

MEMORANDUM No. 21

TO: Kentucky School Architects and School Districts

FROM: Greg Dunbar, District Facilities Branch Manager; greg.dunbar@education.ky.gov

DATE: April 9, 2012

RE: Facilities Process and Funding

One of the many challenges that we face is continuing to inform our districts and design professionals about how our processes have developed and how this development relates to the funding for our school projects. Over the last few months the questions that we have been getting from districts and Architects show an increasing understanding of how funding drives the process. This memo is intended to provide an overview of the process and discusses the funding mechanisms, how they work, and how they change.

The General Assembly is directed in its governance by the Kentucky Constitution and legislated statutes which outline how the issues noted in the Constitution are to be addressed. The different departments within the state government are then charged with promulgating regulations that put into place the rules needed to address the statutory requirements. These regulations are then reviewed and if deemed appropriate, approved by the General Assembly before they are put into place.

The facilities process starts with the General Assembly which is directed by Article 18 of the Kentucky Constitution to; **“by appropriate legislation, provide for an efficient system of common schools throughout the State.”** Article 18 describes this efficient system in nine statements with three of these being directly germane to construction as follows:

- Common schools shall be **substantially uniform** throughout the state.
- Common schools shall be monitored by the General Assembly to assure that they are operated with **no waste, no duplication, no mismanagement**, and with no political influence.
- The General Assembly shall provide funding which is sufficient to provide each child in Kentucky an **adequate education**.

The direction to provide, “Common schools shall be **substantially uniform** throughout the state” is addressed in our regulations to set a standard for each school depending on type and student population in our Model Programs in 702 KAR 4:180. These Model Programs provide for an “adequate” facility of net program spaces as well as providing a net/gross conversion for each building type. These spaces can be adjusted by the Local Preference allowances and can be further adjusted by the provisions of 702 KAR 4:170.

The “monitoring” of the common schools is a part of all of KDE’s regulations which provides us with the authority to review projects for compliance with the regulations.

To address provision of “sufficient” funding for construction, the General Assembly has put into place two types of funding groups; unrestricted and restricted funds. Unrestricted funds are commonly called the “General Fund” which is used for virtually all of the school district’s expenses; employee salaries, transportation, energy, etc. Restricted funds can only be used for capital construction and major renovation.

These **restricted funds** fall into three primary sources of funding which are designed to address the construction needs of our districts. Dr. Robert Tarvin, Executive Director of the School Facility Construction Commission, (SFCC) refers to these as the “three legged stool” which supports our facilities. These funding sources are based on different aspects of each district to provide a holistic approach of finance. **Each funding source is identified by different statutes which legislate how the money is to be raised and spent;**

Leg 1 - Student Population Based Funds – KRS 157.420 - Capital Outlay

These funds are issued to each district annually based on \$100 per each district’s Average Daily Attendance (ADA). These funds can be used for building maintenance and 80% of these funds can be used for debt service to undertake large projects noted on the District Facilities Plan in priorities 1 through 4.

- A district with an ADA of 2,000 students, would receive \$200,000 in cash annually from the State. This can be spent for maintenance or saved from year to year (see note 1).
- Because the ADA will theoretically not change much annually, each district can pledge 80% of this amount toward “debt service” for bonding of construction projects. The 80% maximum can be increased, with KDE approval, but this maximum is in place to help insure that the pledged amount will still be in place if a district’s attendance declines and they receive less money from the State.
- In this example, \$160,000 (80% of \$200,000) could be pledged annually toward debt service.
 - In today’s market place this annual pledge would bond about \$2,160,000. Of course this varies with the bond market.

Leg 2 - Property Value Based Funds – KRS 157.440 - Facilities Support Program of Kentucky (FSPK)

The authority to levy these taxes is given to each district by the General Assembly. The funding is based on the assessed value of the property in each district. These funds are in two components, the local tax and the State equalization.

