
Recommendations

Recommendation 1. If the General Assembly wants to eliminate litigation from the local education funding dispute process, then the General Assembly should revise state law for settling local education funding disputes to preserve the benefits of the pre-litigation phase while replacing the litigation process with a default funding mechanism.

As discussed in Findings 1 through 3, the local education dispute resolution process is used infrequently and seldom results in litigation. The pre-litigation stages of the process (joint meeting and formal mediation) can produce non-financial outcomes that improve the local education budgeting and finance environment. However, the litigation stages are costly and time-consuming, and leave both boards of county commissioners and local boards of education short of needed resources.

In Finding 4, the Program Evaluation Division found that Tennessee, which like North Carolina has elected school boards that are fiscally dependent on county commissioners, offers an alternative method for settling local education funding disputes. In lieu of litigation, local education funding disputes in Tennessee are settled using a statutorily prescribed default funding mechanism.

Building on the Tennessee concept of a default funding mechanism, the Program Evaluation Division has created one tailored to North Carolina. This default funding mechanism would allow the General Assembly to eliminate the litigation phase of the dispute resolution process while preserving the benefits of the joint meeting and formal mediation stages.

The default funding mechanism is not meant to determine the appropriate level of local funding for operations and capital, but rather should act as a deterrent discouraging failure to come to a resolution through the annual budget process. Stakeholders have expressed concerns that capital appropriations to local boards of education may vary from year to year and have advocated for exempting capital appropriations from the default funding mechanism. However, exempting capital appropriations would negate the purpose of the default funding mechanism serving as a deterrent for failure to come to a resolution when capital appropriations are at issue.

This proposal preserves state law directing the joint meeting and formal mediation stages of the dispute resolution process before triggering a default funding mechanism. As currently prescribed by state law, the board of county commissioners and local board of education would still be required to arrange a joint meeting to negotiate an agreement. If no agreement is reached during the joint meeting, both boards would engage in formal mediation, sharing the costs equally, to resolve the funding dispute. If the board of county commissioners and local board of education cannot resolve their funding dispute during the joint meeting or through formal mediation, the default funding mechanism would be triggered.

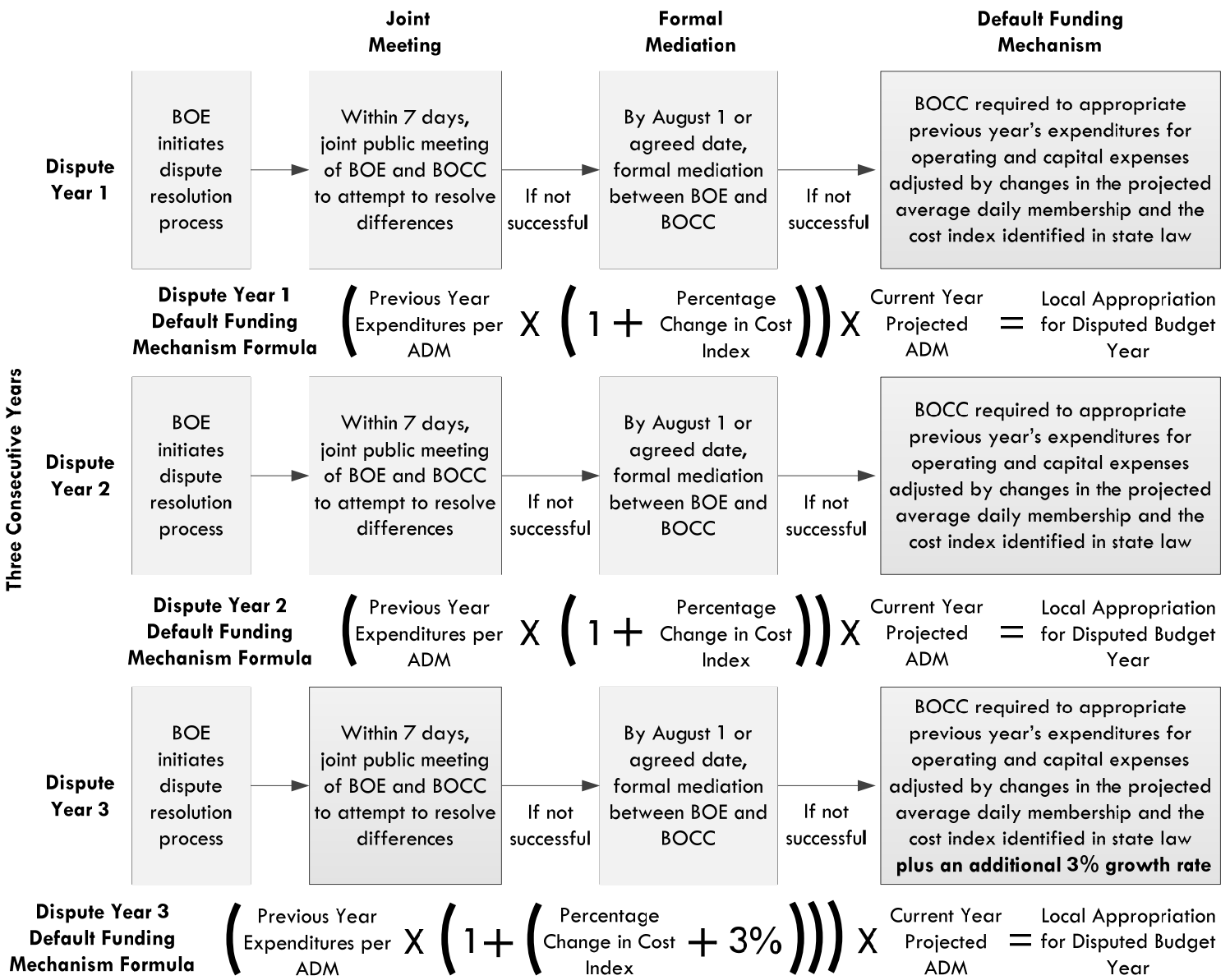
The default funding mechanism establishes a consecutive three-year framework for settling recurring local education funding disputes. The board of county commissioners would appropriate local education funds as determined by the default funding mechanism once it has been triggered. Under the default funding mechanism, local appropriations for the first

