



## SECTOR COMMENT

## Colorado School Districts' Subdued State Funding Ruled Constitutional

From U.S. Public Finance Weekly Credit Outlook

---

**Analyst Contacts:**

DALLAS +1.214.220.4350

John Grayson Nichols +1.214.979.6851

Analyst

[john.nichols@moodys.com](mailto:john.nichols@moodys.com)

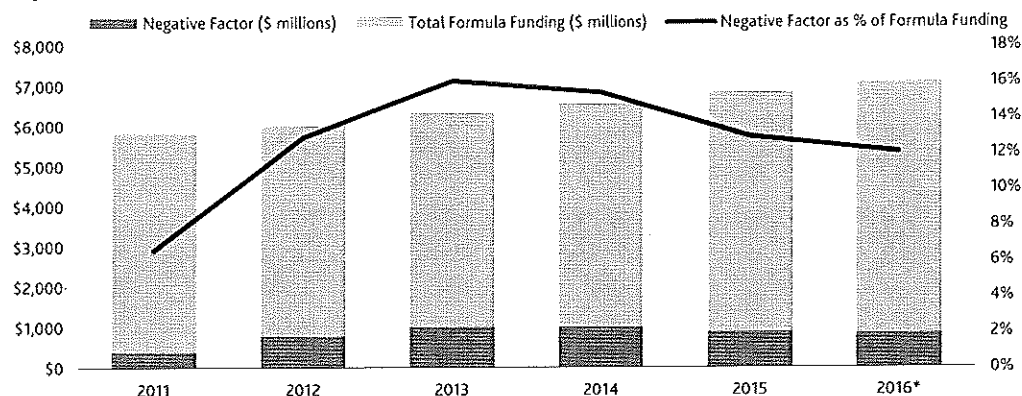
On September 21, the State of Colorado's (Aa1 stable) Supreme Court ruled that recent sizable educational funding cuts were indeed constitutional. Since 2011, the state has cut roughly \$5 billion, which has stressed many local public school district budgets statewide. The state Supreme Court decision foreshadows education funding levels below the state's defined formula for the foreseeable future. Subdued funding levels will continue to place pressure on individual school district budgets, requiring local management teams to hold down expenditures and/or seek additional taxpayer authorization to augment tax rates to maintain operations and reserve levels.

The ruling dismissed a June 2014 lawsuit brought by school districts and parents, which claimed that the educational funding cuts were unconstitutional and did not adhere to Amendment 23. The voter-approved Amendment 23 requires that base per-pupil funding levels increase on an annual basis. The state Supreme Court ruled that the cuts have not affected the base per-pupil funding amount and instead highlighted the state's use of the negative factor provision. This provision allows the state to adopt its budget for education at a level below the calculated funding formula so long as the base per-pupil increases by the rate of inflation.

The negative factor provision has created a \$5 billion discrepancy between the state's defined funding formula and actual total education funding from fiscal 2011 to fiscal 2016. The negative factor amount increased significantly through fiscal 2013 and remained around \$1 billion annually as state legislators have continued to approve educational appropriations below the funding formula (see Exhibit 1). The cuts also reached a high of 16% off the total funding formula amounts in fiscal 2013, though has slightly subsided to an estimated 12% for the current fiscal year.

EXHIBIT 1

## Negative Factor Level Increases Substantially, Remains High Through Fiscal 2016



\*Estimated

Source: Colorado Department of Education

Although the negative factor amount has dropped and actual average per-pupil funding throughout the state has increased by roughly 4% over the last three fiscal years to \$7,294, the cuts have left local management teams with tough budgetary decisions. Most school districts across the state fared well during this period of turmoil by making the necessary expenditure reductions and/or seeking local voter approval for additional ad valorem taxes called mill-levy overrides. The state allows individual school districts to receive up to 25% of total program revenues through these voter-approved override levies. Per the *Colorado School Finance Project*, 72 of the state's 178 public school districts asked voters for mill-levy overrides between fiscal 2010 and 2013. Only 38 were approved. The research further concludes that nearly half of the statewide enrollment benefited from a successful override election.

Exhibit 2 highlights the dollar amount of discrepancies between the state funding formula and actual total program amounts in fiscal 2015 for the state's top 10 districts by enrollment. All of these districts benefit from some level of mill-levy override support from its tax base, but at varying levels. Without the additional property tax support, large budgetary gaps would exist and subsequently lead to tapping reserves or deep budgetary cuts. Six of the top 10 districts had enough additional voter support to outweigh their fiscal 2015 negative factor amounts with mill-levy overrides. All 10 of the largest school districts have maintained strong underlying credit quality at either Aa1 or Aa2 ratings during the period of funding cuts given their willingness and ability to make budget adjustments or the success of mill-levy overrides.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on [www.moodys.com](http://www.moodys.com) for the most updated credit rating action information and rating history.

