



HOLD HARMLESS POLICIES IN EDUCATION FUNDING

This overview provides background on the Hold Harmless (HH) provision in Illinois's last school funding formula change and other recent HH approaches to school funding in Illinois and in other states. This overview closes with suggestions for any hold harmless to be considered as part of the current education funding reform conversations taking place in Springfield.

The Purpose and Impact of Hold Harmless Provisions

HH provisions in the context of education funding “are meant to restrict declines in revenues for school districts, and they may take a number of forms, including limits on the changes in state aid from year to year, supplemental funding for districts with declining enrollment, alternatives for calculating the state aid amount, or use of past enrollments in grant calculations”.¹

While HH provisions ease the transition to changes in policy, it is important to think through their ripple effects. Experts reviewing provisions in several states have noted that the level of funding allocated through an HH can in some instances work against student achievement:

“Districts that are overpaid have no incentive to attract new students, as their state aid would not go up, and, in fact, would be better off on a per-pupil basis if some of their current students left.... An obvious downside is that these policies cause less funding to be available for all other districts. But such allocations also insulate district leaders from having to make tough (and often productivity-enhancing) changes in the way they serve the students they have.”

Illinois: General State Aid Hold Harmless (FY97 – FY10)

With the General State Aid (GSA) formula change in 1997, an indefinite HH provision was added guaranteeing school districts at least the same amount of GSA they received the year before. The first year cost was \$23.2 million and the general expectation was that as increased funding was added to GSA, school districts would naturally grow out of the Hold Harmless.

But it was not so simple. Although there was an inverse relationship between GSA and GSA HH (that is, as the GSA allocation increased, the GSA HH cost decreased), individual districts became eligible for GSA HH for a variety of reasons. In its first year, 261 districts qualified. In Fiscal Year (FY) 2011, as the Illinois State Board of Education (ISBE) was attempting to phase out GSA HH, 101 districts qualified. Just 21 of them were eligible every year. Another 18 were eligible intermittently. The remaining 62 “fell into” the HH sometime in between, for a variety of reasons unrelated to the formula change, including:

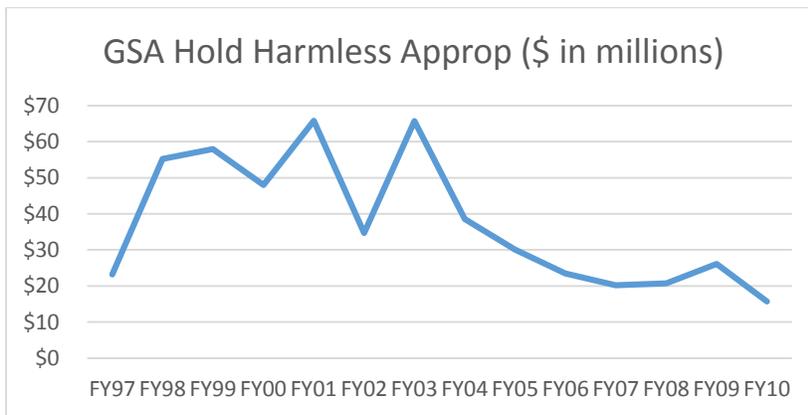
¹ Toutkoushian, R., & Michael, R. (2008). The impacts of school funding formula modifications on equity, fiscal neutrality, and adequacy. *The Journal of Education Finance*, 33, 352- 380.

- Decreased student enrollment;
- Increased local property wealth; and
- Decreased poverty rates.

In its FY10 budget proposal, ISBE recommended beginning a phase out of the HH over three years. The FY10 allocation of \$15.7 million represents 50% proration of the full claim. In FY11, the legislature eliminated the HH.

GSA HH Appropriation (in millions)

FY97	FY98	FY99	FY00	FY01	FY02	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10
\$23.2	55.2	58.0	48.0	65.8	34.7	65.7	38.6	30.1	23.5	20.2	20.7	26.1	15.7



Key Takeaway: A HH that is intended to be narrowly targeted to protect districts from a one-time formula change must be structured carefully. Creating a HH that lasts in perpetuity could have the unintended result of sheltering districts from decreased enrollment, decreased poverty, or increased local wealth, which are unrelated to the formula change.

Other Illinois Hold Harmlesses

Below, five Hold Harmlesses are discussed:

1. The Poverty Grant Hold Harmless (FY03 – FY08).
2. The Special Education Extraordinary Funding Hold Harmless (FY04 – present (unfunded, but still in statute)).
3. The Chicago Block Grants (FY96 – present).
4. Transitional Assistance (FY04 – FY09).
5. The FY17 General State Aid allocation.

