3-16-2007

Writing a New Chapter: A City Club Report on School Funding

City Club of Portland (Portland, Or.)
City Club members will vote on this report on Friday, March 16, 2007. Until the membership votes, City Club of Portland does not have an official position on this report. The outcome of the vote will be reported in the City Club Bulletin dated March 30, 2007 and online at www.pdxcityclub.org.
The mission of City Club is to inform its members and the community in public matters and to arouse in them a realization of the obligations of citizenship.

Additional copies of this report are available online at www.pdxcityclub.org or by contacting the City Club office:

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Many observers inside and outside Oregon claim Oregon is in a statewide school-funding crisis. By most accounts, the situation is particularly grave in Portland. City Club of Portland initiated this study in the summer of 2003 after Multnomah County voters approved a three-year income tax to fund schools and social services. The tax was intended to be a temporary source of revenue, with the hope that the Legislature would devise an adequate and stable source of funding for kindergarten through twelfth grade education in Oregon. This was an unprecedented tax initiative, adopted after years of program cuts in Portland’s schools and highly publicized labor and leadership disputes left school administrators, parents and community groups deeply concerned about the funding of public education. Now, more than three years later, the county tax has expired, and no fundamental changes have been made regarding how schools are funded in Oregon.

While much of the public debate is about how much money should be spent on schools and how schools spend the money entrusted to them by taxpayers, many school officials and observers assert that the stability of funding is at least as important as the level of funding. In response, this report focuses on the issue of funding stability, which is rooted in Oregon’s tax structure and the state’s mechanism for allocating funds to school districts, while also addressing some issues related to the adequacy of education funding.

Study Scope and Objectives

The purpose of this study was to determine how to best finance operating costs for K-12 education in the five public school districts operating entirely or partially within Portland’s city limits. These districts are Centennial, David Douglas, Parkrose, Portland Public Schools and Reynolds. While the geographic scope of the research was limited to these five school districts, your committee believes that this report contains useful information and viable recommendations that will benefit school districts throughout Oregon.

Your committee was charged with identifying stable sources of revenue for K-12 education and recommending how to finance “quality education” as determined by federal and state laws, local school boards and communities. Your committee was
instructed not to attempt to define “quality education” or the cost of quality education and assumed for the purpose of this study that the debate about how much money schools should receive is secondary to the need for stable funding. This study rested on the premise that federal and state law and local school boards have defined, and will continue to define, education standards. Your committee focused exclusively on how to finance quality education, regardless of how it is defined or how much it costs. Likewise, your committee did not attempt to audit the educational performance or financial practices of schools in the Portland area or elsewhere.

Your committee was charged with three objectives listed below:

- Recommend solutions for the Legislature and Governor to stabilize the state’s financial contribution to K-12 education.
- Develop a contingency plan to stabilize funding levels for Portland’s five school districts in the event that statewide funding is unstable to the degree that the school districts cannot provide what they believe to be quality education.
- Recommend school funding options that could be implemented in the event that state funding is insufficient to provide what the school districts believe to be quality education.

Through the course of this study, your committee learned that stable funding and adequate funding are each important in their own right, yet are not completely independent of one another. Because the charge to your committee was focused on stability, this report addresses adequacy only to the extent that it is interrelated with stability.

Members of your committee were screened for conflict of interest to ensure that no member of the committee had a direct economic stake in the outcome of this study or had a public position on education funding.
The 1990s were a time of significant change for school funding in Oregon. During this period, voters capped and limited the growth of property taxes with Measures 5, 47 and 50. As a result, the primary source of education funding shifted from locally controlled property taxes to the state income tax. Before 1990, state funding accounted for about 30 percent of school support. By 1997 the state’s share was about 70 percent. From the 1970s to 2006, the share of state general fund revenue from corporate income tax collections declined from about 15 percent to about 5 percent due to a number of changes to the way corporate income taxes are calculated. The combined effect of these shifts increased reliance on personal income tax collections to finance state services and education.

Measure 5, which passed in 1990 with approximately 52 percent of the vote, limited the amount of property tax revenue available for school funding. Measure 5 restricted taxes on each parcel to a rate of $5 per $1,000 of real market value for schools and $10 per $1,000 for local governments, which reduced local property tax revenue for most school districts in the state. The measure provided no new source of funding for K-12 education. The assumption by both opponents and proponents of the measure was that the state would allocate money from the general fund to make up the difference between prior school district budget levels and their future budgetary needs.

Even with Measure 5 in place, property taxes increased as property values increased, and since residential property values generally appreciate faster than business properties, residential property owners found themselves paying an increasing share of property taxes compared to businesses. Measure 47, which passed in 1996 and was replaced by Measure 50 in 1997 to improve implementation, limited the effect of increasing property values on property tax collections. Measure 50 limited the growth in the assessed value of properties to 3 percent per year and no longer based property taxes on real market value. Measures 5 and 50 severely limited growth in property tax revenue over time, making funding for public education increasingly dependent on state income tax revenue.
Also during the 1990s Oregon enacted two pieces of legislation that significantly increased state spending without increasing revenue. Measure 11, a mandatory sentencing measure, forced the state to build new prisons to house an upsurge in the number of inmates created by the provisions of this initiative. Measure 11 is estimated to have added 3,700 inmates to Oregon’s prison population.

In addition, the state implemented the ambitious Oregon Health Plan, which increased spending on health care for low-income Oregonians. Oregon’s 2005-07 general fund budget allocates more than $2.5 billion for health services. These two initiatives are financed from the same revenue streams that previously funded a more limited set of government programs and now support public education.

Yet another ballot measure approved by the voters in 2000 reduced the state’s ability to stabilize its finances by investing money in a rainy day fund. Voters passed Measure 86, which locked Oregon’s unique budget surplus mechanism known as the “kicker” in the Oregon Constitution. Under the kicker law, if revenue exceeds budget estimates by two percent or more, all unbudgeted revenue is refunded to taxpayers. The kicker law makes directing budget surpluses into a reserve fund difficult. For example, in the fall of 2001, with Oregon’s economy in decline, state officials were required to refund $253.6 million in revenue generated during stronger economic conditions. Without the kicker, the Legislature would have been able to place that revenue into a reserve fund in anticipation of the dramatic decline in state income tax revenue that was then just starting.

The full fiscal impact of all these changes was masked by the thriving economy of the 1990s. During those years, income tax revenue, boosted by capital gains, continued to rise, cushioning the impact of Measures 5 and 50. Without this significant surge of income tax revenue, the state would have faced financially hard times in the 1990s. Whether or not the unusually high revenue from capital gains in the 1990s repeats itself, it is likely that the state will continue to oscillate between revenue shortfalls and surpluses.

The shift from local to state school funding, combined with other state spending decisions since 1990, makes schools tremendously dependent on income tax revenue, the state’s primary source for discretionary spending. Schools now compete with both new and traditional state programs, such as children and family support services, colleges and uni-
versities, and public safety programs. While income taxes collected by the state increased year-to-year in the 1990s, competition among programs for funding was intense.

As noted previously, Oregon benefited from increased revenue during the economic boom of the late 1990s. When the boom ended, the resulting decline in tax revenue caused the Legislature, after calling five special sessions in 2002, to cut programs, reduce services, borrow against future revenue and refer Measure 28 to voters. Measure 28 would have created a temporary one-percent increase in Oregon’s income tax. The tax package, which had bipartisan support in the Legislature, was rejected by voters, leading to a significant drop in funding for schools in the 2002-03 school year. (See Figure F on page 47.)

The following year, as part of a compromise to balance the state budget, the Legislature passed House Bill 2152, a tax package designed to raise state revenue and avoid budget cuts. This compromise was reached during the longest legislative session in Oregon history. Using Oregon’s referendum process, citizens opposed to the tax increases successfully petitioned to refer House Bill 2152 to voters. The referendum, certified as Measure 30, appeared on a February 2004 special election ballot. Measure 30 would have created a surcharge on Oregon’s income tax, raised the minimum tax corporations pay in Oregon income taxes, and made other changes to the tax code to increase state revenue. Like Measure 28, Measure 30 was defeated at the polls. Consequently, school funding for the 2004-05 school year was once again lower than it was the previous year. (See Figure C on page 9.)
State and Local School Funding Today

Oregon allocates funding to local school districts through the State School Fund. This fund is the collective term for state general fund money (primarily income tax revenue), local property taxes, the Common School Fund and lottery dollars appropriated by the Legislature for schools. In addition to supporting the State School Fund, lottery dollars also have been used since 1997 to finance an Education Endowment Fund, which was converted in 2002 to the Education Stability Fund, a “savings account” for schools. The Common School Fund was established at statehood as a mechanism to collect revenue from state and federal land assets and direct it to schools. As of 2005-06 it has a total value of $900 million. Managed by the State Land Board, distributions fluctuate with the value of the fund and investment market conditions. More than $13 million was distributed to the State School Fund in 2004 and $40.2 million in 2005, due to favorable market conditions and a high fund value.

