defendants), Index No.: 111070/93, September 17, 2004. Available at http://cpr.maxwell.syr.edu/efap/CFE_Articles/Amicus_brief.pdf.

"opportunity" to pass all the Regents examinations. This appears to be a very high standard, although it is difficult to know what it means in practice. The rows of this table refer to different approaches. The first, third, and fourth rows make use of the approaches described above. The second row, labeled "teacher cost," represents an approximation to the professional judgment approach based on selected class sizes and teacher salaries.

The results in Table 1 indicate that the legal/political step of selecting a performance standard has a larger impact on the cost of achieving a sound basic education than does the technical step of selecting an estimating approach. When they apply to the same performance standard, the various approaches yield similar estimates of this required cost. The CFE estimate is considerably higher than the others. However, this estimate appears to be based on a relatively high performance standard, and extrapolating the results of the other methods to a higher standard yields similar cost estimates. In addition, the successful schools approach yields cost estimates that are similar to those of the other approaches for a performance standard of 160, but does not appear to be as well suited as the other approaches for estimating how costs change as the performance standard changes.

How should foundation spending be adjusted for educational costs?

Two elements of educational costs have been universally recognized in the CFE debate: the added costs of educating disadvantaged students and the higher wages that some districts must pay to attract teachers of a given quality.

The *CFE* decision says that the opportunity for a sound basic education must "be placed within the reach of all students," including those who "present with socioeconomic deficits." One possible interpretation of this requirement is that reforms to the state education finance system must recognize that it costs more to educate students from poor families or with limited English proficiency than it does to educate other students.

This interpretation is in line with current practice in many states, including New York, which gives extra weight to various categories of students in state aid formulas. Many states, for example, give extra weight to students from poor families (usually measured by whether they are eligible for a free or reduced price lunch) or students with limited English proficiency. An extra weight of 1.0 for a LEP student, for example, indicates that it costs twice as much to educate a LEP student as it does to educate a student who is proficient in English. The

extra weights given to these types of students vary widely from state to state, however, and some states, again including New York, use weights only in a few, relatively small categorical aid programs.

This variation in practice reflects the fact that educational cost adjustment is easier said than done, and there is a wide range of opinion about the best way to adjust for educational costs. Moreover, different approaches to this issue have very different implications for the overall cost of reaching the selected student performance standard in disadvantaged districts, such as New York City.

The successful schools approach is a poor tool for estimating the higher cost of education in some districts. This approach is based on spending per pupil in districts that meet a selected performance standard, but the key performance problem motivating education finance reform is the extremely low performance in districts with a concentration of disadvantaged students. In fact, it is almost impossible to find a poor, urban district that meets even a relatively modest standard, so this method has no information to work with.

In recognition of this fact, the report by S&P does not attempt to calculate adjustments for poverty or other student disadvantages. Instead, it observes the poverty and limited-English weights in state aid formulas around the nation and selects figures that are roughly at the median, 35 percent for a student from a poor family and 20 percent for a student with limited English proficiency. S&P's description of their procedure has caused some confusion. The S&P's report says that it "uses weightings drawn from a review of the research literature concerning the coefficients that education agencies use in practice" (p. 20). The "research" in this quotation refers to professional articles that present descriptive information on state aid formulas, not to professional articles that actually estimate the appropriate cost weights for various student categories.

The report by the NYSED, which is also based on the successful schools approach, followed a similar procedure but with a much higher weight. To be specific, it used an extra weight for students from poor families that had a maximum value of 100 percent in the highest-poverty districts. This report did not include an extra weight for LEP students. The special masters report, which was endorsed on this point by Justice DeGrasse, used extra weights of 50 percent for students from poor households and 20 percent for students with limited English proficiency.

The "professional judgment" approach addresses the question of educational costs by asking the educators on the panels to determine the extra programs that are "needed" for students with various disadvantages and then adding in the cost of these programs.

This approach is somewhat vague, since educators cannot be expected to describe a set of programs they have never observed, namely, the programs that would boost the performance of disadvantaged students up to the performance standard. Nevertheless, it has a certain appeal because educators are the ones who experience the operation of various programs in the schools. This approach was used in the AIR/MAP report. Although this approach does not lead to explicit student weights, D&Y estimate that the extra weights for a student in poverty are 0.81 for elementary to 0.37 for middle school to 0.49 for high school. The estimated extra weights for LEP are approximately 0.18 for all levels.

The great advantage of the "cost function" approach is that it provides direct estimates of the added costs facing schools with disadvantaged students, controlling for other factors. Because this procedure holds student performance constant, these estimates apply to schools at all performance levels. These are, of course, still estimates, but they are estimates based on current cost experiences in all the state's school districts, including those with both high and low student performance and those with high and low student disadvantage.

