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DR. GERALD FAVERMAN, Chairman GERRIT VAN COEVERING, Senior Consultant ROBERT J. KLEINE, Editor

The Lottery and School Aid

The conversation often goes like this . . .

Harry: I see the school district is asking for another millage increase.

Joe: I don't understand it, I thought the lottery money was supposed to take care of education.

Harry: That's right. I heard the State is taking in nearly one billion dollars with this new Lotto game.

Joe: A billion dollars should buy a lot of education. What do you think they're doing with all that money?

Harry: I don't know. They must be wasting a lot of it.

Joe: Somebody ought to find out what the State is doing with that money.

Harry: That's right. I'm not voting for more taxes until I find out.

The relationship of the lottery to school financing is one of the most misunderstood aspects of the state budget. When the lottery was approved by the electorate in 1972, many voters believed the money was to be earmarked for education. Although doing so was widely discussed, the implementing law did not earmark the lottery money for education. Finally, in 1981 legislation was approved that restricted the lottery money to the state school aid fund (SAF). This, however, does not necessarily mean more money for education, as will be explained below.

THE STATE LOTTERY

The distribution of revenue from the sale of lottery tickets is shown in Figure 1. In fiscal year (FY) 1984-85, total ticket sales were $887 million and the profit was $359.6 million. The percentage of ticket sales for each of the various games is shown in Figure 2. The Lotto game has been a major success story, with sales that reached as much as $24 million a month in its first year of operation. Due to the Lotto game, the state profit from the lottery increased almost 50% in FY 1984-85. **Despite its rapid growth, the lottery still provides only 6% of the $5.5 billion spent on K-12 education.**

SOURCES OF SCHOOL FINANCING

School operating revenues come from three main sources: local property taxes, state aid, and federal aid. Table 1 compares the percentages of revenues from each of these sources for selected fiscal years. Of particular interest is the decline in state aid as a share of total support from 45% in FY 1976-77 to 37.4% in FY 1984-85. This decline was due to the State's poor fiscal condition in the early 1980s, the rapid increase in property taxes during the same period, and declining enrollments. From 1977 to 1981, the assessed value of Michigan property increased 54.3%, as

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FIGURE 1

Distribution of Lottery Revenue, FY 1984-85

$887 Million

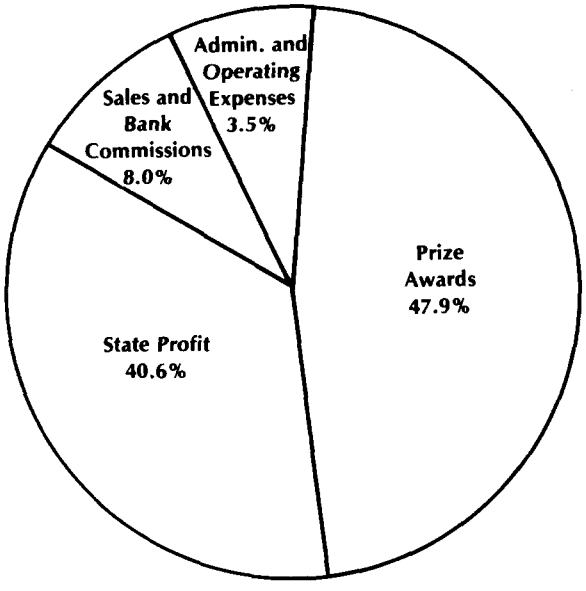
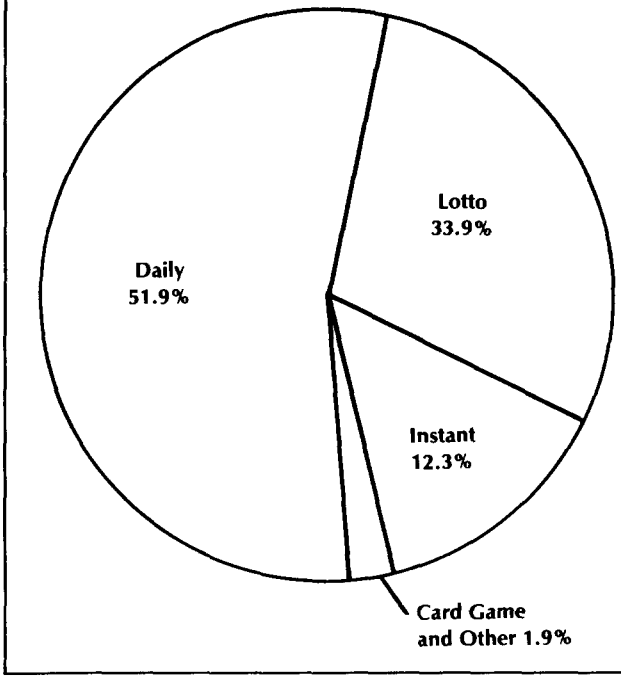


FIGURE 2

Lottery Ticket Sales by Game, FY 1984-85



raging inflation caused property values to skyrocket. During those years, the average millage rate for all jurisdictions declined about one-half mill, while the average millage rate for schools increased by about the same amount. Because a large share of state aid is tied to the value of property per pupil, the increase in property values caused a decrease in the amount of aid from the State (see explanation of school aid formula below). On a per pupil basis, total school operating revenues increased 116.6% from FY 1976-77 to FY 1984-85, with state aid increasing only 89.4% and local property tax revenue increasing 162%.

