Exhibit 4

MEMORANDUM

TO: Representative Joyce Elliott, Chair
House Interim Committee on Education

Senator Jim Argue, Chair
Senate Interim Committee on Education

FROM: Tristan D. Greene, Special Assistant to the Commissioner
Arkansas Department of Education

CC: Mark Hudson, Legislative Analyst

DATE: February 14, 2006

RE: Anticipated testimony for the February 22, 2006, meeting of the House and Senate Interim Committees on Education.

This memorandum was prepared in response to Mr. Mark Hudson's letter to Dr. Don Stewart, Deputy Commissioner of Education, dated January 25, 2006, requesting a presentation on the ~~above~~ below-referenced subjects at the February 22, 2006 meeting of the House and Senate Interim Committees on Education. This memo outlines my anticipated testimony.

I. Introduction

The Foundation Formula is both complex and simple. It is an attempt to convert the Odden and Picus matrix of per-school funding to a per-student funding formula. Both the matrix and the Broadway / Bisbee spreadsheets are approximations of what is necessary to provide an equal opportunity to an adequate education for all students in Arkansas. The problem with any evidence-based attempt to create a funding formula is that it is an imprecise attempt. But it is one of the best methods of attempting to determine what the necessary basket of goods is to provide an equal opportunity to an adequate education that we have. To quote Dr. James Guthrie of Vanderbilt University: "Determining adequacy is more of an *art* than a *science*."

The biggest problems with the current system are three-fold. First, we as a State do not know what is – or should be – included in the "Carry-Forward" of $1,152. Secondly, the assumptions leading to the $5,400 foundation level is no more than the best educated "guess" of what is the cost of the correct basket of goods. Thirdly, the Broadway / Bisbee spreadsheet is similar to the Odden and Picus matrix in that it is a revenue stream – not an expenditure requirement.

Most of these problems will be addressed by the General Assembly through its current contract with Lawrence O. Picus and Associates. Hopefully, this new study will give the State the answers to the first two questions. The third question is one of public policy that only the General Assembly itself can answer – or determine.

These are not questions to be answered in the short term. The State needs to take its time based on the results of the current Lawrence O. Picus and Associates study, and any future studies before the General Assembly makes major changes to the school funding system.

II. Specific Questions Posed

A. What amount of funding is needed for foundation level and should the General Assembly apply an inflation adjustment to the foundation funding system?

The first part of this compound question is unanswerable at this time. As I stated above, the foundation system has not been in place long enough for there to be sufficient data to analyze its effectiveness.

As to the second part of the question, that is a matter of public policy for the General Assembly to determine. If the General Assembly does determine to apply an inflation adjustment to the foundation system, I am in agreement with the methodology developed by Richard Wilson.

B. What changes need to be done to the benefits packages to make it correlate with current laws and rules?

In 2003, Dr.'s Odden and Picus set forth a very simple benefits package that equated to approximately twenty-five percent of average salary. Their benefit package was set forth as follows:

> The fringe benefit percentage was determined by the average salary and the following: 13 percent for state retirement, 6.2 percent for social security, 1.45 percent for Medicare, and $131 per month for a minimum health insurance benefit.

(Odden, Picus, and Fermanich, 2003, at 63).

In the Broadway / Bisbee matrix, an average teacher salary of $39,000 was used. (When benefits were added, a total compensation package of $48,750 was achieved.) If one adds the percentages together, one gets 20.65% for retirement, social security and Medicare. Add to that health insurance[1] at 4.0% at 100% participation, the result is actually a 24.65% benefit package rounded up to 25%.

[1] Take $131 times 12 months and divide the result by $39,000.

If the testimony received by the Committees on February 7, 2006, is correct, then we know that the actual participation rate is approximately 63%. This would lead to the conclusion that only 2.52% of the current benefits package is being used currently for health insurance premiums of certified employees.

Obviously, the assumption of a teacher retirement rate of 13% is now out of date. The teacher retirement rate for FY 2006 is 14%, and the Arkansas Teacher Retirement Board of Trustees has recently voted to increase the rate to 15% for FY 2007. There are a variety of policy choices that the General Assembly has to address this issue. One would be to increase the benefits package by one percent for FY 2006 and two percent for FY 2007. Another would be to allow a COLA (as discussed above) to capture this increase in teacher retirement. A third would be to not increase the benefits package for FY 2006 because of ~~law~~ low health insurance participation, but to increase the benefits package for FY 2007 by one percent.

C. Does the method of funding the categorical programs account for increases or decreases in students eligible for the categorical program?

Foundation funding is based upon the previous three quarter average average daily membership (ADM). Foundation funding does take into account new students in the current year. The State compares the two quarter average ADM's from the previous and current year. If there is an increase in students, the district receives ~~$5,400~~ $5,528 for each ADM that is increased. But the State *does not* reduce (or take away) foundation funding from school districts that have less students in the current year than in the previous year. This one year "cushion" has been part of the Arkansas funding system for years. The cushion allows school districts to have one year to figure out how to cut expenses in the succeeding school year.

Take the following example: Look at the DeWitt School District on Exhibit F submitted as part of my testimony on February 15, 2006. In FY 2005, the school district was funded as though it had 1,681 ADM's instead of the 1,639 ADM's that it actually educated in FY 2005. This gave the Dewitt School District one-year to figure out how to trim expenses by approximately $200,000 for the FY 2006 school year.