Figure A: Funding Snapshot: K-12 in Oregon (2004-05 Fiscal Year)

<table>
<thead>
<tr>
<th>Source: Legislative Revenue Office</th>
</tr>
</thead>
<tbody>
<tr>
<td>State School Fund</td>
</tr>
<tr>
<td>Property taxes and other local revenue</td>
</tr>
<tr>
<td>Federal forest fees and other federal revenue</td>
</tr>
<tr>
<td>Debt</td>
</tr>
<tr>
<td><strong>TOTAL REVENUE</strong></td>
</tr>
<tr>
<td>Beginning Balance</td>
</tr>
<tr>
<td><strong>TOTAL RESOURCES</strong></td>
</tr>
<tr>
<td>Less expenditures</td>
</tr>
<tr>
<td><strong>ENDING BALANCE</strong></td>
</tr>
</tbody>
</table>
As a result of Measures 5 and 50, property tax dollars for schools are pooled with the state general fund and then distributed back to school districts through a formula intended to equalize funding on a per student basis. Oregon began phasing in a school funding equalization formula in 1991, with implementation completed by 2001. The starting point for the formula is an allocation based on Average Daily Membership (ADM), which is the number of students in attendance. Weightings are added to the base formula for various factors. For instance, kindergarten students are weighted as half students, and students with special educational needs are weighted as the equivalent of two students to account for the higher average cost of providing their education. Additional factors, such as a transportation reimbursement, also augment the basic formula.

**Figure B: Methods of Counting Student Populations**

<table>
<thead>
<tr>
<th>Formula</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ADM or Average Daily Membership</td>
<td>The sum of the number of days in membership for all students divided by the number of school days in a term.</td>
</tr>
<tr>
<td>ADMr or Resident Average Daily Membership</td>
<td>Year-to-year average of daily student enrollment for students residing within the district. Some resident students attend school in other districts. Kindergarten students are counted as half-time students.</td>
</tr>
<tr>
<td>ADMw or Average Daily Membership Weighted</td>
<td>The sum of the number of days in membership for all students adjusted for specific factors and divided by the number of school days in a term.</td>
</tr>
</tbody>
</table>
The formula is intended to approximate the higher cost of educating some categories of students, although the approximation is not based on actual cost data. The Legislature established the formula using weightings that are rough estimations of the true costs of educating all students.

While this system has increased equity in school funding, it has also created new winners and losers, with poorer and often rural areas seeing an increase in per student funding and some areas, such as Portland, becoming net exporters of tax dollars for schools. Analysis by The Oregonian revealed that Multnomah and Washington counties generated $200 million more in income and property taxes than they received back from the state in 2003-04. Critics of Oregon’s system of equalizing per student spending across the state argue that the benefits accrued from taxation should correlate more directly with taxes paid at the local level.

Figure C illustrates State School Fund allocations through the equalization formula. The figure shows a reduction in funding for 2004-05, which corresponds with voters’ rejection of Measure 30 in February 2004.
Figure D shows the per student amount received from the State School Fund by each district in Portland. Reflecting the overall state revenue distribution shown in Figure C, Figure D also shows a significant drop in funding for each district in 2004-05.

In addition to state funds, each district in Multnomah County received funds from the Multnomah County income tax and federal money for students with special needs. Portland Public Schools also received funds from a local option property tax.

**Figure D:**
State School Fund Distribution to Portland Schools (per student)

<table>
<thead>
<tr>
<th>School Districts</th>
<th>2003-04 per ADMw</th>
<th>2004-05 per ADMw</th>
<th>2005-06 per ADMw</th>
</tr>
</thead>
<tbody>
<tr>
<td>Centennial</td>
<td>$5,248</td>
<td>$5,219</td>
<td>$5,295</td>
</tr>
<tr>
<td>David Douglas</td>
<td>$5,331</td>
<td>$5,019</td>
<td>$5,365</td>
</tr>
<tr>
<td>Parkrose</td>
<td>$5,295</td>
<td>$5,039</td>
<td>$5,355</td>
</tr>
<tr>
<td>Portland Public Schools</td>
<td>$5,393</td>
<td>$5,126</td>
<td>$5,499</td>
</tr>
<tr>
<td>Reynolds</td>
<td>$5,402</td>
<td>$5,086</td>
<td>$5,460</td>
</tr>
<tr>
<td>State Average</td>
<td>$5,374</td>
<td>$5,104</td>
<td>$5,437</td>
</tr>
</tbody>
</table>

*Source: Legislative Revenue Office*
A Closer Look at Portland

Portland’s five school districts have been differently affected by changes in state and federal law since 1990. As a result of the school funding equalization formula, Portland Public Schools and Parkrose, with relatively high property-tax bases, saw their funding reduced to the state average per student, while low-property-tax districts like Reynolds, Centennial and David Douglas were brought up to the state average. Portland Public Schools, which historically has enjoyed broad financial support from local residents, is now constrained by Measure 5 and Measure 50 from determining its level of funding.

In roughly the last ten years, Portland Public Schools’ constituents approved three property tax measures. First, the district passed a ten-year infrastructure bond in 1995 that was used to fund earthquake upgrades, building repairs, and to purchase computers and other equipment. Then in 2000, voters approved a five-year local option property tax, which provided about 7.5 percent of the district’s operating budget in 2005-06. Most recently, voters living in the district approved a new five-year, $33.3 million local option levy in 2006.

During the same time period, Portland’s four smaller districts also attempted to pass local option operating levies and capital improvement bonds, but with less success. In 1998, Centennial and Reynolds failed to pass bonds, and in 1994 Parkrose and Reynolds voters rejected bond measures. In 2000, voters in Centennial, David Douglas and Reynolds districts approved capital construction bond measures. In 2002, voters in Parkrose and Reynolds rejected proposed increases to the districts’ operating levies. David Douglas and Reynolds both ran and failed to pass capital bond measures in 2006.

Multnomah County Income Tax

In 2003, Multnomah County voters approved Oregon’s only county income tax. This tax produced $618 per student in its first year, and $863 in 2005-06, or 10 to 12 percent of the five districts’ operating budgets. The county income tax was the product of a discussion among school administrators and teachers, school activists, and city and county officials about ways to close the gap between what funding the state was likely to provide to Portland area schools in the 2003-05 biennium and what local authorities believe was necessary to provide basic education services. The parties involved agreed that the tax would be a temporary stopgap measure until the 2005 Legislature adopted a
stable and adequate funding stream for schools statewide.

The county income tax was designed to maintain the spirit of the state’s funding equalization formula, meaning funds were apportioned based on each district’s student population rather than the tax base of each district. A former officer of the Portland Public Schools board who weighed alternative proposals told your committee that avoiding tax and funding differences between participating districts was an important factor in the decision to propose a countywide tax.

The Multnomah County income tax expired at the end of 2005 with no change.

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**Figure E:**
Select Characteristics of Portland’s Five School Districts

<table>
<thead>
<tr>
<th>District</th>
<th>Student Population (ADM, FY04-05)</th>
<th>Operating Expenditures Per Student (ADM, FY04-05)*</th>
<th>Students Eligible for Free and Reduced-price Lunches as % of enrollment</th>
<th>English Language Learners as % of ADMr</th>
<th>Special Education Students as % of ADMr</th>
</tr>
</thead>
<tbody>
<tr>
<td>Centennial</td>
<td>6,260</td>
<td>$8,137</td>
<td>4,213 (67.3%)</td>
<td>983 (15.7%)</td>
<td>801 (12.8%)</td>
</tr>
<tr>
<td>David Douglas</td>
<td>9,259</td>
<td>$7,370</td>
<td>6,407 (69.2%)</td>
<td>2,407 (26%)</td>
<td>1,111 (12%)</td>
</tr>
<tr>
<td>Parkrose</td>
<td>3,468</td>
<td>$8,215</td>
<td>2,070 (59.7%)</td>
<td>569 (16.4%)</td>
<td>420 (12.1%)</td>
</tr>
<tr>
<td>Portland Public Schools</td>
<td>44,233</td>
<td>$10,138</td>
<td>19,949 (45.1%)</td>
<td>4,821 (10.9%)</td>
<td>6,060 (13.7%)</td>
</tr>
<tr>
<td>Reynolds</td>
<td>10,328</td>
<td>$8,674</td>
<td>5,742 (55.6%)</td>
<td>2,334 (22.6%)</td>
<td>1,590 (15.4%)</td>
</tr>
</tbody>
</table>

Source: Joint report from Multnomah County auditor and city of Portland auditor, “Students, Spending, Services, and Accomplishments, Multnomah County School Districts (2005).”

* Operating cost per student was calculated by dividing each district’s total revenue by the number of students. Total revenue is the state general fund money allocated to each district through the State School Fund plus any dedicated revenue funds, most notably federal and state grants for students in the three specialized categories in Figure E, and other sources such as food service sales and grants.
in the state funding mechanism. With the county income tax revenue no longer available beginning with fiscal year 2006-07, all districts in the county once again faced a potential decline in revenue.

**Cost Factors**

Variances in the student populations of Portland’s five districts affect their financial needs. For example, enrollment is growing in east Portland, where Centennial, David Douglas and Reynolds districts have experienced significant increases in student populations since 1999. Districts with growing student bodies require revenue to hire additional teachers and support staff, build classrooms and purchase supplies. Portland Public Schools has an overall declining student population with some schools growing and others declining. Coupled with aging facilities, this is a costly combination of factors because of the high fixed costs associated with the physical infrastructure of the district.

