

THE STATE OF NEW HAMPSHIRE
SUPREME COURT

2024 Term

SUPREME COURT DOCKET NO. 2024-0121

Contoocook Valley School District & a.
Plaintiffs/Appellees

v.

The State of New Hampshire & a.
Defendants/Appellants

BRIEF OF AMICUS CURIAE
AMERICAN INSTITUTE FOR ECONOMIC RESEARCH

Appealed from Rockingham County Superior Court
Docket No. 213-2019-CV-00069

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IDENTITY OF AMICUS CURIAE

The American Institute for Economic Research (AIER) is a nonpartisan research and education nonprofit 501(c)(3) organization focused on the importance of markets, with a full range of programs and publications on the social sciences with a primary emphasis on economics. AIER as an institution affirms free enterprise, economic liberty, property rights, sound money, and legal institutions that shore up the rights of individuals to be free to the extent that their actions do not impinge on the rights of others.

AIER's mission is to educate people on the value of personal freedom, free enterprise, property rights, limited government, and sound money. AIER's ongoing scientific research demonstrates the importance of these principles in advancing peace, prosperity, and human progress.

This is the first amicus curiae brief that AIER has ever submitted. We have chosen to engage on this case because it relates directly to our ongoing research programs on fiscal federalism, school finance, and local land-use regulation in the United States, particularly New England. We have found that judicial decision-making in school finance cases has to date been remarkably bereft of economic reasoning and evidence. We believe that this brief will be of service to this Court by explaining the now-considerable research on the consequences of school finance equalization programs.

We are submitting companion briefs in this case and the *Rand* case. This brief focuses on the issues relating to education finance centralization, that is, the assumption of a greater proportion of school funding by state rather than local governments, as would be required by an increase in the

state adequacy grant. The companion brief focuses on the “recapture” mechanism ordered by the Superior Court in the *Rand* case. We have avoided redundancies in the two briefs.

SUMMARY OF ARGUMENT

This brief focuses on the claim by the State that the Superior Court order infringes on separation of powers. In particular, if the public finance research shows that an increase in the State’s base adequacy grant could have unintended consequences, and alternative policy solutions might be of superior efficacy, it supports the State’s contention that the General Court may reasonably keep the base adequacy law as-is (RSA 198:40-a, II(a)) as part of an overall scheme of education finance that meets its constitutional duty.

As shown in our companion brief in the *Rand* case, every community in the state already has ample fiscal capacity to provide an adequate education to its students under the current finance system. In this brief, we make three further points: 1) increasing the adequacy grant merely by increasing the state education tax (SWEPT) as currently administered would have minimal impact, 2) increasing the adequacy grant through other funding mechanisms would have several deleterious consequences, and 3) the General Court could secure students’ right to an adequate education through many other, superior policy mechanisms besides an increase in state funding to public school systems.

ARGUMENT

Currently, the State funds adequacy grants to school districts through a uniform property tax add-on to the local property tax, known as SWEPT. The question presented in this case is whether the State Constitution

requires an increase in the base adequacy grant, in order to secure a right to an adequate education previously recognized by this Court.

The State contends that a judicially ordered minimum amount of the base adequacy grant represents a judicial infringement on legislative powers. (Defendants’ Motion to Stay, February 28, 2024, p. 6) In this brief, we show that it would be reasonable for the State to satisfy its constitutional duty to provide access to an adequate education while keeping the existing adequacy grant, as part of a broader scheme of education finance. Therefore, a finding that the existing adequacy amount is unconstitutional is premature.

Among scholars of fiscal federalism, the assumption of a greater share of revenue and expenditure by a higher-level government from a lower-level government is known as “fiscal centralization.” The term “education finance centralization” refers specifically to this phenomenon in the context of funding for K–12 public schools.

The research on these topics shows that education finance centralization would have at best minimal effects on access to quality education, and quite possibly could have significant negative effects on both education and other aspects of the economy.

I. All communities in New Hampshire possess ample fiscal capacity to provide an adequate education under the current adequacy grant.

