The Tennessee Advisory Commission
on Intergovernmental Relations

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MEMORANDUM

TO: Commission Members

FROM: Cliff Lippard
Executive Director

DATE: 28 August 2025

SUBJECT: Education Finance Subcommittee

During the June 12, 2025, commission meeting, several members expressed concern with distortions in TACIR's fiscal capacity calculation caused by virtual school student counts, the effect of Greenbelt property assessments on fiscal capacity, and the fiscal capacity of counties with large tourism industries. Staff analysis came to the following conclusions:

- Including virtual school students in TACIR's fiscal capacity calculation can increase the fiscal capacity of a county that hosts a virtual school. Keeping all else the same, this decreases the fiscal capacity of the other 94 counties. Including virtual school students can also decrease the fiscal capacity of the host county, which increases the fiscal capacity of the other 94 counties. Whether a county's fiscal capacity increases or decreases depends on the effect of the virtual school students on that county's fiscal capacity variables. See figure 1. Consequently, the state share of funding and the local contribution can either increase or decrease for all counties.
- A decrease in residential or farm assessment in a county, because of Greenbelt or for any other reason, can increase or decrease the county's fiscal capacity as calculated by TACIR, so the effect on state funding varies across counties.
- Tourism can increase a county's fiscal capacity, which can decrease its state share funding percentage under the Tennessee Investment in Student Achievement Act (TISA).

As a reminder, below are the variables used in TACIR's fiscal capacity calculation.

Figure 1. Fiscal Capacity Model Components and Factors

Components		Factors
Local Revenue	⟷	Own-source Revenue per Pupil
Tax Base (Pupil Equity)	⟷	Taxable Sales per Pupil Property per Pupil
Ability to Pay (Taxpayer Equity)	⟷	Per Capita Income
Resident Tax Burden (Taxpayer Equity)	⟷	Ratio of Residential & Farm Assessment to Total Assessment
Service Responsibility (Pupil Equity)	⟷	Ratio of Average Daily Membership to Population
Methodology	⟷	Ordinary Least Squares Multiple Linear Regression
Output	⟷	Fiscal Capacity per Pupil

Distortions in Fiscal Capacity Caused by Virtual Student Counts

Virtual school students distort TACIR's fiscal capacity calculation, which can result either in an increase or a decrease in the fiscal capacity of counties.

For school year 2025-26, virtual school students

- decrease fiscal capacity through the local revenue and tax base variables because it increases average daily membership (ADM) in their denominators;
- increase fiscal capacity through the service responsibility factor because it increases ADMs in the numerator; and
- increase the multiple that is used to calculate total fiscal capacity for each county.

Virtual school students are counted as enrolled in the school system where the virtual school is located. TACIR's model normalizes based on ADM for the local revenue, sales and property tax bases, while the service responsibility variable is ADM divided by population. These students increase the host county's service responsibility variable—the number of public school K-12 students that the county has to serve as a percentage of total population. But when they don't reside in that county, their families don't necessarily contribute to the county's property or sales tax revenue—some of the other variables that determine that county's fiscal capacity.

The Department of Education does not have residency data for students. For the purposes of this analysis, commission staff reached out to the county with the largest virtual school—Union County—and found that nearly all of their 2,685 virtual students ADM do not reside in Union County.

Union County hosts the statewide virtual school with the highest number of ADMs, and the county's state share percentage of Basic Education Program (BEP) funding increased from 88.9% to 93.2% from school year 2017-18 to school year 2022-23. Similarly, Johnson County began hosting a virtual school in school year 2020-21, and the county's state share percentage of BEP funding increased from 80.5% that year to 90.2% in school year 2022-23. See table 1. There are multitude of factors that affect fiscal capacity and the funding formula, not just changes in the number of virtual school students.

Beginning in school year 2023-24, the TISA funding formula replaced the BEP. TISA provides base funding, weighted funding, direct funding, and outcomes funding. Only the base and weighted funding components are equalized using TACIR's and Center for Business and Economic Research's (CBER) fiscal capacity calculations. Direct and Outcomes funding are 100% funded by the state and are not equalized. Table 2 shows the change in the state share of funding after the implementation of the TISA funding formula. Since school year 2023-24, Union County's state share percentage of TISA funding has increased, but Johnson County's has decreased. As with the BEP funding formula, within TISA there are a multitude of factors that affect fiscal capacity and the funding formula, not just changes in the number of virtual school students.

