



4-1-1998

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#### Recommended Citation

Treaster, Sharon and Thompson, David C. (1998) "Kansas Public Education and Property Tax Relief in the 90's," *Educational Considerations*: Vol. 25: No. 2. <https://doi.org/10.4148/0146-9282.1375>

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Taxpayer dismay with rising property taxes was the reason for lowering the mill levy, but . . . the legislature has created another monster.

# Kansas Public Education and Property Tax Relief in the 90's

Sharon Treaster and David C. Thompson

Equity is one of the main objectives of school finance. School finance formulas are supposed to emphasize two aspects of equity: fairness for the children who are being educated and fairness for the taxpayers who defray the cost of education. In 1905 Ellwood P. Cubberly alleged that all the children of the state are equally important and are entitled to the same advantage. Maintaining that it was the state's responsibility to establish and sustain public schools and that all children were entitled to a basic education regardless of the wealth of the district, Cubberly sought to establish the impetus for state aid to local districts to fund the operation of schools.

In 1991, 86 years later, Judge Terry Bullock of Kansas declared that he wanted the Legislature to enact legislation that would provide an equal education for all children of Kansas, and they were to have this accomplished in the legislative session of the spring of 1992. Judge Bullock was reiterating what Cubberly had said 86 years earlier: all children are entitled to an equal education.

Yet Kansas lawmakers continue to search for solutions to this problem of equity and the school finance structure is eventually affected. This paper reviews Kansas' current public school finance system, and discusses the recent efforts of the legislature to provide property tax relief.

## Historic Background

Kansas did not enact its first educational state aid plan until 1937, a temporary act that became permanent in 1939 (Kester & Kester, 1988). From 1939 until the passing of the School Foundation Act in 1965, the financial support of school districts in Kansas was a melange from at least a dozen local and state sources.

In 1961 there were more than 2,000 school districts in Kansas. Historically, tangible property valuation, either assessed or adjusted, had been the sole basis for determining local 'need' under the Kansas school aid programs that were in effect. An elementary aid law, enacted in 1949, required the deduction from each school district's guarantee of an amount equal to two mills on the assessed valuation of the district. The

high school aid law, enacted in 1955, provided for a two-mill deduction on the adjusted valuation to be determined by use of the annual assessment ratio study made by the Property Valuation Department (KLC, 1960).

The State School Foundation Fund, SB 281, enacted in 1965, provided for state financial aid to elementary and high schools; created a state school foundation fund and a country school foundation fund; provided for the distribution of these funds under formulas stated in the act; and created a school budget review board and authorized tax levies (1965 Laws of Kansas, Ch 402).

Reform interest escalated to historic proportions during the 1960s and 1970s. The period of the 1970s in particular, saw many court decisions which ruled state systems for financing education unconstitutional because of extreme variations in wealth. In 1972, *Caldwell v State of Kansas* determined the Kansas school finance formula unconstitutional. The state was prohibited by the court from operating the foundation school finance system and was ordered to: (a) reallocate the funds available for support of the system, including funds derived from property taxes levied by school districts, and (b) restructure the financial system in such a manner that would not violate the required equal protection of law.

The decree of this Johnson County district court case in 1972 led to the demise of the foundation plan and the enactment of the School District Equalization Act. No specific system of financing or taxation was mandated by the court nor did it prohibit the use of property tax to finance schools.

## The School District Equalization Act

The School District Equalization Act (SDEA) was enacted in 1973. The general state aid formula in the SDEA was based on the 'district power equalizing' concept. In general, the formula was one under which a district local effort rate (LER), a percentage, was set by the state board of education in accord with law for a specified or "norm" budget per pupil (BPP) as determined under a schedule which divided districts into five enrollment categories. Under the SDEA, lawmakers were trying to balance the cost and quality of education. Fairness was to come by giving more state aid to districts less able to pay for their schools. Most of the aid was intended to cut reliance on the property tax so all students received an equal education, regardless of how wealthy their districts.

The School District Equalization Act was driven by the idea that districts of different sizes needed to spend at different levels and the districts of the same size should spend about the same (*Wichita Eagle*, January 26, 1992). What the SDEA accomplished was to increase the amount the poorest districts could spend and limited the amount richer districts could spend. What it did not accomplish was to eliminate the disparities in spending between rich and poor districts, nor evened out the property tax burden statewide. Some districts had five times the property tax rate of others.

