Annual Report on Fiscal Capacity

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Four Steps in Determining BEP Funding

1. **Basic Education Program Funding Formula**: It determines the amount required to fully fund the BEP based on the cost of providing more than forty components necessary to operate schools

2. **Local Share, State Share**: Set by law to divide responsibility between the state and local governments
   - **Instructional salary and wages costs**: 30% local, 70% state
   - **Instructional benefit costs**: 30% local, 70% state
   - **Other classroom costs**: 25% local, 75% state
   - **Non-classroom costs**: 50% local, 50% state
     - School system will receive no less than a 25% state share in non-classroom components (Davidson and Sevier receive a 25% state share in non-classroom because of this provision)

3. **Fiscal Capacity:** Used to allocate local share among counties   **50-50 TACIR-CBER**

4. **State makes up the difference:** Total cost of the BEP minus the local share for each school system

Fiscal Capacity

Answers the question	Measures	County-level model
How much must each local government contribute to the BEP?	The potential ability of local governments to fund education from their own taxable sources, relative to their cost of providing services.	All systems within each county pay the same percentage of their BEP allocation.

TACIR

Method

- A set of averages drawn from actual tax bases, income, etc. is compared with actual revenue.

- The amount of weight to give each factor is determined by estimating the statistical relationship between them.

- Multiple regression analysis
  - a common statistical method used to understand relationships among factors for a wide range of issues
  - simultaneously compares all variables for all counties to determine how much weight to give each factor

- Weights are multiplied by the factors for each county to estimate potential local revenue for each of the 95 counties.

- Actual revenue is used as a control.

Factors Used in TACIR's Fiscal Capacity Regression

- **Own-Source Revenue Per Student:** The actual amount of money local governments raise to fund their schools divided by enrollment (average daily membership (ADM)), the control factor that keeps the estimates within the bounds of what local governments actually do.

- **Sales Tax Base Per Student:** The locally taxable sales for the county-area divided by ADM. This is a measure of the local ability to raise revenue.

- **Equalized Property Assessment Per Student:** The total assessed property value for the county-area, equalized across counties using appraisal-to-sales ratios, and then divided by ADM. This is also a measure of the local ability to raise revenue.

Factors Used in TACIR's Fiscal Capacity Regression (cont.)

- **Equalized Residential and Farm Assessment Divided by Total Equalized Assessment (Tax Burden):** A proxy for a county's potential ability to export taxes through business activity—the higher this number, the lower the level of business activity and the higher the risk of heavy tax burdens on county residents.

- **Per Capita Income:** A proxy for county residents' ability to pay for education and for all other local revenue not accounted for by property or sales taxes.

- **ADM Divided by Population (Service Burden):** A reflection of spending needs. The larger the number of public school students per 100 residents, the greater the fiscal burden for each taxpayer.

Effect of Changes in Fiscal Capacity Factors

The relationship between fiscal capacity and specific variables (other things being equal)		
Factor Increases	**Effect on Fiscal Capacity**	
Property Tax Base Increases	Fiscal Capacity Increases	↑
Sales Tax Base Increases	Fiscal Capacity Increases	↑
Per Capita Income Increases	Fiscal Capacity Increases	↑
Residential/Farm Share of Property Increases	Fiscal Capacity Decreases	↓
Service Burden Increases	Fiscal Capacity Decreases	↓

# County Trends in Share of Statewide Fiscal Capacity

- The change in a county's share of statewide fiscal capacity depends on its growth in fiscal capacity relative to the 95-county average growth in fiscal capacity.