These estimates can be used to calculate either a cost index, which indicates how much each district would have to spend, relative to the state average, to reach any performance standard, or a weight that indicates the extra cost of each student in poverty, with limited English proficiency (LEP), or with a disability.[9] Once a performance standard is selected, the cost index or the student weights can be used to calculate how much it would cost each district to reach the standard.

Using this approach, D/L/Y estimate that the per-pupil cost of education in New York City is 36 percent above the state average based on student needs alone. These estimates correspond to an extra cost weight of about 1.2 for a student in poverty and of 1.0 for a student with limited English proficiency. These weights are close to the weights in a recent aid program in Maryland and, in the case of poverty, in the aid program proposed by the Regents.

The second type of cost adjustment is for wage costs. Some districts are in high-wage regions so they must pay more to attract teachers away from the private sector. In addition, some districts have harsh teaching conditions, such as a high concentration of disadvantaged students or dilapidated buildings, so they must pay more to attract teachers away from other districts. All parties to the *CFE* case agree that some adjustment for wage costs is appropriate.

[9] The formal relationship between cost indexes and student weights is explained in W. Duncombe and J. Yinger, "How Much More Does a Disadvantaged Student Cost?" *Economics of Education Review*, October 2005, pp. 513-532.

The problem is that wage costs are difficult to estimate. The approach preferred by most scholars is to estimate a wage equation for a sample of individual teachers, with wage as the dependent variable and with teacher and market characteristics as explanatory variables. The problem is that most data sets do not have adequate information on teacher quality, and other variables, such as concentrated poverty, may have biased coefficients because they are picking up the impact of omitted teacher characteristics.

One well-known application of this approach to national data, called the NCES index because of its publication in a volume published by the National Commission on Education Statistics, has been widely used in the debate about educational costs in New York.[10] This study, which has limited information on both teacher quality and the school environment, concludes that the cost of teachers in New York City is only 10 percent above the cost in the average district. That is, teacher salaries would only have to be 10 percent higher than in the average district to attract a teacher of a given quality to New York City. Some observers (including D/L/Y) find this implausible on its face. Nevertheless, this estimate is used in the S&P and Zarb Commission reports and in the AIR/MAP and CFE reports.[11]

Two alternative estimates of wage costs are available. One, developed by NYSED, is to determine the average salary in each region for people in occupations with qualification similar to those of teachers. The second uses the same general approach as the NCES index, but uses data for New York State. Both of these alternatives find a much higher difference between New York City and the average district in the state. These differences are highlighted in Figure 2, which compares the D/L/Y and NCES wage indexes for types of types of districts.

As indicated earlier, a full adjustment for costs recognizes both student need and wage components of costs. Figure 3 shows how the full cost indexes developed by D/L/Y vary across districts in New York State. Table 2 presents cost estimates for New York City with various student need and wage adjustments.

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[10] Chambers, J. (1997). *A Technical Report on the Measurement of Geographic and Inflationary Differences in Public School Costs*. Prepared for the National Center for Education Statistics, Washington, DC.

[11] The appearance of this index in the AIR/MAP report can be explained by the fact that the person who developed the NCES index, Jay G. Chambers, was a member of the AIR/MAP team. The Campaign for Fiscal Equity, S*ound Basic Education Task Force: Ensuring Educational Opportunity for All: Final Report*, New York: Campaign for Fiscal Equity, May 2004 (available at http://www.cfequity.org/SBETaskForceFinalReport.pdf). The New York State Commission on Education Reform, *Ensuring Children an Opportunity for a Sound Basic Education: Final Report*, Albany, NY: The New York State Commission on Education Reform, March 2004 (available at http://www.state.ny.us/pdfs/finalreportweb.pdf).

Not surprisingly, decisions about cost adjustments have an enormous impact on the cost of education finance reform holding the performance standard constant. Table 3 presents the cost of bringing New York City up to various performance standards (the rows) under various assumptions about the costs (the columns). For example, in the third row, which corresponds to a performance standard of 160 using the D/L/Y index, the cost of reform ranges from $4.5 billion to $7.2 billion, depending on which cost estimates are used. These calculations indicate that the $5.6 billion in Justice DeGrasse's compliance order is roughly equivalent to a requirement for a 160 standard for the D/L/Y index with the NCES adjustment and the D/L/Y pupil weights.

Tables 4 and 5 provide additional information on costs. Table 4 shows the required spending per pupil with three types of cost adjustment: the teacher wage adjustment calculated by D/L/Y, the NCES wage adjustment used by the Zarb commission and CFE, and the D/L/Y full cost adjustment. Table 5 shows foundation aid per pupil for the same three approaches to educational costs.