Poverty Grant Hold Harmless

In FY04, the methodology for counting low-income students changed from decennial census data to enrollment in Department of Human Services programs. The change initially passed with a four-year phase-in guaranteeing districts 100% of their FY03 low-income grant allocation. Each year from FY05 – FY07, the HH was extended in the Budget Implementation bills, maintaining the 100% Hold Harmless to FY03, while continuing to phase in the increases. It was fully implemented in FY08.

Key Takeaway: The structure of the Poverty Grant HH reflects lessons learned from the GSA HH seven years previously. The built-in end date provided time for adjustment to a new metric, but not so much time that it would significantly distort poverty distribution overall.

Special Education Extraordinary Funding Hold Harmless

In 2004, the legislature changed the “Special Education – Extraordinary” program, which was based on claims reimbursement for special education costs, to “Funding for Children Requiring Special Education Services,” which was based on a formula of average daily attendance and poverty rates. A HH was in place from FY05 – FY07 guaranteeing at least the same amount allocated to each district in FY04. In FY08, the legislature added a continuance to the HH without an end date, though the regular formula claims are paid first and the HH is only paid if addition amounts are appropriated. The program was funded in FY08 through a supplemental appropriation (\$21.0 million). (It is unclear if it was funded within the line item in subsequent years.)

Key Takeaway: Again, the formula change initially built in an end date to the HH after learning from the experiences of the GSA HH. But districts that were not pleased with the new formula and their legislators lobbied to re-instate the HH in statute where it remains today.

The Chicago Block Grant

As one component of a major Chicago school reform package in 1995, the Chicago Block Grants were created to reduce bureaucracy and maximize flexibility for Chicago Public Schools (CPS). Mandated categorical programs, the Early Childhood Block Grant, bilingual education, and other programs were subject to the block grant, which guaranteed CPS would receive the same percentage of each line item as it received in 1995, regardless of changes in student enrollment and service levels.

In 2011, P.A. 97-238 (Althoff/Eddy) was enacted, requiring CPS to begin reporting claims data. Based on ISBE’s report analyzing that data, the Chicago Block Grant has resulted in CPS receiving about \$250 million more in state funding than it would receive if it filed claims for reimbursement in the same way as other districts.

Key Takeaway: The Chicago Block Grant has become a highly-politicized issue. While some call it a perk for Chicago, CPS would point out that it has to pay \$650 million in pension costs that no other district pays. Undoing this HH without hurting CPS students is challenging in a vacuum, but it makes sense to look holistically at pension parity and phasing out the Chicago Block Grant at the same time.

Transitional Assistance

As a component of a budget deal in FY04, a new budget line was introduced that would hold every school district harmless to its total state appropriation the prior year. That is, if a district’s total state claim for all programs (GSA, MCATs, Bilingual education, etc.) is less than its FY03 claim, it would receive a grant to bring it up to its FY03 amount for one year only. The cost was \$5.2 million. The program was funded the next four years, up to a high point of \$36.8 million in FY09. It has not been funded since then.

Key Takeaway: When the budget crunch hit, Transition Assistance quit getting funded. The one-year, subject-to-appropriation nature allowed the legislature to thoughtfully prioritize spending without locking them in.

The FY17 GSA Appropriation

This year, amid a budget stalemate and multiple school reform proposals, a GSA funding scheme was enacted that essentially created an FY16 HH and an equity grant based on FY16 poverty levels. Districts that would have received an increase in FY17 were brought up to their FY17 GSA level.

With or without formula changes, districts' GSA allocations fluctuate each year based on a variety of inputs: Equalized Assessed Valuation of its property, average daily attendance, the number and concentration of students enrolled in DHS programs, the amount of Corporate Personal Property Replacement Tax it received, the change to the amount of property taxes tax-capped counties are eligible to collect. HH provisions do not just isolate the difference of having a new formula; they also lock in place all of these factors that shift year to year.

If GSA were fully funded in FY17, 323 school districts would have received less GSA than they received in FY16 despite a small increase in the total appropriation.

Key Takeaway: The plan works for a one-time budget proposal, but is not a long-term solution since it relies on demographic data that will shift over time. Both Equalized Assessed Valuations and Low-Income Counts are frozen at FY16 levels in the FY17 education budget, which sets the stage for a formula overhaul in FY18.