Including the service responsibility factor in TACIR's model is worsening the distortion. This is because increasing a county's service responsibility by increasing the number of virtual school students can increase the county's fiscal capacity, not decrease it as expected. TACIR's staff report *A User's Guide to Fiscal Capacity in the Tennessee Investment in Student Achievement Funding Formula* said a potential change to TACIR's model could be to eliminate the service responsibility factor:

> The influence of the service responsibility variable—average daily membership divided by population—has decreased to the point where, in some years, it unintentionally increases fiscal capacity for counties with greater service responsibilities and decreases their state funding. Eliminating the service responsibility variable would eliminate this possibility.

Table 1. State Share of Total BEP Funding for Union and Johnson County Schools School Years 2017-18 to 2022-23

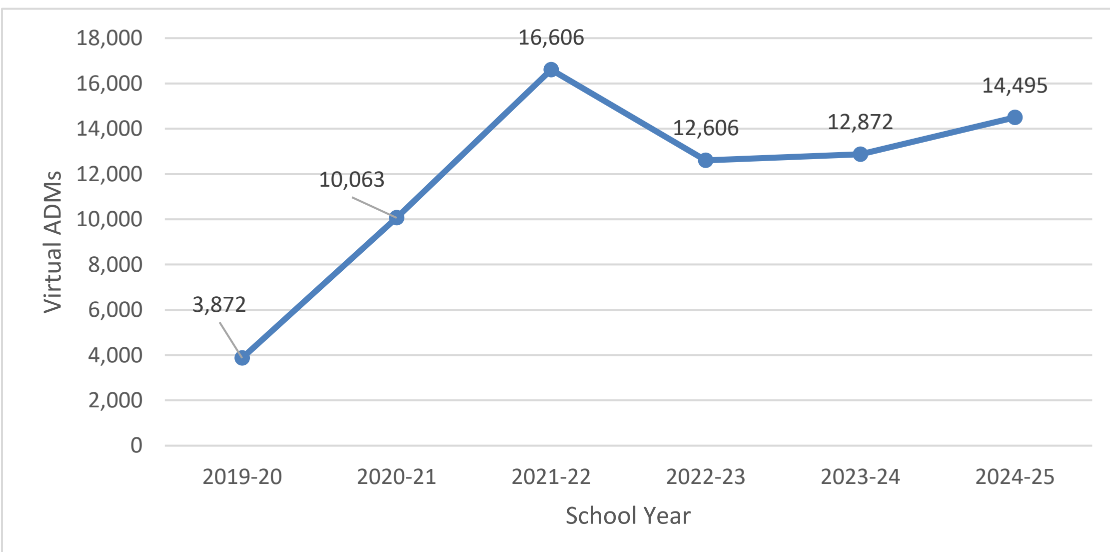
	Union		Johnson	
School Year	State Share	State Share (%)	State Share	State Share (%)
2017-18	$ 22,782,000	88.9%	$ 11,451,000	77.6%
2018-19	$ 26,313,000	90.0%	$ 11,942,000	78.6%
2019-20	$ 29,013,000	90.7%	$ 12,475,000	79.7%
2020-21	$ 31,275,000	91.4%	$ 12,706,000	80.5%
2021-22	$ 36,813,000	92.4%	$ 14,982,000	83.2%
2022-23	$ 43,230,000	93.2%	$ 29,061,000	90.2%

Table 2. State Share of Total TISA Funding for Union and Johnson County Schools School Years 2023-24 to 2025-26

	Union		Johnson	
School Year	State Share	State Share (%)	State Share	State Share (%)
2023-24	$ 46,982,813	94.0%	$ 38,551,259	93.2%
2024-25	$ 50,129,543	94.2%	$ 37,862,310	92.7%
2025-26	$ 49,847,444	94.3%	$ 40,130,819	92.8%

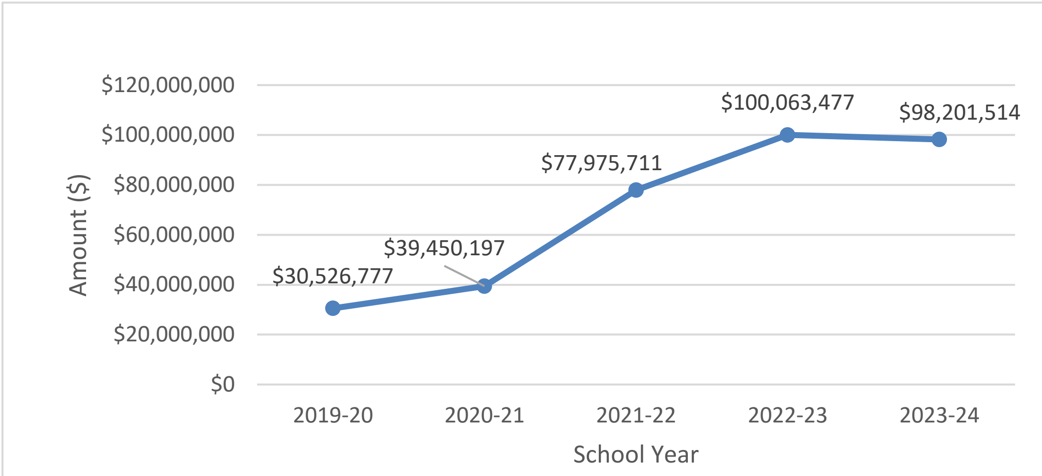
Average daily membership and, as a result, state funding have both increased for virtual schools in Tennessee. ADM in virtual schools increased from 3,872 to 14,495, from school year 2019-20 to school year 2024-25, while state funding of virtual schools increased from $30.5 million to $98.2 million from school year 2019-20 to school year 2023-24. See figures 2 and 3. By statute, virtual school students are not included when calculating infrastructure funding or the fast-growing district stipend.