Because educational costs are so difficult to estimate and are not likely to remain constant over time, one of the great challenges of any education finance reform effort is to set up a process for calculating and updating these cost figures.

Should a minimum tax rate be imposed?

The *CFE* decision focuses on expenditures, not on revenues, and has little to say about the appropriate methods for funding a sound basic education in New York City. Nevertheless, the framework provided by a foundation formula reveals that one key aspect of funding needs to be considered.

As noted earlier, a foundation aid program provides each district with the difference between that district's foundation amount and its expected local contribution. Thus, a final step in a designing a foundation aid program is deciding what the local contribution should be.

Moreover, unless this contribution is required, not simply recommended, a district may not achieve the spending level needed to reach the adequacy target. After all, a large influx of state aid allows a district to cut its own school tax contribution and use the money for other public services or for property tax relief. Indeed, school districts with a relatively large amount of state aid often have a relatively low school tax rate. To prevent this type of response, most states with foundation plans make the "expected" contribution mandatory. New

York State has not taken this step with its (small) existing foundation plan, but the mandate of the Court of Appeals cannot be satisfied without making the local contribution a requirement.

In most states this required contribution is expressed as a share of the local property tax base. This approach is used because the local property tax is the main source of local revenue for schools, but it causes no difficulty in a city like New York in which the income tax also provides school revenue. The expected contribution is defined as a share of the property tax base, but it need not be collected through the property tax.

Setting a required minimum local property tax rate is equivalent to turning a portion of the property tax into a state tax. Some states, including Kansas and Michigan, have followed this logic and formally changed some or all of the property tax into a state tax, which is then used to help fund education. If this state tax has a relatively low rate, as in Michigan, then the switch to a state tax is little more than an administrative change. If this state tax has a relatively high rate as in Kansas, however, it will collect more revenue from wealthy districts than it returns to them in the form of aid. This is a disguised form of recapture.

What is an equitable way to spreading the burden?

The funding for any education finance reform must come from some combination of (1) a required minimum tax rate above the rate currently charged by some schools, including many low-performing schools; (2) contributions from wealthy schools, also known as re-capture, and (3) state revenues. An evaluation of alternative sources of state revenues is not on the agenda for the up-coming conference, but the distribution of the burden across these three sources is going to be a subject for discussion.

A required minimum tax rate places some of the burden for the reform on the low-performing schools the reform is designed to help. Most commentators agree that it is appropriate for these schools to make a higher sacrifice as a part of a reform plan, but there is no agreement on the appropriate magnitude of this sacrifice. A minimum tax rate of 1.5 percent would require a rate increase in only a few districts in the state, almost all of which are relatively poor.

Three forms of re-capture have appeared in the education finance reform plans in other states. The first is to implement a power-equalizing aid program. This approach has no support in New York State. The second is to transform some or all of the property tax into a state tax. Full transformation of the property tax into a state

tax would not be feasible in New York, but some portion of the tax, such as the tax on commercial and industrial property, could be turned into a state tax with the revenues used to fund education.[12]

The third approach to re-capture is to phase out the hold-harmless clauses that currently guide state aid to education. Under current practice, no district ever experiences a cut in the aid it receives from the state. With a relatively low performance standard, such as a value of 130 on the D/L/Y index, eliminating hold-harmless provisions would save up to $2 billion a year. These large savings reflect the design of a foundation aid program. Districts that can raise enough money to cover their foundation spending level at the minimum local property tax rate receive no aid. With low foundation spending levels and a reasonable minimum local tax rate, many districts would therefore receive no aid under such a plan—and hence would experience a large cut in aid if that plan were implemented without a hold-harmless provision. The savings would be smaller with a high performance standard because fewer districts would raise enough money at the minimum local tax rate to cover their higher foundation spending level. This conclusion is illustrated in Figure 4.

Most politicians in the state have defended hold-harmless provisions, and indeed have declared their opposition to any “Robin Hood” component in an education finance reform plan. "Forget about Robin Hood," said Edmund J. McMahon, an analyst at the Manhattan Institute, a conservative policy group. "It's Santa Claus. Everybody gets something under the tree." CFE is not immune to this argument. Its reform proposal boosted aid in 517 of the state's 680 school districts. "We really came to the decision that if we could get a functioning lab in every school, decent class sizes, gym facilities, an adequate education in every school—to get there is such a huge battle," said the executive director of the Campaign for Fiscal Equity, Michael A. Rebell. "Maybe in 20 years, if we ever get that, somebody else can say that they want to go for equity. But that's not our battle."

