Funding the Child

Getting Results In South Carolina Through Weighted Student Funding

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Executive Summary

While South Carolina's school finance system has many positive attributes, it still suffers from substantial shortcomings that limit the ability of the state's educators to use funding in ways that produce the best results for students, and especially for students most in need of academic improvement. This report outlines a set of changes to South Carolina education finance that would make school spending more efficient, more effective, and more equitable.

The Problem: South Carolina's Reliance on Categorical Program Funding

Fully 45 percent of state funding in South Carolina – $1.2 billion – comes to school districts in a set of categorical programs. These funding streams include 74 different revenue codes, each with its own allocation formula, criteria, and prescriptions for use. In their sheer number, these programs place South Carolina near the top of the national ranking in proliferation of funding programs. According to an *Education Week Research Center* survey of the 50 states and DC, only four states had more categorical funding programs in fiscal year 2004 than South Carolina, with California topping the list.

Restrictive categorical funding makes it difficult for districts and schools to use funds in ways that meet the needs of their students because categorical funds:

- *Inhibit spending coherence* at the district and school level. Regulations often require separate accounting, place limits on what can be purchased with funds, and prescribe in detail what services are to be provided and how, making it difficult to pull funds from different program line items to design an intentional, coherent program.
- *Impose burdensome accounting and fund management.* Funds from each source need to be accounted for separately. As a result, districts or schools may have hundreds of different funding sources to manage. These requirements often necessitate that a portion of the funds go to a program manager to take on administrative tasks, diverting funds from educational activities.
- *Create unpredictability.* With resources coming from myriad different programs, each with its own complex formula for allocation, districts have a difficult time predicting from year to year what their entire resource picture will look like.
- *Force a one-size-fits-all approach* to addressing each problem. Districts and schools differ in their needs and in their capacities to solve the problems they face. Categoricals that come with prescriptions for use limit districts and schools from using funds in ways that they may believe are the most efficient and effective.

The Solution: Shifting Dollars into Weighted Student Funding

To address these shortcomings, this report proposes that South Carolina shift a substantial portion of the $1.2 billion in categoricals into a *modified version of its existing weighted student funding system.* While doing so would present some significant challenges – addressed in the following section – it would also generate substantial benefits to the state and its students by allowing districts and schools to use resources more effectively to achieve results for students.

Specifically, a shift toward funding the child would entail:

- Expanding the Education Finance Act's weighting system to include additional groups of students not currently weighted, namely low-income and gifted students;
- Converting categorical funds intended to serve a specific student type into new or existing weights in EFA;
- Converting other categorical funds into per pupil funds within the basic EFA allocation; and
- Distributing funds (including those for public charter schools) on the basis of each child's new weighted amounts.

It is worth noting how much would *not* change as a result of this shift in approach to funding. The share of state vs. local dollars would not change. The amount of funding dedicated to meeting the needs of different groups of students would not change. The amount of state funding received by most individual districts would not change markedly, with the exception of a drop in funding for some districts that are now particularly successful at winning competitive state grants. Overall, the state's funding priorities would remain the same.

What would change is the value of state funding to districts and schools. This increase in value would be two-fold. First, the administrative costs of handling the complex array of categorical funds, with all of their attendant requirements and paperwork, would diminish. Districts and schools could then reallocate those administrative funds into efforts to raise student achievement. Second, because state funding would become dramatically more flexible, districts and schools could shift resources into initiatives and activities that can make a real difference for their students. While there is no way to predict exactly how districts and schools would use this new flexibility, the streamlined system would open up infinite possibilities for educators to respond more effectively to the needs of their students. Transparent auditing and reporting would effectively ensure that dollars were spent on instructing the children who generate the money.

This approach to state funding of education has gained wide support across U.S. school districts as diverse as Seattle, Houston, Cincinnati, and Milwaukee. These and other districts, and some states, have implemented key aspects of the ideas. In 2006, the Thomas B. Fordham Institute issued a manifesto entitled *Fund the Child: Tackling Inequity and Antiquity in School Finance,* calling for just such a system. By the end of 2006, the manifesto had garnered 231 signatures from across the political spectrum, from former Republican education secretaries William Bennett and Rod Paige to Democratic leaders such as former Clinton chief of staff John Podesta and former North Carolina Governor James Hunt. The idea's bipartisan appeal stems from the multiple objectives weighted student funding achieves in one fell swoop, fostering equity and providing flexibility.

Challenges of Weighted Student Funding and How to Meet Them

Ensuring the funding follows the child to school. The system proposed here would, by itself, only guarantee that money follow the child to the district, not the school. To ensure that funds are used to serve their intended beneficiaries, the state should:

- *Require that money be spent on schools according to how much money their students generate.* South Carolina should require that money generated by a student via the new weighted funding system be spent proportionately on that child's school.
- *Require transparent reporting of how funds are spent at the school level.* In addition to continuing to follow and use the existing SC financial accounting requirements, each district should be required to report publicly (a) the amount of funding "generated" by each of its schools, based on their student populations; and, (b) the amount of resources devoted to each school by student type. In addition, the state should make available school-level expenditure reports through the use of In$ite and make it possible for citizens to "query" the online financial information system to obtain additional information.
- *Encourage responsible moves toward school-based funding control.* One strategy would be to place schools into tiers of increasing financial independence, based on schools' demonstrated capacity to handle budget control. All schools could immediately be empowered to develop draft budgets linked to their annual school improvement plans, submitting these for approval to their local school boards. Schools could apply to the local school board for greater levels of school-level financial independence after demonstrating their capacity to carry out the responsibility. State oversight, and an appeals process to the state board of education, would ensure that districts grant financial independence to schools that deserve it.

Potential resistance to change. Each categorical program in a state has numerous and varying special interests that are likely to try and protect specific pots of money. All of these potential opponents of change could very easily undermine the shift before it happens. A one-year gap between enactment and implementation would give all parties time to adjust. In addition, where possible, some flexible funds could be used to hold allocations constant in some areas to minimize the impact of otherwise abruptly withdrawing some categoricals. This explicit "grandfathering" would be highly transparent, and it would phase out quickly with a "sunset" provision.

The need to continue managing the system's weights. The system proposed above would simply convert the implied weights of South Carolina's categorical programs into an explicit set of weights. We recommend this approach to minimize the degree of change in the state's priorities initially. Over time, the state would need to revise those weights as required to align them with student needs and state priorities. '

Rethink other state policies that restrict local spending decisions. In its efforts to promote flexible use of funds, the state should continue to review other state policies that impose restrictions. For instance, the EFA requires districts to compensate teachers based on each person's experience and class. Such uniform salary scales can work against local efforts to use targeted salary incentives as a way to more evenly distribute teacher effectiveness among more and less disadvantaged schools in the same district.

