Fiscal Policy Work Group - Commission to Study School Funding

Notes 9/14/20 10AM

Attendees: Dave Luneau, Chris Dwyer, Mel Myler, John Beardmore, Bill Ardinger, Rick Ladd. Also in attendance: Jordan Hensley, Monica Mezzapelle, Rachel Miller, Becky Benvenuti, Bruce Mallory, Jenn Foor, Bruce Kneuer. 14 public attendees.

Just after 10am Dave Luneau called the meeting to order.

Dave introduced the work group's guests to fiscal policy's work around SWEPT and considerations related to statewide property taxation. Noted that the Commission is interested in learning more about how possible changes in a state property tax, whether in amount raised or rate, would impact both the state and municipalities in various ways. Discussion was then had recapping previous conversations of the FPWG around a statewide property tax, bringing the FPWG's guests up to speed on the current thinking.

Rick – are we talking about states remitting excess dollars or all SWEPT dollars? Some conversation was had about the fact that this is an open question, and that in fact being the reason for bringing the state treasurer and NH municipal association to the table. John – the question I would like to know the answer to, is, putting aside hypotheticals, what if the only change to policy that was made for the state property tax was instead of the municipal tax collection process holding on to all of the state property tax, what if all those dollars were remitted to the state as it comes in, and then the state sent dollars back in the four payments it already sends to districts? Then can add further what ifs in.

Dick – I think we need both features – what John spoke about re: all money sent to state and then out via formula, and also the "lesser" option where the excess goes to the state. Would like to hear about both.

State Treasurer Monica Mezzapelle began by talking about the state treasurer role – don't collect taxes (DRA), but ensure that there is sufficient cash in operating accounts to make payments. Currently the SWEPT of $363million is not collected by state, so does not impact cash flows. The adequate education payments are disbursed 20% Sept 1, 20% Nov 1, 30% April 1, 30%, June 1. Treasury monitors closely to ensure liquidity in accounts. If Treasury doesn't have sufficient liquidity, needs to consider alternatives like moving money from one account to another or short-term borrowing. Adequacy payments are large and consider those items when thinking about paying. This year has been particularly challenging, fortunately was able to make payments on Sept 1 of this year. The structure for making payments is based on calculations done and certified by DOE. If something were to change in the way that the state pays education grants, there are a few major considerations for review. The first is – if the state's obligations will increase, perhaps the timing of collections and disbursal should be more closely coordinated. Noted that 63% of unrestricted revenue comes in the second half of the year. Need to make sure there is sufficient liquidity. Second – need to think about frequency of payments – 4 times still or more evenly spread throughout the year? Second option might be easier for towns/help improve cash flows. From the state's perspective it doesn't matter as long as there is sufficient cash available. It could become a problem during times of economic distress or during revenue shortfalls, but have to meet obligations regardless from Treasury's perspective. Treasury doesn't take a position on policy, will do what legislature decides.

Rachel Miller – agreed with Monica. This year has been strange, but normally, with cash flow the more you can sync the in and out of dollars the better. Would prefer not to borrow. Have tools they can use to move things smoothly. As payments grow larger, it is optimal to have cash in hand before making payments – sync is the most important. Strongest most salient point.

Dave – what happened from your office on Sept 1? Monica – we were able to make payments. Our liquidity levels are lower than previous years due to COVID. Revenues currently coming in lower, have projections to work with but those are exactly that. Monitoring our cash position on a daily basis, and when Treasury knows they will have a big disbursement have to plan and figure out if they can make payments required by law. Were able to pay without having to borrow, but more difficult than usual. Watching cash position daily. If treasury needs to borrow, has to do ahead of time. At this moment concerned given the number of moving pieces. Rachel – one extra point is that we were very fortunate that we had historically high cash levels (liquidity and rainy day fund). Even though burning through cash now, were able to get through Sept 1 $130million payment without borrowing. As you can imagine we are rechecking and projecting 10x more than normal. Leading up to Sept 1 – you don't know with revenue uncertainty alone, but revenue typically comes in the middle of the month, so sometimes working somewhat out of sync. Dave asked about payments – answer: 90% ACH payments, directly to school districts (at least mostly). Some discussion of Manchester perhaps being somewhat different.