Starting in the 1988-89 school year a provision for 'hold harmless' aid was added to the SDEA. If the general state aid and income tax rebate combined were less than the amount received in the preceding year, the district would receive hold harmless aid equal to 50% of the difference in 1987 and 87.5% in 1989.

Trouble surfaced in 1989. There was an alarming shift in the formula of school district wealth; a crucial factor in setting the amount of aid for districts. Federal tax cuts, effective in 1988, exposed more income to Kansas taxation. Kansas property reappraisal in 1989 skewed the traditional results further. Suddenly, taxable income comprised an average 56% of the wealth of state school districts and property values only 44%. Many districts by 1990 faced dramatic cuts in state aid without revision of the formula. Districts were guaranteed the same

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per-pupil aid that they had received in 1989, but more than 20% of the state's 304 school districts were losing enrollment and losing aid.

The original basis for implementing the SDEA was to provide an adequate level of funding for school districts, to determine local capacity to pay for educational services, and to recognize the impact of resources on educational opportunity through the principle of state aid in inverse proportion to local ability to pay. According to a study by Thompson, et al (1991) two factors profoundly affected the equitable operation of the SDEA: (a) the equalization of property wealth as a major element in determining local ability to pay for education, and (b) the establishment of median budgets per pupil based on the enrollment size of the school district.

Lawmakers promised to offer a new formula for the 1991 legislative session and many school districts promised to sue. Three lawsuits were filed against the state claiming that state aid to schools was no longer equitable in spite of the formula designed to guarantee it. The Wichita school district, citing a \$10 million loss in state aid, filed the fourth challenge to the state school finance law (Wichita *Eagle*, Oct. 16, 1991). Because state aid is determined on a per-pupil basis, the ceiling might force large districts to lose more in dollars than districts with small enrollments. Thus, the claim was that the hold harmless ceiling discriminated against large districts and shattered the provision for "equalizing" in the aid formula.

The provision tried to protect districts from huge losses by guaranteeing that a district would lose no more than 12.5% of state aid. But the state set a \$700,000 ceiling on the protections. Because of that, when the Wichita district lost \$12.4 million, it could recover only \$700,000.

The 18-year-old school finance formula was designed to distribute aid in such a way that students would receive comparable educations whether they came from rich or poor districts. The main factors in the 'equalization' formula were district wealth (property values plus a percentage of taxable income), enrollment and the size of school budgets. Equity was supposed to come from giving more state aid to districts less able to pay for their schools. But the equalization formula wasn't used in calculating all state aid. In 1991, the formula applied to \$527 million in direct aid to school districts, but it didn't figure in the distribution of \$121 million in special education aid, \$45 million in transportation aid, or \$199 million in income tax rebates to local districts. Thus 41% of the \$892 million in major school aid escaped the equity formula.

Many districts complained that the income tax rebate was a special windfall for wealthy school districts. The rebate returned a fourth of the state income taxes to the districts from which they were collected. In wealthy Johnson County, six school districts received 40% of the total.

Shawnee County District Judge Terry Bullock had been assigned to hear four lawsuits challenging the way Kansas paid for taxes. But instead of bringing the cases to trial in October 14, Bullock called Governor Joan Finney and legislative leaders together and asked them to try to resolve the problems raised by the plaintiffs. Judge Bullock declared that he wanted the Kansas legislature to enact legislation that would provide an equal education for all children of Kansas, and they were to have this accomplished in the legislative session of the spring of 1992. Judge Bullock said the Kansas Constitution required the legislature to distribute money so that each child has an equal opportunity for a good education. He noted that providing each school child an equal opportunity for education is not the same as spending the same amount on every child. The legislature has to spend more on some children to give them the same opportunities enjoyed by others. He also said the legislature must have a rational educational explanation for any difference in how much is spent on one child compared to another. Bullock said the system was so unfair that it was

denying children equal opportunities to education. He especially criticized the way school districts levy property taxes, noting that the level of property taxation ranged from a low of 15.55 mills in the town of Burlington to 110.85 mills in Olathe.

If property taxes are set by local school districts, what right does the state have to intervene in mill levy rates? Judge Bullock argued that, essentially, school districts are merely political sub-divisions of the state. Any taxes they raised could be polled by the state and distributed throughout the state based on need. That varied radically from the system then used, where property taxes were levied by each district and used within that district to pay for education (Wichita *Eagle*, Nov. 24, 1991).

Politicians were frantic: how could they satisfy all constituents and Judge Bullock? Not an easy task!

