

State Foundation Payment Process

Publicly funded education in Ohio dates back to the 1820s when the state issued a property tax in order to finance the new schools that were being established throughout the state. While the makeup of funding has changed over time, the State continues to provide financial support to local districts. Today, this support is provided, based on a variety of factors, through Foundation Program payments which are administered by ODE based on a formula set in code by the General Assembly.¹ These payments are designed to ensure a basic, or foundational, level of support is provided for every public school student in Ohio. In FY 2018, 48.8 percent, or nearly half of all public school funding came from state sources. While this section covers the Foundation payment process, our examination focused on the end-of-year closeout process.

Background

Ohio Revised Code (ORC) §3317 tasks ODE with calculating and distributing foundation program funding to local education agencies (LEAs) based on the formula set by the General Assembly. The state foundation funding formula undergoes periodic revisions and the current formula has been in place since FY 2014.² Traditional schools, which make up the bulk of public education agencies, receive foundation funding based on the following components:

- **Opportunity grant**³: An amount set by the General Assembly in the biennial budget which provides a uniform per-pupil funding amount and which makes up the largest portion of foundation aid; districts receive a proportion of this grant based on their identified state share index;⁴
- **Targeted assistance and capacity aid**: Additional funding for districts with lower capacity to raise local revenues and to small districts with relatively low property values;
- **Categorical add-ons**: Variable funding components which assess the needs of students who are considered non-standard, such as those who have limited English proficiency or those who receive special, gifted, or career-technical education services;
- **Performance bonuses**: Formula funding which is available and incentivizes academic performance based on four-year graduation rates and third-grade reading proficiency; and
- **Additional funding adjustments**: in order to address large fluctuations in state aid, the formula includes temporary transitional aid, a gain cap, and a cap offset payment.

In FY 2019, traditional school districts received between 5.0 and 90.0 percent of the opportunity grant based on the state share index. A variety of factors, including the state share index calculation, can cause districts to receive reduced funding year over year. Temporary transitional aid, known as the guarantee, provides districts with a consistent level of foundation funding,

¹ ORC § 3317.022

² H.B. 166 of the 133rd General Assembly provides every traditional school district and joint vocational school district with the same amount of funding in FY 2020 and FY 2021 as they received in FY 2019.

³ In FY 2019 and FY 2020, the opportunity grant was \$6,020 per pupil.

⁴ The calculation of the State Share Index is specified in ORC §3317.017. The purpose of the index is to measure the wealth of each school district in terms of property tax base and residents' ability to pay.

generally ensuring that districts receive no less than their guaranteed base from the preceding budget cycle. Similarly, as funding is based on student enrollment, an influx of students may cause a district to see an increase in foundation funding based on the formula. The gain cap (the cap) limits the amount of additional funding a district can receive due to increased enrollment or changes in district demographics.⁵ Since FY 2017, the number of traditional districts that were formula funded has decreased significantly while the number of districts that are on the guarantee or cap has increased.

Funding is calculated on a per-pupil basis as identified through an annualized full time equivalent (FTE) enrollment calculation as reported through EMIS. The information which is reported through EMIS allows ODE to track specific attributes of a student, such as being eligible for special education assistance, as that student moves across districts. Through FY 2014, LEAs reported enrollment based on a count of students for one week in October. Beginning in FY 2015, LEAs have been required to report daily enrollment figures for students; while this requires more data entry and analysis, it results in a more accurate reflection of actual student population throughout the course of a school year.

LEAs receive either 12 or 24 foundation payments annually.⁶ While state funding accounts for nearly half of all public education funding in the state, in FY 2019 state funding ranged between 10.8 percent and 78.5 percent of total traditional district funding.⁷ At the end of each fiscal year, ODE reviews each district’s total payment history and makes adjustments based on data corrections, outstanding invoices⁸, and LEA appeals⁹. These adjustments are factored into payments that are received in the following fiscal year.

Why We Looked At This

The Foundation payment process was reviewed in a prior performance audit in 2013. At that time, there was a significant lag between the final payment requests submitted by districts and the receipt of that final payment. The audit found that the balance of FY 2009 encumbrances carried over to FY 2012 is \$7,873,261. In the 2013 audit, ODE explained that stimulus funds to districts led to the significant open encumbrances; however, the lag in payment and large balance of carry-over encumbrances continued for several years after the stimulus payments were terminated by the federal government. These encumbrances, while permitted by state law for subsidy funds, indicated that LEAs were waiting long periods for receipt of revenues. This impacted the LEAs’ ability to engage in ongoing, close financial management of district resources. Last, ODE invests significant time and effort on this process and, if the Department is

⁵ See **Appendix E** for additional information

⁶ Community Schools and Joint Vocational School Districts receive 12 payments and Traditional districts, Educational Service Centers and County Boards of Developmental Disabilities receive 24 payments.

⁷Information from the ODE District Profile Report (Cupp Report). State revenue includes sources other than foundation funding, including homestead and rollback funding.