- A county whose fiscal capacity grows faster than the 95-county average will increase its share and vice versa.
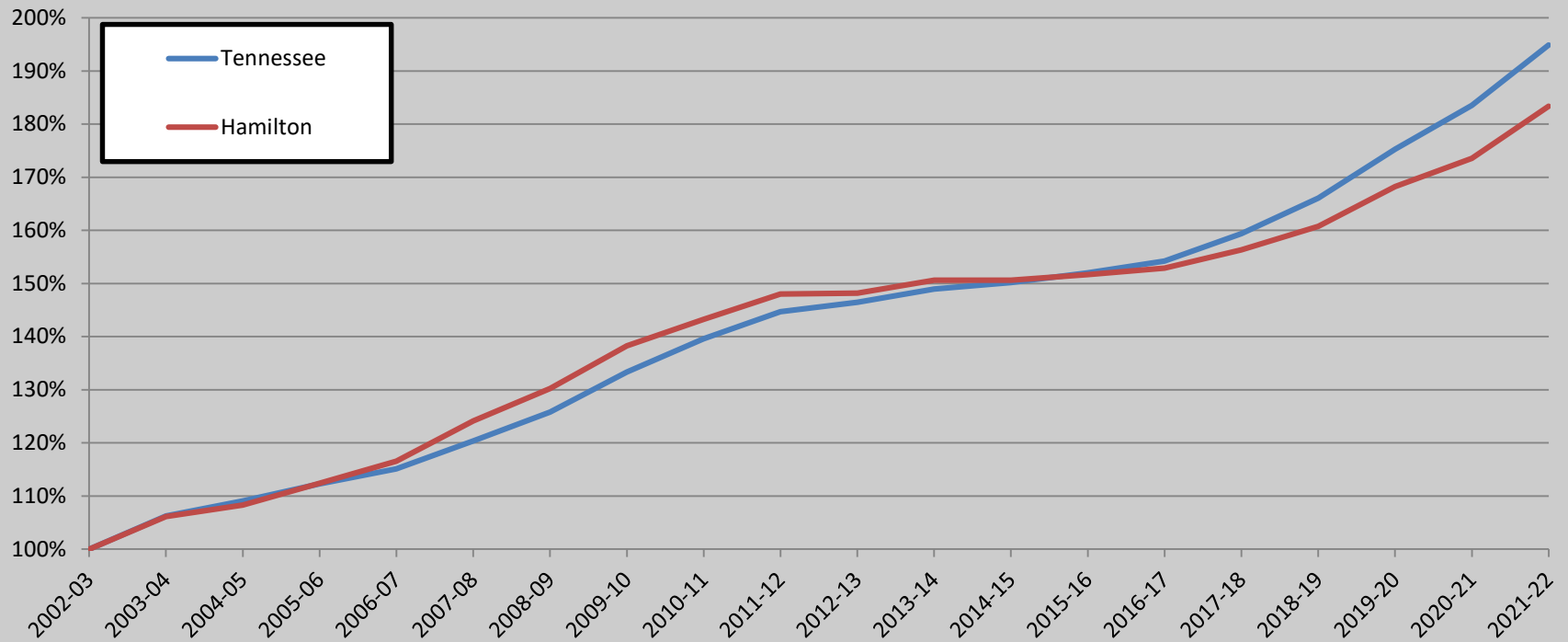
Long Term Fiscal Capacity Trends by County