Dave – so a school district would get some funding directly from Treasury and some funding from town. Town also collects taxes for the county as well. Rick – towns and school districts sometimes make other working agreements.

John – hearing that to the extent state is paying more, would like to have money to do that. Sounds like there are three entities at table: state, town, and school district. Don't have school district rep here currently, could be worth it to bring to discussion. All will want cash up front and there is a shuffle – will be hard to devise something where all three entities are better off than status quo. The other change we could think about is when the state pays out. State probably has best tools to maintain liquidity. Question becomes best method even if liquidity is harmed for a brief period of time? Dave – agreed. Question about districts borrowing. Should model, if changes are being made, all three concerns and seeing what can be done re: timing of collections to have least impact on liquidity.

Rick – what is the rationale for the payment schedule to school districts? Monica – don't have it, but written into law that way. John – you'll notice it is back loaded, which tracks with state dollars come in. Dick – agree, need to be attentive to cash flow issues when thinking about funding adequacy. As I understand it, there was a period of time when SWEPT flowed to state and then out – if that is the case, some history the Commission should look at.

Next, the FPWG received comment from Becky Venvenuiti from the NH Municipal Association. Becky – of the municipalities, not all are on the fiscal year. Only 38 that run on a fiscal year. Remaining 196 are on calendar year. 6 collect once per year in Dec. 249 collect semi-annually – bills in July and December. 2 of those are actual semi annual but running 6 months behind the state, still in June and Dec. There are 4 municipalities that collect quarterly. They all have different agreements with their schools with the frequency that they send funding. Municipalities with least implications would be the quarterly ones (Concord a good example of that – cut a check every 2 weeks). Could consider that as monies are collected get remitted directly to the state. Important to realize that the tax collector for each municipality is collecting on these various schedules, with some delinquency (sometimes up to three years from bill). Municipality has the liability to school and county regardless, but can collect interest on delinquent amounts. All about timing – this would all depend on timing. A lot of municipalities where if they need to remit dollars they don't have yet, would put them in the position of doing a tax anticipation note (TAN).

Dave – is there a report available showing the different collections from various municipalities and lays that out? Becky – I don't think there is. I was a tax collector and active in the state, had reached out to Bruce at DRA.

Bruce Kneuer – the total number includes the unincorporated, FYI. DRA keeps track of the status of municipalities for their records, happy to send to Commission. Also would confirm that at the municipal level the flow of funds from taxpayer to collector to treasurer to district relies on agreements. RSA 198:5 that gives the authority to the school district. Cash flow to counties is by statute on or before Dec 17. At the municipal level, going to make payments and if not sufficient cash will borrow. School districts don't have tax anticipation notes (RSA 128:D), but do have some tax anticipation authority, has to do mostly with special education or adequacy aid itself. Those two amounts could be used as a reason why they would borrow short term, but would show up on school's revenue estimates, hasn't seen it. Might be something to keep in mind.

Dave – you can provide a list of municipalities with collection frequencies? Bruce K – yes. Dave – interested in outliers, for instance if Manchester is an outlier and the impact vs several unincorporated places.

Bill – Several times during deliberations people have focused on SWEPT and said it is not a state tax, but others have said it is in an accounting sense, treated as a state revenue. Monica – can't speak for comptroller's office but it is an amount that is budgeted and because it is used to balance budget it is accounted for in the education trust fund.

Rick – a municipality collects money and distributes to county. Is that all in one or over multiple payments? Becky – one payment in December, think that is statutorily required.