Other States and Hold Harmless Provisions

A 2014 analysis of Hold Harmless in main education funding formulas across states found that 12 states had true "Hold Harmless" provisions, 22 states (including Illinois) had provisions to ease loss of state funding for declining enrollments, and 16 states had neither of these.² Of the 12 states with Hold Harmless, three are being phased out:

- Louisiana: A HH was included when the formula was changed in FY01 and began a 10-year phase out in FY08. Funding collected through the phase-out was first distributed on a per-pupil basis to non-HH districts, and later became a source for performance-based funding.
- Mississippi: A HH component was included when MS enacted its formula in 1994. In 2014, the legislature put in place a phase-out that would eliminate the provision by 2018. Just seven of MS's 145 districts qualify for HH funding.
- Rhode Island: RI changed its formula in 2010, effective in 2012, and included a seven-year phase-in for districts receiving increases and a 10-year phase-out for districts with decreasing state revenue.

² Michelle J. Atherton and Meghan E. Rubado, "[Policy Brief: Hold Harmless Education Finance Policies in the U.S.: A Survey](#)," Center on Regional Politics, December 2014.

The nine states with HHs with no phase-out are Connecticut, Massachusetts, Maryland, Nebraska, New Hampshire, North Dakota, New York, Ohio, and Pennsylvania. The study found that HHs were correlated with region (northeastern states had them more than others) and state share of resources (where the state share of funding was lower, HHs were more likely).

In their 2013 article,³ Jon Fullerton and Marguerite Roza (who worked with ISBE on an SB16 analysis) calculated that Massachusetts's HH provisions account for 3% of the total education budget. They call these provisions (and their article) "Funding Phantom Students," arguing that

"Districts that are overpaid have no incentive to attract new students, as their state aid would not go up, and, in fact, would be better off on a per-pupil basis if some of their current students left.... An obvious downside is that these policies cause less funding to be available for all other districts. But such allocations also insulate district leaders from having to make tough (and often productivity-enhancing) changes in the way they serve the students they have."

Other examples of unusual structures of Hold Harmless or Declining Enrollment Provisions include:⁴

- Pennsylvania seems to have the most egregious HH in the country: districts are held harmless to their 1993 allocation and are guaranteed a portion of increases to other programs, regardless of local wealth or declining enrollment.
- Missouri holds districts harmless to the prior year's per pupil funding amount. (The authors did not consider this a HH, though some would dispute that categorization.)
- California's new formula, effective in FY14, holds districts harmless per pupil to FY13 levels if a loss was due to the formula change, but not if due to declining enrollment.
- New Jersey's [unfunded] HH provision does not apply to districts that have lost over 5% of enrollment.
- Wisconsin does not allow districts to lose more than 15% in total funds from the prior year.

Key Takeaway: There are plenty of ways to structure a HH provision, some good and some not-so-good, reminding us again that these policies should be well thought-out before proceeding.

Options

The structure for a Hold Harmless that Illinois selects will need to strike an appropriate balance between the need to efficiently invest limited state resources and the need to provide sufficient planning time to districts during the transition. It should also account for changing enrollments, demographics, and property wealth over time. Here are some ideas, most of which have smart minds who have been pondering this topic for years now. They are not necessarily mutually exclusive and two or more could be used jointly:

1. **A per-pupil, per Available Local Resources HH.** If District X has Available Local Resources (ALR) of \$2,000 per pupil and its local wealth grows to \$3,000 per pupil, the HH should account for that change. Perhaps instead of being held harmless to, for example, \$8,000 per pupil, the HH

³ Marguerite Roza and Jon Fullerton, "[Funding Phantom Students](#)," Education Next, Summer 2013.

⁴ Atherton and Rubado.

would have a corresponding adjustment and decrease to \$7,000. In other words, if local wealth increases, the HH would not shield districts from the intent of the equalization formula.

2. **A two- (or three- or four-) year HH followed by a two- (or three- or four-) year phase-out.** This provides time for districts to adjust to the new funding level. Four years after a formula is put in place, demographics and property wealth will have shifted, and at eight years, those changes will have been significant.
3. **A loss limit HH.** A district's per pupil decrease in state resources could not grow more than \$1,000 (or \$500 or \$100) per year until the new formula is fully phased in.
4. **Once out, always out.** After a district grows out of its HH in a year, it is no longer eligible to receive HH funds for the duration of the HH. (Recall that of the 261 districts eligible for IL's GSA HH, only 21 were eligible each year. Eighteen were eligible intermittently and others "fell into" the HH.)

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