Funding the Child

Getting Results in South Carolina
through Weighted Student Funding

Background

For three decades, South Carolina policymakers have sought to develop a school finance system that promotes equity and student achievement. From 1977's Education Finance Act (EFA), to 1984's Education Improvement Act (EIA), to 2006's property tax reform, the state legislature has aimed to increase the state's financial commitment to K-12 education, spread resources evenly through the state, and target funding to high-priority programs and initiatives. In 2000, voters amended the state's constitution to pave the way for the South Carolina Education Lottery, which has generated $390 million in K-12 funding since its inception.

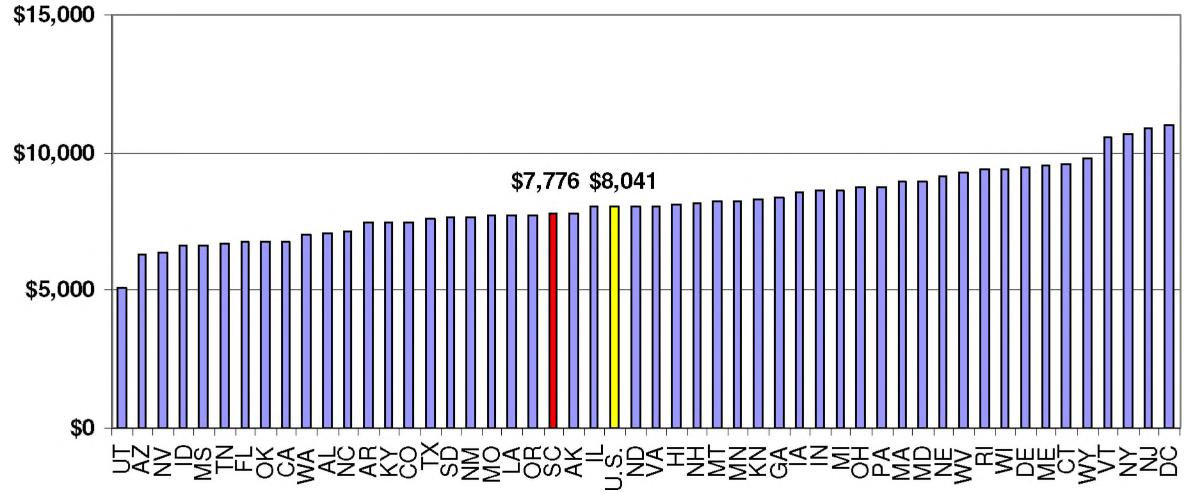
Federal Funding in South Carolina

In addition to the education funding that comes from the state and local governments, South Carolina receives a large amount of education funding – $639,783,460 in 2006-07 – from the federal government. While the exact distribution of funding varies slightly from year to year, in 2003-04, 11% of overall education funding came from the federal government, 46% from the state, and the remaining 43% from the local government. South Carolina's 11% share is somewhat above the national average, which is 9%.

The majority of the federal funding that South Carolina receives is designated for disadvantaged groups such as students in poverty and special education students, but the federal government also provides funding for certain programs such as Reading First and the Mathematics and Science Partnership Program. Though this report does not analyze federal funding, as policymakers consider the overall funding system in South Carolina, it is important to consider the entire picture, including federal funds, and how all funding streams together align with the state's goals for public education.

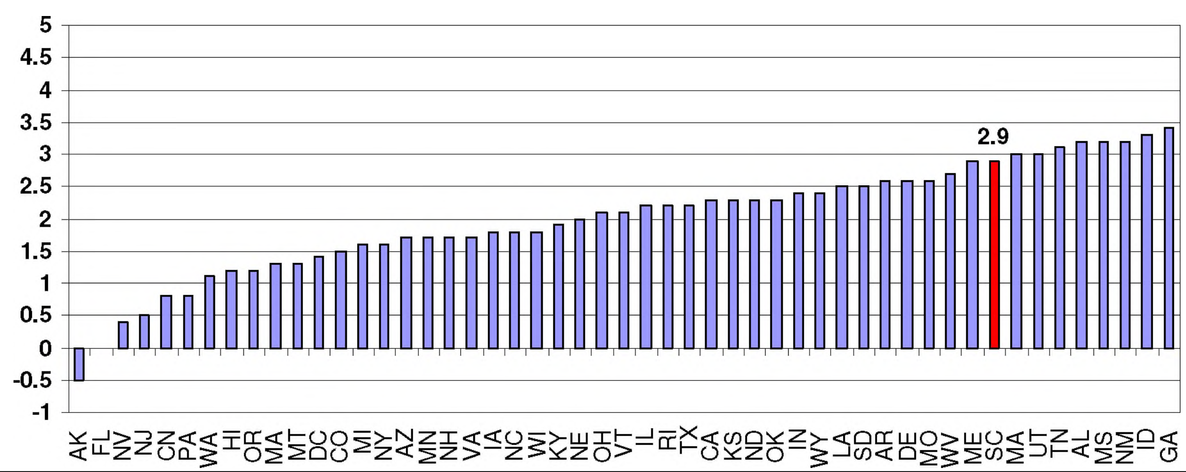
While per pupil K-12 spending in the Palmetto State is near the national average (Figure 1), South Carolina's spending is high relative to many other states in the Southeast. Only Georgia and Virginia surpass it. In addition, South Carolina ranked 9th among states in how quickly it increased K-12 expenditures in the 1990's, elevating spending at an average annual rate of 2.9% after adjusting for inflation (Figure 2). And relative to the size of its total taxable resources, South Carolina devotes a large share to education, ranking 11th nationally in 2002-03 (Figure 3).