We refer the Court to our companion brief, which demonstrates this point. But we illustrate it here with a couple of examples. The town with the lowest fiscal capacity in the state according to Department of Education

data, Charlestown, participates in the Fall Mountain Regional School District, which spends over \$23,000 per student,¹ above the state average, and the median home-owning taxpayer in the town pays only \$4,716 a year in total property taxes, well below the state average.² The town with the lowest local tax effort per student and the lowest median home value, Berlin, spends \$21,635 per student, far more than the wealthy communities of Brookline (\$16,708) and Windham (\$16,962).

II. Increasing the adequacy grant creates “vertical fiscal imbalance,” with at best useless effects, and quite possibly negative effects, on the productivity of public education.

In the fiscal federalism literature, “vertical fiscal imbalance” refers to a situation in which the territorial scale at which the revenue is collected to fund a public service does not match the territorial scale at which the public service is funded and provided.³ In these circumstances, it is tempting for the provider of the public service, say a local government providing elementary and secondary education, to “externalize” the costs of

¹ New Hampshire Department of Education, “Financial Reports,” <https://www.education.nh.gov/who-we-are/division-of-educator-and-analytic-resources/bureau-of-education-statistics/financial-reports>.

² U.S. Census Bureau. "Selected Housing Characteristics." *American Community Survey, ACS 5-Year Estimates Data Profiles, Table DP04*, 2022, [https://data.census.gov/table/ACSDP5Y2022.DP04?q=rent&g=040XX00US33,33\\$0600000](https://data.census.gov/table/ACSDP5Y2022.DP04?q=rent&g=040XX00US33,33$0600000). Accessed on August 10, 2024.

³ Shah, Anwar. 2007. “A Practitioner’s Guide to Intergovernmental Fiscal Transfers.” In *Intergovernmental Fiscal Transfers: Principles and Practice*, edited by Robin Boadway and Anwar Shah, 1–53. Washington, DC: World Bank.

its expenditure on the service to the higher-level government providing the revenue, such as a state government. Researchers have noted that when a higher-level government pays for a service that a lower-level government budgets for, it is often difficult to prevent the lower-level government from over-spending, a problem known as “soft budget constraints.”⁴ It can also weaken the lower-level government’s incentives to grow its own tax base.

We now elucidate these issues in the context of New Hampshire education finance.

- a. Increasing the current SWEPT to fund a higher adequacy grant has minimal consequences.

If the Court were to uphold the Superior Court’s ruling in this case while overruling the Superior Court in *Rand*, the most likely outcome is that the General Court would simply increase the existing SWEPT to fund a higher adequacy grant. But because the combined state and local education property tax effort is already higher than the adequacy amount specified by the Superior Court in every single community across the state, this move is simply a shell game. It does not increase overall education funding; it simply relabels a greater proportion of the education property tax as “state” rather than “local.” The only substantive effect it would have is to prohibit

⁴ Rodden, Jonathan. 2002. “The Dilemma of Fiscal Federalism: Grants and Fiscal Performance Around the World.” *American Journal of Political Science* 46 (3): 670–87; Rodden, Jonathan A., Gunnar S. Eskeland, and Jennie Litvack, eds. 2003. *Fiscal Decentralization and the Challenge of Hard Budget Constraints*. Cambridge, MA: MIT Press.

communities from reducing property tax effort per student below the specified adequacy level.

By the same token, of course, if the Court were to overturn the *Claremont* precedents and the General Court were to *reduce* the adequacy grant, that move also would not affect education funding at all, because, once again, communities already choose to implement an above-minimum level of education property tax effort.

- b. Funding the adequacy grant through other sources attenuates local fiscal responsibility.

If this Court were to uphold the Superior Court's rulings in both cases, the General Court could well look at alternative sources of revenue to fund the adequacy grant, because as demonstrated in our companion brief, revising the SWEPT to recapture excess revenue from donor towns is a patently irrational funding mechanism. The legislature has previously considered income and sales taxes as replacement funding mechanisms.