## EXHIBIT 2

### Largest School Districts Show Resiliency and Utilize Mill-Levy Overrides to Help Offset Cuts Fiscal 2015 (\$ millions)

District	Moody's Underlying GO Rating/Outlook	Actual Funded Pupil Counts	Formula Funding at 100%	Negative Factor	Total Program After Negative Factor	Override Property Tax Revenues	Override as a % of Total Program	Override as a % of Negative Factor
<u>Denver City and County School District 1</u>	Aa2/Stable	84,044	\$710	\$(92)	\$618	\$131	18.5%	142.4%
<u>Jefferson County School District R-1</u>	Aa2/Stable	81,130	\$639	\$(83)	\$556	\$113	17.7%	136.8%
<u>Douglas County School District RE 1</u>	Aa1/Stable	63,354	\$492	\$(64)	\$429	\$34	6.8%	52.8%
<u>Arapahoe County School District 5 (Cherry Creek)</u>	Aa1/Stable	51,433	\$413	\$(54)	\$359	\$85	20.5%	158.1%
<u>Adams 12 Five Star Schools</u>	Aa2/No Outlook	41,182	\$325	\$(42)	\$282	\$35	10.9%	84.1%
<u>Adams &amp; Arapahoe Counties Joint School District 28J</u>	Aa2/Stable	39,600	\$334	\$(43)	\$291	\$37	11.0%	85.0%
<u>El Paso County School District 11 (Colorado Springs)</u>	Aa2/No Outlook	30,135	\$240	\$(31)	\$209	\$27	11.2%	86.8%
<u>Boulder &amp; Gilpin Counties School District RE 2 (Boulder Valley)</u>	Aa1/Stable	29,398	\$234	\$(30)	\$204	\$64	27.3%	210.8%
<u>Poudre School District R-1</u>	Aa2/Stable	28,935	\$221	\$(29)	\$193	\$35	15.8%	121.9%
<u>St. Vrain Valley School District RE 1J</u>	Aa2/Stable	28,741	\$227	\$(29)	\$197	\$32	14.3%	110.5%

Source: Colorado Department of Education, Moody's Investors Service

The Colorado Supreme Court decision means that subdued state funding is likely for the foreseeable future. During a period of statewide enrollment growth, muted funding levels will likely continue to present operational pressures for public school districts. Districts may be challenged to make expenditure reductions and/or seek voter approval for mill-levy overrides to help sustain operations. We note a history of anti-tax sentiment within the state can impact voter approval. Continual use of the aforementioned remedies is not viable for long-term operating sustainability. Any increases to the current education cuts in the future would put greater stress on district budgets, which may lead to downward shifts in creditworthiness.

Report Number: 184791

Author  
Grayson Nichols

Senior Production Associate  
Amanda Kissoon

© 2015 Moody's Corporation, Moody's Investors Service, Inc., Moody's Analytics, Inc. and/or their licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ISSUED BY MOODY'S INVESTORS SERVICE, INC. AND ITS RATING AFFILIATES ("MIS") ARE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND CREDIT RATINGS AND RESEARCH PUBLICATIONS PUBLISHED BY MOODY'S ("MOODY'S PUBLICATIONS") MAY INCLUDE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MOODY'S DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS AND MOODY'S OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. MOODY'S PUBLICATIONS MAY ALSO INCLUDE QUANTITATIVE MODEL-BASED ESTIMATES OF CREDIT RISK AND RELATED OPINIONS OR COMMENTARY PUBLISHED BY MOODY'S ANALYTICS, INC. CREDIT RATINGS AND MOODY'S PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. NEITHER CREDIT RATINGS NOR MOODY'S PUBLICATIONS COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS AND PUBLISHES MOODY'S PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL, WITH DUE CARE, MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

MOODY'S CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT INTENDED FOR USE BY RETAIL INVESTORS AND IT WOULD BE RECKLESS FOR RETAIL INVESTORS TO CONSIDER MOODY'S CREDIT RATINGS OR MOODY'S PUBLICATIONS IN MAKING ANY INVESTMENT DECISION. IF IN DOUBT YOU SHOULD CONTACT YOUR FINANCIAL OR OTHER PROFESSIONAL ADVISER.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process or in preparing the Moody's Publications.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability to any person or entity for any indirect, special, consequential, or incidental losses or damages whatsoever arising from or in connection with the information contained herein or the use of or inability to use any such information, even if MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers is advised in advance of the possibility of such losses or damages, including but not limited to: (a) any loss of present or prospective profits or (b) any loss or damage arising where the relevant financial instrument is not the subject of a particular credit rating assigned by MOODY'S.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability for any direct or compensatory losses or damages caused to any person or entity, including but not limited to by any negligence (but excluding fraud, willful misconduct or any other type of liability that, for the avoidance of doubt, by law cannot be excluded) on the part of, or any contingency within or beyond the control of, MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers, arising from or in connection with the information contained herein or the use of or inability to use any such information.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

Moody's Investors Service, Inc., a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by Moody's Investors Service, Inc., have, prior to assignment of any rating, agreed to pay to Moody's Investors Service, Inc., for appraisal and rating services rendered by it fees ranging from \$1,500 to approximately \$2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at [www.moody's.com](http://www.moody's.com) under the heading "Investor Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

For Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657 AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail clients. It would be dangerous for "retail clients" to make any investment decision based on MOODY'S credit rating. If in doubt you should contact your financial or other professional adviser.

For Japan only: Moody's Japan K.K. ("MJKK") is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly-owned by Moody's Overseas Holdings Inc., a wholly-owned subsidiary of MCO. Moody's SF Japan K.K. ("MSFJ") is a wholly-owned credit rating agency subsidiary of MJKK. MSFJ is not a Nationally Recognized Statistical Rating Organization ("NRSRO"). Therefore, credit ratings assigned by MSFJ are Non-NRSRO Credit Ratings. Non-NRSRO Credit Ratings are assigned by an entity that is not a NRSRO and, consequently, the rated obligation will not qualify for certain types of treatment under U.S. laws. MJKK and MSFJ are credit rating agencies registered with the Japan Financial Services Agency and their registration numbers are FSA Commissioner (Ratings) No. 2 and 3 respectively.

MJKK or MSFJ (as applicable) hereby disclose that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MJKK or MSFJ (as applicable) have, prior to assignment of any rating, agreed to pay to MJKK or MSFJ (as applicable) for appraisal and rating services rendered by it fees ranging from JPY200,000 to approximately JPY350,000,000.

MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.