⁸ The Jon Peterson and Autism scholarships are included in the School Finance Payment Report (SFPR) as deductions to the districts’ state foundation funding. The scholarship deductions are based on the actual amounts invoiced by the provider.

⁹ Data appeals that impact foundation funding calculations are Student Appeals, Funding Appeals, Staffing and Course Appeals, and Calendar Appeals.

able to shorten the window for processing final payments, it would free up its staff to engage in other mission-critical activities.

In FY 2019, ODE distributed over \$9 billion in foundation funding to schools, which was more than 10 percent of the State's total budget of just more than \$67 billion. This funding is both a significant portion of the State's budget and critical to LEAs. Ensuring the efficient and effective delivery of these resources helps to ensure quality public education is accessible to all Ohioans.

What We Looked At

We reviewed ODE's internal process for issuing regular foundation payments as well as the process for calculating and issuing final reconciliations. We also reached out to LEA officials in order to understand how entities receiving funding believe the process impacts operations.

We paid particular attention to the processes in place relating to final payment adjustments, which occur after the end of the fiscal year during the first half of the following fiscal year.¹⁰ While the second payment in June is the final regular payment of the fiscal year, due to adjustments that must be made as a result in fluctuations in student enrollment and other factors, such as processing of invoices related to educational services, ODE issues final payments to LEAs after the close of the fiscal year.¹¹ We reviewed the reconciliation to determine if there were opportunities to decrease the length of time between the close of the fiscal year and issuing the final reconciliation payment.

Because the funding ultimately is received and used by LEAs, we also reviewed both their role in the process in regards to providing data and also how they believe the process directly impacts their operations. In order to obtain information related to how the process directly impacts LEA operations, we sent a survey to superintendents, treasurers, and EMIS coordinators.

In order to understand the reconciliation and final payment process we analyzed historic data related to foundation payments. This allowed us to identify potential opportunities for improvement relating to the adjustment process as well as understand how that process was impacting LEAs in regards to their annual budget.

What We Found

We found that the foundation payment process has been increasingly efficient over the past several years and ODE has significantly improved in this area. The internal process for issuing foundation payments occurs twice a month and ends with a payment being disbursed to LEAs. While payments at the beginning of the year are based on the previous year's data, ODE incorporates updates as data becomes available through EMIS and adjusts the foundation payment calculations. As discussed in **Section 3: EMIS**, this process includes regular data

¹⁰ The last regular payment is received in June, the final reconciliation payment is typically received prior to the end of that calendar year. In FY 2019, ODE issued two final payments to LEAs: one in August 2019 and one in December 2019.

¹¹ The final payments may be a positive or negative adjustment and are included in a regularly scheduled payment.

validation checks, which helps to prevent significant changes after payments have been disbursed.

There is a necessary reconciliation process after the close of the fiscal year to finalize payments for LEAs. This portion of the foundation payment process has become more efficient based on the available data. In FY 2016, the final reconciliation payment for traditional districts was processed on May 19, 2017, or 323 days after the end of the fiscal year. By FY 2019, this timeframe had been cut to 166 days and was issued on December 13, 2019.

We reviewed the variation in annual funding based on the final regular payment in June against the final reconciliation payment received by each LEA. For traditional school districts, we found that the median variation has remained below 1.0 percent and has decreased over the past five years, beginning in FY 2014. This variance can be either positive or negative, that is the reconciliation process may result in LEAs receiving additional funding or having funding taken away. While the median variation has been historically low, there have been districts that experienced significant changes to state foundation funding based on the reconciliation process. However, in FY 2019, the greatest amount of variation was only 1.8 percent and the median variation was negative 0.0042 percent, meaning that there was an extremely small percentage of funding that was taken away. Our analysis for both community schools and joint vocational school districts resulted in similar results.¹²

The total amount of dollars distributed after reconciling data has also decreased; in FY 2014, ODE distributed nearly \$6.5 million in additional funding due to adjustments to traditional school districts and in FY 2019, it distributed just over \$2.3 million.¹³ Further, in FY 2014, 26 traditional school districts had an adjustment that represented more than 2.0 percent of total annual funding; in 2019 there were none. For all types of LEAs, the variation between the final regular payment and the final reconciliation payment was below 1 percent for the timeframe analyzed.

The decrease in both variation in funding levels for LEAs and the amount of funding issued is likely a result of consistent formula funding. The formula process has not changed since 2014, which has allowed LEAs to better learn and adjust to it. While changes to data reporting did cause issues in 2015, these changes have been identified and ODE has provided guidance through the EMIS manual which allows LEAs to accurately reflect enrollment data. Additionally, between 2017 and 2019, a large number of districts were moved to either temporary transitional aid or the gain cap which reduced variation in funding and resulted in fewer funding adjustments.