Figure 2. Statewide Average Daily Membership (ADM) of Virtual Schools School Years 2019-20 to 2024-25



Source: Tennessee Department of Education.

Figure 3. State Funding of Virtual Schools
School Years 2019-20 to 2023-24



Source: Commission staff analysis of Tennessee Department of Education's Virtual Education annual reports. School year 2023-24 is the most recent data available.

The Effect of Greenbelt Property Assessments on Fiscal Capacity

Designating a farm or residential property as Greenbelt in a county can increase or decrease the county's fiscal capacity in Tennessee Advisory Commission on Intergovernmental Relations' (TACIR) model. This is because decreasing residential or farm property assessment, for Greenbelt purposes or for any other reason, decreases the county's property tax base and decreases residential and farm property as a percentage of total assessments. These two effects partially offset each other.

Property owners in Tennessee can apply for Greenbelt status to reduce the property taxes owed for that property. Once a property qualifies for Greenbelt status, it is assessed based on its current use—such as agricultural, forest, or open space—rather than its market value. This valuation approach not only supports land conservation and agricultural sustainability but also results in a lower property tax base for counties with large rural or agricultural areas.

Tennessee state law establishes three classifications of Greenbelt properties:

- Agricultural land: requires a minimum 15-acre tract used fully or partly for agricultural purposes and which may include woodlands and wastelands as part of the tract. If a landowner initially qualifies a minimum 15-acre tract, an additional tract of at least 10 acres will qualify if both tracts are being used as a farm unit. The land is assumed to be in agricultural production if the $1,500 annual income minimum is reached. Approximately 95% of Greenbelt valuations in Tennessee are for agricultural land.
- Forest land: requires a minimum of 15 acres of forest under a forest management plan. This may involve little more than an inventory of trees on the land and minimum management of the forest over time.
- Open space land: requires minimum of three acres excluding agricultural and forest land maintained as open space and "included within a plan for preservation approved by state or local planning agencies."

The use value is determined by state law and varies depending on land use (agricultural, forest, or open space) and the location of the property. Additionally, the extent of the acreage that qualifies under Greenbelt significantly affects the amount of tax savings realized.

In 2009, TACIR staff published a comprehensive report on the state's Greenbelt law. This report highlighted several significant issues with the legislation:

- The effect of the Greenbelt program on the local property tax base varies extensively from county to county, significantly reducing the tax base in many counties, and likely causing a combination of higher property tax rates and taxes on those property owners not enjoying Greenbelt valuations.
- The effect on property owners also varies extensively from county to county, with the greatest relative benefits accruing to landowners in urban and other high-growth areas where land values greatly exceed use values.
- Greenbelt land in some urban areas can enjoy valuations for tax purposes of less than 1% of market value.
- Rollback taxes, as currently calculated, do not in most cases reflect any consideration for the actual selling price of a parcel that was previously classified as Greenbelt eligible.

The 2009 staff report recommended the following options to address the identified problems:

- Limit agricultural, horticultural, husbandry, and forestry Greenbelt subsidies to those who actually depend on such activities for a significant portion of their livelihood rather than engage in them as a hobby.
- Establish a minimum valuation of Greenbelt eligible land equal to 10% of the county assessor's market valuation of the Greenbelt eligible land.
- Modify the existing rollback tax calculations to include interest on the calculated value of the tax subsidies enjoyed for the three years preceding the sale of the property.
- Modify the existing rollback tax calculation to include the sale price of the land in the year when sold, thereby including in the rollback calculations the only true measure of the likely value of the land in the past.
- Limit Greenbelt valuations for "open space" tracts to only land identified as having outstanding natural values, such as lands owned or identified for acquisition by the Nature Conservancy and similar organizations and lands with permanent conservation easements.
- Give county assessors the right to inspect properties for which Greenbelt status is requested to ensure that the tax-subsidized activity claimed is actually taking place every year.