disputed budget year would be the previous year's expenditures for operating and capital expenses adjusted by changes in the projected average daily membership (ADM) for the Local Education Agency (LEA) and changes in an employment cost index of salaries and wages for elementary and secondary school personnel.²⁰ If a funding dispute cannot be resolved during the second consecutive budget year, the default funding mechanism described previously would again determine the local appropriation for education. If a funding dispute cannot be resolved during a third consecutive budget year, the default funding mechanism adds an additional 3% growth rate to the mechanism used during the previous two years.

Exhibit 19 provides a diagram and a hypothetical example illustrating how the default funding mechanism works if funding disputes occur during three consecutive budget years. If funding disputes occur during non-consecutive budget years, the default funding mechanism would restart each time. If funding disputes between the two boards continue to occur after the initial three-year time period, the default funding mechanism process would restart and cycle through the three-year time period until such time that the boards can settle their funding disputes without resorting to the default funding mechanism.

²⁰ This cost index was chosen because the majority of public education expenditures are for personnel salary and benefits. The cost index (Bureau of Labor Statistics' Employment Cost Index Series Id: CIU30261000000001) is reported quarterly for a calendar year, and second quarter data would be the most recent data available during the local education funding dispute resolution process.

Exhibit 19: Revised Dispute Resolution Process Replaces Litigation with a Default Funding Mechanism



Hypothetical Example	Base Year	Dispute Year 1	Dispute Year 2	Dispute Year 3
	Fiscal Year 2013–14	Fiscal Year 2013–14	Fiscal Year 2013–14	Fiscal Year 2013–14
Projected Average Daily Membership (ADM)	1,000	1,013	1,042	1,071
Cost Index Percentage Change	N/A	0.95%	1.89%	1.52% + 3.0%
Local Operational Expenditures per ADM	\$ 100	\$ 100.95	\$ 102.86	\$ 107.51
Total Local Expenditures	\$ 100,000	\$ 102,266	\$ 107,180	\$ 115,138

Notes: BOCC stands for board of county commissioners. BOE stands for local board of education. For the hypothetical example, the Program Evaluation Division used the Bureau of Labor Statistics' Employment Cost Index for elementary and secondary school workers for calendar years 2012 through 2016 (Series Id: CIU30261000000001). This cost index is reported quarterly for a calendar year, and second quarter data would be the most recent data available during the local education funding dispute resolution process. To calculate the Cost Index Percentage Change for each disputed budget year, the second quarter cost index data from the previous calendar year was compared it to the second quarter data for the current year.

Source: Program Evaluation Division.

Recommendation 2. The General Assembly should direct the Local Government Commission and School of Government at the University of North Carolina at Chapel Hill to convene a working group to develop and recommend statutory parameters for fund balances maintained by local boards of education.

As discussed in Finding 5, many local boards of education are retaining large unencumbered fund balances. Fund balances can be an issue in disagreements between local boards of education and boards of county commissioners but also represent resources being withheld from K-12 public education. Local boards of education do not need to maintain large unencumbered fund balances because their operational needs are different from county governments and the majority of their operational funding comes from state appropriations. The Local Government Commission (LGC) does not currently provide guidance for local boards of education because these boards are not authorized to levy taxes.

To address unencumbered fund balances maintained by local boards of education, the General Assembly should direct the LGC and the School of Government (SOG) at the University of North Carolina at Chapel Hill to develop and recommend statutory parameters for fund balances maintained by local boards of education. The working group should include representatives from the North Carolina Association of County Commissioners, North Carolina School Board Association, and North Carolina Association of School Business Officers. The parameters should provide direction for local boards of education on

- minimum and maximum fund balances with a focus on unencumbered funds,
- appropriate uses of fund balances,
- annual reporting requirements of fund balances,
- how fund balances should be factored into annual local budgets for education, and
- the role of boards of county commissioners in determining the use of fund balances maintained by local boards of education.

The working group should recommend statutory parameters for local board of education fund balances to the Joint Legislative Education Oversight Committee no later than March 30, 2018.

Appendix

Appendix: Judicial Decisions Relating to the Local Education Funding Dispute Resolution Process

Agency Response

A draft of this report was submitted to the North Carolina School Boards Association and the North Carolina Association of County Commissioners. Their responses are provided following the appendix.