

# **NEPC Review: Public Education Funding Without Boundaries: How to Get K-12 Dollars to Follow Open Enrollment Students (Reason Foundation, January 2023)**



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**Reviewed by:**

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**National Education Policy Center**

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## Acknowledgements

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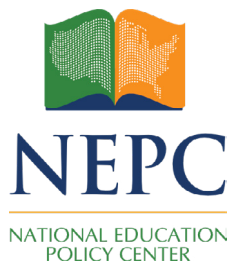
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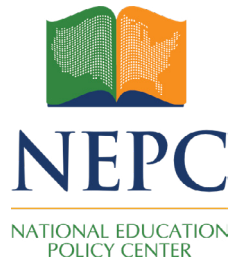
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## Summary

The Reason Foundation, a vigorous advocate for choice policies such as vouchers and charter schools, recently published *Public Education Funding Without Boundaries: How to Get K-12 Dollars to Follow Open Enrollment Students*. The report advocates for the increased “portability” of school revenues, allowing for “money to follow the students” and, therefore, the expansion of interdistrict choice programs. It attempts to show that many current features of state-level school funding formulas inhibit such portability. While there are sound policy reasons to facilitate greater interdistrict choice, this report’s prescriptions are not sound, in large part because they betray a lack of understanding of a core principle of school finance: Different students in different districts have different costs to achieve educational outcomes. The funding portability systems touted by the report do not account for many factors that determine student costs. This results in a mismatch between costs and revenues that advantages some districts while disadvantaging others when students transfer. Policymakers should avoid the facile recommendations in this report and instead carefully consider the many complexities in designing a portability system for interdistrict choice programs.



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## I. Introduction

The recent surge in state-level legislation that allows public funds to be used for private schools raises the issue of how to appropriately allocate revenues dedicated to public education across a variety of school “choices.” The issue is complicated: Public school funding comes from a variety of sources based on an interplay of student need, desired outcomes and programs, local tax capacity, and many other factors. School choice proponents have obscured these complexities by reducing the issue to a single, simplistic term: *portability*. Their conception is alluringly basic: School funding should attach to each student, like a backpack full of money.<sup>1</sup> Students and their families could then use these funds at a variety of school “choices.”

One of the most ardent proponents of portability is the Reason Foundation, a libertarian think tank whose preferred educational policies owe much to economist Milton Friedman, a vigorous advocate for school choice. Reason’s latest report, *Public Education Funding Without Boundaries: How to Get K-12 Dollars to Follow Open Enrollment Students* by Aaron Garth Smith, Christian Barnard, and Jordan Campbell, makes the case for funding portability within the context of interdistrict school choice.<sup>2</sup> The report compares several states’ policies that enhance or impede funding portability, arguing that “school finance systems should ‘attach’ dollars directly to students so that all state and local education funds flow seamlessly across district boundaries.”<sup>3</sup>

## II. Findings and Conclusions of the Report

The report begins with a summary of Friedman's advocacy for school choice, including interdistrict choice, which allows for students to cross district boundaries and enroll in public school districts other than where they reside. Next, the report attempts to describe the workings of state school funding systems, focusing on foundation formulas, which determine the amount of state aid a school district receives. The report then argues that the structure of foundation formulas inhibits funding portability which, in turn, stymies interdistrict school choice.

Specifically, the report describes three supposed problems, each illustrated with an example from New Hampshire. First, school districts that receive little or no state aid have no incentive to accept students from other districts, as enrolling additional students from outside their districts would not result in additional revenue. Second, local education revenues do not change based on enrollment, so there is, again, no incentive to enroll additional students. Third, some sources of state aid (facilities funding and hold-harmless aid) are not dependent on student enrollment, which once again removes the incentive for increasing enrollment.

The report gives examples of states that have supposedly improved funding portability. Wisconsin transfers a preset statewide per-pupil amount from a sending district to a receiving district for each student who transfers; additional funds are provided for students with special education needs. The report points to Indiana as an exemplar for funding portability; the state shifted more of the revenue used for school operations from local to state sources, facilitating cross-district enrollments.

The report offers three recommendations for state policymakers:

1. Set a single statewide base pupil amount that “. . . follows students across school boundaries . . .”<sup>4</sup>
2. Allow for adjustments to this amount based on student need. As an example, the report notes Wisconsin allots a greater per-pupil amount for students with disabilities.
3. Make local revenues portable. The report suggests one method would be to deduct state aid from districts whose students transfer out and give it to receiving districts.

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

Taking inspiration from Friedman, the report conveys the sense that increased school “choice” is, in itself, a desirable outcome. While a brief nod is given to the purportedly beneficial outcomes of interdistrict transfer programs, discussed below, the report is not concerned with justifying this policy; it instead concentrates on how to enact it.