Other commentators have pointed out, however, that the current education aid system, including its hold-harmless provisions, is precisely what was declared unconstitutional in the *CFE* decision. As Diana Fortuna, the president of the Citizens Budget Commission put it: "Obviously, they feel a political imperative to spread this money around, and make the solution more politically acceptable," she said. "But that's not what the court case was all about. Giving away money to low-needs districts makes the proposals more expensive and less likely to be successful."[13]

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[12] This particular proposal would also eliminate competition among school districts for commercial and industrial enterprises. With the rate controlled at the state level, no district could attract businesses using property tax breaks. Some scholars believe inter-district competition is inefficient so that eliminating it would be a good thing, but others believe that property-tax relief programs are helpful for local economic development.

[13] The quotations in this and the preceding paragraph come from Michael Cooper, “Robin Hood, Santa Claus and Financing for Schools”, *The New York Times*, June 6, 2004.

Some other commentators have suggested a compromise approach, involving a guaranteed minimum aid per pupil for every district and a phase-down period to reach this minimum. This compromise would not cut the aid of many wealthy districts, but it would not cut their aid to zero and it would give them time to plan for less aid from the state.

How can inefficiency be minimized?

Of course states want their education aid money to be well spent. Even before the federal No Child Left Behind Act was passed in 2001, states around the country were implementing school accountability programs. Most of these programs are based on student test scores (or changes in test scores) and some of them involve rewards and sanctions based on the level or change in a school district's test scores. New York State, for example, not only publishes school report cards, but also places the lowest-performing schools "under registration review," and shuts these schools down if they do not improve within a few years. In addition, concern about effective use of resources is heightened when an education finance reform leads to a large increase in state aid to a particular district.

The trouble is that it is very difficult to separate the impact on student performance of factors inside a school or school district's control, such as its choice of a curriculum or management system, from the factors outside its control, such as the amount of aid it receives or its concentration of disadvantaged students. The passing rate on a state test obviously reflects both types of factors, so an accountability system that simply rewards or punishes districts (or schools) based on test scores is inherently unfair and ineffective. Does it make sense to punish a district because it has a high concentration of disadvantaged students—and therefore has relatively low test scores? Of course not. It also makes no sense to punish a district that has low scores because it has a large influx of immigrant children who do not speak English or because it has not received its fair share of revenue from the state.

Another important challenge for an accountability system is that knowledge is limited about the best curricular and management programs to implement. A school district may not know what programs are needed to bring student performance up to a performance standard, but it is unlikely to refuse to implement programs that are known to work. Most school districts cannot afford their own research department to address this problem on their own, and elected officials have not provided NYSED with enough resources to serve this function. The question remains: In a reformed education finance system, should the acquisition and

dissemination of knowledge about effective educational programs be the responsibility of each district or of NYSED?

The Zarb Commission recommends that schools failing to raise test scores will be closed and then reconfigured, turned into charter schools, or, in extreme cases, taken over by the state. An alternative approach, recommended by D&Y, combines (a) giving NYSED enough resources to identify curricular and management programs that boost student performance under various circumstances (b) a program to initiate conversations between NYSED and schools that do not meet standards, conversations designed to identify programs likely to raise the district's performance, and (c) a program of sanctions for schools that do not cooperate in this conversation.

The Conference

Politicians in New York have been actively sparring about education finance reform since the *CFE* decision was issued in June 2003. Governor Pataki and Joseph L. Bruno, the Republican leader of the State Senate majority leader, have offered similar proposals, but these proposals are vastly different from the one preferred by Sheldon Silver, the Democratic speaker of State Assembly. Each of these politicians has gone out of his way to blame the others for the state's failure to respond to the mandate by the Court of Appeals.[14]

Governor Pataki called the legislator back for a special session on school aid reform in July of 2004, but this session failed to yield a compromise solution. Some people called the Governor's action a serious attempt to come up with a compromise solution, others called it political grandstanding. Michael Rebell, for example, was hopeful that the Legislature would come up with a plan, but, in reference to the plan presented by Governor Pataki at this session, he said that "The governor's plan rehashes an inadequate proposal that was dead on arrival six months ago."[15]

Other parties who have been active in the debate include Michael R. Bloomberg, the Mayor of New York City; Stephen Sanders, Chairman of the Assembly's Education Committee; Joel I. Klein, the Chancellor

[14] Although the politicians on this list have spent most of their energy criticizing each other instead of coming up with a serious response to the *CFE* mandate, some of them have criticized the court as well. In June 2004, for example, Senator Bruno said: "The judge I think, and the judges that ratified the original judge's agreement, didn't understand what they were doing, in plain English." This quotation is from Michael Cooper, "No Agreement on Education of Other Sticky Issues as Legislative Session in Albany Ends," The *New York Times*, June 23, 2004.