While ODE has improved the timeline for final foundation payments, the last payment typically occurs nearly six months after the end of the fiscal year. We identified one recommendation that would assist the Department in improving operational efficiency and effectiveness in relation to the foundation payments:

¹² See [Appendix E](#) for additional analysis

¹³ This reflects the net amount of additional funding received by traditional districts, for full analysis see [Appendix E](#).

- **Recommendation 4.1:** Because districts are reliant on their final payments for continued operations, ODE should review current procedures and implement strategic changes which would allow the Department to finalize foundation funding payments in a more efficient manner.

Recommendation 4.1: Foundation Payment Process

ODE should implement strategic changes to internal processes in order to finalize school foundation funding as soon as possible, potentially prior to November 30th when OBM closes encumbrances for non-subsidy funds.¹⁴ These changes may include:

- An earlier window for Funding Appeals;
- An earlier deadline for provider invoicing for the Jon Peterson and Autism scholarships;
- An earlier deadline for completion of Community School FTE reviews; and
- A reevaluation of staffing commitments during Report Card processing.

Finalizing payments earlier would allow for a more streamlined budget process at the state level and reduce the amount of time invested by LEAs and ODE in the adjustment and appeals process. Additionally, the shorter time frame would benefit LEAs and their budgeting and financial management processes as well.

Overall, ODE should consider the tradeoffs in terms of time and effort for it and LEA representatives in the adjustment process considering the small magnitude of changes the process currently yields. While internal controls over payments and reimbursements are critical for safeguarding taxpayer funds, the process may be sufficiently mature to lead to diminishing returns in the adjustment process.

Background

The State has used the current foundation formula since FY 2014.¹⁵ The foundation payment process has multiple steps which require input or action by a variety of internal and external stakeholders. Because of the complex nature of the process, prior to conducting any analysis, we first worked with several key areas within ODE in order to develop an internal process map for foundation funding. We interviewed the following offices within ODE to develop the map:

- **Data Quality and Governance/EMIS**, which is responsible for calculating student enrollment data and reviewing data appeals from LEAs;
- **EMIS/Foundation Payment Application Services**, which is responsible for calculating each LEA's funding and generating payment reports; and,
- **Office of Budget and School Funding**, which is responsible for conducting the final review before payments are disbursed.

Together, these three offices are responsible for taking the data provided by LEAs in order to process and distribute foundation payments.

¹⁴ November 30th is the current deadline for finalizing encumbrances from the prior fiscal year as set by the Office of Budget and Management.

¹⁵ Although the current formula has been in place since 2014, in FY 2020, the General Assembly suspended the formula and all districts received the same amount of funding as in the prior year. However, this audit does not cover this FY 2020 payment due to timing.

At the end of each fiscal year, ODE issues reconciliation payments based on the full year of data. These adjustments can either be positive or negative and are incorporated into a future payment. LEAs are also offered four appeal windows in order to correct any data errors. These appeal windows are typically short in duration, approximately two weeks long. While the gap between student appeals and the first reconciliation payment is approximately one month, ODE takes nearly two months to fully process funding appeals and issue final reconciliation payments.

Methodology and Analysis

Once a process map for both the standard foundation payments and the annual appeals process was created, we developed and distributed survey questions to external stake holders; specifically, superintendents, treasurers, and EMIS coordinators for LEAs.¹⁶ We asked respondents about their experiences with filing appeals and how foundation payment adjustments after the fiscal year affect their entity. Our survey revealed that 41.8 percent of superintendents and treasurers across all LEAs felt that the timing of the final payment significantly impacted budgeting. Several officials noted that the final reconciliations were difficult to track and to appropriately plan for in their November forecast.¹⁷ While an adjustment may represent a small percentage of overall funding for an LEA, for those districts that may be experiencing acute fiscal distress the information can be critical to proper budgeting and decision making. One District Superintendent responded to our questions by stating:

“...Delayed foundation payments have a significant impact on our district, we are in fiscal... [oversight] and it is critical we have our funding and data as quickly as possible. This is needed so we can make decisions regarding appropriations, personnel, spending, and financial projections based on information that is as current and accurate as possible.”

We then reviewed ODE’s internal processes as they relate to the final reconciliation process in order to identify potential opportunities for increased efficiency within the Department. Part of this review was identifying additional factors which may cause delays to this process. For FY 2019, there were five main activities which impacted when final payments were issued:

- **Ohio Facilities Construction Commission (OFCC) data reporting:** ODE is required to report data calculations to the OFCC that use ADM as reported by districts through EMIS. The due date for reporting this information is specified in ORC §3318.011;
- **Jon Peterson and Autism scholarship invoicing:** These scholarships are included in the School Finance Payment Report as deductions to the districts’ state foundation funding. The deductions are based on the actual amount invoiced by providers and ODE sets the deadline for providers to submit invoices;
- **Report card data processing:** Per ORC §3302.03, ODE must publish Ohio School Report Cards by September 15th. Many staff members, whose main job duty is to process

¹⁶ We sent survey questions to representatives from traditional school districts, community schools, joint vocational schools, information technology centers, educational service centers, STEM schools, and some private companies that support schools.