## IV. The Report's Use of Research Literature

The report fails to use any relevant literature to support its most basic, but unwritten premise: that school choice, and its expansion through portability, has merit as a policy matter. Indeed, it cites only two sources to support its claim of the value of school choice and, importantly, both have significant shortcomings. For example, it notes that *The 123's of School Choice*<sup>5</sup> purports to show the benefits of school voucher programs; however, as an NEPC review of the 2019 edition notes, this report “ . . . cherry-picked studies chosen from an ‘overwhelming’ number, largely from sources that are not peer-reviewed (68%) and primarily authored by voucher advocates.”<sup>6</sup>

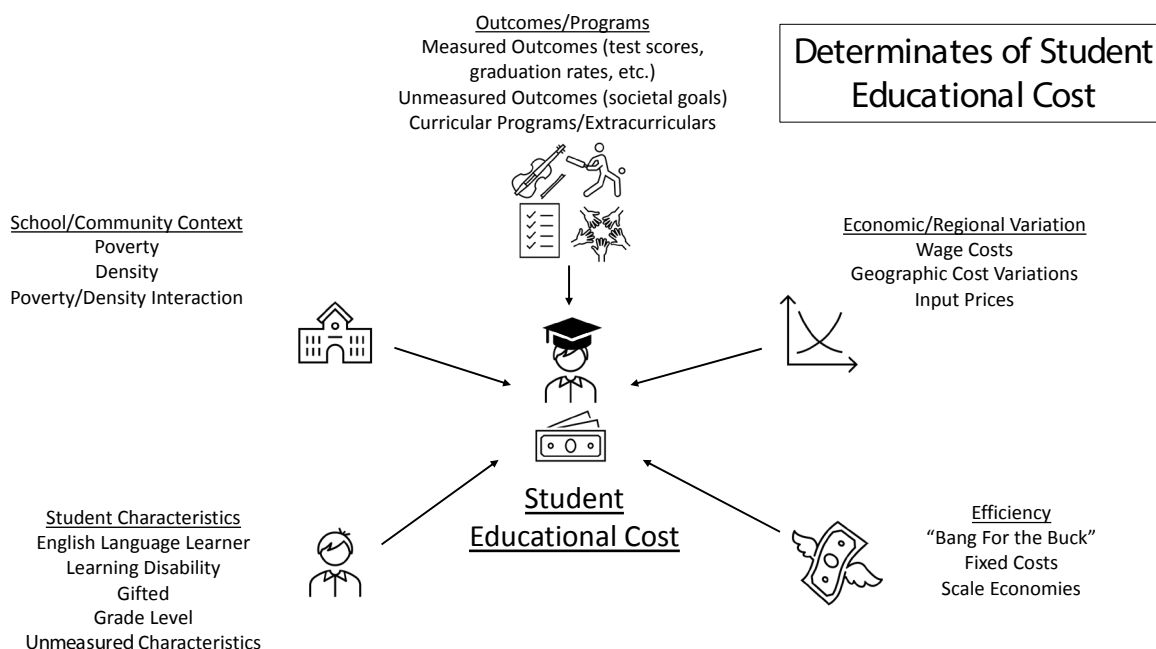
The second source, also from the Reason Foundation, is a commentary from one of the report's authors.<sup>7</sup> Five studies related to student outcomes are cited, varying in research questions, methods, and data. None make a causal claim about the effects of interdistrict choice programs on school district efficacy or efficiency.

## V. Review of the Report's Methods

The report has significant methodological flaws, all stemming from its simplistic view of school “costs.” By way of background, in school finance literature “cost” has a specific meaning: It is the minimal amount needed for a student or group of students to have the opportunity to achieve a specified educational outcome.<sup>8</sup> Because students have different characteristics—different abilities, different home lives, different needs, and so on—students will have different costs to meet a particular educational goal. Foundation formulas for school aid are premised on this idea: Students with a learning disability or who don't speak English as their first language are assumed to have a higher cost than other students; revenues are accordingly allotted based on these characteristics.

Educational costs, however, do not vary solely with the characteristics of students; this is a core concept of school finance that the report does not consider. In fact, many other factors play an important role in determining educational costs. Figure 1 is a conceptual model of factors affecting the cost of educating a student. I classify these into five broad categories: student characteristics, school/community contexts, outcomes/programs, economic/regional variation, and efficiency.<sup>9</sup> Importantly, many of those factors are outside of the control of school districts, which cannot change regional wage pressures, population density, poverty concentration, or a host of other factors that affect costs.