[15] This citation is from Michael Cooper, "Pataki Orders Legislators to Session on School Aid," *The New York Times*, July 21, 2004.

of the New York City Schools; Randi Weingarten, president of the United Federation of Teachers; and Timothy G. Kremer, the executive director of the New York State School Boards Association.[16]

The SARC conference will bring together interested parties to discuss alternative ways for elected officials to respond to the *CFE* case. This conference will build on the two key items on which all parties seem to agree. First, education reform should apply to the state as a whole, not just to New York City. This point of agreement is a key motivating factor for the conference; if legislators do not come up with an education finance reform package that is acceptable to the Court of Appeals, then the Court will impose its own solution for New York City alone. Second, education finance reform should be based on a foundation aid plan. This point of agreement still leave many issues up for debate, of course, such as how to adjust for costs, whether to impose a minimum tax rate, and whether to include a new accountability system. This conference is limited to issues surrounding school operating spending. Capital spending will be considered on another day.

You have been asked to make a presentation at this conference. You are not expected to comment on every issue raised by the *CFE* case, but instead have been asked to identify the issues that you think are most important and to make a reform proposal that addresses them. Although you should not make proposals that are clearly outside the realm of political feasibility, such as getting rid of the property tax altogether, you have been asked to focus on the analytical issues, not the political ones. At this stage, the leaders of SARC want to identify the reform options that would be most effective in achieving various objectives. A later conference is scheduled to put together a final proposal that is effective and politically feasible.

[16] The views of three participants in the debate are presented in the appendix to this case.