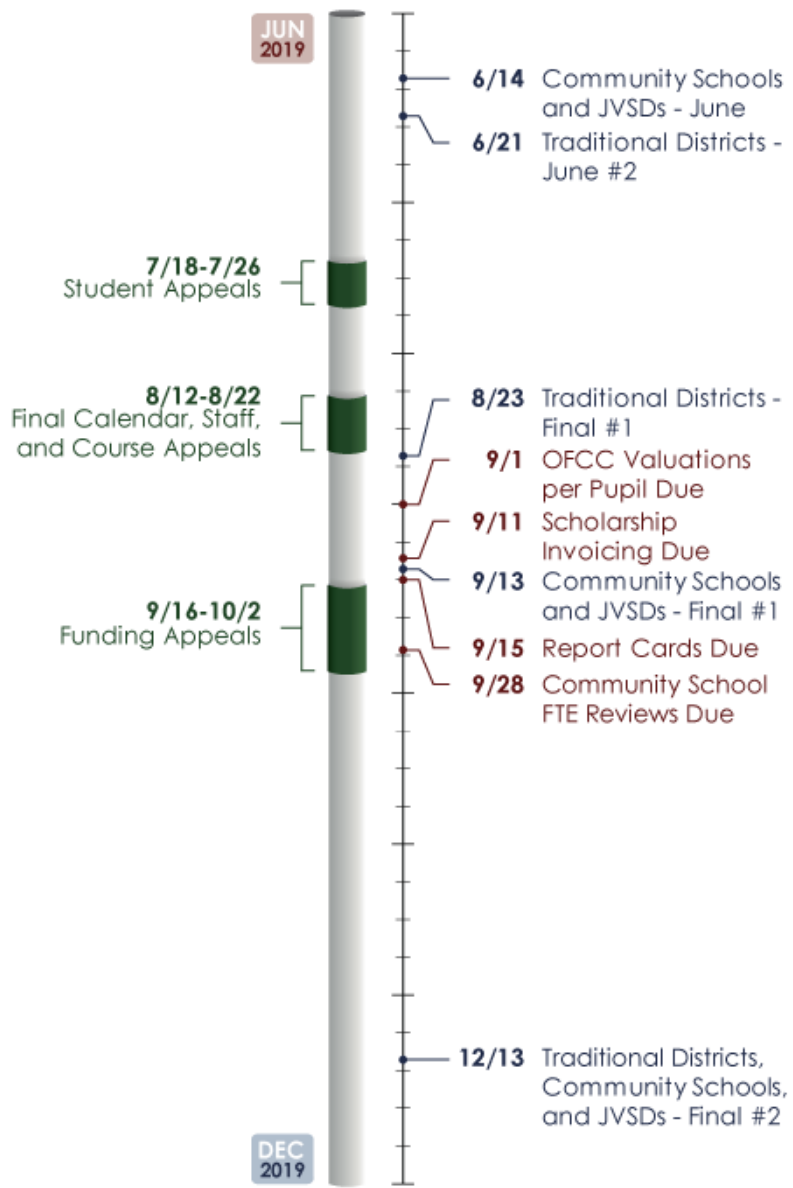
¹⁷ Ohio school districts are required to submit a Five Year Forecast showing projected financial conditions to ODE in November of each year.

EMIS data, are pulled away from their normal duties to work on the Report Cards from early August until mid-September. This reduces staff availability to work on processing the foundation payments;

- **Community school FTE reviews:** Per ORC §3314.08(K), ODE is given authority to conduct FTE reviews of Community Schools, but is required to complete the review within 90 days of the end of the fiscal year, with an optional 30 day extension. The results of an FTE review may result in adjustments to state foundation funding; and,
- **Student Appeals and Funding Appeals:** The student appeals process occurs in July shortly after the fiscal year closes and is completed prior to the first reconciliation payment (issued 8/23/19). The Funding Appeals window, however, is not opened until mid-September. In contrast to the Student Appeals, where 76 appeals were filed and 70 approved in FY 2019, only 6 appeals were filed under the Funding Appeals. Of those 6, 4 were approved, affecting only 3 students.

As seen in the timeline, each of these activities is occurring prior to early October, yet for FY 2019, the last final payment was not issued until December 13th. Making adjustments to the deadlines or workload associated with one or multiple of these activities should allow the last final payment to be issued earlier than the middle of December. This analysis did not assess the workload associated with these activities or the payment process itself, and therefore cannot determine which activities, if moved earlier, would have the greatest impact on when the last final

School District Payment Processing Timeline



Source: ODE

payment can be issued. ODE should assess each of these activities and prioritize changes that would have the most influence on how early the last final payment can be made.