**Figure 1: A Conceptual Model of the Determinates of Educational Cost**



School funding portability, then, is not solely an issue of spending and revenue: It is also an issue of cost. While it is alluringly simple to think of school revenues as “attached to the student,” we must also realize that different students have different costs: Their characteristics help determine the amount of funding needed to provide them with an adequate education.

It is on this point that the report makes its fundamental error: It focuses almost exclusively on revenue transfers without fully exploring differences in cost. The report, consequently, ignores three (at least) important problems that must be addressed in any school revenue transfer system: 1) unequal financial incentives between districts to enroll students, 2) the lack of uniformity among individual students in a subpopulation, and 3) the disincentivizing of local tax effort. Without a discussion of these issues, the report’s methods are called into serious question.

## Unequal Incentives

The importance of addressing the unequal incentives, which must be considered in assessing an interdistrict choice program, is best illustrated by an example. Imagine two students, similar in all measured and unmeasured characteristics, each residing in a different school district. One district is in a relatively high cost-of-living region; one is in a relatively low-cost region. Each student transfers to the other’s district; the revenue “attached” to each student follows.

Unless some accounting is made for the relative difference in wage costs, the district in the lower-cost region will have an advantage: It is receiving a greater amount of revenue



because the cost of education in the other district is greater. Conversely, the district in the higher-cost region has little incentive to accept the student from the lower-cost region: The revenue received will not be enough to cover the higher costs in that district.

The report suggests Wisconsin has solved this problem by setting a uniform per-pupil amount across the state. In fact, Wisconsin's system makes the problem worse: None of the factors that cause variations in costs across districts are accounted for when a uniform base amount is set by the state. Big districts, which enjoy economies of scale, receive the same as small districts, which do not. Districts with concentrated poverty receive the same amount as relatively affluent districts, even though their costs are higher.

Unless *every* factor that affects educational cost can be accounted for, there will always be a winning and a losing district when a student transfers. This report's methodology, to the extent it exists, fails to consider this. But even if a highly complex formula—with variables for all factors—was developed, it would still be inappropriate to use at the student level for reasons discussed below.

### **Assumed Uniformity**

The report erroneously assumes that that a state's foundation formula calculation is made in specific relation to the individual student to which those dollars attach. But foundation formulas, and the average dollar number that they yield, do not work this way. They are, instead, estimates of the cost of educating *populations* of students. Certainly, using base per-pupil figures to determine costs for school districts is useful; at a minimum, it helps make the formula transparent and comprehensible for stakeholders and policymakers. But it does not follow that those figures validly estimate the cost of transferring a *single* student from one district to another.

State funding formulas that employ weighting systems for student characteristics rely on crude measures: usually binary variables representing characteristics such as student economic disadvantage (free or reduced-price lunch qualification) or English Language Learner status. But there are wide variations among students who fall into these simple binning systems, and these variations will affect costs. A student classified with a special need, for example, may have a relatively low-cost learning impairment, or have profound needs that require costly programs and services. Even though foundation formulas use these metrics as a general guidepost, it does not mean that every *individual* student will have an educational cost equal to the average, because there are variations between students in terms of cost.

Unless a portability system can accurately measure student costs at the individual student level, receiving districts will have an incentive to accept only those students whose costs are below average for their subpopulation. Districts could, for example, only accept students with disabilities so long as those disabilities were classified in low-cost categories such as speech/language disabilities.