Figure E (page 12) compares information about each of the districts. Your committee found several reasons for this. According to Multnomah County Auditor Suzanne Flynn, on a percent-

* Eligibility for the federal free and reduced-price lunch program is based on family income and is commonly used as an indicator of poverty.
age basis, Portland Public Schools receives a much larger share of its operating budget from funds designated for students with special needs than any other district in Multnomah County. Portland Public Schools is the regional service provider for many special education students living in the three-county metropolitan area. As such, the district receives funding for these students, but because the students do not reside in the district, they are not counted in the ADMr statistics. As a result, when the average cost per resident student is calculated, the cost is exaggerated for Portland Public Schools and, in some cases, is under reported for the districts where these students reside but are not enrolled.

Several other factors contribute to the appearance of an unusually high level of funding for Portland Public Schools. Portland Public Schools runs grant-funded programs, such as Head Start, which in other districts are almost always run by non-profit organizations. Portland Public Schools, unlike other districts in Portland, also receives money in lieu of contractual services from Multnomah Education Service District. In addition, variances in reporting methods among the districts contribute to misunderstandings about how special-needs programs are funded. Finally, voters in the Portland Public Schools district have a history of taxing themselves more than those living in the other Portland districts. Consequently, those districts have had less money to spend for education. Together these factors explain in large part why the reported per student spending for Portland Public Schools appears inordinately high.

Regardless of overall funding levels, the five Portland school districts spend their funds fairly consistently. Most of the expenses are tied to classroom instruction and other related costs, amounting to between 88 and 90 percent of all costs for the districts. (Related costs include operational and support expenses such as transportation, food, maintenance, technology, supplies, counseling, health, speech pathology, library and extracurricular activities.) Spending on administrative functions (superintendent’s office, finance, personnel, etc.) was 5 percent or less of overall spending for the districts. Portland Public Schools’ administrative costs were 3 percent of its budget.

All school districts experienced increases in the number of English language learners between 1998-99 and 2004-05. Centennial increased 146 percent, David Douglas 124 percent, Parkrose 62 percent, Portland Public Schools
20 percent and Reynolds 13.6 percent during this seven-year period. Student transportation spending per mile driven is also increasing, primarily due to rising fuel prices.\textsuperscript{11}

Oregon schools, not just in Portland, have also had to weather the increased costs of meeting federal and state student performance standards, special education requirements, and rapidly rising employee health care and retirement expenses. These matters of cost-containment exceed the scope of this study, so for the purposes of this report, your committee will simply cite research from the Chalkboard Project, which analyzed teacher salaries and benefits. This research indicates that when the salaries of Oregon’s teachers are compared on a \textit{per teacher} basis with those in other states, Oregon teachers receive higher benefits than almost all other states and salaries that are well above average.\textsuperscript{12} However, in 2002-03, Oregon spent significantly more \textit{per student} on teacher benefits and considerably less \textit{per student} on salaries than other states. When salaries and benefits were combined, Oregon spent somewhat below the national average for its teachers on a \textit{per student} basis.\textsuperscript{13} In other words, when class size is included as a factor in evaluating teacher compensation, Oregon pays below the national average. How districts plan for uncertain times also affects funding stability. Some districts stabilize their year-to-year finances by setting aside reserves. District officials struggle to find the right balance between spending as much as possible directly on students and allocating money for contingencies. During the 1990s, Portland Public Schools made difficult choices to balance the budget, including minimizing the amount of money placed in reserves in order to maximize dollars for the classroom. More recently Portland Public Schools’ board allocated a slightly greater percentage of its budget to reserves despite, or perhaps because of, anticipated declines in revenue. According to Parkrose Superintendent Michael Taylor, Parkrose built up its reserve fund in the 1990s and then tapped into it to reduce the impact of lost revenue when the county tax expired.
Nongovernmental Funding Sources

Other sources of funding for K-12 education include private nonprofit organizations such as foundations that raise money for schools and school districts and other grant-making organizations to which schools and districts can apply. The Portland Schools Foundation is the largest foundation of its kind in the area. The foundation contributed approximately $5 million to schools for the 2004-05 school year. Every school in the Portland Public Schools district has an account with the Portland Schools Foundation. Of them, 31 schools operate local foundations under the fiscal umbrella of the Portland Schools Foundation. Because not all schools can raise significant private money, the Portland Public Schools board requires that one-third of the funds raised by local school foundations be collected in a common fund that is distributed to all schools in the district. The remaining two-thirds of the money raised by a local foundation stays with the local foundation.

Centennial, David Douglas, Parkrose and Reynolds school districts also have foundations to support classroom instruction through community fundraising. Each uses a variety of fund-raising methods such as auctions and bottle and can drives to raise money. Some school systems have been successful raising funds through grant writing. Grants have been used to fund after-school homework programs, school counselors, preschool programs and other K-12 programs and services. Grants are generally for specific purposes, and often cannot be used for general operating expenses. Grants are rarely, if ever, a permanent funding source for schools. As a result schools and districts often have to cut programs and services when grant funding expires.
This section of the report is divided into five topic areas for discussion and analysis. Your committee determined that these areas encompass the primary sources of funding instability and inadequacy, not only for school districts in Portland, but also for many others throughout the state. The analysis begins with the requirements placed on local school districts, because they set the stage for how school districts are required to spend money. This is followed by an explanation of how the state and local school districts shape their education budgets. Finally, a discussion of federal, state and local sources of funding for education leads to recommendations on ways to generate more stable revenue for schools.

Federal Requirements

For most of our nation’s history, the federal government has played a minor role in education. Local districts have had tremendous freedom in how they deliver public education. In general, state governments set broad standards, leaving the details to school districts. While the importance of local autonomy has long been a hallmark of the American education system, school districts have become increasingly subject to mandates from both state and federal authorities. With the United States Supreme Court’s 1954 decision in Brown v. Topeka Board of Education and then with legislation in the 1960s, the federal government took a more active role in education, ensuring that all children had equal access to the public school system and aiding students living in poverty and with special needs.

With this aid came rules and regulations from the federal government and the state of Oregon, as they increased their roles in setting education standards. These new standards and requirements have added to the financial burden of local school districts.

In the 1960s, Congress passed the Elementary and Secondary Education Act. Title 1 of ESEA funded education for children living in poverty and imposed
standards for how these funds are to be used. While Congress allocates money for this program, it does not fully fund it. If the program had met its own definition of full funding, Oregon would have received approximately $180 million in additional federal support in 2004.*

The 1975 Individuals with Disabilities Education Act introduced additional requirements for the education of students with special needs. When adopting IDEA, Congress said, as a condition for receiving federal funds, states must ensure children with special education needs receive free and appropriate education. The needs of individual students requiring special services must be met, even if this requires hiring full time staff to serve one student. Parents who believe their child’s needs are not being met have grounds to sue the school district. A school district official told your committee that school districts must balance the cost of special education against the risk of possible litigation based on failure to meet the needs of all children.

Oregon and the federal government provide supplemental funding for students with special educational needs. Whether the funds provided fully cover the cost of educating the targeted students remains unclear to your committee. School district officials interviewed by your committee could not say with certainty whether the supplemental funds cover the full cost of additional services. They speculate that the Portland metropolitan area attracts families with special needs, particularly those with the most significant health care requirements, because of professional services available in the area. These officials also expressed concern that the number of special needs students, and the cost of serving them, will continue to increase without a corresponding increase in state and federal assistance.

In 2001, Congress approved amendments to ESEA known as the No Child Left Behind Act. These provisions were intended to establish new mechanisms of accountability for the performance of public schools. A goal of these amendments was to ensure that public schools would be evaluated by the performance of all their students, including students with special needs. The act requires states to measure the yearly progress

* The definition of “full funding” of Title I is an allocation of 40 percent of state average per pupil expenditures (APPE) for each Title I eligible student. Under this definition, the Congressional Budget Office estimates a shortfall of $18 billion in fiscal year 2004. Assuming Oregon has about 1 percent of the nation’s poverty level students, about $180 million of additional federal assistance would come to Oregon under full funding for Title 1. National Conference of State Legislatures report, February 2005.
of students through specific testing and reporting procedures. Schools must achieve “adequate yearly progress” for 99 percent of all students by the 2013-14 school year.*

Oregon uses standards adopted in the Educational Act for the 21st Century as its benchmarks for measuring compliance with No Child Left Behind. However, the goal of Oregon’s act was based on an achievement rate of 90 percent, not 99 percent as required by NCLB. The full impact of the higher target achievement rate set by NCLB looms large over school districts and state officials. Districts that fail to make adequate yearly progress are required to provide additional services, from tutoring to transporting students to providing access to alternative schools within the district. Failure to measure student performance, to achieve adequate yearly progress, or to improve teacher qualifications will result in increasingly severe penalties for schools including ultimately being required to restructure as a charter school or being turned over to private management.14

Regardless of individual school performance, your committee expects that pursuit of NCLB’s 99 percent compliance rate will drive increased funding needs in coming years and force greater spending on a relatively small segment of the student population.

The National Education Association, an employee union representing primarily educators and faculty members, criticizes the NCLB amendment as an unfunded mandate of the federal government because it establishes requirements without appropriating funds to pay for them. The NEA says that the programs required to support NCLB needed $32 billion more in federal funds in 2003 than the $23 billion appropriated by Congress. The U.S.

