The Minnesota Miracle Abandoned? Changes in Minnesota School Funding, 2001-2007

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"The stability of a republican form of government depending mainly upon the intelligence of the people, it is the duty of the legislature to establish a general and uniform system of public schools. The legislature shall make such provisions by taxation or otherwise as will secure a thorough and efficient system of public schools throughout the state."

Constitution of the State of Minnesota, Article 13, Section 1.

The Constitution of the State of Minnesota, unlike the Constitution of the United States, grants its residents a substantive right to education. Minnesota guarantees its residents both a "general and uniform" public school system. The Minnesota Constitution charges the state government with upholding both the assurances of uniformity and efficiency, and the State has attempted to fulfill these requirements since its inception through a variety of school funding policies.

In this paper, we briefly track some of the most important changes to the state's education finance system over its history, including legal challenges that occurred along the way. We then examine in detail the important changes to Minnesota's system of financing that have been implemented since 2001. Finally, we examine what impacts these changes had on local school districts both in the short and medium term.

A Brief History of Minnesota Education Finance

Education finance in Minnesota has developed through many eras, shifting between various combinations of state and local

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funding.[1] Prior to 1956, education funding in Minnesota came primarily from local property taxes. Even prior to 1956, however, there were funding initiatives that were enacted that attempted to shift the financing of public schools from local property taxes to state assistance. For example, in 1915 Minnesota adopted its first form of equalization aid to supplement low-levy districts. Subsequently, when the state income tax was instituted in 1933, a portion of the money it collected was dedicated to school funding and distributed on a per-pupil basis.

Foundation aid emerged in 1957, which for the first time shifted the majority of school funding from local taxes to the state. Initially, the base per-pupil formula allowance covered the majority (84%) of per-pupil maintenance costs, but unfortunately it did not grow fast enough to keep up with inflation and increasing costs. As a result, within 13 years the percentage of costs covered by the state through this allowance formula had fallen back below half (43%) of districts' total costs.

Perhaps not surprisingly, Minnesota's school finance system came under legal attack for the first time. In October of 1971, a federal district court judge ruled in the case of *Van Dusartz v. Hatfield* that the Minnesota school finance system was unconstitutional[2]. Relying heavily upon a California case from earlier that year[3], the judge found that "the level of spending for a child's education may not be a function of wealth other than the wealth of the state as a whole" (*Van Dusartz v. Hatfield)*. The state's system of funding schools at the time was not in compliance with this decision; school funding varied based on property wealth in each district and the system was therefore unconstitutional. It was time for Minnesota to make some major changes.

The Minnesota Miracle and its Effects

Shortly after the *Van Dusartz* ruling, the Minnesota legislature passed a new omnibus tax bill which came to be known as the "Minnesota Miracle." This was not only a response to the recent legal challenge but also part of an effort to reduce property taxes (Knowles & Knowles, 2005). The bill shifted the main source of education funding in the state back off of local taxes and onto the state, reducing property taxes by instead increasing income and sales tax rates. The new legislation also called for classifying school districts based on their spending levels, and it equalized the foundation aid formula based on these classifications. This led to a considerable increase in the formula allowance. Prior to this, the formula allowance had covered only 55% of districts' median maintenance costs; it now paid for 93% of these costs. The exact percentages varied over time, but the state remained responsible for the largest share of school funding after 1971.

The system saw its next major changes in 1991 when the state initiated referendum equalization. The purpose of an equalization program is to reduce the effects of discrepancies in property values between districts and provide property tax relief to lower-wealth districts. When aid is equalized, the state essentially makes up the difference so that poorer districts are not forced to pay higher percentages of their property value in taxes in order to fund their schools. However, since this 1991 equalization program was tied to referendums, it made a portion of state aid dependant on the passage of the local levy. Districts that failed to pass levies did not receive this state aid (Knowles & Knowles, 2005). In some cases, this undoubtedly served to make disparities all the more apparent.