Figure 1. Average Education Spending per Student by State, 2002-2003

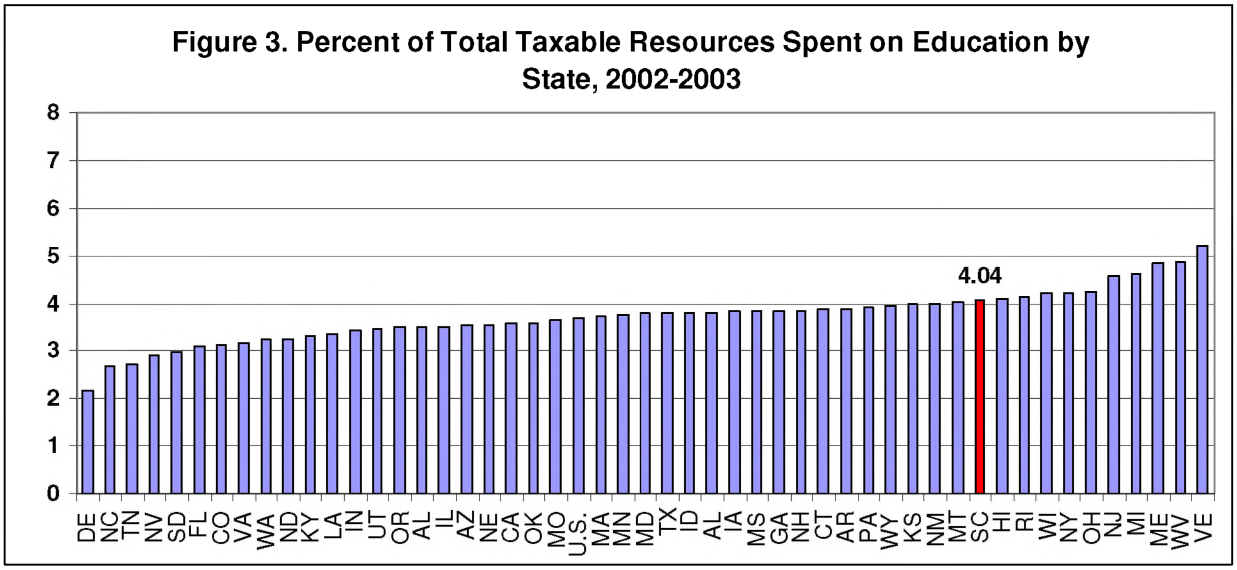


Source: U.S. Department of Education, National Center for Education Statistics, "Revenues and Expenditures for Public Elementary and Secondary Education: School Year 2002-03," April 2005.

Figure 2. Average Annual Rate of Change in Per-Pupil Expenditures Over the Last Ten Years, 1990-1991 to 1999-2000



*Expenditures were adjusted for inflation using the U.S. Department of Labor's Bureau of Labor Statistics Consumer Price Index.
Source: Education Week Research Center analysis of the change in per-pupil expenditures from 1992 to 2002. The per-pupil expenditures (PPEs) for 1991-92 through 1999-2000 are from the National Center for Education Statistics, "Digest of Education Statistics, 2002." The 2000-01 and 2001-02 PPEs are from the National Center for Education Statistics, "Revenues and Expenditures for Public Elementary and Secondary Education," multiple years.

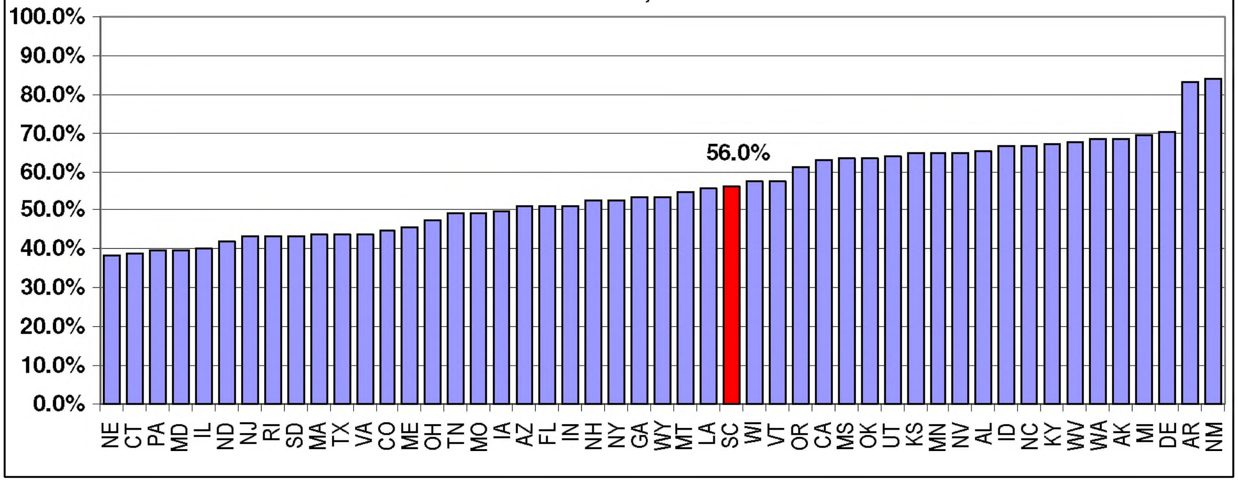


Source: EPE Research Center analysis of state and local revenues from the National Center for Education Statistics, "Revenues and Expenditures for Public Elementary and Secondary Education: School Year 2002-03," April 2005, and the 2003 gross-state-product figures from the U.S. Department of Commerce's Bureau of Economic Analysis. The gross-state-product figures for 2004 were released in time for this analysis. However, the state and local revenues from the NCES report cited above included 2002-03 school year data, so the EPE Research Center used the 2003 gross-state-product figures to calculate each state's total taxable resources dedicated to education. The figures represent resources spent on pre-K-12 education.

In addition to spending relatively generously on education, South Carolina has also sought ways to foster equity across districts which, as in most states, vary widely in their ability to pay for education.[1] The 1977 Education Finance Act (EFA) laid the groundwork for equity enhancement by establishing a base cost per pupil for providing a basic education for each student. Using this base cost, with some adjustments described more fully below, the state calculates each year how much funding each district needs under the EFA. In order to receive EFA funds from the state, each district must use property taxes to raise locally a share of the base cost, receiving much of the remainder from the state. Through this mechanism, the state helps smooth out spending differences between districts. While a property tax reform in 2006 will change the proportion of education funding derived from property taxes, this basic structural approach to setting the state and local share remains in force.

South Carolina falls in the middle of the national range in the percentage of K-12 funding provided by the state, at 56.0% (Figure 4). This share is likely to grow due to the 2006 property tax reform, under which a state sales tax increase will replace funds for schools now generated by local residential property taxes.

Figure 4. Percent of Education Funding Provided by the State in each State, 2002



Source: Special analysis by Greg Orlofsky, private consultant, using the following: 1) the U.S. Census Bureau's Public Elementary-Secondary Education Finance Data for 2002; 2) the NCES Common Core of Data Public Elementary and Secondary School Universe, 2001-02; 3) the Geographic Variations in Public Schools' Costs, 1993-94; 4) the U.S. Census Bureau's Small-Area Income and Poverty Estimates, 1999.

While South Carolina's school finance system has many positive attributes, it still suffers from substantial shortcomings that limit the ability of the state's educators to use funding in ways that produce the best results for students – especially for students most in need of academic improvement. This report outlines a set of changes to South Carolina education finance that would make school spending more efficient, more effective, and more equitable. It proceeds in four main sections. The first sets out a picture of a new approach to school funding that is gaining traction nationally, an approach known as "weighted student funding" or "funding the child." The second explains how South Carolina's system currently falls short of this ideal approach, and the consequences of those shortcomings. The third describes how funding the child could work in South Carolina's unique context. And the fourth addresses some challenges that would arise as the state makes the shift to this new way of funding schools.