Figure 1. Comparison of Student Performance Index by Region

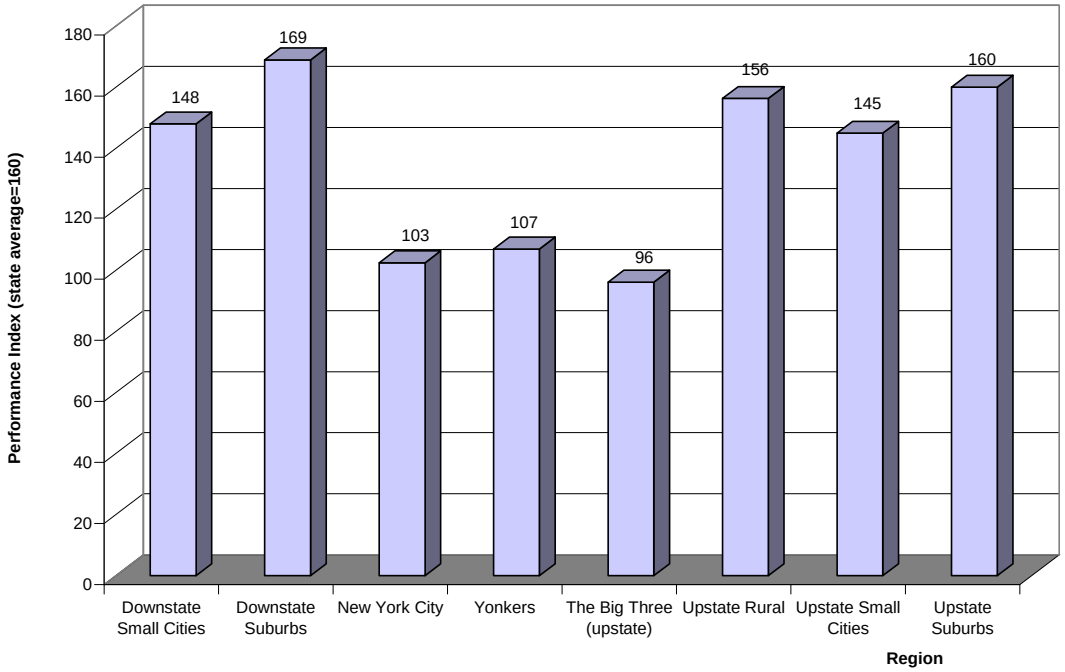

Figure 2. Comparison of Teacher Cost Indexes for New York Regions

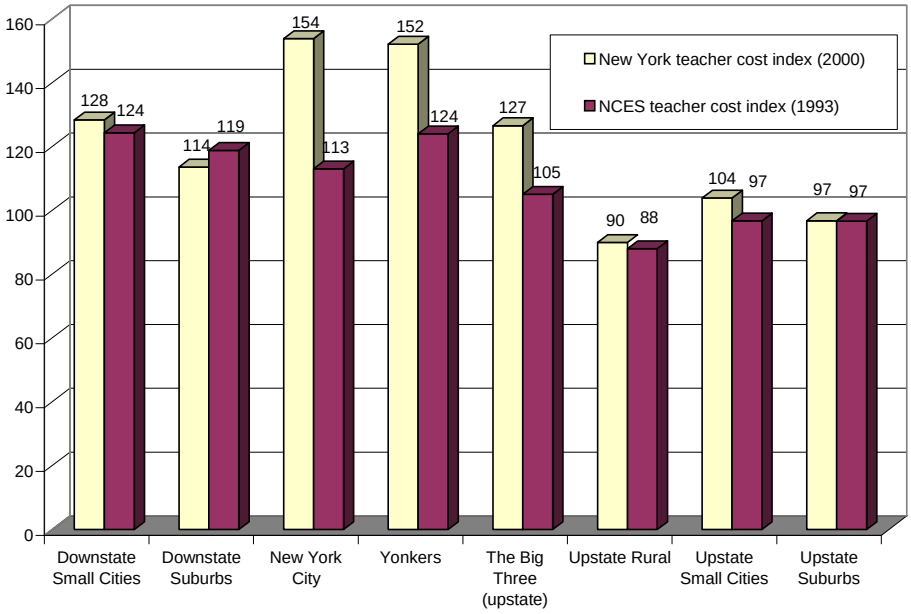

Figure 3. Cost and Student Needs Indexes for New York Regions

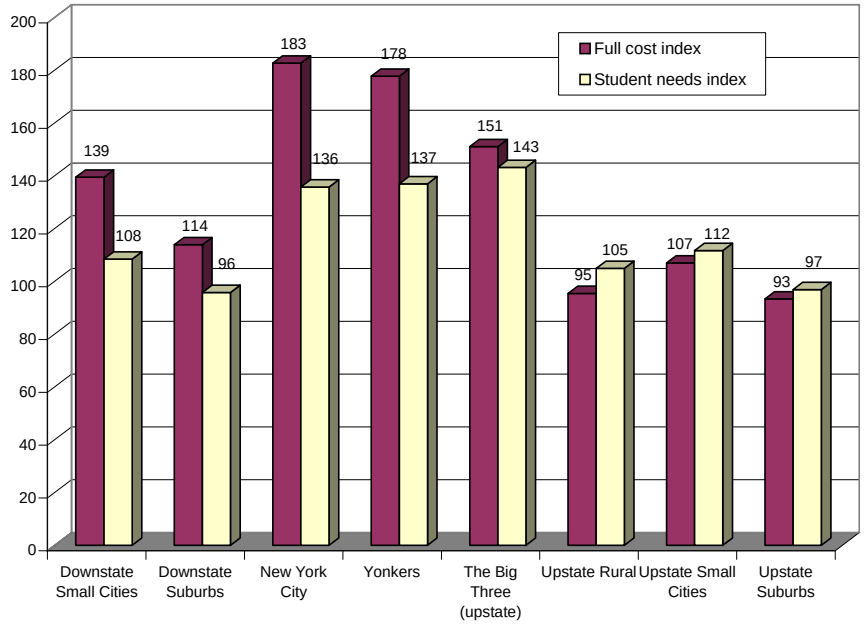

Figure 4: Performance Outcomes for Various Aid Budgets

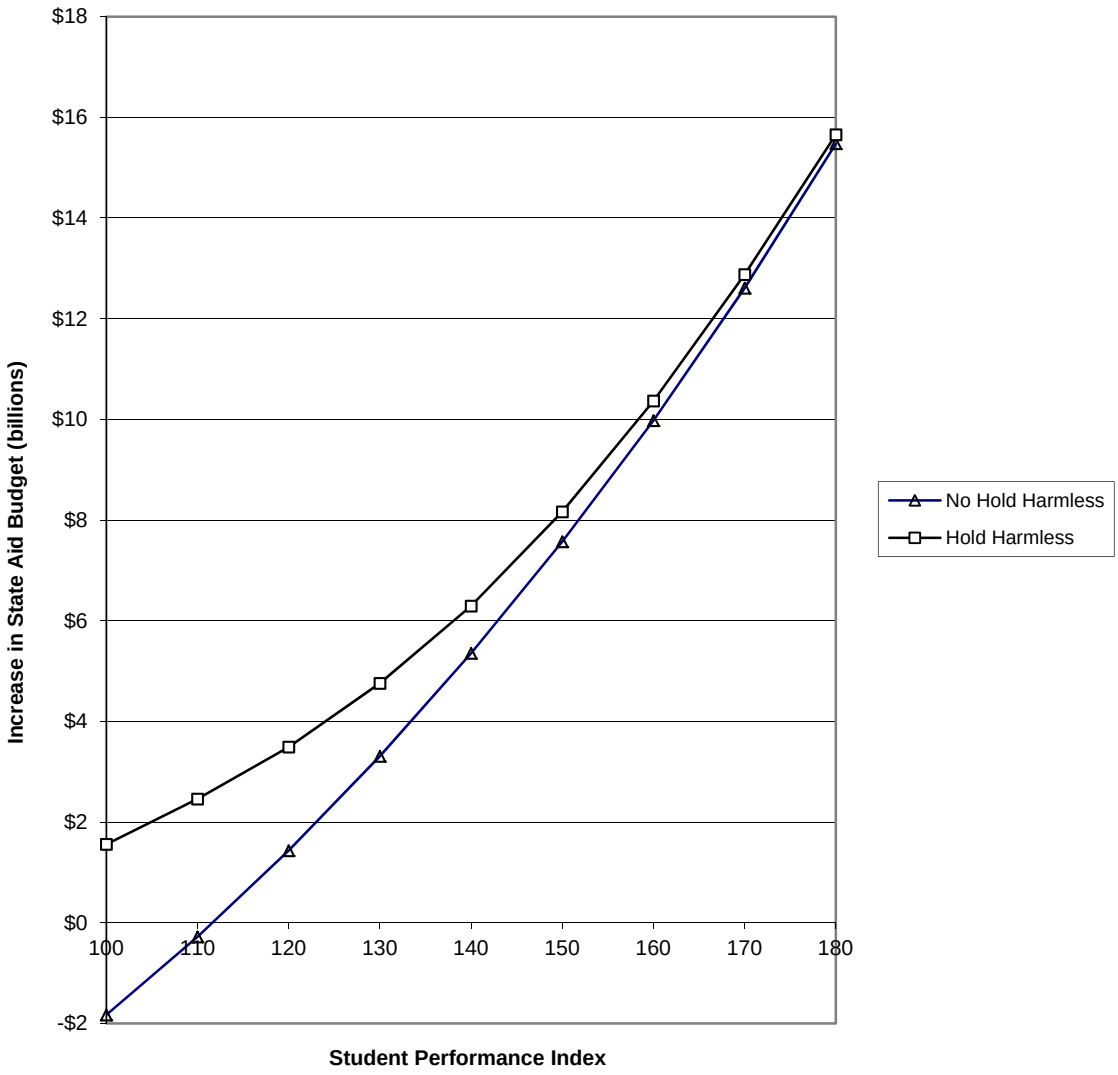

Table 1. Estimated Per-Pupil Operating Cost of a Sound Basic Education in an Average District, by Approach and by Student Performance Standard

	Student Performance Standard				
Approach	130	140	150	160	CFE
Professional Judgment					$12,890
Teacher Cost		$9,510	$9,629	$10,038	
Successful Schools		$10,280	$10,375	$10,812	
Cost Estimation	$8,626	$9,301	$10,027	$10,811	

Note: The estimates in all rows apply to school year 2001-2002.

Table 2. Estimated Per-Pupil Operating Cost of a Sound Basic Education in New York City, by Approach and by Student Performance Standard

Approach (and standard) for Determining the Cost in a Typical District	No Wage or Student Need Adjustment	Combination of Wage and Student Need Adjustment				
		Wage: AIR/MAP		Wage: NYSED		Wage: DLY
		Need: AIR/MAP	Need: Cost	Need: AIR/MAP	Need: Cost	Need: Cost
Professional Judgment (Regents Learning Standards)	$12,890	$17,724	$19,283	$19,980	$21,738	$20,861
Teacher Cost (Index Value of 160)	$10,038	$13,802	$15,017	$15,559	$16,928	$16,245
Cost Estimation (Index Value of 160)	$10,811	$14,865	$16,173	$16,757	$18,232	$17,497
Cost Estimation (Index Value of 130)	$8,626	$11,861	$12,904	$13,370	$14,547	$13,960

Notes: The figures in this table equal the figures in Table 1 adjusted for the estimated wage costs and pupil needs in New York City. The row labels indicate the starting point from Table 1. The column headings come in two parts. The first part indicates the method for making the wage cost adjustment and the second part indicates the method for making the pupil need adjustment.