Conclusion

While ODE has reduced the amount of time between the end of the fiscal year and the final reconciliation, the current foundation payment process results in a reconciliation period of nearly six months after the end of the fiscal year. During this timeframe, ODE employees who typically work on the reconciliation process are required to shift focus and perform other tasks, such as processing data for the Ohio School Report Cards. Expediting the payment process through strategic process improvements would result in a more efficient allocation of funds.

Allowing the subsidy encumbrances for ODE Foundation payments to remain open for several months beyond the close of the fiscal year or even multiple years, while allowed, is not a good business practice. Closing these encumbrances and making the final payments sooner has multiple benefits to ODE and the LEAs. In many cases, this multi-month process results in marginal changes and ODE should weight the benefit of these changes in light of total payments and the small magnitude of changes occurring with adjustments. In this case, the internal controls over Foundation payments should not be a barrier to efficient processing. If future changes to the Foundation formula or other school funding model occur, ODE should examine ways to ensure LEAs are able to submit as accurate of information so that the volume and amount of adjustments and duration of the adjustment period is not extended.

In FY 2020, ODE has already made changes that could reduce the timeline for the final payment. The Department opened the Funding Appeals window approximately two weeks earlier than in the previous fiscal year and will close it approximately one week earlier. This should allow the Department to process appeals more expediently.

Appendix E: Foundation Funding

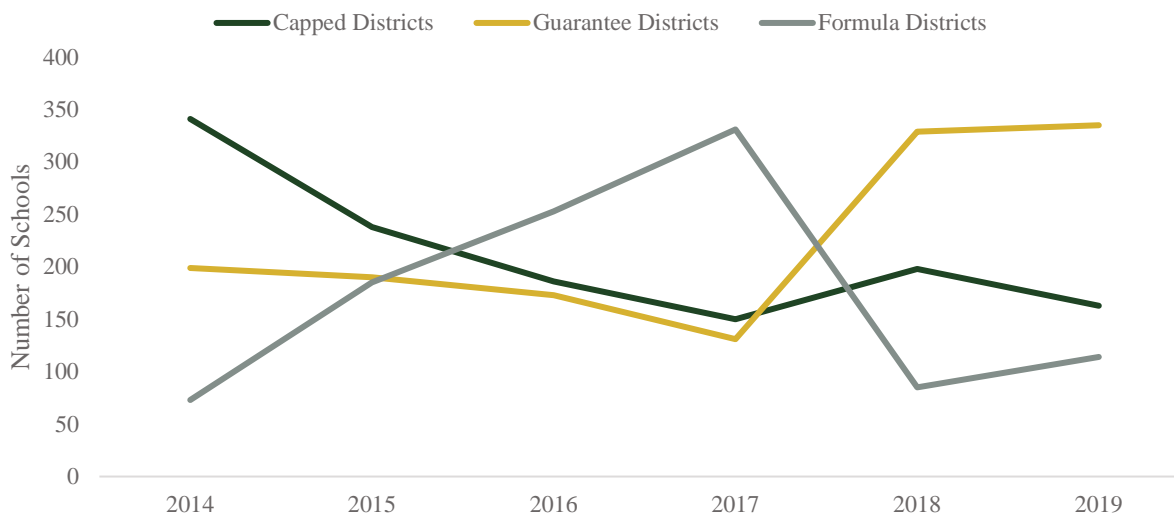
Foundation Formula Funding

ODE calculates the level of funding for traditional school districts based on the formula identified in ORC §3317.022. Detailed information regarding the funding process can be found in the following documents:

- *School Funding Complete Resource* (Legislative Budget Office, Ohio Legislative Service Commission, February 2019), and www.lsc.ohio.gov/documents/reference/current/schoolfunding/sfcr_feb2019.pdf
- *FY20 School Finance Payment Report (SFPR) Line by Line Explanation* (Ohio Department of Education, November 2019), www.education.ohio.gov/Topics/Finance-and-Funding/School-Payment-Reports/State-Funding-For-Schools/Traditional-School-Districts.

To avoid significant variation in funding levels, districts may receive temporary transitional aid or be placed on the gain cap and may move on or off these designations as EMIS data is updated.

Total Districts by Funding Type



Source: ODE

In 2019, the guarantee ensured that districts received at least the same amount of state aid as in FY 2017. However, districts with declining enrollment were given a scaled amount of funding. Districts with an ADM decrease between 5.0 and 10.0 percent from FY 2014 to FY 2016 had funding scaled between 95.0 and 100.0 percent. Districts with an ADM decrease of 10 percent or greater from FY 2014 to FY 2017 received funding equal to 95 percent of the district’s FY 2017 foundation funding.

The gain cap sets a limit on how much additional funding a district can earn from FY 2017 due to increasing enrollment. In FY 2018 districts with increasing enrollment were able to receive up to 105.5 percent of FY 2017 their funding, and in FY 2019 districts with increasing enrollment were able to receive up to 106.0 percent of their FY 2018 funding. So combining those two years, districts in some cases would have been able to receive 11.83 percent more foundation funding in FY 2019 than they did in FY 2017.