The Case for Funding the Child

Nationwide, many states are rethinking their systems of state allocation, the mechanisms or vehicles for distributing resources to districts and schools, for any of the following reasons:

1. *Provide for greater spending transparency and clarity.* With increased evidence of spending disparities among districts or among schools within the same district, stakeholders at multiple levels are seeking clarity about how state resources are divvied up and sent out.
2. *Allow for more flexibility and strategic use of resources at the district and school levels.* Faced with increasing accountability demands, some district leaders, school board members, and school leaders have requested that funds arrive with fewer financial restrictions to enable them to make more strategic resource allocation decisions. The demand for school-based discretion over resource use in particular has

risen with school-based accountability, school-based management reforms and school restructuring efforts where the underlying rationale is that decisions made closer to the student are more effective and efficient.

3. *Increase equity among districts or among schools within districts.* Some have argued that finance systems should take steps to ensure that high-poverty districts and schools have the resources they need to meet the challenges they face.
4. *Encourage innovative or promising approaches to meeting the needs of students.* Restrictive funding systems impose constraints on how dollars are deployed, making it difficult for educators close to students to try innovative approaches, or even tried and true approaches that fall outside of funding guidelines.

In pursuit of all of these objectives, a common target of reform is the system of "categorical" funding used by many states, so called because they require that funds be spent within certain categories or programs rather than deployed flexibly to meet students' needs. Reformers have categorical programs in their sights because they:

- *Inhibit spending coherence* at the district and school level. Each distinct state allocation (or "categorical") is intended to serve a specific group of students or further some specific program. As a result, regulations often require separate accounting, place limits on what can be purchased with funds, and prescribe in detail what services are to be provided and how. The effect is to prohibit commingling of funds across categories, making it difficult to pull funds from different line items to design an intentional, coherent program. The result in many cases is the layering of programs on top of one another over time, making it difficult to align the use of funds with district and school strategies and priorities or evaluate how well different programs are working.
- *Impose burdensome accounting and fund management.* Funds from each source need to be accounted for separately. As a result, districts or schools may have hundreds of different funding sources to manage. These requirements often necessitate that a portion of the funds go to a program manager to take on administrative tasks, diverting funds from educational activities.
- *Create unpredictability.* With resources coming from myriad different programs, each with its own complex formula for allocation, districts have a difficult time predicting from year to year, what their entire resource picture will look like.
- *Force a one size fits all approach* to addressing each problem. Districts and schools differ in their needs and in their capacities to solve the problems they face. Categoricals that come with prescriptions for resource use limit districts and schools from using funds in ways that they may believe are the most efficient and effective.

To be sure, there are reasons for earmarking and sending out separate "pots" of funds
Grants and categoricals have grown up in state allocation systems as a well-intentioned response to some real needs that may still be present, such as the need to bring additional funds to districts with unique student populations; the need to counter local forces that push for disproportionate funding to go to wealthier schools; the need to deliver additional funds to districts to offset costs associated with unique geographic district conditions, such as high transportation costs in small

rural districts; the desire to promote spending on a particular priority or advance new and innovative solutions to improving student achievement.

While these needs are real, categorical funding is not the best mechanism to meet them. Instead, policymakers can turn to an approach called "weighted student funding" (WSF), also known as "funding the child." Under WSF, funding follows children to the districts or schools they attend based on their characteristics. Students with greater needs (and thus higher costs) generate more revenue for the institutions that educate them. The institutions, in turn, have great flexibility over *how* they deploy resources to meet the needs of their students. Instead of detailed regulations tied to categorical funds, the state influences district and school behavior by:

- Setting clear standards for student performance, assessing students, and holding schools and districts accountable for results; and,
- Requiring school based accounting and monitoring whether additional resources earmarked for high needs students do indeed boost spending and results in those schools.

In short, weighted student funding, combined with standards, information, and accountability, become the critical policy tools for the state, not bureaucratic restrictions on funding.

This approach to state funding of education has gained wide support across U.S. school districts as diverse as Seattle, Houston, Cincinnati, and Milwaukee. These and other districts, and some states, have implemented key aspects of the ideas. In 2006, the Thomas B. Fordham Institute issued a manifesto entitled *Fund the Child: Tackling Inequity and Antiquity in School Finance,* calling for just such a system. By the end of 2006, the manifesto had garnered 231 signatures from across the political spectrum, from former Republican education secretaries William Bennett and Rod Paige to Democratic leaders such as former Clinton chief of staff John Podesta and former North Carolina Governor James Hunt. The idea's bipartisan appeal stems from the multiple objectives weighted student funding achieves in one fell swoop, fostering equity, providing flexibility, and facilitating student choice among schools.

The remainder of this report examines how South Carolina can move its system more in the direction of weighted student funding.

Categorical Allocation in South Carolina

The good news is that South Carolina already has a state education finance system that relies, in part, on what amounts to weighted student funding. This component of the state's system creates a strong foundation on which a broader WSF system can be constructed. At the same time, South Carolina's system also includes a heavy emphasis on categorical allocation. It is this side of the system that will need to change dramatically if South Carolina is going to free up resources so that educators can use them effectively to produce results.

In South Carolina, some $2.6 billion in state dollars was distributed among districts for the purposes of education in 2005-06. According to the most recent Funding Manual of the South Carolina Department of Education, the state's allocation system consists of four parts. One of the four – the Education Finance Act (EFA) – uses a weighted student funding approach to allocating resources. As described above, EFA defines a base cost of providing K-12 education which is then funded by a combination of state and local contributions. This "foundation" amount for each district is computed on a per pupil basis. In 2006-07, each student generated at least $2,367 from this one source of funds (which is just a fraction of the overall amount spent per child in South Carolina). Some students, however, have more "weight" in the system. Kindergartners, for example, generate 1.3 times this basic funding: 30% more than the base amount, or an additional $710. Primary and high school students are weighted at 1.24 and 1.25 respectively. Vocational education students generate 1.29 times the base amount. And students with certain disabilities generate various amounts depending upon their specific disabilities. For example, students with learning disabilities generate 1.74 times the base level due to the additional services they require.

It is important to note that this allocation is not funded fully by the state. Rather, the state requires each district to contribute funds toward this allocation based on its taxpaying ability, with the state providing much of the rest. Since districts with higher local property values provide a greater match, the system is intended to equalize funding to some degree across districts. Districts are permitted to raise additional funds locally to augment the base level of funding.