John – It seems to me that this is a solvable technical question, can be accommodated (on municipal side) increasing amount able to borrow. To me the biggest cash flow concern could be on the school district side. If we changed the currently formula only by requesting the local tax collector to remit to the state and having those dollars flow through the "quarterly" payments that action would adjust a district's cash flow potentially materially. Would go from getting their cut of SWEPT dollars biweekly and now it comes quarterly, even if all else is equal would be impacted. Impact could be positive or negative (probably negative), but districts don't have the same borrowing power. Until recently couldn't even maintain fund balance. Depends so much on what the proposed change is, but seems like school districts have the most to lose. This is highly dependent on policy changes so don't have to run it to ground, but should acknowledge it and make sure not to leave schools short.

Dave – interesting thing you're bringing up, there are these layers of cash flow impact.

Bill – at each level there is a different capacity to solve short term finance issues. A centralized state-level flow may be cheaper than having each district doing it.

Dave – how do we go about modeling cash flows? What's the group of people that can best help us put something like that together? Becky – NH government finance association would be an excellent source; NH municipal assoc. can help facilitate that. Ability of TANs not consistent throughout state. Dave – what I'm hearing is while we recognize and appreciate the importance of cash flow at the state level, the state has the greatest ability to maintain liquidity, so maintaining cash flow at district and municipal level most important. Monica – regardless of how changes are decided, state will do what needs to be done to make payments. Collections and frequency will be key.

Dave – are cash flow challenges different based on different rates? Monica – not a lot of impact, if in flows greater out flows would be similar. That is something the state can handle. State just received $1.2 billion from federal government and could handle that. Can't think of any downside – volume not a factor the same way frequency is. Rachel – depending on the gap between in flows and out flows, currently treasury can only borrow up to $200mil in short terms funds. So if increase in magnitude may want to consider that there is statutory capacity to ensure obligations can be met. Dave – how long does it take to borrow? Rachel – runs the gamut from interfund borrowing being very quick to private placement/banks fairly quick to other kinds of borrowing that might take a couple months.

John – Do you know how common cash flow borrowing is for municipalities? Don't see a lot of local government cash flow debt in NH. Becky – anecdotally, it is something that happens. Some on a regular basis, some never. Bruce K – a regular feature for counties, but on town/city side it's not something DRA tracks so can't say how extensive it is. Agree with Becky. Becky – did a recent survey because very concerned about cash flow during COVID. Fortunately property taxes not one so far, but worried that for future bills will be a greater cash flow issue. Some communities said they would not be able to do a TAN.

Rick – Grafton County does a TAN annually, and Haverhill does an annual TAN. Local relationship is very good.

Mary – The Concord school district is its own fiscal agent. Does that change anything about how that would work? Bruce K – might be part of the district charter, don't know in detail if they could do something another district could not. Bill – the concord school district is fiscally autonomous, but in terms of billing and collecting that is done through the city. Don’t have their own collection structure.

Bruce K – another group with good information could be the NH school administrators, could be sitting on top of the cash flows. Bill – in the original structure of the payment schedule the administrators were involved. Might also be helpful to hear from bond bank.

Rick – with COVID, are we hearing more about delinquent payments? Bruce – don’t have real time monitoring capabilities, but did some informal surveying to get a sense of delinquency rates. Don’t measure or have a historical baseline, but first half of the year went reasonably well. Everyone waiting to see how second half of year revenues come in. John – evidence I have is mostly from Connecticut, follow local governments there. The highly rated towns I see are reporting no material impact to property tax collections for summer. Connecticut mandated extensions or interest relief on delinquency. Fall/winter payment more at risk, especially with extended unemployment ending.

The FPWG then moved on to some discussion of AIR’s presentation last week to the Commission and more specifically an item Bill raised, which is a key assumption in the cost model that the state needs to pay for the first and last dollar.