“Regardless of individual school performance, your committee expects that pursuit of NCLB’s 99 percent compliance rate will drive increased funding needs in coming years and force greater spending on a relatively small segment of the student population.”

* States are allowed to offer alternative tests to the 1 percent of students who have the most significant cognitive disabilities. States may also ask for permission to test an additional 2 percent of students with cognitive disabilities at the lower achievement level.
Department of Education insists that “mandate” is an inappropriate characterization because the federal standards are conditions of federal funding that states voluntarily accept.\textsuperscript{15}

Several states have considered sacrificing federal education aid rather than trying to meet all of the standards of NCLB. In 2004, Utah questioned the U.S. Department of Education about the consequences of not participating in NCLB. The Department’s response was that Utah would not only lose access to Title 1 funding, but also to potentially twice that amount in various other federal grants and aid.\textsuperscript{16}

Oregon has sought approval from the national Department of Education for flexibility in satisfying NCLB’s requirements. Most recently, the state was denied in its bid to be one of several states to test different approaches from that dictated by NCLB in measuring yearly progress of students. State officials believed that Oregon’s approach was more reasonable and would have enabled many schools to show appropriate progress while still ensuring an adequate level of student achievement.

As a result of the nationwide debate generated by NCLB’s requirements and subsequent penalties for non-compliance with them, state education officials and school advocacy groups have proposed a number of changes to the law. Suggestions include targeted federal grants for specific schools and students failing to make adequate yearly progress, incentives for teachers who teach in poorly performing schools and suspending the penalty provisions of the NCLB when the federal government does not fund Title 1 to the fullest extent authorized.

Your committee believes that the federal government’s aspiration of 99 percent compliance with NCLB is commendable, but the goal is quite likely unattainable and the penalties for noncompliance are severe. Because the students who comprise the 9 percent difference between state and federal requirements are the most challenging and most costly to educate, expectations of fully closing the gap are unrealistic. Left in place, the escalating penalties of NCLB are likely to be financially destabilizing for school districts. With Congress just beginning NCLB’s reauthorization process, your committee believes now is the time for policy-makers to carefully consider the destabilizing effects the act is likely to have on schools in Oregon.
State Requirements

In 1991, the Oregon Legislature passed the Educational Act for the 21st Century. The act was intended to change the way Oregon educated its student population, preparing it for an increasingly knowledge-based and international economy. The goal of this reform was to move away from the traditional “three Rs” education of the nineteenth century and the “seat time” and conventional grading of the twentieth century, to newer teaching methods and performance standards that would enable all students to achieve at a higher level.

The act required movement toward a system of testing requirements, standards and benchmarks for elementary, middle school and high school students. The basic benchmark is for 90 percent of students to meet the state’s education standards. Oregon tests students annually to measure each school’s progress toward the benchmarks. The act established a new and controversial set of standards for high school graduation, called the Certificates of Initial Mastery and Certificates of Advanced Mastery, commonly known as CIM and CAM. These high school standards did not gain wide acceptance as tools to measure student achievement and are being replaced.

Testing requirements for the lower grades are also being revised to ensure they accurately reflect changes being made to curriculum and appropriately measure student achievement.

Oregon’s education act also stipulates that local school districts cannot be required to meet these state standards unless adequately funded by the Legislature, which under current state law is estimated by the Quality Education Model. (The Quality Education Model is discussed on page 23.) However, the federal government also requires the same standards to be met in order to measure compliance with NCLB, which essentially subsumes the state provision.

Oregon’s system of measuring student progress and the benchmarks it has set are more realistically attainable than those imposed.
by the federal government. Your committee believes the potential penalties for non-compliance with NCLB’s requirements are excessive. It is unlikely that any school district in Oregon will achieve the 99 percent compliance benchmark.

If allowed to play out, NCLB will significantly undermine the adequacy and stability of funding for all Portland districts, as well as many others in Oregon. Your committee is particularly concerned that, when combined with legal requirements for equal access to a quality education for all students, school districts will be forced to devote an unreasonably high percent of their limited funds to the relatively small number of students who are least likely to meet NCLB’s requirements. Unless overall budgets increase, efforts to better serve a small percent of the student population will come at the expense of the majority of students.

Establishing the State Education Budget

A
fter Oregon voters passed Measure 5 in 1990, the Legislature became responsible for appropriating a total school budget — known as the State School Fund — and allocating those funds to school districts. Duncan Wyse, now president of the Oregon Business Council, was executive director of the Oregon Progress Board when Measure 5 was enacted. Wyse recalled for your committee that the Legislature had no base of information to determine appropriate education funding and the “budgets were little more than just picking a number.” Until that time, establishing school budgets had been the job of local school boards with no common approach among them. During the 1990s, Governor Kitzhaber and legislators collaborated on tools to collect data on the actual costs of education practices as a means of establishing benchmarks for school funding.

Database Initiative

In 1997, the Legislature passed House Bill 3636 requiring the Oregon Department of Education to collect standard data about school district spending and make that data accessible to the public. This led to the establishment of the Database Initiative.
School districts are now required to report a variety of data to the Department of Education. Data are collected at the district and individual school levels. The result is a database that allows users to examine student populations, spending on school administration, classroom and building support, staff counts and student performance.

An example of how the Database Initiative can be used for comparisons between school districts was Oregon Business Council’s analysis in 2000, which used this database to compare operational costs of Portland Public Schools and the David Douglas School District. Teacher salaries and building maintenance costs were analyzed to better understand the business practices of the districts. For example, the study found that David Douglas used instructional assistants, rather than teachers to meet short-term increases in classroom size at a lower cost. The study also documented higher costs for the Portland Public Schools to maintain older school buildings.

The non-profit Chalkboard Project has created the Open Books Project, which organizes and summarizes financial data compiled by the Database Initiative. The online resource summarizes school district spending in five broad categories for comparison among districts. Together, the Database Initiative and the Open Books Project provide tools to examine how school districts manage public funds.

Quality Education Model

The Legislature, in 1995, formed a committee chaired by then-Speaker of the House Lynn Lundquist to study the cost of providing high-quality K-12 education. This committee developed the Quality Education Model. Using information from the Database Initiative, the QEM estimates costs based on the standards set in the Educational Act for the 21st Century. The model is intended to represent typical costs for a hypothetical school district. It does not adequately account for all variations in individual schools or districts, such as the cost of serving special student populations and geographic variations in the cost of living.

In 2000, voters passed Measure 1, mandating that the QEM be used by the Legislature as the basis for funding education, and requiring the Legislature to fund K-12 schools at the basic QEM level or report to the Governor why it has not done so. In 2001, the Legislature established the Oregon Quality Education Commission to review the assumptions of the model and oversee revisions and updates. The com-
mission reported in December 2006 that the school funding shortfall was greater than $1.2 billion per biennium and continuing to fall further behind levels recommended by the QEM.17

Many legislators, according to witnesses interviewed by your committee, do not find the QEM, as it is currently structured, to be a credible tool for establishing the state education budget. As evidence of this, House Bill 2451 has been introduced in the House of Representatives in the 2007 legislative session. The bill, if passed, would abolish the Quality Education Commission. Ken Thrasher, former chair of the Quality Education Commission, characterized the 2005 Legislature as being divided among those who thoroughly understood QEM, those who merely were aware of it, and those who did not want to understand it for political reasons. Thrasher also acknowledged that among those with a functional understanding of the QEM, some remained opposed to it. Critics argue that the QEM inflates administrative costs, and some school funding advocates interviewed by your committee also cautioned against blindly embracing the current model.

In spite of these criticisms, the QEM is the legal basis by which Oregon is expected to measure the adequacy of the state’s K-12 budget. Your committee found the model to be an objective, data-driven basis for estimating the costs to meet the state’s education performance standards. Without the QEM or something similar, your committee finds it difficult to understand how the Legislature could effectively estimate the adequacy of the education budget. Indeed, the state budgeting process has suffered in recent years for not having adequately used the QEM.

Your committee believes that the QEM should be continued and refined to more accurately reflect the true costs of providing the education services that would allow all students the same chance to meet the state’s performance standards. The Database Initiative and other sources provide reliable information that should serve as the basis for enhancing the value of the QEM as a budgeting tool.
State Revenue Options

Measure 5 limited the types of funding mechanisms available for K-12 education, and this limitation has contributed to the funding instability and inadequacy experienced in Portland schools. Your committee analyzed several options for the state to stabilize school funding and increase the adequacy of resources available. This section focuses on four areas that have been prominently discussed as potential mechanisms to diversify the funding base and provide more revenue to fund schools.

Kicker Reform

Oregonians voted in 2000 to cement the nation’s only income tax kicker in the state constitution. The kicker law includes personal and corporate income tax collections. Under the law, when tax receipts exceed budget estimates (made two years in advance) by at least two percent, all of the unanticipated money is returned to individual and corporate income taxpayers. Corporations, whose profits are difficult to project with this degree of accuracy, are projected to receive a rebate of $275 million in 2007.

While changes to the kicker law have for years been deemed a political nonstart-
er, your committee believes political speculation is not reason enough to disregard this approach to stabilizing state revenue, and in fact, momentum is building for change. Governor Kulongoski has proposed diverting this year’s corporate kicker and future corporate kicker rebates into a state savings account. Republican legislators also have proposed reforms to the kicker law paired with other tax changes, and the state’s leading business groups are recommending a one-time diversion of kicker rebates to establish a reserve fund for the state.