These funds, once provided to the district and combined with the local match, are intended to fund the minimum program, covering the cost of providing classrooms, teachers, supplies, etc. in ways that fit the needs of each district. Districts may allocate these resources as they see fit among a broad range of allowed expenditures. While the state does set minimum staff salaries, curriculum, instructional days, and time requirements for each class, districts are permitted to go beyond any of these minimums.

In short, EFA is a weighted student funding model of school finance. It departs from the *Fund the Child* manifesto's recommendations in just one key respect: weighted funds follow children to *districts*, but not necessarily to *schools*.

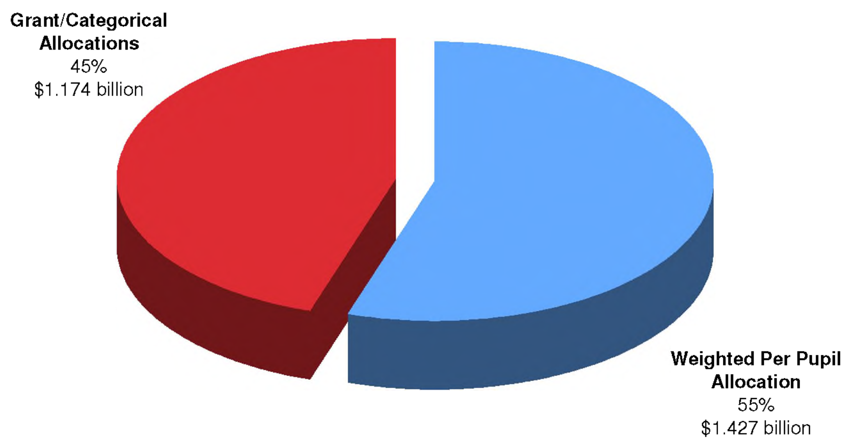
The other three components of South Carolina's allocation system, by contrast, depart markedly from the WSF ideal. Instead, all three allocate funds purely on a categorical or program basis. These are:

1. The Education Improvement Act (EIA), which includes 44 revenue codes primarily for items intended to improve student performance;
2. The State Restricted Funding which includes 26 special revenue codes for various General Fund purposes; and,
3. The Education Lottery Act Programs, which include 4 revenue codes for various enhancement efforts.

Allocations from these three sources include 74 different revenue codes, each with its own allocation formula, criteria, and prescriptions for use. In sum, most of these allocations can be best described as categorical allocations with many of the undesirable characteristics mentioned above.

Together the three groups of categorical/grant allocations amount to 45 percent of the state's nearly $2.6 billion in state aid for education (see Figure 5). In their sheer number, they place South Carolina near the top of the national ranking in proliferation of funding programs. According to an *Education Week Research Center* survey of the 50 states and DC, only four states had more categorical funding programs in fiscal year 2004 than South Carolina, with California topping the list.[2]

Figure 5. Categorical vs. Per Pupil Allocations in State Education Spending, 2005-06



Because the funds arrive to school districts in so many different pots, each with its own restrictions on how it can be used, district services are at times fragmented with multiple programs/services for each type of student. The fragmentation of the funding restricts districts from making decisions about how best to meet the needs of its students and instead forces districts to separate resources according to their categorical source. Consider a few examples of how this system may thwart district efforts to achieve worthy goals:

- *Creating an innovative new school.* Districts cannot, for instance, combine all of their funds to offer a comprehensive, innovative school designed around the unique needs of its students, despite the fact that the state has several categorical allocations intended specifically to help districts fund different school models. Rather, if a district that wants to use funds to finance a new school model with a comprehensive approach, the district might attempt to cobble together some combination of the state's 25 separate categorical allocations earmarked for alternative schools, junior scholars, youth in government, homework centers, and others as a way to fund the school. But some of these allocations are intended only for math and science schools, or schools for arts and humanities, or "lab schools," or SAT improvement. Some of the funds are earmarked only for operating costs; others can be applied only for personnel. Some are intended only for special services (like character education or alcohol abuse services). As a result of all these restrictions, creating a new innovative school means piecing funds together into a patchwork quilt that may or may not have any coherence.

- *Closing achievement gaps*. For a district interested in creating a program to close achievement gaps and better serve low-performing students, there are several different allocations intended for this purpose. But all come with their own restrictions which, in combination, make it difficult or impossible to use them well. Some specify that funds must be used for Reading Recovery (a specific reading program); others focus on class size reduction in the primary years; others are for schools to provide summer assistance to students. While each set of restrictions may have its own logic, districts may find it difficult to meet their own students' specific needs. For example, consider a district with many students who are employed in tourism over the summer. For these locales, restricting funds for use on summer assistance makes little sense. The district would probably achieve better results with these students by using the funds for a Saturday program during the school year.
- *Building teacher knowledge and skills*. The state has 15 different programs designed to fund professional development or enhance teacher quality. Each has its own restrictions, requirements, and specific purpose, making it difficult or impossible for a district to combine the funds into one coherent professional development initiative that truly raises the level of teaching capability.

Fragmenting state funding into 75 different categorical pots also has the effect of requiring districts to dedicate a significant portion of their funds to administration and compliance. In order to satisfy all the requirements of each allocation, districts separate the funds into different district departments with different administrators. In the professional development example cited above, districts may understandably spend more time making sure they comply with the restrictions on each pot of funds than on creating a focused meaningful professional development program. Funds meant to meet a worthy goal end up being diverted to accounting and compliance.

Funding the Child in South Carolina

To address these shortcomings, this report proposes that South Carolina shift a substantial portion of the $1.2 billion in categoricals into a *modified version of its existing weighted student funding system*. While doing so would present some significant challenges – addressed in the following section – it would also generate substantial benefits to the state and its students by allowing districts and schools to use resources more effectively to achieve results for students.

Specifically, a shift toward funding the child would entail:

- Expanding the Education Finance Act's weighting system to include additional groups of students not currently weighted, namely low-income and gifted students;
- Converting categorical funds intended to serve a specific student type into new or existing weights in EFA;
- Converting other categorical funds into per pupil funds within the basic EFA allocation; and
- Distributing funds (including those for public charter schools) on the basis of each child's new weighted amounts.

Analyzing South Carolina's current categorical funding programs, it becomes clear that there are three broad types of categorical programs:

1. programs that target a specific group of students (such as low-income, low-performing, or gifted);
2. programs that further some state spending priority (such as science education);
3. programs that fund services not related to educating K-12 students (such as adult education) or are intended to offset unusual transportation costs of some districts.

Categoricals in type 3 can remain categorical. The proposal here focuses on reallocating funds for type 1 and type 2 programs, in different ways.