This new and supposedly equalized system set the stage for a new legal challenge. A few years after the 1971 *Van Dusartz* ruling, the U.S. Supreme Court had ruled on the case of *San Antonio v. Rodriguez.* In the *Rodriguez* decision, the Court declared that education is not a fundamental constitutional right, relegating it to a state issue and thus ending the first wave of school finance litigation based on the Equal Protection Clause of the U.S. Constitution (Grider & Verstegen, 2000; Verstegen, 1998). The majority of the Court placed the solutions firmly in the political system as they articulated their belief that the Congress or the states would find a solution to funding inequalities. Yet Justice Marshall's dissent expressed concern that "in the meantime, countless children [would] unjustifiably receive inferior educations…" (*San Antonio v. Rodriguez).* Although the majority of the Court chose not to mandate equality of public education under the U.S. Constitution, the door was left open for subsequent litigation across the country based on education provisions found in many state constitutions (Grider & Verstegen, 2000).

In 1991, a district court judge in the case of *Skeen v. Minnesota* ruled that the new referendum equalization system violated the equity guarantee found in the Minnesota Constitution, but the Minnesota Supreme Court reversed this decision two years later.[4] Ultimately, the Minnesota State Supreme Court did *not* find the school funding system to be a constitutional violation, and they did not order reform. However, the lawsuit did reflect the discontent some Minnesotans felt with the school finance system in the 1990s and perhaps served as a catalyst for political change.

School Finance Reform Since 2001

The Minnesota Supreme Court may have overruled the decision in *Skeen* that rendered the state school finance system unconstitutional in 1993, but the legislature continued to make changes to the system. Major developments in education finance came in 2001 in a series of reforms many lawmakers and columnists compared to the 1971 Minnesota Miracle. Writers from as far as Cleveland, Ohio, took notice of this second so-called miracle, recognizing Governor Ventura for the sort of "bold and historic" tax overhaul their state had been demanding for years to no avail (Sheridan, 2001). Ventura himself sang the praises of the 2001 tax bill. He called it "historic and bold to the very last detail" and predicted it would be "a major property tax relief that finally brings fairness to the system" (Baden & Smith, 2001).

However, other state politicians were less enthusiastic. Representative Tom Rukavina (D-Virginia) was one lawmaker who expressed some skepticism. "I don't know how badly this bill will come back to haunt us," Rukavina said, "but I predict in a couple of years it will haunt us" (Baden & Smith, 2001).[5]

Of the reforms that passed in 2001, two were most significant. Perhaps the most important change was a $415 "roll-in" of local referendum revenue per pupil. Under the reforms of 2001, each school district's voter-approved referendums would be reduced by $415 per pupil. That amount would correspondingly be paid to the school district by the state in the form of increased general education formulas. In principle, the goal was to reduce the local share of financing education and replace that revenue using state funds. Indeed, this approach was very similar to the "Minnesota Miracle" of 1971.

Table 1 demonstrates the effect that the "roll-in" had on the general education formula. In 2002-03, the General Education

Table 1: *Basic General Education Formulas, 2001-2003.*

Year	Formula Allowance	% Increase from Previous Year	Inflation Rate
2001-02	$4,068	2.6%	1.6%
2002-03	$4,601*	13.1% (2.9%**)	2.3%

Source: Minnesota House of Representatives Fiscal Analysis Department; Bureau of Labor Statistics

** The 2002-03 includes a $415 conversion of referendum revenue into the basic formula.*

*** Percent increase without referendum revenue roll-in.*

Formula allowance increased from $4,068 to $4,601 per student, a 13.1% increase. While that may appear to be a significant increase for Minnesota school districts, it is important to remember that $415 of that increase did not benefit school districts at all, but rather school district taxpayers in the form of the "roll-in"(i.e. the state taking over $415 of locally approved referendum payments). The actual increase to school districts was a much more meager 2.9%.