### 1992 School Fiscal Policy in Kansas

As the 1992 legislative session began, a great deal of uncertainty surrounded the finance mechanisms for Kansas public schools. The task before the legislature was enormous. In other states, efforts to respond to judicial determinations of unconstitutionality had spanned as long as twenty years without a solution to the problems of inequitable funding. The fiscal issues were arguably the most complex to face the legislature since the last finance formula had been enacted in 1973. (Luckert, *Order and Summary Decision*, Dec. 16, 1993).

The 1992 Legislature finally came up with a revolutionary plan for school funding. By the end of the session, a complete statute had been enacted which radically changed the philosophy and mechanisms of school finance. It gave full control of funding to the state, established a 32 mill statewide property tax levy to pay part of the cost, and raised income and sales taxes by \$349 million to increase the state's share.

The law, adopted under court pressure, dictated that school districts spend no more than \$3,600 per pupil unless they raised local property taxes. The legislature approved a combination of taxing and education law. The \$2 billion measure combined a \$389 million revenue package with a uniform state property tax and a formula to share wealth among rich and poor school districts. It also was designed to ease the pressure on local funding by reducing school taxes more than \$200 million. In return, all education revenues, including local taxes and federal dollars, were pooled in a central school finance fund at the state level.

The districts that were hurt by the new school finance law were the wealthy districts, and the ones that gained the most were the smaller, poorer districts. In ten school districts, mandatory new taxes raised more money than their schools were allowed to spend. Before the law was changed, school taxes in these districts were among the lowest in the state because property values were so high. In the Burlington district of Coffey county, site of the Wolf Creek nuclear power plant, taxes quadrupled. Burlington raised \$10.6 million, but it could only keep \$4.9 million. The rest had to be sent to the state. Hardest hit in southwest Kansas were the Hugoton and Moscow school districts in Stevens County, which sit atop vast gas fields. The districts raised a combined \$8.8 million in taxes, but paid \$2.6 million to the state. The law ignited storms of protest in the rural southwest and several of the school districts threatened to succeed from the state of Kansas and start another state.

Judge Bullock had also urged lawmakers to look at capital improvements and the need of students across the state for adequate school buildings. Kent Glasscock, a Republican representative, introduced legislation that allowed for state participation in capital improvement projects in public school districts. Many districts were having trouble funding major improvements, especially in the rural areas and in the fast-growing areas. By fall, voters had approved 12 of 16 school bonds issues on local

ballots for a total of \$90 million in new construction and improvement.

Within a few short months of the legislation being passed, 97 plaintiffs sought determination that the new scheme was unconstitutional. A manifestation of this controversy was the filing of four consolidated law suits. In August, 1993 Judge Marla Luckert declared two parts of the new finance act unconstitutional: (1) the state could levy a property tax for a period of only two years, not four years and (2) the enrollment size of schools being reimbursed by the "weighting" program was much too large. Low enrollment weighting is one of the factors for which a district would receive a higher or weighted reimbursement per pupil. The justification for the low enrollment weight is to account for the higher cost of operating a district which cannot efficiently, because of smallness, meet the educational needs of students. Any school with less than 1,900 students was being reimbursed by weighting factors. Judge Luckert stated that statistics showed it should only apply to schools with 500 or less students. Judge Luckert stated that the legislature must reenact the provisions of the School District Finance and Quality Performance Act with modification of the provisions regarding the low enrollment weight. Steps must be taken to document a rational basis for the manner in which the formula is constructed (*Order and Summary Decision*, December 16, 1993). The legislature was given until July 1, 1994 to remedy these two flaws in the finance law.

Shortly after the legislative session began in 1994, the Kansas Court of Appeals agreed to shift the issue directly to the state supreme court. The court was to decide whether to postpone a July 1, 1994 deadline imposed by Judge Luckert. On September 14, 1994, the Kansas Supreme Court heard arguments challenging and defending the new system of funding schools. This was two years and eleven months after District Court Judge Terry Bullock issued his "rule of law" on school finance that led to the new system.

The Kansas Supreme Court upheld constitutionality of the entire 1992 School Finance Act on December 2, 1994, including a provision on low enrollment weighting that district court judge, Marla Luckert, had held to be unconstitutional. In an unanimous decision, the seven justices said the legislature had a rational basis for the way it crafted the system for distributing about \$1.9 billion in state aid to Kansas' 304 local school districts each year. It said a provision that gives \$216 million in extra state aid to some 260 school districts with enrollments under 1,900 students met the rational basis test.