While formula-funded districts (those not subject to the cap or guarantee) made up the majority of districts in FY 2016 and 2017, only 13.9 percent of districts in FY 2018 and 18.6 percent of districts in FY 2019 were formula-funded.

ODE Payment Process

The regular foundation payment process is ongoing and follows the steps outlined in the process map linked below.

See http://ohioauditor.gov/performance/ode_audit/ode-payment-process.pdf

Foundation Funding Appeals

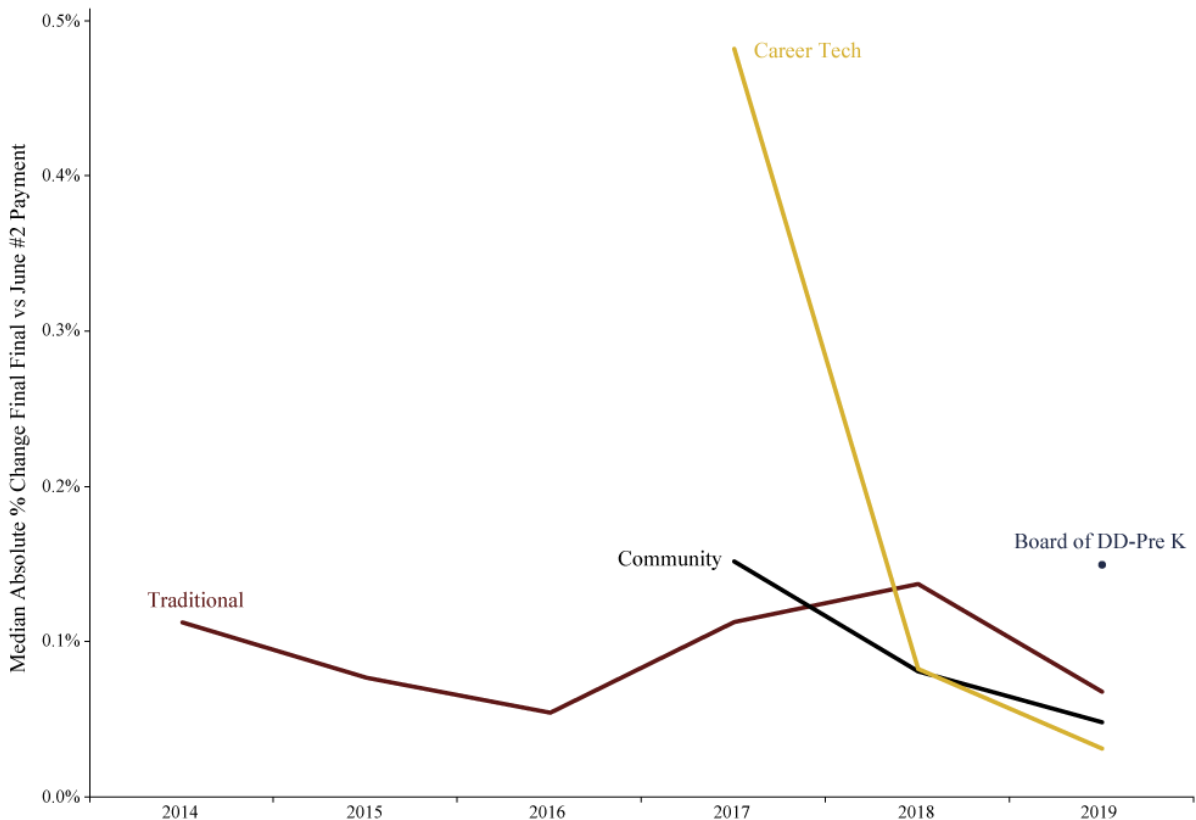
The appeals process is initiated by an LEA and follows the process linked below for both Student Appeals and Funding Appeals. While there are two additional appeal types, we determined they were not significant to the payment process.

See http://ohioauditor.gov/performance/ode_audit/ode-appeals-process.pdf

Funding Variation

As noted, funding due to reconciliation payments does not vary significantly for the majority of LEAs. These adjustments typically are a minimal portion of the total foundation funding received in a particular year. The following charts are additional analyses related to this topic. The chart below shows the median difference in total annual foundation funding between the final regular payment in June and the final reconciliation payment. For the three LEA types where we had sufficient data, we found that the median variation was less than 0.5 percent for all years analyzed. This means that the majority of LEAs experienced a change, whether positive or negative, of less than 1.0 percent of their annual foundation funding due to the reconciliation processes.