These funding mechanisms would represent true education finance centralization, divorcing the revenue source for education at least partially from local property valuation. While, unlike revenue recapture, they would not directly punish localities for growing their tax base, they would still loosen the tie between size of local tax base and quality of local services. As a result, we should expect local governments to become less efficient, as "homevoters" become less likely to monitor local government in the manner described in our companion brief.

Just this dynamic seems to have played out in Vermont, which had a similar education finance ruling in the late 1990s. Rather than enact a state

education property tax that left local control of school finance largely intact, Vermont adopted essentially full state funding, with an optional local property tax add-on. (Vt. Act 60 of 1997)

The Vermont legislature then observed local school budgets increasing, placing a burden on state finances. In order to force local school districts to be more efficient, Vermont passed three state laws between 2010 and 2015 requiring school districts to consolidate.⁵ The number of school districts in Vermont has fallen from 206 to 50 as a result.⁶ That state also penalizes school districts for “excess spending.”⁷ The Vermont legislature has had to revise these laws repeatedly to address unintended consequences of the system.

- c. School finance centralization exacerbates principal-agent problems and could result in State control of school systems.

The Vermont experience demonstrates the truth of the aphorism, “He who pays the piper calls the tune.” Ultimately, growing state financing of K–12 education will lead to growing state control of K–12 budgeting and administration.

This control is a natural consequence of what economists call the “principal-agent problem.” A principal delegates authority to an agent to act

⁵ Vt. Acts 153 of 2010, 156 of 2012, and 46 of 2015.

⁶ State of Vermont Agency of Education, “Act 46: State Board of Education’s Final Report of Decisions and Order,” <https://education.vermont.gov/vermont-schools/school-governance/act-46-state-board-final-plan>.

⁷ Vt. Acts 60 of 1997 and 68 of 2006.

in the interests of the principal. But the agent has separate interests from the principal and may shirk. Therefore, the principal needs to monitor the agent for performance and sanction the agent if the agent does not perform.

The State has delegated authority to local communities to set up and fund public schools and ensure that they are giving students a high-quality education. By matching local revenues to local expenditures, the State has given communities a financial incentive to be productive and efficient. They know that local voters want to see their home values rise and their property tax burdens remain reasonable. High-quality, efficient public schools meet those objectives.

If the State were to assume a large share of the costs of local schools, communities' incentive to spend those taxpayer dollars efficiently diminish, and the costs of any one community's shirking accrue to the population of the entire state, who will then suffer from a higher state tax burden. The State will have to respond by more closely enforcing budget accountability measures on local schools.

The Vermont experience suggests that centralizing school finance hurts educational quality. Vermont's average National Assessment of Educational Progress (NAEP) scores for 4th grade reading and math and 8th grade reading have deteriorated against New Hampshire's over the last two decades.⁸

This result is consistent with what other researchers have found from school district consolidation. Stanford University economist Carolyn

⁸ The Nation's Report Card, "Data Tools: State Profiles," <https://www.nationsreportcard.gov/profiles/stateprofile?sfj=NP&chort=1&sub=MAT&sj=&st=MN&year=2022R3>.

Hoxby has found that horizontal consolidation of school districts (i.e., into larger geographic areas) causes private schooling to rise and test scores to deteriorate.⁹ Our companion brief contains other references to the voluminous literature confirming a negative relationship between school centralization and quality.

- d. School finance centralization creates incentives for exclusionary zoning.

As more of local schools' budgets come from state government rather than local property taxes, local communities have less incentive to grow their property tax base. As a result, they are freer to indulge any anti-growth sentiments they now have. Our companion brief describes AIER scholar Jason Sorens' research finding that education finance centralization correlates significantly with stricter residential land-use regulations, nationwide.

III. Superior policy mechanisms exist for guaranteeing students' right to an adequate education.

- a. Targeted block grants.