Since the 2009 report was issued, none of these recommendations have been adopted.

Fiscal Capacity of Counties with Large Tourism Industries

Increases in tourism-related sales can increase a county's fiscal capacity and decrease state funding, all else being equal. Tourism generates significant tax revenue for state and local governments in Tennessee. In 2024, visitor spending in Tennessee generated $2.0 billion in state tax revenue and $1.3 billion in local tax revenues. Although other counties have significant tourism industries, tourism and tourism-related tax revenue is a larger part of the tax bases of Davidson and Sevier counties. See table 3.

Table 3. Davidson and Sevier, Tourism-related State and Local Tax Revenue Calendar Years 2022 to 2023

		2022	2023	Percent Change
Davidson	State	$ 612,555,100	$ 666,647,500	8.8%
	Local	409,141,700	444,447,300	8.6%
	Total	$ 1,021,696,800	$ 1,111,094,800	8.7%
Sevier	State	$ 241,941,400	$ 247,836,400	2.4%
	Local	173,864,200	182,429,300	4.9%
	Total	$ 415,805,600	$ 430,265,700	3.5%

Growing sales tax bases in these counties contribute to their fiscal capacities, though other variables contribute as well. Both Davidson and Sevier, over the last five years, have seen increases in their share of statewide fiscal capacity. See table 4. All else being equal, increases in fiscal capacity for a county decreases its state share of education funding.

Table 4. Davidson and Sevier Fiscal Capacity School Years 2021-22 to 2025-26

	2021-22	2022-23	2023-24	2024-25	2025-26
Davidson	17.4%	17.0%	17.4%	17.9%	18.6%
Sevier	2.7%	2.9%	3.0%	3.1%	3.2%

Previously, under the Basic Education Program (BEP) funding formula, a provision in state law established a floor for the minimum of nonclassroom funding that a school system could receive, 25%.[1] This had the effect of increasing the state share and decreasing the local share for Davidson and Sevier County schools. No such minimum is included in the Tennessee Investment in Student Achievement Act (TISA).[2] But TISA does hold harmless districts that fall below the BEP baseline—the last year of BEP funding—with the state funding a declining percentage of the difference through school year 2026-27, though neither Davidson or Sevier have received baseline funding. There is also a safety net that prevents more than a 5% decrease to the total TISA allocation.

For both Davidson and Sevier counties, the state share funding percentages were generally decreasing under the BEP from school year 2017-18 to school year 2022-23 (see table 5). Both counties saw their state share percentages increase the first year under TISA but decrease the second year (see table 6).

Table 5. State Share of BEP Funding for Davidson and Sevier County Schools School Years 2017-18 to 2022-23

	Davidson		Sevier	
School Year	State Share	State Share (%)	State Share	State Share (%)
2017-18	$ 300,621,000	46.8%	$ 39,031,000	38.7%
2018-19	$ 296,229,000	44.7%	$ 39,034,000	37.9%
2019-20	$ 296,257,000	43.5%	$ 39,733,000	37.6%
2020-21	$ 286,457,000	41.7%	$ 39,669,000	38.0%
2021-22	$ 268,628,000	39.9%	$ 40,917,000	37.9%
2022-23	$ 284,868,000	40.3%	$ 41,707,000	36.7%

Table 6. State Share of TISA Funding for Davidson and Sevier County Schools School Years 2023-24 to 2024-25

	Davidson		Sevier	
School Year	State Share	State Share (%)	State Share	State Share (%)
2023-24	$ 329,345,483	42.7%	$ 54,873,183	42.1%
2024-25	$ 339,096,744	41.7%	$ 52,910,019	38.8%
2025-26	$ 358,605,637	41.6%	$ 49,912,669	35.5%

[1] Tennessee Code Annotated, Section 49-3-307(12) (repealed): "Each LEA shall receive no less than a twenty-five percent (25%) state share in the nonclassroom components;"
[2] See Tennessee Code Annotated, Sections 49-3-105 and 109.

Included in the state share is direct funding, which is 100% funded by the state. Direct funding amounts for Davidson and Shelby are shown in table 7.

**Table 7. Direct funding for Davidson and Sevier County Schools
School Years 2023-24 to 2024-25**

	Davidson		Sevier	
School Year	Direct Funding	Percent of Total TISA Funding	Direct Funding	Percent of Total TISA Funding
2023-24	$ 32,939,827	4.3%	$ 5,237,532	4.0%
2024-25	$ 33,258,219	4.1%	$ 5,497,808	4.0%
2025-26	$ 35,336,704	4.1%	$ 5,656,195	4.0%