STATE SCHOOL AID FUND

The school aid fund receives revenue from five restricted sources: the sales tax (60% of all collections), the cigarette tax (2 cents per pack), the liquor tax (4% on each bottle), commercial and industrial facilities taxes (100% of all collections), and the lottery (100% of the state profit). In addition, the SAF receives an appropriation from the general fund (GF). The amount of the GF appropriation is determined by the Governor and the Legislature based on their assessment of the needs of elementary and secondary education, the estimated tax revenue and lottery profit available to

TABLE 1

Percentage of School Operating Revenues by Source

Year	Local Property Taxes	State Aid	Federal and Other
FY 1969-70	50.9%	45.4%	3.7%
FY 1976-77	50.2	45.0	4.8
FY 1981-82	62.9	32.6	4.5
FY 1984-85	58.6	37.4	4.0

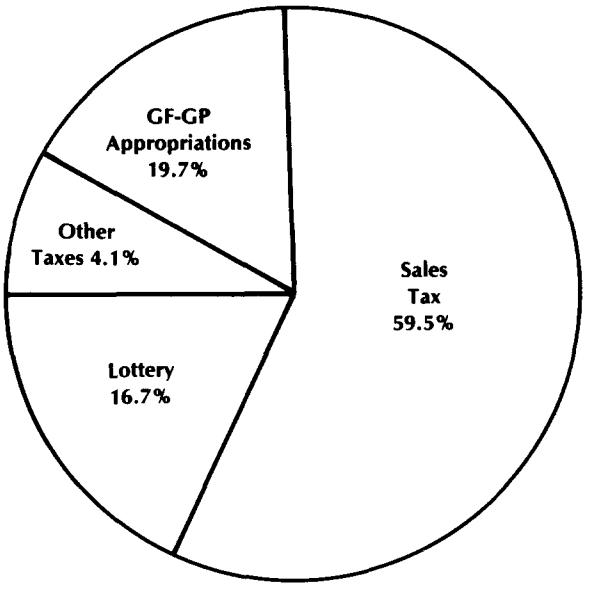
SOURCE: Senate Fiscal Agency, *1985 Statistical Report and Executive Budget*, FY 1986-87.

the SAF, and the revenue per pupil at the local level from the property tax. Figure 3 shows percentages of the total SAF contributed by its several sources in FY 1984-85. Table 2 shows the various sources of SAF revenue for selected years since FY 1971-72. The GF appropriation to the SAF has declined 52.4% from its 1980 peak, while revenue from restricted sources has increased 78.3% since 1980 (see Figure 4). **As a share of total GF spending, the GF appropriation to the SAF declined from 27.2% in FY 1971-72 to 7.7% in FY 1984-85.**

Since FY 1980-81, when revenue from the lottery was first restricted to the SAF, the GF appropriation to the SAF has dropped $223 million because other sources — mainly the lottery — have filled the gap.

FIGURE 3

Sources of School Aid Fund Revenue, FY 1984-85



STATE SCHOOL AID FORMULA

The state school aid formula is one of the mechanisms used to distribute monies from the school aid fund to school districts. The formula is based on the power equalizing concept; that is, the State attempts to equalize the resources of the various school districts, because the property tax base [state equalized valuation (SEV)] per pupil varies widely among districts. For example, the property tax base in Detroit is $25,222 per pupil compared with $175,833 per pupil in Birmingham. This means that in Detroit 1 mill raises only $25.22 per pupil while in Birmingham 1 mill raises $175.88 per pupil.

The 1985-86 school aid formula adopted by the Legislature guarantees $339.35 plus $68.50 per mill for each pupil. (School districts must meet certain requirements to receive the full amount, but most in-formula districts are expected to receive the full guarantee.) The grant from the State is equal to the guarantee less the amount of revenue raised locally. For example, a school district levying 30 mills would be guaranteed $2,394 per pupil. If that school district raised $1,500 per pupil locally, it would receive a state payment of $894 per pupil. There are about 179 out-of-formula school districts, or 31% of all districts, that raise more locally than the guarantee and therefore receive no state aid from the formula.