Richard Sims and Phil Romero, prominent economists with experience in other states, said at a January 2007 joint appearance in Oregon that giving corporations a kicker rebate is a misuse of funds because most of the money is returned to corporations headquartered outside Oregon. Referring to the kicker, Sims said “You couldn’t waste money any better than that.”

Your committee believes that using kicker rebates to finance a rainy day fund would provide the same kind of common sense financial security that many other states, not to mention businesses and households, use to sustain operations when income declines.

Oregon Lottery Revenue

Voters approved the Oregon Lottery in 1984 as an economic-development and job-creation tool. In 1995 voters amended the law to specifically allow lottery dollars to be used for elementary and secondary schools. Lottery proceeds directed to schools initially were deposited in the State School Fund; however, since July 1997, at least 15 percent of the lottery’s net proceeds have been deposited in the Education Endowment Fund.

In a 2003 special election, voters approved Measure 19 which converted the Education Endowment Fund to the Education Stability Fund, transferred $150 million of the principal to the State School Fund for immediate use, and increased the portion of lottery proceeds dedicated to education from 15 percent to 18 percent. The significance of converting the fund is that now the fund’s principal can be spent. Under Measure 19, if the balance of the stability fund reaches 5 percent of state general fund revenue, the lottery dedication is reduced to 15 percent and deposited in a new school capital matching account. Total net proceeds from the lottery in the 2003-05 biennium was $830.5 million, of which $140.5 million was transferred to the Education Stability Fund and $330.1 million to the State School Fund.
Your committee and others have considered the merits of allocating a greater percentage of lottery revenue to schools. Business groups have argued that shoring up funding for Oregon’s education system should be at or near the top of the state’s economic development strategy, which raises the question: Why not spend more of the lottery’s economic development dollars on schools? Your committee’s response is that other vital economic development activities would suffer unless an alternative funding source is provided.

Fixed-percentage Funding Proposals

During the 2005 legislative session, various proposals for changing Oregon’s tax structure and establishing a rainy day fund were discussed. The Legislature also devoted considerable time to debating the amount of the general fund budget for K-12 education; figures ranged from Governor Kulongoski’s initial proposal of $5 billion to the Quality Education Commission’s recommendation of $7.2 billion.

Also in 2005, the Oregon House of Representatives adopted a bill that, had it passed in the Senate and been signed by the Governor, would have dedicated 51 percent of personal income taxes to the K-12 education budget. The bill also would have guaranteed at least 9 percent biennial growth in the State School Fund. Two-thirds of the excess personal income tax collections, beyond the amount necessary to fund 9 percent growth in the State School Fund, would have been deposited in the Education Stability Fund and the remaining one-third into a new fund intended to provide resources to schools to raise student achievement to state standards or to implement or replicate innovative programs. The Education Stability Fund would have been tapped to maintain 9 percent biennial growth in the State School Fund in times of declining income tax revenue.

Late in the 2005 legislative session, Governor Kulongoski proposed a similar plan that would have dedicated 61 percent of income tax revenue for education. A key difference between the two proposals was that Governor Kulongoski’s proposal included funding for post-secondary education.

At first glance, a fixed-percentage allocation method to fund schools seems to imply greater financial stability than the current highly political budgeting process. This turns out not be the case. Your committee acknowledges that, from a political perspective, balancing the state budget may be easier for lawmakers when the largest
Budget allocation is predetermined. However, increased efficiency at the Legislature does not, in this case, translate to increased financial stability for school districts. Allocating a fixed percentage of the general fund, which is highly volatile due to dependence on income tax revenue, would lock in budgetary peaks and valleys as state revenue fluctuates. Simply put, 50 percent of a general fund balance that is down 20 percent from the previous biennium is still a 20 percent decline in revenue for schools. In combination with a mandatory rainy day fund, this approach has more appeal to your committee, but it is still fundamentally flawed because it has no relationship to the state’s mandated student performance standards, the Quality Education Model’s recommended spending level or any other measure of adequacy.

Tax Reform

As discussed in this report and in City Club’s 2002 report titled “Tax Reform in Oregon,” income tax revenue is inherently unstable. Your committee believes that continuing to rely heavily on income tax revenue to fund schools is unwise, and state revenue streams should be diversified. Wholesale reform could include a new tax, such as a sales tax or gross receipts tax. Less sweeping changes could include adjustments to tax deductions and exemptions. Your committee also acknowledges arguments that the need for comprehensive tax reform could be diminished by a robust rainy day fund. Consistent with City Club’s adopted principals for an effective tax structure, tax proposals should be evaluated to determine their impact on the overall tax system using the following criteria: fairness, sufficiency, certainty, clarity, efficiency and neutrality.
Summary

Control of funding for education in Oregon rests largely with the state, and efforts to improve the stability and adequacy of that funding should begin with the state. An effective rainy day fund should be a high priority, and not just for education. The volatility of Oregon’s tax system is the principal problem for all general fund programs, and until that system is stabilized, a significant state “savings account” must be established for the years when income tax receipts are down. Amending the kicker law, beginning with diverting corporate kicker rebates is the most logical place to start building a reasonable rainy day fund.

Your committee believes a fixed-percentage approach to funding schools is not the solution. The education budget should be clearly tied to the performance goals of the education system. If additional resources are warranted, some form of tax change should be enacted to provide those resources. Ideally these changes should include comprehensive state tax reform, but until that is politically feasible, incremental tax changes may be necessary and appropriate.

Local Funding Options

In years past, when state government has failed to fund schools at a level determined to be adequate by school boards, Portland’s five school districts have supplemented to varying degrees state funding allocations with local resources. Your committee identified a number of potential supplemental funding options that could be — and in some cases, have been — used by various local taxing entities.

School Districts

The ability of school districts to generate property tax revenue is restricted by Measure 5 and Measure 50. School district levies also are subject to the state’s equalization formula, which means that funds raised locally (other than local option property taxes) are spread across school districts throughout the state. Some critics object to this system on the grounds that people outside the taxed area would benefit without making a contribution.

Local option property taxes avoid this requirement, but are also limited by Measures 5 and 50. School districts are allowed to ask voters to approve local option property tax revenue up to the lesser of (1) the district’s Measure 5 and 50 tax cap, (2) 15 percent of the equaliza-
tion formula revenue or (3) $750 per weighted student (ADMw). As mentioned previously in this report, Portland Public Schools had a local option operating tax and a capital improvements bond that expired in 2006. Voters approved a new operating levy that took effect in 2007 at the maximum allowed for this type of tax. No other school district in Portland currently has a local option property tax.

With local funding options tightly constrained by state law, your committee sees no feasible means for school districts to directly ensure long-term stable funding on their own.

City of Portland

Cities typically play a minor role in education, and this has been the case in Portland. Whereas most city charters grant city government general authority to act as long as the action does not impinge on powers reserved by other governments, Portland’s City Council has only the powers and authority specifically conferred upon the city by the charter or by general law. Providing K-12 education is not an explicit provision of the charter. City officials have interpreted this to mean that the city’s ability to provide support directly or participate meaningfully in K-12 education is limited to actions that mirror provisions allowed by the city charter. In spite of this legal limitation, the city of Portland has supplemented traditional means of school funding during times of apparent crisis.

In 1996, Mayor Vera Katz was instrumental in securing what was reported to be a $9 million “bailout” for schools. During Katz tenure as mayor, the city also implemented a variety of other mechanisms to help schools, including funding school police, athletic and after-school programs and purchasing surplus school property for parks. In 2003, Mayor Katz and Multnomah County Commission Chair Diane Linn helped broker a deal between Portland Public Schools and the teachers’ union. The deal, which narrowly averted a strike vote included an initial payment of $20 million from the city to restore 14 instruction days lost to declining state revenue, followed by payments up to a maximum of $38 million. A four-year surcharge on Portland’s business license

“With local funding options tightly constrained by state law, your committee sees no feasible means for school districts to directly ensure long-term stable funding on their own.”
fee, which is a tax on net receipts, provided about $22 million of the new revenue; the balance was drawn from the city’s general fund. Under the leadership of Mayor Tom Potter, the city provided an additional $10 million from the general fund in 2006, and the business license surcharge was renewed for the 2006 and 2007 tax years to provide up to $9 million in additional revenue.

Theoretically, the city could once again impose additional taxes or fees on businesses to help fund schools; however, the business license fee is already a source of considerable consternation for some in the business community. In fact, Portland’s City Council reformed the fee structure in January 2007, therein reapportioning the burden among businesses and reducing overall receipts for the city.

City officials have also discussed cell phone and utility taxes as ways to supplement state funding for schools. Your committee did not investigate the merits of these or other new taxes; however, consideration of long-term school funding provided by the city of Portland generated some apprehension among your committee and witnesses interviewed by your committee. Specifically, your committee has concerns about prompting people and businesses to move from Portland to escape additional taxes or fees.