It should also be noted that much of the new revenue tied to the $415 per pupil of referendum value went to the wealthiest districts in the state. Referendum revenues are equalized, with poorer districts paying less of the total excess levy cost than wealthier districts. When the state took over the full cost of the $415 "roll-in," the net effect was to pay districts for the non-equalized portion of the local levy.

The second important component of the 2001 reforms was that the general education levy that was previously administered statewide on all properties to pay for the general education formula was eliminated and picked up by the state for fiscal year 2003 and thereafter. Prior to 2003, each district levied their district taxpayers the uniform state rate (in 2002 the flat general levy rate was 0.3241%), and the state paid the school districts the difference between the amount collected and the general education formula allowance. So for more property-poor districts, the state would pay a higher share of the general education formula. For wealthier districts, more money for the general education formula would be provided through local property taxes.

For fiscal year 2003 and thereafter, the state would pay the entire amount of the general education formula allowance without any contribution from district taxpayers. The cost to the state was staggering. The total cost to eliminate the general levy rate cost the state $1.33 billion in the fiscal 2003 year alone.

Driven largely by the increased state expenditures due to the $415 "roll-in" and the elimination of the general levy rate, state educational expenditures shot higher. Table 2 lists the state education

Table 2: *Education State Aid Entitlement, 2001-2003.*

Fiscal Year	Total State Aid	Percent Change from Previous Year	Aid Per Pupil	Percent Change from Previous Year
2001	$4.27 billion	7.9%	$4,998	7.7%
2002	$4.33 billion	1.6%	$5,090	1.9%
2003	$6.09 billion	40.5%	$7,189	41.2%

outlays from 2001 through 2003. The changes that occurred in 2003 increased the state's overall educational payments by over 40% from the previous year.

So with such a huge investment in state dollars, where did all of this money go? Contrary to what many believed, very little of it went to school districts. As was previously demonstrated, none of the school districts that previously had $415 referendums received any additional revenue from the "roll-in." Only the district taxpayers saw the benefits of that change. Similarly, school districts did not receive any additional revenues by the state eliminating the general education levy. So, of this $1.76 billion of total increased spending on education, very little of it was used to actually benefit school districts. Virtually all of it went to district taxpayers.

So which taxpayers benefited the most, and which districts experienced the greatest increases in state revenue? Not surprisingly, wealth in Minnesota tends to be distributed disproportionately in the Twin Cities metro area. Figure 1 visually displays the average wealth per pupil (referendum market value per pupil) in Minnesota school districts. A close inspection of Figure 1 shows that the school districts with the lowest 20% of wealth in the state of Minnesota are scattered throughout rural Minnesota, and the wealthiest districts tend to be located in the Twin Cities metro area.

Minnesota's property wealth also tends to be distributed disproportionately among the largest school districts in the state. Table 3 shows that in school districts with the lowest enrollments, the average property wealth per pupil is just over $113,000. In the largest school districts in the state, average property wealth is over $260,000 per pupil.

Table 3: *District Wealth in Minnesota School Districts, by Enrollment Quintile, 2003.*

Enrollment Quintile	District Wealth Per Pupil (Average)	District Wealth Per Pupil (Median)
Lowest 20%	$113,680	$102,105
21 – 40%	$134,067	$120,682
41 – 60%	$132,869	$124,349
61 – 80%	$178,849	$141,253
Highest 20%	$260,814	$223,540