For type 1 – targeted to specific groups of students – funds would be converted to "weights" used to calculate how much funding each district or public charter school would receive to educate its students. If a group is already weighted under EFA, such as vocational education students, then converting categoricals into weighted funds would mean increasing the weight assigned to that group. If a group is not currently weighted (such as low-income, low-performing, or gifted students), EFA's weighting system would need to be expanded to include weights for those groups.

Funds of type 2 – programs that further some state spending priority, like science education – are not targeted to specific groups of students, and thus they cannot be converted to weights. Instead, they can be added to the basic per pupil allocation generated by all students. Instead of promoting these priorities by restricting districts' and schools' use of funds, state policymakers could do so by refining state standards and accountability systems, or by training district and school leaders on how to align their programs with state priorities.

In this approach, converting categoricals to weights would shift funds toward a weighted student funding approach *without changing the state's priorities with regard to the student groups it wants to serve.* Over time, if state policymakers wanted to change the priority of funding for certain groups, or add new groups to the mix, they could do so easily by changing the system of weights.

To see how such a modified system would work in practice, it is helpful to consider a demonstration of how this kind of reallocation could take place. To create such an example, we conducted an analysis of South Carolina's categorical programs, provisionally assigning each to one of the three types listed above. Though this is simply an *illustration* of how such an assignment *could* work, the analysis yields the following breakdown and implications, shown graphically in Figure 6:

- 8% of categoricals (the bottom stripe in Figure 6) fall into type 3 – unrelated to K-12 education or intended to reimburse unusual costs and thus not applicable to the proposed reallocation. These funds would remain categorical in their distribution.
- 67% of categoricals (the large middle stripe in Figure 6) appear intended to serve all student groups, or at least do not specify a particular target group. These funds would be rolled into the basic per pupil allocation under this proposal.
- The remaining 25% of categoricals (the top stripes in Figure 6) seem designed to serve particular student groups. These include some groups currently included in the weighted

funding model: vocational education and special education. Weights for these groups would increase with the addition of categorical funds. They also include some groups not currently included in EFA: low-income/low-performing students[3] and gifted students (including Advanced Placement funding). For these groups, new weights would be created in EFA. Funds currently targeted at low-performing schools could be converted into weights for poverty, which is highly correlated with performance. Weighting low-performance itself creates perverse incentives to under-perform in order to increase revenue. Weighting poverty, by contrast, directs funds towards lower-performing students without creating any such incentive.

Figure 6. Demonstration of How Categorical Funds Could Convert to Per Pupil Funds

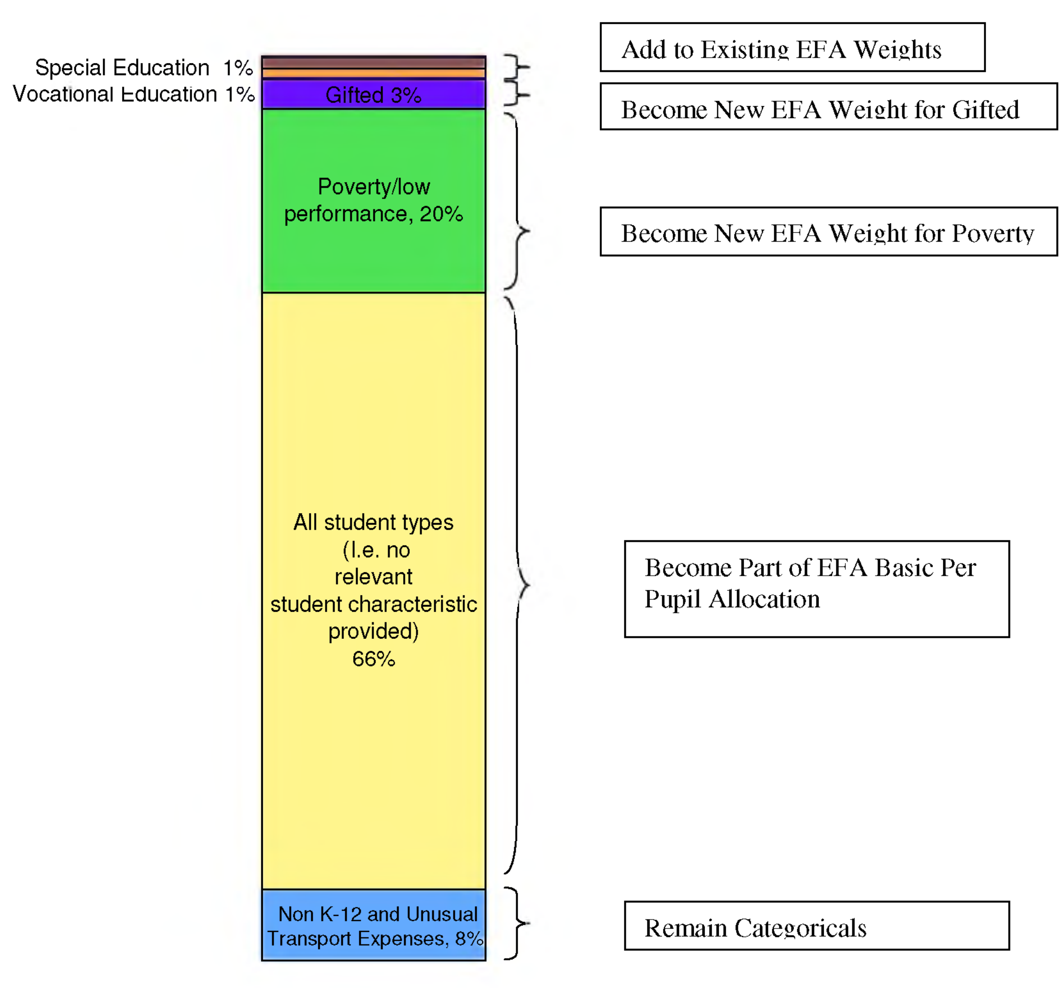


Table 1, below, shows how each type of funds would flow into the EFA system. Table 2, in turn, shows what the new EFA weighting system would look like after the addition of these funds.

What Would NOT Change

It is worth noting how much would *not* change as a result of this shift in approach to funding. The share of state vs. local dollars would not change. Since the new weights are based on how much South Carolina *currently spends* to meet the needs of different groups of students, the amount of funding dedicated to these groups would not change, as Table 2 displays in the columns showing the percentage of funds for each group. The amount of state funding received by most individual districts would not change markedly, with the exception of a drop in funding for some districts that are now particularly successful at winning competitive grants or obtaining reimbursement for spending on state-funded programs. Overall, the state's funding priorities would remain the same.