- The **local** portion of this tax is determined by dividing the district’s property assessments by 100 and then multiplying the quotient by 5 cents. That is why this is sometimes called the “**nickel**”. The annual cash generated by this tax can only be spent on projects noted on the District Facilities Plan in priorities 1 through 4. These tax receipts can be spent, saved from year to year (see note 1) or pledged toward “debt service”.
 - A district which has property assessments of \$500,000,000 this tax would result in annual tax revenues of \$250,000 ($\$500,000,000/100 \times 5$ cents).
 - In today’s market place this annual pledge would bond about \$3,375,000. Of course this varies with the bond market.
- The **State** portion is determined by reviewing the property assessment per pupil in each district and comparing it to 150% of the Statewide property per pupil assessment which is currently about \$736,000. Districts with per pupil assessments that are below 150% of the Statewide average receive annual payments from the State that equal the difference in the two numbers. The annual cash generated by this “equalization” can only be spent on projects noted on the District Facilities Plan in priorities 1 through 4. This “equalization” can be spent, saved from year to year* or pledged toward “debt service”.
 - Our sample district, noted above, would have a per pupil assessment of \$250,000 ($\$500,000,000/2,000$). This would result in annual equalization of about \$486,000 ($\$736,000 - \$250,000$).
 - In today’s market place this annual pledge would bond about \$6,561,000. Of course this varies with the bond market.
- When combined, these two funding sources make up almost half of the funding used for construction.

- The General Assembly has granted districts the ability to raise additional nickels which generally follow the same requirements of the first nickel, but these are generally subject to voter recall and equalization is not guaranteed by the General Assembly.
- **Leg 3 - Needs Based Funding – KRS 157.611 - School Facilities Construction Commission (SFCC)** This funding is intended to address a districts “unmet need” or the **needs that are not met by the other restricted funding noted above**. These funds are based on the “Needs” identified on the District Facilities Plan (DFP) that is in place on July 1 of each odd numbered year, less projects completed since the DFP was completed, less other restricted funds that are available (local available revenue). These costs are assembled statewide and the total is presented to the General Assembly during their even year funding session. The legislature then appropriates a specific amount of money that is distributed to each district base on their pro-rata share of the Unmet Need. These monies can only be spent on projects on the DFP in the highest priority group.
 - **Needs Minus Local Available Resources = Unmet Needs**
 - Distribution of Legislative Appropriation is as follows:

State Appropriation	<u>Unmet Needs of a Local District</u>		Amount Available
to SFCC	X Total State Unmet Need	=	to Local District
 - **Needs** = The estimated cost of implementing the KBE approved DFP for each district.
 - **Local Available Revenues** are determined based on end of year financial reports as of June 30 in odd numbered years before the Legislature meets. The sum of the following equals Local Available Resources
 - Cash in Building Fund account **Plus**
 - Cash in Capital Outlay account **Plus**
 - Eighty percent of the bonding potential of Capital Outlay appropriation **Plus**
 - Bonding potential of \$.05 local levy, growth, additional nickels and FSPK’s equalization **Plus**
 - Escrowed SFCC offers and Cash **Minus**
 - Existing Debt Service
- These funds are granted by the General Assembly in the form of “offers of assistance” to bond capital construction projects. Each district has a specified time, generally 8 years (this was originally 6 years), to commit these funds or they return to the SFCC for redistribution.

Note 1 – Restricted cash (annual receipts from the restricted funds) that is not spent or committed to a specific project by the submission of a BG-1 prior to July 1 of the odd year must be “escrowed” by the district. This money can still be used for construction projects, but the rules for its use are the same as those for SFCC funds, i.e. these monies can only be spent on projects on the DFP in the highest priority group.

Note 2 - In recognition of the difficult financial situation over the last few years, in 2010, the General Assembly approved a process by which districts may access Capital Outlay cash, FSPK cash and the 2011 FSCC cash for any purpose within the district. This allows the district to conserve their General Fund while only affecting their restricted funds for a short period of time. To access this cash each district must submit a Capital Funds Request Form to KDE for review and approval. This statutory provision is subject to change by the General Assembly, but has been reenacted in the 2012 session.

As you can see from the information noted in this memo, the process and rules utilized for school construction in Kentucky, crafted by the General Assembly, and administered by KDE, are dependent upon the funding that is used. The Constitutional mandate to address a Statewide system of “Common Schools” resulted in the development of the funding sources which drove development of regulation and the administration of these regulations. These actions are intended to work together to form a complete system. It is virtually impossible to secure enough money to address all of the needs of our schools, particularly when the concept of what constitutes “adequate and equitable” facilities is a moving target. From our view, every dollar that is spent over and above the “adequate” facility outlined in regulation is a dollar that cannot be spent to address the needs of other facilities. It then becomes a much greater challenge to address the need for “equity” when some schools are overbuilt and then others have nothing.

This will be an ongoing discussion within which you will be an active participant with the design profession, KDE and the General Assembly. We hope that providing you with as much information as possible will help in this discussion and in your work with our clients, the children of Kentucky. Thank you for your assistance. If you have any questions, please contact me at 502-564-4326.