### Multnomah County

In 1998, Multnomah County enacted a one-year, half-percent increase to its business income tax to support schools. Your committee believes that increasing the county’s business income tax is unlikely to happen in the near future. In fact, the county is reviewing its business tax structure in response to criticisms from the business community, just as the city of Portland did. Multnomah County Commission Chair Ted Wheeler has directed the county’s finance staff to evaluate ways the county’s business income tax could be reformed. Wheeler said the county is looking at the fiscal impact of alternatives, including adopting the city of Portland’s plan. Wheeler also said that the business income tax has fluctuated by as much as 40 percent per year, which, in the eyes of your committee, makes it an unattractive option when seeking long-term stability for school funding.

As mentioned earlier, Multnomah County enacted Oregon’s only county income tax for three years ending in December 2005. The tax generated about $90 million per year mostly for schools in Multnomah County. Theoretically, the county could enact a similar tax once again and make it permanent; however, this too is unlikely to happen. The tax was
ultimately unpopular with citizens and narrowly avoided repeal by voters in 2004.

**Metro Regional Government**

Metro has broad regional authority and its charter leaves open the possibility of funding any service the Metro Council decides has regional significance. Metro’s regional taxing authority would obviate commonly voiced concerns about disparities in tax burden based on geography since all Metro constituents would be subject to the tax. Your committee believes that in the absence of a statewide financing solution, a regional tax has appeal because it minimizes the economic disparities among neighboring jurisdictions.

In early 2006, Mayor Potter prompted a public discussion among metro area school districts and local governments about imposing a tax that would benefit school districts in Portland and throughout the region. This idea failed to gain consensus among the districts that would have been affected.

**Summary**

Recent history highlights difficulties with local funding alternatives to the property tax. While several temporary measures recently have been approved, each has been short-lived, and public sentiment for new taxes turned especially sour after passage of the Multnomah County income tax. State law limits local option property taxes, but some form of property tax still appears to have the most political acceptance as a means of supporting schools. Your committee found few reasonable options for local funding, none of which would provide long-term financial stability for schools.
Federal Funding Sources

According to the U.S. Department of Education, responsibility for K-12 education falls to the state “because the U.S. Constitution does not designate a public education role for the federal government.” However, due to “a compelling federal interest in the quality of the nation’s public schools, the federal government, through the legislative process, provides assistance to the states and schools in an effort to supplement, not supplant, state support.”

Federal education dollars are allocated to Oregon as categorical funds. They are designated for specific categories of students and are restricted in their use and cannot be used to replace local and state revenues. For fiscal year 2005, Oregon received $367 million from the federal government for elementary and secondary education. Included in that total is the Elementary and Secondary Education Act, the primary source of federal K-12 support. In fiscal year 2005 the act provided $38.7 billion for K-12 education nationwide, of which Oregon’s share was $223 million. Individual schools use these funds for the purposes defined in the programs, including aid for schools with disadvantaged children and a variety of special assistance grants.

Another category of federal money is the IDEA (Individuals with Disabilities Education Act), which assists states and local schools in educating children with disabilities. Part B of the act, the second largest federal K-12 program, provides over $11 billion to states and local schools to assist their special education efforts. Oregon received $127 million from IDEA in 2005.

As mentioned earlier, federal appropriations from these sources serve approximately 20 percent of the identified need for the students who qualify for these federally funded programs. The original intent of Congress was to provide funding for 40 percent. Your committee would support efforts to pressure Congress to meet its existing funding obligations to schools.

“Your committee would support efforts to pressure Congress to meet its existing funding obligations to schools.”
Though your committee’s charge focused on schools in Portland, this study’s findings, conclusions and recommendations have regional and statewide implications. Multiple sources of funding instability, including government mandates, fluctuating revenue and rapidly rising costs make a simple solution to unstable funding unlikely. A satisfactory response will require multiple actions to address multiple sources of instability.

Oregon’s constitution holds the Legislature and Governor primarily responsible for K-12 school funding, and the fundamental problems that school districts in Portland and throughout the state are experiencing can be effectively addressed only at the state level. Your committee’s examination reveals that Portland’s five school districts have precious few tools at their disposal to achieve a measure of improved financial stability. Your committee concludes that Portland’s school districts cannot stabilize funding without significant changes from the state. The federal government also must be held accountable for its obligations to fund programs for special needs students and provide flexible overall guidance for student performance.

While politicians wrestle with tax and spending issues, and funding levels fluctuate over the decades, children continue to enter the public school system. These students are captive to the funding realities of their time. They lose when school years are shortened and staff members are laid off. Students forego opportunities to learn when arts, outdoor education and other enrichment programs are eliminated. Some students do without sports and other activities as a result of fees now commonly imposed on those who participate. For your committee, these are the foremost consequences of Oregon’s unstable funding.

Your committee also cannot help but wonder if Oregon’s chronic school funding woes are not at least partly responsible for causing a growing number of Oregonians to lose faith in public K-12 education. According to the most recent data released by the Oregon Progress Board, the number of respondents who ranked K-12 education in Oregon as doing well or very well dropped from 64 percent in 2004 to 60 percent in 2006. All of this points to an urgent need to stabilize funding for K-12 before public discourse becomes so colored that reasoned thought and rational problem-solving no longer seem possible.

Your committee has not lost hope. We offer the following conclusions and recommendations as guideposts for voters, elected officials and other community leaders — all of whom have a hand in funding public education in Oregon.
CONCLUSIONS

Collection and Distribution of State Funds

1 Since the passage of Measure 5 in 1990, school funding in Oregon competes with other programs supported by the general fund. Oregon voters and political leaders have since mandated new additional programs and services without sufficient additional revenue to cover their costs. This has placed extreme pressure on the state’s primary source of revenue, personal income tax collections, to fund schools and other public services.

2 Measures 5 and 50 made school funding overly reliant on the state income tax and more vulnerable to economic declines. Until comprehensive tax reform improves this situation, Oregon’s schools will be subject to uncertain revenue.

3 With Measures 5, 50 and 86, voters embedded property tax limitations and the kicker in the Oregon Constitution, and in doing so, limited the ability of the Legislature to establish an adequate rainy day fund and stabilize funding for schools.

4 Measures 5 and 50, combined with the current school funding equalization formula, have created a ceiling on school funding that is difficult for local taxing districts to exceed. Consequently, the ability of school districts to address the basic educational needs of all students is severely limited.

5 Control of and responsibility for funding schools is consolidated mostly with the Legislature. As a result, school districts have few funding options within their control, and none of them can provide long-term financial stability.

6 A fixed percentage of an unstable revenue stream is by definition unstable. Therefore, a fixed-percentage funding method would not provide adequate financial stability for schools. Furthermore, fixed-percentage funding methods do not correspond with the needs of students and have no relationship to Oregon’s mandated student performance standards, the Quality Education Model’s recommended spending level or any other measure of adequacy.
Assessment of Needs and Distribution of Funds

7 Oregon’s Database Initiative and Quality Education Model are objective tools that form a powerful basis for evaluating the adequacy of funding for K-12 education. Both need to be revised and regularly updated to better document the cost of school programs needed to meet performance expectations for students, and to educate the general public and decision-makers about the critical linkage between the two.

8 The lack of an agreed-upon methodology for establishing Oregon’s K-12 budget contributes to instability in school funding.

9 The Quality Education Model does not adequately document or assess potentially significant local differences in education costs, such as those for students with special needs, transportation and employee cost-of-living differences across the state.

10 An equalization formula could be a fair and transparent means to allocate funds across Oregon’s school districts; however, the weightings used in the current formula are coarse estimates and do not adequately account for the differences in actual per-student costs.

Local Planning and Budgeting

11 Chalkboard Project’s Open Books Project demonstrates how school districts can use data collected by the state to monitor and analyze their costs and those of other districts, and make clear to the public the true costs and benefits of individual budget categories, particularly non-classroom costs.

12 In years when funding is relatively robust school districts are able to build financial reserves against future declines in state funding. Without reserves, school districts are vulnerable to reductions in program offerings, elimination of school days, and teacher and staff layoffs.
Federal Education Requirements

13 The federal Individuals with Disabilities Education Act destabilizes school funding because districts (1) are sometimes unable to anticipate and budget for the costs of special education student needs, (2) do not receive adequate resources from federal or state sources to pay for the full cost of educating these students and (3) face lawsuits from parents when districts allegedly fail to meet the individual education needs of all students.

14 The federal No Child Left Behind Act penalizes individual schools that fail to meet performance standards, regardless of clear and meaningful progress they otherwise may be making.

15 If the penalties included in the No Child Left Behind Act are not significantly revised and federal funding increased, Oregon (and other states) will be in a “no win” situation; unable to meet the federal government’s requirement of 99 percent compliance with NCLB benchmarks, and yet unwilling to forgo the critical federal financial contributions for special education students, students living in poverty and other programs.

16 Achieving No Child Left Behind’s requirement of 99 percent compliance by 2013-14 will require inordinate resources to be focused on a small percentage of students with the greatest educational challenges.
The Legislature and Governor should change Oregon’s guiding principle for distributing money to schools from equal funding to equal opportunity for every student to meet the state’s performance standards. Specifically, funding for K-12 education should be on a per student basis that more accurately reflects the true cost of providing a quality education to all students rather than methods, such as the current equalization formula, that do not correlate well with actual costs or education goals.

The Governor and both houses of the Legislature should agree to a common methodology and common data to use as the basis for establishing Oregon’s K-12 budget. Your committee recommends continuation and improvement of the Quality Education Model for this purpose.