Table 3. Added Total Annual Cost to Achieve a Sound Basic Education in New York City, by Approach, Student Performance Standard, and Cost Estimation Method (in millions)

	Combination of Wage and Student Need Adjustment				
	Wage: AIR/MAP		Wage: NYSED		Wage: DLY
Approach (and standard) for Determining the Cost in a Typical District		Need: Cost	Need: AIR/MAP	Need: Cost	Need: Cost
Professional Judgment (Regents Learning Standards)	$7,443	$9,048	$9,764	$11,573	$10,671
Teacher Cost (Index Value of 160)	$3,408	$4,657	$5,215	$6,624	$5,922
Cost Estimation (Index Value of 160)	$4,501	$5,847	$6,448	$7,965	$7,209
Cost Estimation (Index Value of 130)	$1,410	$2,484	$2,963	$4,174	$3,570

Notes: The figures in this table equal the figures in Table 2 multiplied by the number of students in New York City, 1.029 million, less current school revenue raised by the City, $5.08 billion, and the amount of state aid currently received by the city, $5.715 billion.

Table 4. Required Spending Per Pupil for Adequacy For Different Cost Indexes[1]

Regions	1999-2000 Per Pupil Expenditure	Standard of 130 New York Teacher Cost Index (2000)	Standard of 130 NCES Teacher Cost Index (1993)	Standard of 130 New York Full Cost Index (all cost factors)
State Average	$9,781	$7,606	$7,606	$7,606
Downstate Small Cities	$10,400	$9,765	$9,458	$10,502
Downstate Suburbs	$11,723	$8,642	$9,038	$8,573
New York City	$8,823	$11,701	$8,597	$13,758
Yonkers	$12,437	$11,569	$9,430	$13,384
The Big Three (upstate)	$9,289	$9,627	$7,990	$11,372
Upstate Rural	$9,509	$6,842	$6,693	$7,181
Upstate Small Cities	$9,335	$7,902	$7,357	$8,054
Upstate Suburbs	$8,307	$7,361	$7,348	$7,028

	2000 Average Performance	Standard of 160 New York Teacher Cost Index (2000)	Standard of 160 NCES Teacher Cost Index (1993)	Standard of 160 New York Full Cost Index (all cost factors)
State Average	160	$9,532	$9,532	$9,532
Downstate Small Cities	148	$12,236	$11,852	$13,161
Downstate Suburbs	169	$10,829	$11,326	$10,744
New York City	103	$14,663	$10,773	$17,241
Yonkers	107	$14,497	$11,817	$16,772
The Big Three (upstate)	96	$12,063	$10,012	$14,251
Upstate Rural	156	$8,574	$8,387	$8,999
Upstate Small Cities	145	$9,903	$9,220	$10,093
Upstate Suburbs	160	$9,224	$9,208	$8,808

[1]Calculated by estimating the cost in district with average cost to reach the given standard multiplied by the cost index (divided by 100).

Table 5. Distribution of Cost-Adjusted Foundation Aid For Different Cost Indexes[1]

Regions	2000-2001 Per Pupil School Aid[2]	Standard of 130: New York Teacher Cost Index (2000)	Standard of 130: NCES Teacher Cost Index (1993)	Standard of 130: New York Full Cost Index (all cost factors)
Total Aid Budget (millions)	$16,642	$19,664	$14,310	$22,800
State Average	$4,053	$2,856	$2,784	$2,836
Downstate Small Cities	$3,205	$2,291	$1,971	$2,828
Downstate Suburbs	$2,419	$1,312	$1,531	$1,204
New York City	$3,949	$6,922	$3,817	$8,979
Yonkers	$3,112	$5,837	$3,697	$7,652
The Big Three (upstate)	$5,835	$6,516	$4,879	$8,261
Upstate Rural	$5,203	$3,099	$2,877	$3,397
Upstate Small Cities	$4,937	$4,321	$3,800	$4,496
Upstate Suburbs	$4,031	$3,365	$3,358	$3,039

	Standard of 160: New York Teacher Cost Index (2000)	Standard of 160: NCES Teacher Cost Index (1993)	Standard of 160: New York Full Cost Index (all cost factors)
Total Aid Budget (millions)	$29,147	$22,452	$33,031
State Average	$4,448	$4,440	$4,397
Downstate Small Cities	$4,340	$3,887	$5,145
Downstate Suburbs	$2,505	$2,834	$2,334
New York City	$9,884	$5,993	$12,462
Yonkers	$8,765	$6,084	$11,040
The Big Three (upstate)	$8,953	$6,901	$11,140
Upstate Rural	$4,680	$4,351	$5,066
Upstate Small Cities	$6,289	$5,626	$6,497
Upstate Suburbs	$5,133	$5,108	$4,716

[1]Cost-adjusted foundation aid is calculated by taking the estimated per pupil spending to reach the standard, and subtracting from it the required minimum local tax contribution (1.5 percent of property values) and federal aid. If the calculated aid is negative, it is set equal to zero.

[2]Includes all formula aid except Building Aid, Transportation Aid, and Reorganization Building Aid. Based on estimates of aid distribution in May 2001.