Source: 2003 Referendum Market Value per Pupil, Minn. Department of Education

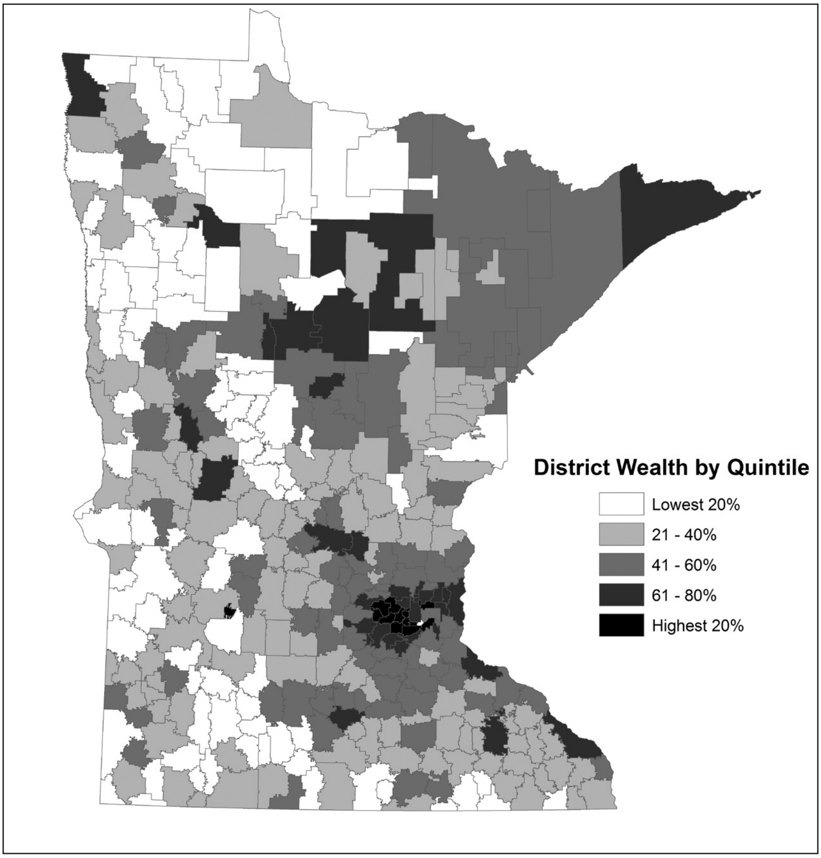


Figure 1: *Wealth per Pupil in Minnesota School Districts, 2003.*
Source: 2003 Referendum Market Value per Pupil, Minnesota Department of Education.

Table 4 shows then where the additional state revenues went to pay for the elimination of the general levy. The school districts with the lowest property values received an average of just over an additional $1,100 per pupil in aid from the state while those districts with the most wealth received over $2,200 in new aid from the state due to the elimination of the general levy.

Table 4: *Additional State Revenue Per Pupil Paid to Districts in FY 2003 Due to Elimination of Basic Levy, by Wealth Quintile.*

Wealth Quintile	Additional State Dollars Per Pupil (Average)
Poorest 20%	$1,107
21 – 40%	$1,255
41 – 60%	$1,190
61 – 80%	$1,375
Wealthiest 20%	$2,240

Source: Minnesota Department of Education

Table 5 translates this into the percentage change in total state aid due to these changes. While the poorest school districts saw their percentage increase in funding grow over 42%, the wealthiest school districts had mean increases of more than 109%.

Table 5: *Percentage Change in Total State Aid to Minnesota School Districts, 2002-2003 (by Wealth Quintile).*

Wealth Quintile	Percentage Change in Total State Aid (Average)	Percentage Change in Total State Aid (Median)
Poorest 20%	+42.3%	+33.1%
21 – 40%	+46.5%	+39.1%
41 – 60%	+37.5%	+32.8%
61 – 80%	+43.1%	+43.1%
Wealthiest 20%	+109.2%	+61.3%

State Mean: +51.5% ($1.7 Billion Increase)
Source: Total State Aid to School Districts, Minnesota Department of Education

The Fallout from the 2001 Reforms

The 2001 reforms were very costly and committed the state to billions of dollars of new spending for the benefit not so much of school districts but for the district taxpayers in the wealthiest school districts in Minnesota. However, hard times fell on the state almost immediately following the reforms.

The slowing of the national economy had significant effects on Minnesota tax revenues. The effects were most pronounced on taxable incomes, which were hit hardest by the slowdown. Saddled with an enormous amount of new entitlements toward education and other programs while simultaneously experiencing slow revenue growth, deficit estimates for the 2004-2005 biennium topped $4.2 billion.