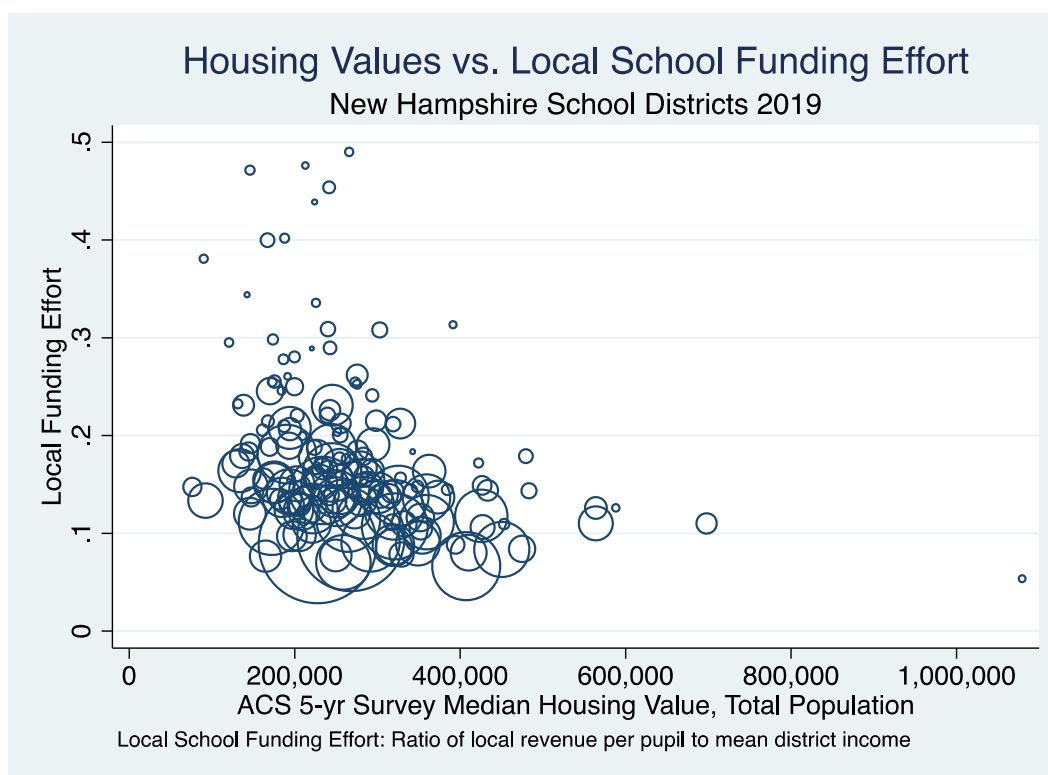


## Disincentivizing Local Effort

The methods do not account for the impact on local tax effort that any portability and inter-district choice program would trigger. To begin with, local taxpayers have an incentive to invest in their community's schools, as perceived school quality increases property values.<sup>10</sup> When, however, local revenues are transferred to other school districts, the incentive to raise local revenues for local schools is reduced. This creates a potential downward spiral: Local revenues fall, diminishing school quality, which causes more students to seek to transfer, which causes local revenues to fall further, and so on. None of this dynamic is accounted for in the report's design.

The districts most likely to fall victim to this decline are ones with relatively low property values. These districts already make a greater effort to raise local revenues than higher-value districts: They pay a higher percentage of their incomes toward local school taxes than more affluent communities. Figure 2 shows the median property values for school districts in New Hampshire plotted against their local revenue effort (ratio of local revenue per pupil to mean district income). There is a clear trend: As property values rise, effort declines.

**Figure 2**<sup>11</sup>



As it is likely students will transfer from low-value to high-value districts, revenues will move away from districts that make a greater effort to fund their schools. Local taxpayers will essentially be hit twice: once for living in a district with lower property values (which raises their effective property tax rates), and once for seeing more of their taxes transfer, through portability policies, to districts with lower local revenue effort.

## **VI. Review of the Validity of the Findings and Conclusions**

The report's fundamental misunderstanding of educational cost and its role in portability policies greatly impedes the validity of its recommendations. Because it focuses almost exclusively on revenue transfers, and not on the factors that influence educational cost, the report badly underestimates the likely consequences of its preferred policies.

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

Policymakers and other stakeholders who are predisposed toward expanding school "choice" will doubtless find the Reason Foundation's report appealing: Its facile descriptions of portability and its recommendations could lead readers to believe that portability can be easily scaled up with few dire consequences for public schools. In fact, the issue is highly complex, and the potential for fiscally damaging school districts is significant. Lawmakers who are considering policies to expand interdistrict choice would do well to seek out other sources of analysis to guide their work.

## Notes and References

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- 2 Smith, A.G., Barnard, C. & Campbell, J. (2023, January). *Public education funding without boundaries: How to get K-12 dollars to follow open enrollment students*. Los Angeles, CA: Reason Foundation. Retrieved February 20, 2023, from <https://reason.org/policy-brief/public-education-funding-without-boundaries-how-to-get-k-12-dollars-to-follow-open-enrollment-students/>
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- 5 EdChoice (2019). *The 123s of school choice: What the research says about private school choice programs in America, 2019 edition*. Indianapolis, IN: EdChoice. Retrieved February 20, 2023, from <http://www.edchoice.org/wp-content/uploads/2019/04/123s-of-School-Choice.pdf>
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- 8 Baker, B.D. (2021). *Educational inequality and school finance: Why money matters for America's students*. (p. 25). Boston, MA: Harvard Education Press.
- 9 Efficiency is usually conceived as separate from cost, as cost is often described as the *minimal* amount needed to reach an educational goal, with inefficiency accounting for spending above cost. For the purposes of this discussion, however, it is most useful to simply include efficiency as one of several determinates of student-level educational cost.
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