Threats of lawsuits started surfacing again in 1996. On May 30, 1997 Kansas House Speaker Tim Shallenburger said the school finance formula, crafted by the legislature in 1992, is so flawed that he would support an effort by school districts to challenge the funding plan in court. The consideration of a lawsuit is the effort of a group called Schools for Fair Funding, made up of 24 school districts across Kansas that see unfairness in state-set school funding.

The dominant issue of the 1997 legislative session concerned school finance. A strong Kansas economy throughout 1996 boosted tax receipts far beyond expectations. That allowed the 1997 Legislature to cut school district property taxes by \$127 million, replacing those revenues with state aid, and increasing funding for school aid programs by an additional \$95 million (1997 Legislative Summary, KASB).

## **Kansas's Current School Finance System**

### *The Organization of Public Education*

Educational services for Kansas' K-12 students are provided by a combination of various entities. In the 1996-97 school year, Kansas had 304 K-12 districts.

In 1966 the Kansas State Board of Education was created by Article 6 of the Kansas Constitution. The ten member State

Board of Education has authority for the general supervision of public schools and has supervisory responsibilities for area vocational-technical schools, community colleges, and other educational institutions, excluding Regents institutions. Board members are elected for four-year terms and represent specific geographic areas of the state. The Board appoints a Commissioner of Education who serves at the pleasure of the Board and is responsible for administration of the Department of Education.

The primary duties of the Board include classification and accreditation of schools, approval of teacher preparation programs, establishment of graduation requirements in the public schools, certification of teachers and administrators, distribution of state and federal financial aid, administration of school lunch and nutrition programs, regulation of proprietary schools and regulation of programs and services for area vocational-technical schools and community colleges (Kansas FY 1998 Governor's Budget Report),

### *School Improvement and Accountability*

A key goal of the Kansas State Department of Education is for all schools to demonstrate continuous improvement in student learning, as indicated by state assessment tests and other measures. This goal is consistent with the 1992 School District Finance and Quality Performance Act, which mandates state accreditation of schools based on outcomes for school improvement and student performance established by the Kansas State Board of Education. Although many states have reformed their school finance formulas in recent years, Kansas is one of only a few states that requires systematic improvement of schools and accountability to the taxpaying public in conjunction with school finance reform (Kansas FY 1998 Governor's Budget Report).

## **1997 Legislative Summary**

A strong Kansas economy throughout 1996 boosted tax receipts far beyond expectation. That allowed the 1997 Legislature to cut school district property taxes by \$127 million, replacing those revenues with state aid, and increasing funding for school aid programs by an additional \$95 million. The total increase in school aid spending for 1997, \$222.5 million, represented a 13% increase over funding approved for 1996 (Tallman, *Legislative Summary of the 1997 Session*, KASB).

The legislature passed two significant school finance bills. H.B. 2031 combined the property tax reductions with changes in the school finance formula. The tax package cut the statewide levy from 35 to 27 mills and created a \$20,000 residential property exemption from the statewide levy. It also reduced the income tax rate paid by single Kansans to the rate paid by married couples. The school finance portion raised the base budget for all school districts from \$3,648 to \$3,670: an increase of just 0.6% at a cost of 12.2 million. However, the state increased the correlation weighting factor for districts with enrollments of 1,800, directing nearly \$19 million to those districts. The at risk weighting factor, based on the number of a district's students eligible for free meals, was increased by 30% at a cost of \$6 million. The "declining enrollment" feature was also made more generous: districts were able to use either the current year's enrollment or the previous year's enrollment to determine budget entitlement.

As a result, school district general fund spending, the portion of school district budgets determined by the state through the base budget, increased nearly \$47 million, or about 2.3%. Total general fund budgets exceeded \$2 billion in 1998 for the first time. However, student enrollment was projected to increase 0.6%, which meant the increase per student was 1.7%: still well below the rate of inflation. The changes in the formula, however, did not treat all districts the same. Because

of the increase in correlation weighting and other factors, the budget per pupil for districts with enrollments of 1,800 or more increased by 2.5%, while the budget per pupil for districts with less than 1,800 students increased only 0.9%.

The second major school finance bill, S.B. 36, made significant changes in the Local Option Budget process. The Local Option Budget is a mix of local and state taxes a district can call upon to supplement base state aid. For the first time, school boards were able to adopt a portion of LOB authority without being subject to protest petition. In districts where the per pupil budget is below the average of similar sized districts, boards were allowed to adopt LOB's that would allow them to spend at the average without that increase subjected to protest petition. This provision provided an additional \$91.7 million in budget authority.