Not surprisingly, the state moved to slow education spending. Table 6 shows that after the increase in the General Education Formula allowance in 2002-03, the state actually froze the formula for both 2003-04 and 2004-05.

Table 6: *Basic General Education Formulas, 2000-2006.*

Year	Formula Allowance	% Increase from Previous Year	Inflation Rate
2002-03	4,601*	13.1% (2.9%**)	2.3%
2003-04	4,601	0.0%	2.7%
2004-05	4,601	0.0%	3.4%
2005-06	4,783	4.0%	NA
2006-07	4,974	4.0%	NA

Source: Minnesota House of Representatives Fiscal Analysis Department; Bureau of Labor Statistics

** The 2002-03 includes a $415 conversion of referendum revenue into the basic formula.*

*** Percent increase without referendum revenue roll-in.*

The effects of this freeze were severe for local school districts. While overall inflation increased over 6% during this period, the costs of employee healthcare and fuel costs rose even more significantly.

Compounding the problem were widespread declining enrollments in Minnesota schools. Table 7 shows the change in enrollments in Minnesota school districts between 2001 and 2005. Over 10% of districts lost 15% or more of their enrollment, while 30% of districts lost over 10% of their enrollment. Over 75% lost at least some enrollment during this period.

Table 7: *Change in Enrollment in Minnesota School Districts, 2001-2005.*

Change in Enrollment	Percent	Cumulative Percent
15.0% or Greater Decline	10.8%	10.8%
10% to 14.9% Decline	19.2%	30.0%
5% to 9.9% Decline	24.2%	54.2%
0.1% to 4.9% Decline	22.7%	76.9%
Percent with Enrollment Losses		**76.9%**
0.0% to 4.9% Gain	10.3%	87.2%
5.0% to 9.9% Gain	5.5%	92.7%
10.0% to 14.9% Gain	2.8%	95.9%
15.0% or Greater Gain	4.1%	100.0%
Percent with Enrollment Gains		**23.1%**

Note: Enrollments standardized using current WADM calculations.

Table 8 shows that much of this decline disproportionately affected the smallest school districts in the state. In previous work (see Thorson and Edmondson, 2000; Thorson and Maxwell, 2002), we found that the smallest school districts in the state were being hit the hardest by stagnant budgets. Table 9 shows that the smallest schools were hit the hardest by these enrollment declines as well. While the smallest school districts in the state lost an average of 10% of their student populations, the largest districts in the state had small but measurable increases.

Table 8: *Change in Enrollment by Quintile, 2001-2005.*

Quintile	Mean Enrollment Decline
1^{st} (smallest)	-10.1%
2^{nd}	-4.9%
3^{rd}	-6.6%
4^{th}	-4.0%
5^{th} (largest)	+1.4%
State Mean	**-5.1%**

Table 9: *Levy Amounts Subject to Equalization, 2001-2007.*

Year	Equalization
2001-02	$415
2002-03	$126
2003-04	$126
2004-05	$405
2005-06	$500
2006-07	$600
2007-08	$700

Coupled with stagnant per-pupil general education revenues, these enrollment drops precipitated the need for school districts to balance their budgets using a combination of steep cuts and the reinstatement of local levies. The state responded accordingly. Realizing that state revenues were insufficient to meet the obligation of providing the entire general education costs, the state moved to increase the local levy amounts that would be eligible for equalization.

Table 9 shows that after the "roll-in" of $415 per pupil that was enacted in 2001, the state quickly moved to increase the local financing of public schools through its attractive equalization program. After declining to just $126 in 2002, the state increased the amount subject to equalization to $405 in 2004, $500 in 2006, and $700 in 2007.

The state had now come full-circle with regards to the financing of its public schools. While conceptually wanting to fully fund Minnesota public schools at the state level in 2001, by the 2007 school year, the state had offered greater incentives than ever for schools to fund locally.