*5-year average compared with 15-year average*

County Fiscal Capacity Index Trend

- Trending Up (37)
- Holding Steady (8)
- Trending Down (50)
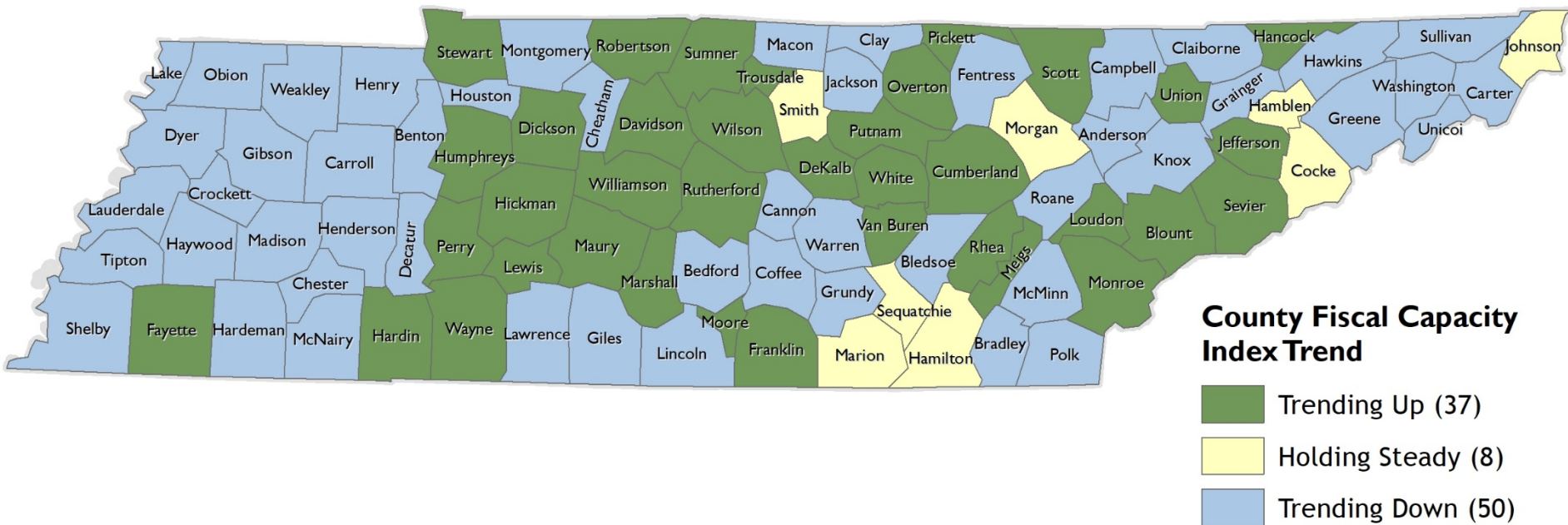
Combined Tax Base per Student (Sales and Property) as a Percentage of 2002-03 Combined Tax Base per Student
Fiscal Years 2002-03 to 2021-22

As fiscal capacity for a county decreases, the other 94 counties are responsible for a greater share of the BEP local match.
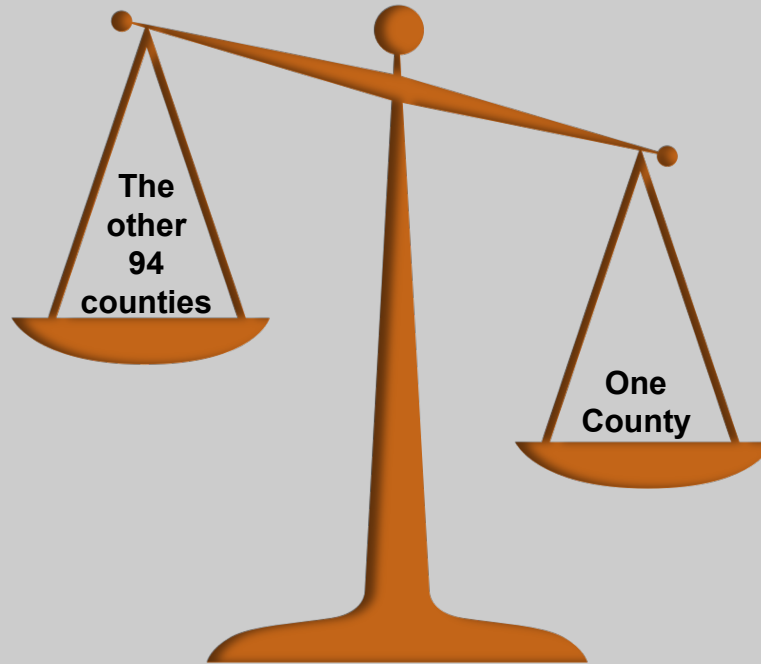
Effects of Pandemic (COVID-19)

- Cannot confidently predict effect on fiscal capacity
  - Fiscal capacity is relative to the other 94 counties
  - TACIR Model uses three year averages
- Fiscal capacity factors
  - Overall statewide local sales tax base increased 1% from FY 2019 to FY 2020
  - The latest property tax base and PCI data used in the model pre-date the pandemic