What would change is the value of state funding to districts and schools. This increase in value would be two-fold. First, the administrative costs of handling the complex array of categorical funds, with all of their attendant requirements and paperwork, would diminish. Districts and schools could then reallocate those administrative funds into efforts to raise student achievement. Second, because state funding would become dramatically more flexible, districts and schools could shift resources into initiatives and activities that can make a real difference for students. While there is no way to predict exactly how districts and schools would use this new flexibility, the streamlined system would open up infinite possibilities for educators to respond more effectively to the needs of their students.

Table 1. Conversion of categoricals into basic funds or weights in EFA

Type of Categorical	Targeted Enrollment	Total value of current categorical/grant allocations intended for each type	Per targeted pupil
Type 1: Targeting Specific groups			
Poverty (includes funds intended for low performance)	366,794	$238,341,565	$650
Gifted (includes AP)	69,195	$39,527,356	$571
Vocational Education	28530	$12,767,551	$448
Various Special Education Categories*	98,544	$15,719,495	$160
Type 2: Targeting Spending Priorities			
All students (i.e., no relevant student characteristic provided)	675,038	$774,847,960	$1,148
Total funds redeployed as weighted allocations		**$1,081,203,927**	
Type 3. Existing categoricals not appropriate for WSF		$92,600,817	

*While this table groups all the special education categories together, special education needs differ dramatically according to the disability, and as such, the state should continue to deploy funds on the basis of different disabilities.

Table 2. Combined weighting system after shifting categoricals into EFA

	Current System				New System		
	Existing EFA (2006-07)		Existing categoricals if delivered as a weighted student allocation		Combined		
Student Characteristic	**Per Pupil**	**Weight**	**Per Pupil**	**% of State Funds**	**New per pupil allocation**	**New weight**	**% of State Funds**
All students	$2,367	1.00	$1,148*	73%	$3,515	1.00	73%
Kindergarten	$710	1.30	*	1%	$710	1.20	1%
Primary	$568	1.24	*	2%	$568	1.16	2%
High School	$592	1.25	*	1%	$592	1.17	1%
Poverty (includes funds intended for low performance)	None	none	$650	9%	$650	1.18	9%
Gifted (includes AP)	None	none	$571	2%	$571	1.16	2%
Vocational Education	$686	1.29	$448	1%	$1,134	1.32	1%
Various Special Education Categories	Depends on student disability		$160	~11%	Depends on student disability		~11%

* Existing categoricals were not separated out by the grade targeted, but this can be done and would yield different weights by grade level

Challenges with Making the Shift

Any kind of major change in a funding system creates challenges, and a move toward more weighted student funding is no exception. South Carolina would encounter several such challenges under this proposal, but none are insurmountable.

Ensuring the funding follows the child to school. The system proposed here would ensure that state money follows children, but only to the district level. Once a district receives state funding, it would have great latitude to spend the dollars as it sees fit. While this latitude is the great advantage of this approach, it also creates a danger: districts might not allocate resources to meet the needs of the intended beneficiaries of state funds.

We propose three strategies to ensure that funding benefits the children who generate it:

1. *Require that money be spent on schools according to how much money their students generate.* South Carolina should require that money generated by a student via the new weighted funding system be spent on that child's school, in one of two ways. Funds could be spent directly; for example, by paying salary and benefits of teachers working at the school. Or funds could be spent indirectly on shared or centrally provided services that tangibly benefit the school in an equitable fashion; for example, by paying for specialist instructors who serve multiple schools. Even costs for reasonable leadership and district operations could be accounted for in per pupil terms to each school to achieve full transparency.

2. *Require transparent reporting of how funds are spent at the school level.* South Carolina should institute a clear regime of fiscal reporting to ensure that targeted funds have their intended effect of boosting spending on a particular student type. In addition to continuing to follow and use the existing SC financial accounting requirements, each district should be required to report publicly and include in their certified required outside audits (a) the amount of funding "generated" by each of its schools, based on their student populations; and, (b) the amount of resources devoted to each school by student type. The state's existing In$ite tool (http://ed.sc.gov/agency/offices/finance/insite) could be fully implemented to serve as the expenditure tracking system. It currently reports expenditures by broad function area, such as instruction or operations; but the In$ite software has the capacity to report by all sub-functions and funding sources at the state, district and school level, aligned with the codes in the required SC Financial Manual. Of particular importance is ensuring that figures represent actual (and not the district average) salaries of the employees at each site. Or, the state could create a combined data collection and reporting system to consolidate all relevant data in one location. Texas has such a system, accessible on the web at: http://www.tea.state.tx.us/perfreport/aeis/2005/index.html. Whatever tool the state used, a key to this reform would be making the resulting data widely available in a user-friendly form so that schools, districts, and the public could easily access and use it. In particular, the state must take responsibility for producing school-level expenditure reports in an easy-to-understand format, and make it possible for citizens to "query" the online system in flexible ways, just as school administrators can do now.

3. *Encourage responsible moves toward school-based funding control.* With a system of weighted student funding in place, South Carolina would be in a position to move toward more school-level control of education dollars. One strategy for this shift could take the form of placing schools into tiers of increasing financial independence, based on schools' demonstrated capacity to handle budget control. With this approach, all schools could move immediately to the first rung on this ladder, on which schools would develop draft budgets linked to their annual school improvement plans, submitting these for approval to their local school boards. The state could then follow the lead of large school districts like New York and Boston, allowing schools to apply to the local school board for greater levels of school-level financial independence after demonstrating their capacity to carry out the responsibility, such as by obtaining relevant training in budget and financial management. Schools could maintain or increase their independence over time by showing strong results in student achievement *and* meeting the state's standards for fiscal responsibility. This tiered structure would enable the state to take advantage of the potential benefits of school-level budget control, such as the ability to tailor services to

the needs of particular students, while avoiding some of the potential pitfalls, such as lack of current capacity on the part of some school leaders to handle school-level financial control responsibly.

If it placed decision-making authority about each school's independence in the hands of local school boards, the state would need to provide oversight to ensure that this process was open, accountable, and not unnecessarily burdensome. This would include:

- issuing guidelines regarding the criteria and processes local school boards must use as they review schools' requests for additional independence; boards that were overly restrictive would be required to bring their procedures into compliance with these state guidelines;
- granting the right of appeal to the state board of education for schools that believe their petitions for greater independence have been unfairly denied by local boards; and,
- accelerating the movement of schools up the tiers by offering or sponsoring training to help more school-level officials gain the capacity needed to manage funds.