Figure 2: *Total Minnesota school district referendums passed, 1991-2005.*

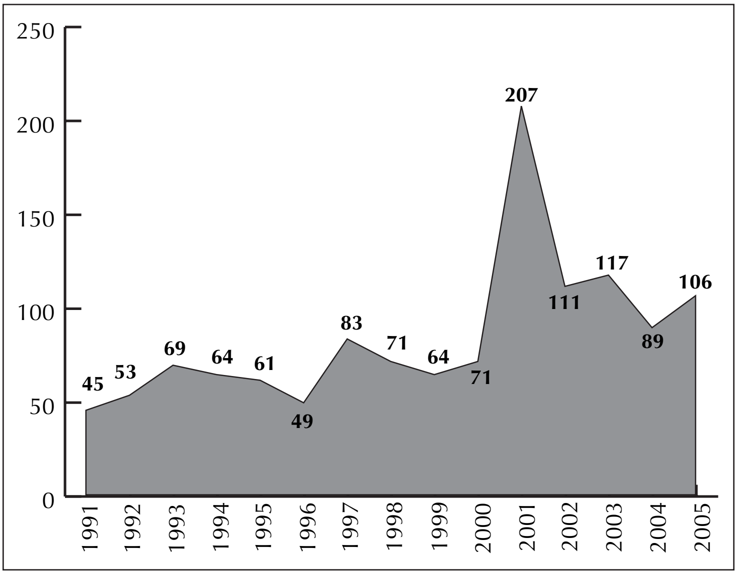


Figure 2 shows that a number of Minnesota school districts accepted these incentives for local levies. Minnesota school district voters passed large numbers of local referendums over this period. Indeed, many school districts, to the consternation of Governor Ventura, passed new school referendums at the same time that the state was "rolling in" their previous referendum. A whopping 207 school districts passed operating referendums in 2001. Figure 2 demonstrates that although the number of referendums passed lessened a bit in subsequent years, it has remained nevertheless historically very high.

The result of this activity is summarized in Figure 3. Despite the state's interest in fully funding the education of Minnesota's students, it has largely been unable to do so. The average referendum has increased for all size of school districts since 2003, and for many school districts, the amount levied is now more than prior to the "roll-in" in 2001.

The aggregate impact is visually displayed in Figure 4. While the percentage change in total state aid increased dramatically in 2003 due to the state eliminating the general education levy and the $415 per-pupil roll in of local referendums, few school districts saw much new revenue. Since that time, the percentage actually decreased in 2004 and 2005. In fact, the total Minnesota state spending on education entitlements *decreased* during that period from $6.08 billion to $6.01 billion.

Figure 3: *Minnesota school districts' average referendum per pupil by enrollment quintile, 2000-2006.*