Even if the State is found to have a duty to increase its adequacy grant to local school districts, it could do so more cheaply and effectively by targeting block grants to local communities to ensure adequate fiscal capacity. The General Court could set a minimum threshold of local

⁹ Hoxby, Caroline M. "Does competition among public schools benefit students and taxpayers?" *American Economic Review* 90, no. 5 (2000): 1209-1238.

property valuation per student that counts as “adequate fiscal capacity” to fund a defined adequate education. Communities falling below the threshold would then receive a per-student grant from the State to ensure that they have adequate capacity to fund an adequate education.

b. Open enrollment laws and school choice

The Court has interpreted Part II, Article 83 of the New Hampshire Constitution to guarantee to the public a right to an adequate education system. (*Claremont School District v. Governor (“Claremont I”)*, 138 N.H. at 192, 635 A.2d at 1381) The language of this Article implies that this duty can be discharged in a number of different ways: “it shall be the duty of the legislators and magistrates, in all future periods of this government, to cherish the interest of literature and the sciences, and all seminaries and public schools, to encourage private and public institutions, rewards, and immunities for the promotion of agriculture, arts, sciences, commerce, trades, manufactures, and natural history of the country; to countenance and inculcate the principles of humanity and general benevolence, public and private charity, industry and economy, honesty and punctuality, sincerity, sobriety, and all social affections, and generous sentiments, among the people.” Literary and scientific institutions and programs, seminaries, public schools, private schools, and programs and institutions for the arts, agriculture, commerce, and natural history are apparently among the means by which the State may discharge its duty.

Accordingly, there is no reason to think that State funding of students in district-assigned public schools is the exclusive manner in which the State ensures an adequate education system. This Court could

explicitly recognize that the General Court may discharge its duty through open enrollment programs and other forms of school choice.

Open enrollment laws permit parents to send their children to districts to which they are not assigned. Under such a law, if an adequate education is not available in a student's home district, the student may obtain that education elsewhere.

Open enrollment might work in New Hampshire in the following fashion. If a student attends an out-of-district school, any per-student State aid will be sent to the district of attendance rather than the district of residence. The "sending" town must also transfer its average per-student expenditure from own resources to the "receiving" district, up to the average per-student expenditure from own resources of the "receiving" district. If the receiving district's average per-student expenditure from own resources is higher than that of the sending town, the receiving district may charge tuition to the student in that amount. Receiving districts may or may not be required to accept out-of-district transfers, in the judgment of the legislature, but the revenue available for attracting such transfers would give school districts a strong incentive to accept them.

Such a law could be a part of an overall system that ensures students have access to quality education even if not in their home district. Other elements of such a system could include charter schools and Education Freedom Accounts for nonpublic education.¹⁰

CONCLUSION

¹⁰ RSA 194-F "Education Freedom Accounts."

Increasing the state adequacy grant by means of an increase in the existing SWEPT is nothing more than a shell game, relabeling revenue as “state” rather than “local.” It would be surprising if the Constitution were to require a pointless remedy in this case.

But centralizing school finance through other funding mechanisms would risk significant negative consequences for the quality of New Hampshire public education. Evidence shows that where education finance centralization increased, state governments took more of a role in local school budgeting and administration, with negative consequences for school quality. Moreover, schools become less efficient the more the state foots the bill for them, because the local community has less incentive to spend state money wisely.

Even if the State is found to be in some way deficient in securing the public’s right to a system of adequate education, the solution need not to be a substantial hike in the State’s adequacy grant that goes to all communities, rich and poor. The Court should leave it up to the General Court to determine how to provide a system of adequate education, which may contain elements of targeted fiscal support, an open-enrollment law, and/or other forms of school choice.

STATEMENT OF COMPLIANCE

I hereby certify that pursuant to Rule 16(11) of the New Hampshire Supreme Court Rules, this brief contains approximately 2,972 words, which is fewer than the words permitted by this Court's rules. We relied upon the word count of the computer program used to prepare this brief.

/s/ Jason Sorens

Jason Sorens

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was served this 14th day of August 2024 through the electronic-filing system on counsel for the Petitioners (Michael J. Tierney, Esq.) and the Respondents (Anthony J. Galdieri, Esq.).

/s/ Jason Sorens

Jason Sorens