The Legislature should authorize refinement of the Quality Education Model to establish a clear linkage between the general education services provided to meet the needs of all K-12 students and the money necessary to support those services. This refinement should include estimating the cost of serving students with special needs (e.g. special education students, English language learners and students living in poverty) and cost-of-living differences across the state.

The Legislature should revise the state’s education funding distribution formula to reflect costs from the Quality Education Model (refined as suggested in this report), and any offsetting federal funds, in order to distribute money to individual school districts based on the needs of their students. The formula should be reviewed periodically against actual costs and revised when warranted.

The Legislature should initiate the changes, including constitutional changes, necessary to allow school districts to provide additional local funding if the state budget allocation does not provide full funding as determined by the Quality Education Model. When state funding falls below that indicated by the Quality Education Model, school districts and their local government partners should be permitted to use any taxing method within their charter, including exceeding the Measure 5 property tax limit. These local option taxes should not be subject to the state’s school funding equalization formula.

The Legislature should establish a rainy day fund to ensure stable funding for programs supported by the general fund, including K-12 schools. The value of the rainy day fund, combined with the Education Stability Fund, should be sufficient to ensure stable operations for general fund programs during a significant economic downturn lasting at least one biennium.
The Legislature should redirect kicker payments into a non-restricted rainy day fund, beginning immediately with the corporate kicker, and as necessary with the personal kicker, to fully fund and then replenish a rainy day fund.

The Legislature should convene a citizen commission with representatives from business, labor and civic organizations to analyze Oregon’s tax system and recommend improvements for the Legislature to consider in its next regular session.

Each Portland school district should track and report their actual costs in a manner that makes clear to parents, taxpayers, local governments, civic organizations and the media the linkage between education funding and the true costs of achieving state and federal education standards.

Oregon’s congressional delegation should advocate for the following changes to federal education laws:

a. Fund federal education programs to historically promised levels (e.g., 40 percent of nationally identified need for Title 1);

b. Revise compliance requirements for No Child Left Behind to reflect more realistically attainable benchmarks for schools, such as Oregon’s goal of 90 percent compliance;

c. Eliminate the costly and destabilizing penalties for school districts’ non-compliance with No Child Left Behind and replace them with incentives that encourage communities to adopt and build upon proven programs that enhance the performance of all students.

Respectfully submitted,

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David Mandell, research adviser
Wade Fickler, policy director
Your committee acknowledges the many people who helped produce this report, beginning with the City Club members who began this study in 2003 but were unable to complete the project. We thank you for your contributions.

Your committee is particularly grateful for the assistance of its three research advisers who guided us during our research and the preparation of this report. Denise Bauman was generous with her time and enthusiasm and extended her term on the City Club Research Board to support this study until she moved from Portland. David Mandell stepped in following Denise’s departure and provided invaluable assistance and good humor as we labored to completion. Tom Deering challenged us to build a strong framework of analysis. From the beginning, he helped us look behind the many statistics we encountered and think about what they really meant. Tom’s assistance was only a very small part of his many contributions to our community, and we are grateful to have had his time and wisdom before his death in February 2005. With appreciation and humility, we dedicate this report to Tom.

Wade Fickler, City Club’s Policy Director, was our taskmaster and cheerleader. This volunteer effort is part of City Club’s unique tradition dating back 90 years. Volunteers need support, and Wade coached us, encouraged us and helped with so many of the details of this study.

Finally, we grew to admire the expertise of our witnesses and other information sources. Among them we especially acknowledge the time and assistance of the superintendents and financial staff of the school districts and the staff members of the Multnomah County auditor’s office and the city of Portland auditor’s office.
WITNESSES

(In most cases, titles are as of time of interview.)

Gary Blackmer, City Auditor, City of Portland
Julia Brim-Edwards, Board Co-chair, Portland Public Schools
Dave Fajer, Director of Business Services, Multnomah Education Service District
Suzanne Flynn, Multnomah County Auditor
Heidi Franklin, Interim CFO and Controller, Portland Public Schools
Cynthia Guyer, Executive Director, Portland Schools Foundation
John Kitzhaber, former Governor, State of Oregon
Terry Kneisler, Superintendent, Reynolds School District
Rick Larson, Finance Manager, Centennial School District
Clem Lausberg, Education Consultant
Lynn Lundquist, President, Oregon Business Association
Don McIntire, Citizen Activist; President, Taxpayer Association of Oregon
Bob McKean, Superintendent, Centennial School District
Karen Minnis, Speaker of the House, Oregon House of Representatives
Brian Newman, Metro Councilor
Steve Novick, Legislative Coordinator, Office of Susan Castillo, Superintendent of Public Instruction
Vicki Phillips, Superintendent, Portland Public Schools
Wendy Puriefoy, President, Public Education Network
Brian Reeder, Assistant Superintendent, Office of Analysis & Reporting, Oregon Department of Education
Jim Scherzinger, former Superintendent, Portland Public Schools
Edward Schmitt, Superintendent, Multnomah Education Service District
Ed Sheets, consultant, School Efficiency and Quality Advisory Council
John Tapogna, Senior Policy Analyst, ECONorthwest
Mike Taylor, Superintendent, Parkrose School District
Ken Thrasher, Chair, Quality Education Commission
Paul Warner, Director, Legislative Revenue Office, State of Oregon
Courtney Wilton, Business Manager, David Douglas School District
David Wynde, Board Co-chair, Portland Public Schools
Duncan Wyse, President, Oregon Business Council
BIBLIOGRAPHY


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Oregon Department of Education Database Initiative Web site found at www.ode.state.or.us/data/reports/toc.aspx.


CITATIONS


5 Oregon Department of Human Services budget development presentation, spring 2006.


10 All statistics in this paragraph were obtained from a joint report of the Multnomah County auditor and the city of Portland auditor: Students, Spending, Services, and Accomplishments, Multnomah County School Districts 2005.

11 ibid.


13 Chalkboard Project, “Condition of K-12 Education in Oregon, 2006 Update.”


16 National Conference of State Legislatures report; February 2005.


19 ORS 461.540.


22 www.ed.gov/about/overview/fed/role.html.


24 ibid.

**APPENDIX**

### Figure F: Major Revenue Sources for Portland’s Five School Districts

#### Centennial

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Local</td>
<td>$8,623,846</td>
<td>$8,827,491</td>
<td>$9,099,825</td>
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<tr>
<td>County/ESD</td>
<td>$226,875</td>
<td>$238,841</td>
<td>$219,549</td>
<td>$1,327,978</td>
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<td>State</td>
<td>$27,207,173</td>
<td>$28,986,873</td>
<td>$30,984,535</td>
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<td>$30,652,582</td>
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<tr>
<td>Federal</td>
<td>$1,807,625</td>
<td>$1,880,420</td>
<td>$2,315,394</td>
<td>$2,202,354</td>
<td>$4,288,382</td>
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<td>Total</td>
<td>$37,865,519</td>
<td>$39,933,624</td>
<td>$42,619,303</td>
<td>$40,430,941</td>
<td>$54,382,338</td>
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#### David Douglas

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<tr>
<td>Local</td>
<td>$11,655,544</td>
<td>$11,197,925</td>
<td>$12,483,552</td>
<td>$13,960,264</td>
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<td>County/ESD</td>
<td>$286,752</td>
<td>$429,950</td>
<td>$342,944</td>
<td>$2,937,503</td>
<td>$43,416,031</td>
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<tr>
<td>State</td>
<td>$38,483,780</td>
<td>$41,025,204</td>
<td>$45,540,775</td>
<td>$41,463,450</td>
<td>$43,416,031</td>
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<tr>
<td>Federal</td>
<td>$3,610,636</td>
<td>$4,430,780</td>
<td>$5,345,615</td>
<td>$6,127,197</td>
<td>$8,447,400</td>
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<td>Total</td>
<td>$54,036,712</td>
<td>$57,083,859</td>
<td>$63,712,887</td>
<td>$64,488,414</td>
<td>$74,857,584</td>
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#### Parkrose

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<tr>
<td>Local</td>
<td>$12,019,948</td>
<td>$12,782,208</td>
<td>$13,825,986</td>
<td>$14,981,545</td>
<td>$13,419,892</td>
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<tr>
<td>County/ESD</td>
<td>$211,081</td>
<td>$192,128</td>
<td>$215,273</td>
<td>$289,652</td>
<td>$4,400,986</td>
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<tr>
<td>State</td>
<td>$9,799,734</td>
<td>$10,257,398</td>
<td>$11,467,779</td>
<td>$8,767,160</td>
<td>$10,865,683</td>
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<tr>
<td>Federal</td>
<td>$1,189,800</td>
<td>$1,450,298</td>
<td>$1,879,535</td>
<td>$1,927,778</td>
<td>$2,432,938</td>
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<td>Total</td>
<td>$23,220,563</td>
<td>$24,682,032</td>
<td>$27,388,573</td>
<td>$25,966,135</td>
<td>$31,119,499</td>
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### Portland Public Schools