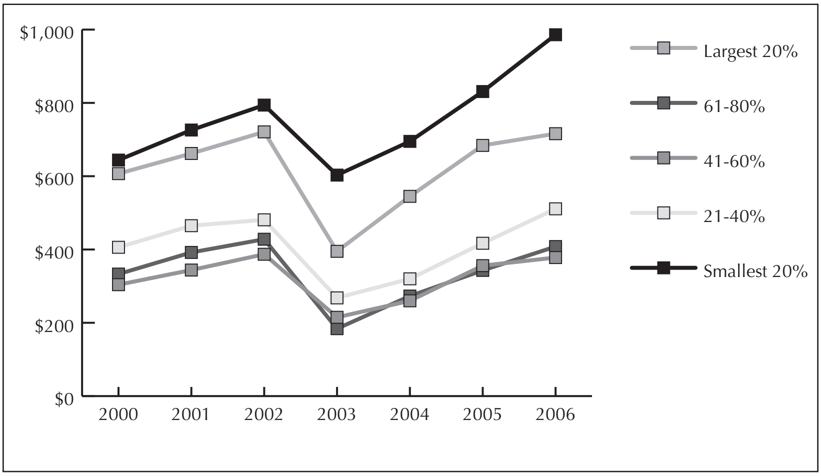
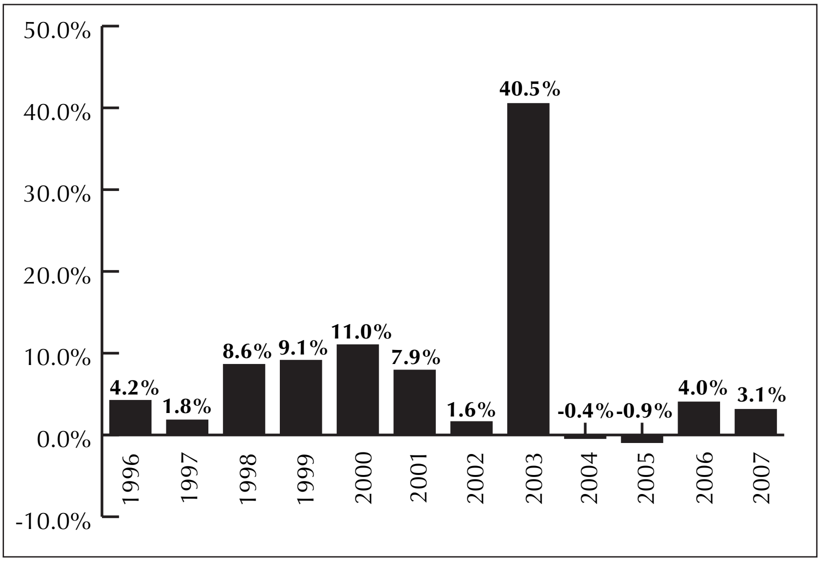


Figure 4: *Percentage change in total state aid entitlements, 1996-2007.*



Conclusion

Supporters of the education reforms passed by the state of Minnesota in 2001 pledged that a new era was unfolding in Minnesota where the state would finance the full educational costs of Minnesota's public school children. Many thought that these reforms would finally realize the vision established in the 1971 "Minnesota Miracle."

In reality, however, the reforms delivered little to Minnesota's school districts except for financial distress. Very little of the more than $1.7 billion pumped into education by the state even went to school districts. Most of the money went to reduce the property tax burden of district taxpayers by eliminating not only most local school referendums, but also the general education levy that previously paid for much of the cost of educating Minnesota's school children. Indeed, most of the money went to relieve the wealthiest property tax owners in the wealthiest school districts in Minnesota.

The aftermath of the reforms was also poor for Minnesota's school districts. The state's decision to offer tax relief to district taxpayers was untimely. When significant fiscal stress subsequently occurred, the state could not even meet the continuing inflationary needs of the state's school districts. Combined with widespread declining enrollment, Minnesota school districts were forced to cut educational programming as well as go back to the taxpayers and reinstate levies that in many cases were even higher than those that existed prior to the 2001 reforms.

Ultimately, the 2001 reforms did little to move Minnesota closer to the promise of the "Minnesota Miracle." Enormous state expenditures that appeared to direct more state spending to school districts instead simply served to provide tax relief disproportionately to the wealthiest Minnesotans living in its wealthiest school districts. The "Minnesota Miracle," with its promise to provide full state funding for the public education of every child in the state, appears today as elusive as it did in 2001.

Endnotes

[1] Unless otherwise noted, the data from the pre-2001 period was taken from the Minnesota School Finance History report from 1849-2005 issued by the Minnesota Department of Education.
[2] Plaintiffs in *Van Dusartz v. Hatfield* alleged that Minnesota's school finance system was in violation of the Equal Protection Clause of the 14th Amendment of the U.S. Constitution.
[3] *Serrano v. Priest* was decided in California in August of 1971.
[4] The Minnesota Supreme Court reversed the trial court's decision, ruling that "the current system of state funding of education does *not* violate the Education Clause of the Minnesota Constitution" (*Skeen v. State*, 1993; italics added).
[5] The two articles in which these quotes were found ran in the Star Tribune on July 1 and June 29, 2001, respectively. Both were co-authored by Patricia Lopez Baden and Dane Smith, and both were front-page stories.

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