Potential resistance to change. Each categorical program in a state has numerous and varying special interests that are likely to try and protect specific pots of money. These special interests may include the program officers, grant administrators, and service providers affiliated with each categorical at both the state and district levels (and even some school levels). The work being done in state and district offices would change, often significantly, under the proposed systems. It is not necessarily the case that the number of state or district personnel would change, but specific jobs would certainly disappear or be changed fundamentally. In addition, some districts that disproportionately benefit from a particular allocation (e.g., districts that are successful in competitive grant programs) could lose money.[4] In some cases, the state legislators responsible for a particular allocation could be its biggest defenders. All of these potential opponents of change could very easily undermine the shift before it happens.

This issue would be partially addressed by a one-year lag between the enactment of new policy and its implementation – giving districts, schools, and the state department time to adjust to the changes in staffing and revenue streams that would inevitably follow such a transformation. In addition, where possible, some flexible funds could be used to hold allocations constant in some areas to minimize the impact of otherwise abruptly withdrawing some categoricals. This explicit "grandfathering" would be highly transparent, and it would phase out quickly with a designated "Sunset Date" in the legislation.

These mechanisms would also give state policymakers time to devise new ways to promote state priorities even as they are giving up the control they now wield via restrictions on funding. For example, if a science education funding program were to sunset after three years, policymakers could use that time to develop new standards and accountability systems for science learning. While they would no longer be able to require districts to allocate specific funding sources to science education, they would still influence district practice through standards and accountability policy.

Loss of targeting for low-performing schools and students. Some categorical allocations are currently targeted to low performing schools and students. It would be possible to continue this targeting by adding weights to the system that boost funding to districts with students who do not meet standards. Doing so would, however, create a perverse incentive whereby districts could earn more state dollars by having more underperforming students.

Instead, in our example demonstration above, we have combined these low-performing allocations in with the poverty weighting, since low performance and poverty are so closely correlated.

Categorizing students under the new weighting system. This approach to allocating funding requires an accurate picture of the student population of every school. By linking dollars more closely to student characteristics, this policy creates an incentive for districts to inflate the number of students enrolled who fall into the different weighting categories. Under the proposal above, there are only two new weights proposed, the weights for poor and gifted students. For poor students, there is already a well-honed process for identifying eligible students, namely the free and reduced price lunch program. For gifted students, however, the state would need to create a centralized auditing function to ensure the identification process is done fairly and consistently across all districts. This system could involve standardized tests identified by the research as appropriate for the identification of gifted students, perhaps administered regionally, or state review, approval, and audit of district- and school-run identification approaches to ensure they meet state standards.

The need to continue managing the system's weights. The system proposed above would simply convert the implied weights of South Carolina's categorical programs into an explicit set of weights. We recommend this approach to minimize the degree of change in the state's priorities initially. Over time, the state would need to revise those weights as required to align them with student needs and state priorities. Increasing the weight for one group of students would not even necessarily require new state resources; rather, increasing the weight just changes the distribution of resources across student types. Some locales using WSF have instituted a "weights committee" with representatives from every level tasked with reviewing the weights every year and recommending modifications. When considering changes to the weighting system, policymakers should look at the whole picture of school funding in the state – including federal funding, which already weights funding in certain ways. Policymakers should aim to bring the overall funding system, considering all sources, in line with their priorities.

Rethink other state policies that restrict local spending decisions. In its efforts to promote flexible use of funds, the state should continue to review other state policies that impose restrictions. For instance, the EFA requires districts to compensate teachers based on each person's experience and class. Such uniform salary scales can work against local efforts to use targeted salary incentives as a way to more evenly distribute teacher effectiveness among more and less disadvantaged schools in the same district. Rethinking some of these kinds of state-wide mandates may be necessary as districts work to more efficiently and effectively deploy their resources to meet the unique needs of the students in their districts.

Conclusion

While these challenges are significant, they are greatly outweighed by the potential benefits of shifting more funds into a weighted student model. Coupled with transparent reporting of how districts allocate funds to schools, weighted student funding has the potential to reduce administrative costs, increase the coherence of education spending at the district and school levels, and enable educators closest to the children to exercise their professional judgment about how to apply funds in ways that will boost student learning. By funding children rather than a byzantine array of categorical line items, South Carolina's policymakers can align the state's considerable resources with what matters most in public education: the needs and achievement of individual students.

-End-

About This Study:

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Bryan C. Hassel is Co-Director of Public Impact. He was a principal author of the Thomas B. Fordham Institute's weighted student funding proposal, Fund the Child: Tackling Inequity & Antiquity in School Finance. Other areas of education reform in which he has worked extensively include state charter school policies, charter school accountability, charter school facilities financing, school district restructuring, comprehensive school reform, and teaching quality. President Bush appointed him to serve on the national Commission on Excellence in Special Education, which produced its report in July 2002. In addition to numerous articles, monographs, and how-to guides for practitioners, he is the co-author of Picky Parent Guide: Choose Your Child's School with Confidence and author of The Charter School Challenge: Avoiding the Pitfalls, Fulfilling the Promise. Dr. Hassel received his doctorate in public policy from Harvard University and his masters in politics from Oxford University, which he attended as a Rhodes Scholar.

Marguerite Roza serves as a Research Assistant Professor at the Daniel J. Evans School of Public Affairs at the University of Washington. Dr. Roza's research focuses on quantitative policy analysis, particularly in the area of education finance. Dr. Roza is a leading national expert on weighted student funding approaches to school finance. Her recent research has documented inequities and inefficiencies in spending within school districts and identified budgeting mechanisms for enabling strategic budgeting decisions for districts. This work is documented in publications available through the Center on Reinventing Public Education, the Brookings Institution and through Annenberg's project on School Communities that Work. In addition to school finance, Professor Roza focuses on principal and teacher labor supply and demand, and leadership shortages. Dr. Roza earned her PhD in Education from the University of Washington.

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ENDNOTES

[1] A ruling in the *Abbeville* case found that the state was meeting its basic educational obligations with the exception of early childhood education, but it did not specifically rule on inter-district equity.
[2] Education Week Research Center annual state policy survey, 2004. Generated using Education Counts "create a table" feature at http://edcounts.edweek.org, December 2006.
[3] Though EFA does not weight for poverty of individual students, EFA's funding mechanism is designed so that the state assumes a greater share of educational expenses in low-wealth districts. This mechanism does not, however, cause more spending in districts or schools with more poor students. Instead, it simply changes the proportion of funding provided by state vs. local sources. Poverty weights are needed to direct additional funds to poor students.
[4] In some states, smaller districts and schools would be adversely affected by such a change because a significant portion of state aid flows out on a per-school or per-district basis, irrespective of size. In South Carolina, however, only 2% of categoricals go out on a per-district basis, and only 4% flow on a per-school basis. As a result, the effect of the change on a typical small school or small district would be minimal.