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<tbody>
<tr>
<td><strong>Local</strong></td>
<td>$147,099,569</td>
<td>$162,662,751</td>
<td>$173,564,408</td>
<td>$174,902,869</td>
<td>$189,908,545</td>
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<td><strong>County/ESD</strong></td>
<td>$23,610,611</td>
<td>$10,824,770</td>
<td>$10,395,465</td>
<td>$23,406,010</td>
<td>$63,746,510</td>
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<tr>
<td><strong>State</strong></td>
<td>$218,378,589</td>
<td>$213,602,539</td>
<td>$218,425,821</td>
<td>$187,553,789</td>
<td>$168,428,681</td>
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<tr>
<td><strong>Federal</strong></td>
<td>$32,601,955</td>
<td>$52,626,497</td>
<td>$49,073,114</td>
<td>$49,329,997</td>
<td>$52,827,919</td>
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<tr>
<td><strong>Total</strong></td>
<td>$421,690,724</td>
<td>$439,716,557</td>
<td>$451,458,808</td>
<td>$435,192,666</td>
<td>$474,911,655</td>
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### Reynolds

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</thead>
<tbody>
<tr>
<td><strong>Local</strong></td>
<td>$14,590,536</td>
<td>$16,565,148</td>
<td>$16,429,475</td>
<td>$17,611,696</td>
<td>$27,106,689</td>
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<tr>
<td><strong>County/ESD</strong></td>
<td>$734,783</td>
<td>$435,945</td>
<td>$327,171</td>
<td>$1,172,928</td>
<td>$520,342</td>
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<tr>
<td><strong>State</strong></td>
<td>$41,555,638</td>
<td>$43,488,657</td>
<td>$49,528,336</td>
<td>$43,404,716</td>
<td>$53,316,819</td>
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<tr>
<td><strong>Federal</strong></td>
<td>$3,219,053</td>
<td>$3,806,025</td>
<td>$4,496,963</td>
<td>$4,731,967</td>
<td>$8,336,200</td>
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<tr>
<td><strong>Total</strong></td>
<td>$60,100,010</td>
<td>$64,295,774</td>
<td>$70,781,945</td>
<td>$66,921,307</td>
<td>$89,280,050</td>
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</table>

Numbers reflect total actual revenue for operating funds (General, Special Revenue, Enterprise and Food Services Funds) by source (local, county/ESD, state and federal) for school districts. Reporting methods for the Multnomah County income tax varied among districts and changed during the years reported, which accounts for some of the year-to-year fluctuations in the Local and County/ESD subcategories.

Local — revenue from local property taxes, tuition, fees, investment earnings, etc.

County/ESD — revenue from Multnomah County and Multnomah Education Service District.

State — includes State School Fund payments, grants, reimbursements, etc.

Federal — includes federal grants, school lunch subsidies, federal forest fees, etc.
Profiles

Centennial School District No. 28J
Established: 1975
Number of schools: 9
Student population: 6,260 (growing)
Households with children in poverty: 4,023 (67.3%)
English language learners: 983 (15.7% of ADw)
Students receiving special education services: 801 (12.8%)
Operating expenditures per student: $8,137 (ADMr, FY 2004-05)
Median household income: $44,353 (2000)
Total assessed property value: $30.5 billion (FY 2005)

Centennial School District was created from two former K-8 elementary districts (Lynch and Pleasant Valley) and Centennial High School. Residents voted in 1976 to combine the two districts and the high school, which previously was part of the Gresham Union High School District.

Centennial has grown steadily and is expecting accelerated growth through the next decade. The district built a new elementary school and completed a major renovation of Centennial High School in 2003. The district's student population increased 11 percent from fiscal year 1998-99 to fiscal year 2004-05 and is becoming increasingly diverse, evidenced by the 46 languages spoken in the district's schools. The number of students who speak English as a second language increased 146 percent during this period.

Reynolds School District No. 7
Established: 1954
Number of schools: 15
Student population: 10,328
Households with children in poverty: 3,468
English language learners: 2,407 (26.2% of students receiving special education services: 1,111 (12%)
Operating expenditures per student: $7,370 (ADMr, FY 2004-05)
Total assessed property value: $3.9 billion (FY 2005)

Reynolds School District was formed in 1954 when the elementary schools districts of Fairview, Troutdale and Wilkes consolidated. In 1975, Rockwood School District merged with Reynolds. The district spans from 141st Avenue to the Sandy River and from the Columbia River to the Clackamas River, with an area of 9.5 square miles.

The student population has grown and become increasingly diverse, with a slight decline expected in 2006-07. Hispanic students now represent 25 percent of the student population. The number of students who speak English as a second language increased 146 percent during this period.

Sources: Joint reports of Multnomah County auditor and city of Portland auditor and districts' Web sites.
A look back underscores the significance of decisions made by elected leaders and voters since 1990.

**1990**
- Voters pass Measure 5, limiting property taxes for schools and local governments
- Oregon begins phasing in statewide equalization of K-12 funding
- Legislature adopts the Educational Act for the 21st Century, a bill that set in motion sweeping reforms for public schools, including student performance standards

**1991**
- Voters pass Measure 11, creating mandatory prison sentences and spurring extraordinary prison construction

**1992**
- Legislature enacts Oregon Health Plan, placing increased responsibility on the general fund for covering health costs for Oregonians without health care coverage
- Voters pass Measure 47, capping the growth of property taxes
- Portland City Council provides a $9 million “bailout” for schools
- District voters approve a five-year local option property tax

**1993**
- Oregon begins to use lottery revenue to finance education reserve fund
- Voters pass Measure 1, mandating that the Quality Education Model be used by the Legislature as the basis for funding K-12 schools
- Voters pass Measure 86, adding the personal and corporate income tax kicker to the Oregon Constitution
- District voters approve a five-year local option property tax for Portland Public Schools

**1994**
- Voters pass Measure 50, replacing and clarifying the intent of Measure 47
- Legislature passes House Bill 3636, creating the Database Initiative

**1995**
- Voters pass Measure 47, capping the growth of property taxes
- Portland City Council provides a $9 million “bailout” for schools
- District voters approve a five-year local option property tax

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- Voters pass Measure 86, adding the personal and corporate income tax kicker to the Oregon Constitution
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**2000**
- Oregon economy enters an economic recession
- Legislature approves conversion of Education Reserve Fund to Education Stability Fund
- Quality Education Commission establishes the Quality Education Commission to oversee the QEM
- Voters approve conversion of Education Reserve Fund to Education Stability Fund

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**2002**
- Voters approve conversion of Education Reserve Fund to Education Stability Fund
- City of Portland grants Portland Public Schools an initial payment of $20 million to restore 14 instruction days followed by payments up to a maximum of $38 million. A four-year surcharge on Portland’s business license fee provides about $22 million of the new revenue
- Multnomah County voters approve a three-year income tax to fund schools and social services
- At the end of the longest session in Oregon history, the Legislature passes House Bill 2152, a tax package designed to raise state revenues
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**2004**
- Voters reject Measure 30, causing the repeal of the tax package adopted by the Legislature in 2003
- Multnomah County voters reject Measure 26-64, narrowly defeating an attempt to repeal the county income tax
- The Quality Education Model estimates that state funding of $7.1 billion is required in the 2005-07 biennium for 90 percent of Oregon students to meet the state’s academic standards
- Voters reject Measure 30, causing the repeal of the tax package adopted by the Legislature in 2003
- Multnomah County voters reject Measure 26-64, narrowly defeating an attempt to repeal the county income tax
- The Quality Education Model estimates that state funding of $7.1 billion is required in the 2005-07 biennium for 90 percent of Oregon students to meet the state’s academic standards

**2005**
- Portland Public Schools’ infrastructure bond, local option, and desegregation funds expire
- Quality Education Commission reports that the Legislature has under-funded schools by $1.75 billion for the 2005-07 biennium, up from $1.64 billion the previous biennium
- Multnomah County income tax expires on December 31, 2005, reducing revenue for schools in the 2006-07 fiscal year
- City of Portland provides $10 million from the city’s general fund in 2006. A business license surcharge is renewed for the 2006 and 2007 tax years to provide up to $9 million in additional revenue
- Full compliance with No Child Left Behind required to avoid penalties

**2006**
- Quality Education Commission recommends state funding of $7.92 billion for the 2007-09 biennium
- Multnomah County income tax expires on December 31, 2005, reducing revenue for schools in the 2006-07 fiscal year
- Quality Education Commission reports that the Legislature has under-funded schools by $1.75 billion for the 2005-07 biennium, up from $1.64 billion the previous biennium
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**2013-14**
- Portland Public Schools’ infrastructure bond, local option, and desegregation funds expire
- Quality Education Commission reports that the Legislature has under-funded schools by $1.75 billion for the 2005-07 biennium, up from $1.64 billion the previous biennium
- Quality Education Commission recommends state funding of $7.92 billion for the 2007-09 biennium
- Full compliance with No Child Left Behind required to avoid penalties

**2019**
- Oregon economy enters an economic recession
- Legislature approves conversion of Education Reserve Fund to Education Stability Fund
- Voters approve conversion of Education Reserve Fund to Education Stability Fund
- City of Portland grants Portland Public Schools an initial payment of $20 million to restore 14 instruction days followed by payments up to a maximum of $38 million. A four-year surcharge on Portland’s business license fee provides about $22 million of the new revenue
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**2020**
- Voters approve conversion of Education Reserve Fund to Education Stability Fund
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