Median Absolute % Difference of Last Final vs June #2 Net State Funding



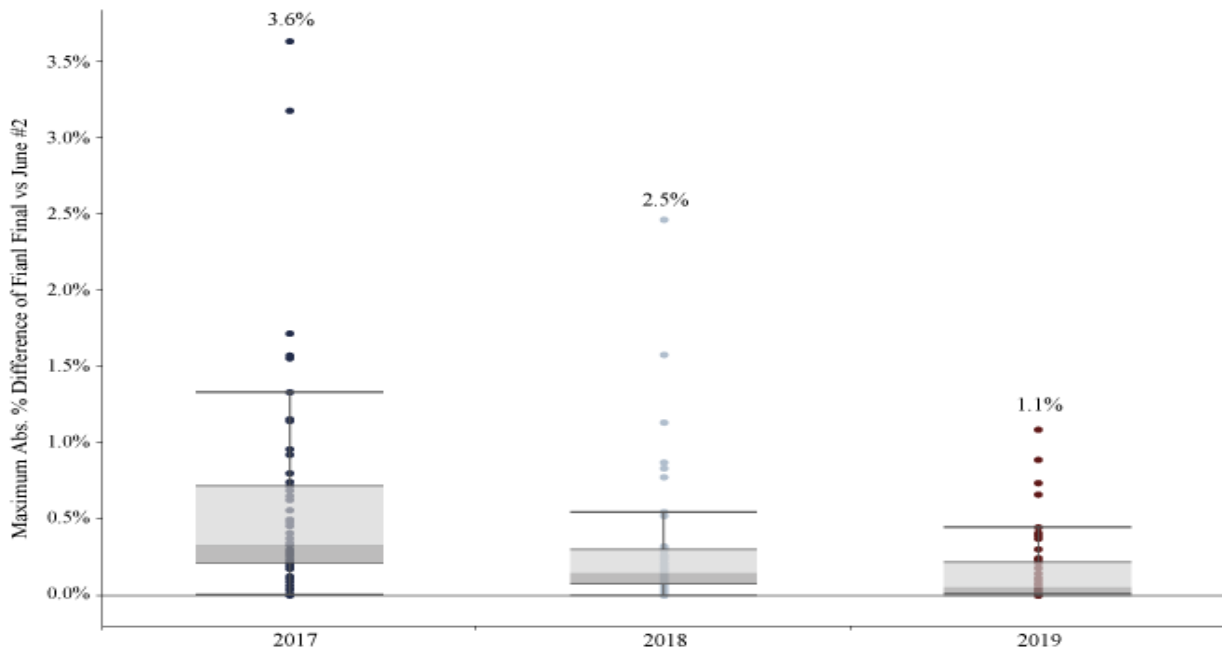
Source: Local Education Agencies

Note: Board of DD-Spec Ed and ESC's are 0.0% in FY 2019 (only year analyzed) and are therefore not pictured.

Note: Excludes Bettsville Schools (49692) which merged with Old Fort Local Schools.

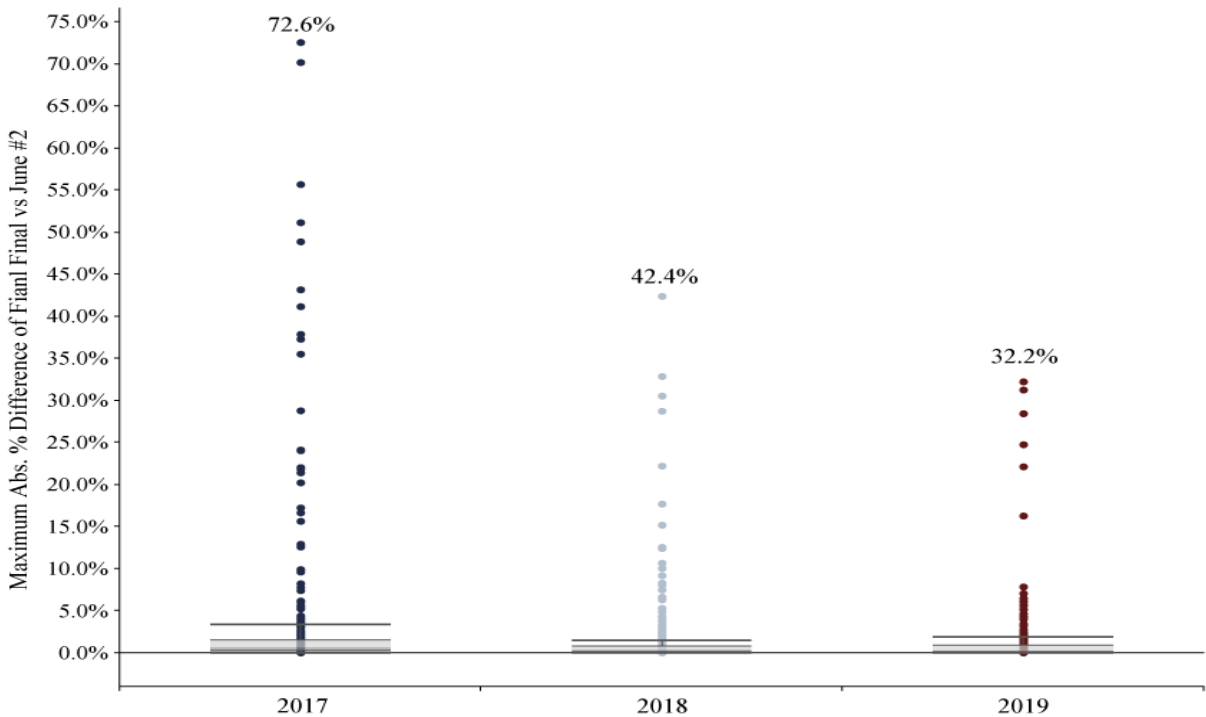
The charts on the following page show the variation for JVSDs and Community Schools for FY 2017, FY 2018, and FY 2019. These charts show the percentage range for the middle 50.0 percent of LEAs as well as identifies individual outliers. As seen in the charts, both LEA types have had decreasing variation both for the middle 50.0 percent as well as a reduction in the variation for outliers.