Bill – we now have the AIR report in front of us, and it talks about targeted total resources/total spending approach that combines state and local funding. If their targeted state spending number per pupil is $20,000, that number is paid for by a combination of state and local revenues. If the ultimate result here were to define adequacy as $20k, the question arises whether there is a constitutional rule that says all dollars must be paid by the state, because the model provided by AIR has local dollars contributing to adequacy. In my view, requiring full state financing is bad policy. Different than whether that is a matter of law. The legislature is said by the court to have primacy in policy issues, and if this Commission and legislature goes down this path, will run into that wall. Have to face this issue head on and whether we believe this is a good policy or not. Next step of the Commission is to go from the AIR report to tangible recommendations.

Dick – a very important line of conversation. Two fundamental questions not yet fully addressed. One is – what is the adequacy number/formula? AIR has done a fantastic job in presenting us with a formula that is at the high end of where we thought we would be with adequacy. That number will drive educational outcomes to the state average – is that where constitutional adequacy should reside or should it be at some other level? Simulator tool allows us to go above or below that level. Need to decide what Commission thinks adequacy is. At the same time need to address the first/last dollar discussion. Simulator formula uses potentially a minimum local contribution, which is not really state money. Question of whether a local contribution is consistent with state’s obligation is a big question. Need to have more conversation about the mandatory local contribution and talk that through and get a handle on the legal argument as well as how that might work. Grows out of MA policy, which includes other measures of ability to pay.

Mary – love the idea of a minimum local contribution. Manchester uses money from the state but puts less local money in, for instance. Combination of money from state and local results in an amount that should fund cost for students.

Dave – have heard things from constituents and more about fairness and property taxes than first/last dollar. Not doing right by many students and their families, so fairness becomes really important for everyone here. To get there, are we willing to model things that aren't first and last dollar to see how it looks and works? Judiciary may not have looked at this as closely as Commission has.

John – AIR report tells us that current system is grossly unfair to students and taxpayers. As a Commission, we are trying to solve a judicial directive that is completely squishy and may even evolve under our feet with a new decision. And we are trying to make the system more fair. If we take AIR's proposal, is it more fair than the current system? I think it is. Is it perfect? Probably not. But moves fairness question down the field. Could shave on edges and go in different direction, but big picture it seems like a fairer way to do business. Bill is raising the question about the minimum local contribution's constitutionality.

Bill – agree, because it targets dollars to those places with the most need. Impacts both students and property taxpayers. But does state prohibit targeting? Have to face that head on, because only way to achieve equity is focusing on inequity.

John – this is a different spin on targeting. Concept of having a local contribution hasn't been done before. Bill – agree, but don't think this Commission with roots in legislative branch should try to predict judicial decisions. Should get into policy.

Rick – 193:1 annotation: whatever state defines as adequacy, has to pay for. Londonderry case.

Dave asked the Carsey team to brief this for the Commission to give time to read and discuss.

Bill posted in chat:

198:42 Distribution Schedule of Adequate Education Grants; Appropriation. – I. The adequate education grant determined in RSA 198:41 shall be distributed to each municipality's school district or districts from the education trust fund in 4 payments of 20 percent on September 1, 20 percent on November 1, 30 percent on January 1, and 30 percent on April 1 of each school year; provided that for a dependent school district, the grant determined in RSA 198:41 shall be distributed to the municipality, which shall appropriate and transfer the grant funds to its dependent school department.

33:7 Tax Anticipation Notes. –
I. Cities and Towns. Cities and towns may incur debt in anticipation of the taxes of the financial year in which the debt is incurred, in order to pay current maintenance and operation expenses, and may issue notes therefor to an aggregate principal amount not exceeding the total tax levy during the preceding financial year, provided that after the tax levy of the current year has been

determined any city or town may borrow an amount not exceeding in the aggregate the total tax levy of the city or town for the current financial year. In order to meet necessary expenses which may arise during the period from the beginning of the financial year to the date of the annual town meeting, the treasurer of any town, with the approval of the selectmen, may issue notes, without a vote of the town therefor, to an aggregate principal amount not exceeding 30 percent of the total receipts from taxes during the preceding financial year.

II. Village Districts. Village districts may incur deb