S.B. 36 also contained a provision for districts which spend above the average per pupil. The boards of these districts were allowed to adopt an LOB equal to 100% of their current authorization next year without being subject to protest. That percentage then falls 5% a year until FY 2002, when boards will be permanently able to keep 80% of the current LOB.

### School Finance

#### Property tax provisions.

The 1997 Legislature reduced the statewide mill levy from 35 mills to 27 mills for FY 1998 and granted a \$20,000 residential exemption from the statewide mill levy.

The income tax rate for single taxpayers was reduced to the rate for married taxpayers over four years; an adoption tax credit was created and the homestead tax rebate was expanded.

#### School finance provisions.

The following changes were made in the school finance act:

- \* Base state aid per pupil was increased \$22 to \$3,670.
- \* Correlation weighting was increased to equal low enrollment weighting at 1,800 students, or about \$65 per student for districts with 1,800 students or more.
- \* At-risk weighting was increased from 0.05 to 0.065 for each student eligible for free lunch.
- \* Districts were allowed to use either the previous year's enrollment or current year's enrollment for determining their budget.

The total Governor's recommendation for FY 1998 for the base school finance formula was \$1,452.3 million and will fund the enhancements, as well as the agreed to estimated enrollment growth for the year. The state's share of the local option budget was recommended at \$52.1 million. The demand transfer from the State General Fund of \$29.0 million to aid school districts and bond and interest payments was also included.

#### Uniform Property Tax Mill Levy Reduction.

The Governor recommended, as part of his tax reduction package, a reduction in the uniform property tax levy of 4.0 mills, or 29.0, in 1997 and an additional reduction of 4.0 mills, or 25.0 mills, in 1998 and an additional reduction of 4.0 mills, or 20.0 mills, in 1999. The 29.0 mill uniform property tax levy would finance 28.8 percent of the school finance obligation in FY 1998, and the State General Fund would pay the remaining 71.2 percent. In addition, the Governor recommended creation of the Education Property Tax Relief Fund to be used in out-years to fund part of the increased school finance cost resulting from the lower uniform property tax mill levy.

### Lawsuits May Lead to School Funding Reform

A study of the merits of a lawsuit challenging the state's school finance formula is the latest effort of a group called School for Fair Funding. The group, made up of 24 school districts across Kansas that sees unfairness in state-set school funding, lobbied legislators in 1997 for change. The Kansas House Speaker, Tim Shallenburger, Republican, said he thought the revision of the school-funding formula in 1992 was premature. That legislation, coincidentally, was written as a result of a court ruling that the previous school-funding formula was unfair. Shallenburger said the new funding formula was based not on what was fair, but on what would receive enough votes to be enacted. A lawsuit, he added, might be the catalyst to spur school-funding reform (*Salina Journal*, May 30, 1997).

### Summary

Kansas school finance has been the center of considerable debate in the 1990s. Judge Terry Bullock's decision in 1991 to close Kansas schools if the legislature couldn't come up with an equitable finance measure was the impetus for a scramble to satisfy Judge Bullock and also their constituents. The school finance and accountability system enacted in 1992 was accompanied by a significant increase in overall school district budgets, but the level of budget support provided by the state since 1992 has fallen far below the growth in school district costs.

Governor Bill Graves cut property taxes in 1997 to quiet the cries of the taxpayers. The base budget per pupil was only raised \$22, bringing the total to \$3,670 for 1997.

Today, school district operating budgets are declining when adjusted for inflation even as demands on schools are increasing. One major reason is the failure of the base budget per pupil to keep pace with inflation. Failure to adjust the base has led to rapid growth in local option budgets as districts have struggled to keep pace with rising costs.

Litigation again looms on the horizon in Kansas as school districts struggle to fund the rising costs and demands of education. Taxpayers are going to become unhappy when they realize that even though the mill levy on property tax was cut, the mill levy for a local option budget may increase their total mill levy. In many cases, the legislature made it possible for districts with below-average "local option budgets" to raise their LOBs a certain amount for five years, until per-pupil spending matches the average of like-sized districts elsewhere in the state. Previously, increases in LOBs were subject to citizen protest petitions, but the lawmakers stripped voters of their rights to block LOB hikes.

Clearly, taxpayer dismay with rising property taxes was the reason for the lowering of the mill levy, but in providing property tax relief, the legislature has created another monster. Debates over Kansas school finance are inevitable as school districts struggle to meet the financial demands of maintaining their educational systems.

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