TABLE 2

State School Aid Fund Revenue from Various Sources, Selected Years[a]
(in millions of dollars)

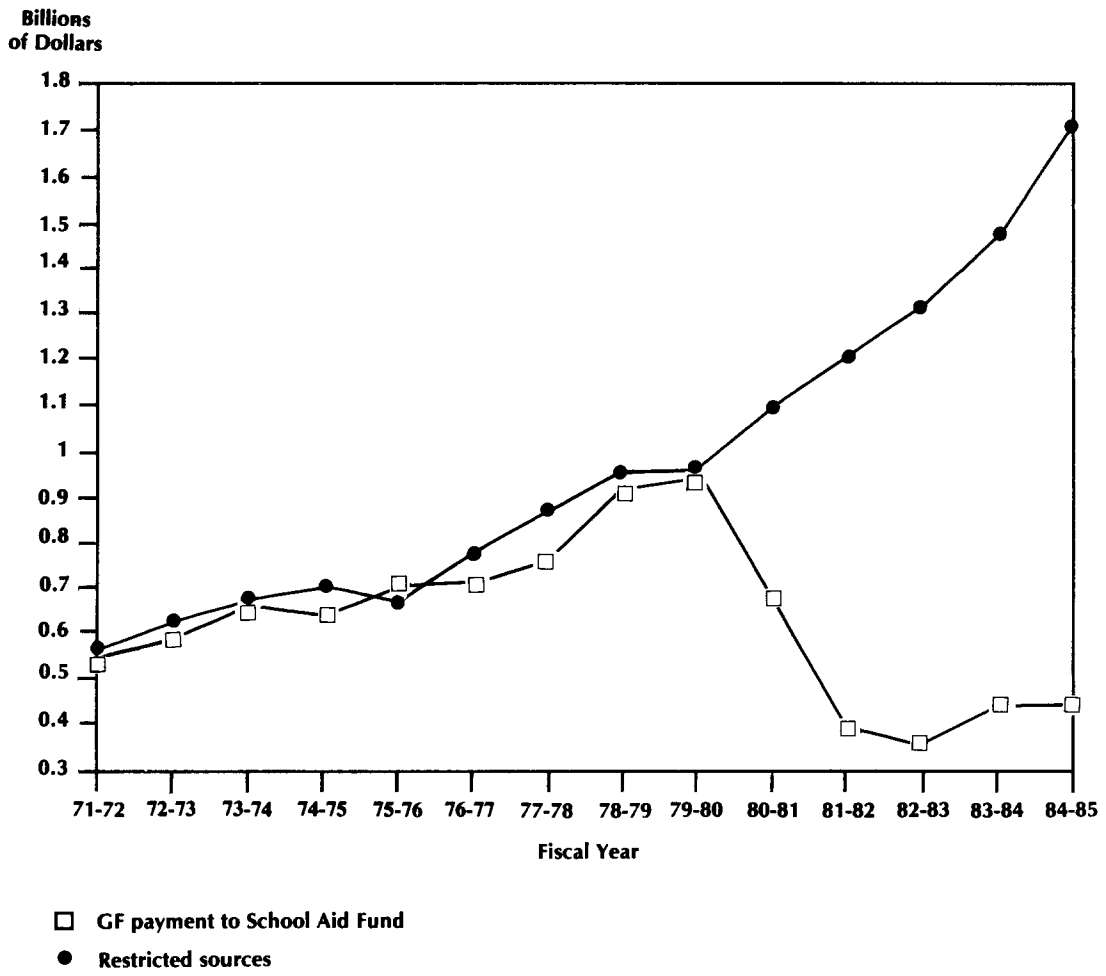
	Sales Tax	Lottery	Other Taxes	GF-GP Appropriation	Total	Total SAF Revenue per Pupil	GF-GP Appropriation as/of Total GF-GP Budget
FY 1971-72	$ 528.2	—	$36.9	$542.3	$1,107.4	$ 501	27.1%
FY 1976-77	734.2	—	43.4	712.8	1,490.4	710	21.5
FY 1979-80	902.4	—	62.4	945.3	1,910.1	994	19.8
FY 1980-81	957.0	$79.4	68.2	682.9	1,787.5	954	15.5
FY 1981-82	942.2	205.5	68.1	405.5	1,621.3	897	9.1
FY 1982-83	1,019.4	221.9	74.5	360.1	1,675.9	953	7.4
FY 1983-84	1,155.0	236.5	83.3	444.0	1,918.8	1,109	8.2
FY 1984-85	1,283.4	359.6	88.3	426.1[b]	2,157.4	1,273	7.7

[a]Federal aid is excluded.

[b]Includes $13.6 million payment from the local government fund to comply with Section 30.

FIGURE 4

General Fund Payment to School Aid Fund and Restricted Sources



CONCLUSION

The lottery is an important state revenue source, but contrary to public perception it provides a relatively small share (6%) of the funding for K-12 education. In fact, as long as the annual GF appropriation to the SAF is variable, there can be no guarantee that increased lottery revenue will result in more spending on education, because as lottery and other contributions to the SAF grow, the GF contribution can shrink. However, any growth in revenues improves the State's ability to increase spending on state services, among which education is likely to remain a high priority.