Career Tech Max Absolute % Difference of Last Final vs June #2



Source: Local Education Agencies

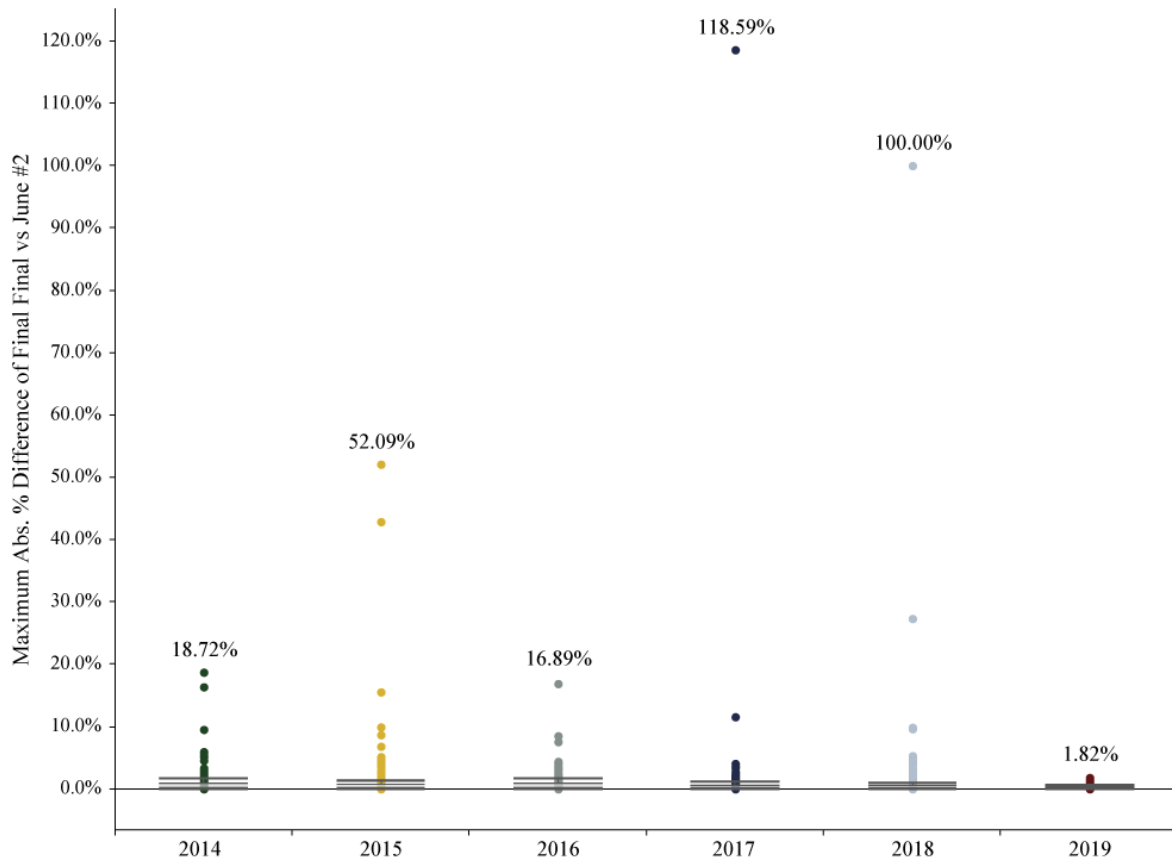
Community School Max Absolute % Difference of Last Final vs June #2 Net State Funding



Source: Local Education Agencies

The chart below shows the same variation data for traditional school districts over a five year period. The middle 50.0 percent of districts had very little variation over the course of the analyzed period. There was a spike in FY 2015, both in the number of outliers and the amount of variation, which was likely due to changes in EMIS reporting. Additionally, there were individual outliers in FY 2017 and FY 2018, however these were due to unique circumstances and were not tied to the funding process overall. As seen in the chart, the greatest amount of variation in FY 2019 was only 1.8 percent.

Traditional Districts Maximum Absolute % Difference of Last Final vs June #2 Net State Funding



Source: Local Education Agencies