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## To What Extent Can a State Consider Federal Impact Aid When Distributing State Educational Aid?

by Jay E. Grenig

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### ISSUE

Did the secretary of education have the authority to create and impose a formula and certify New Mexico's operational funding for fiscal year 1999–2000 as "equalized," thereby diverting Impact Aid subsidies to the state?

### FACTS

The Zuni Public School District No. 89 is a New Mexico public school district located entirely within the Pueblo of Zuni Reservation. It has virtually no tax base. More than 65 percent of the Gallup-McKinley County Public School District No. 1 is Navajo Reservation lands that are not taxable by state school districts.

Under the Impact Aid Program (20 U.S.C. § 7709 et seq.) public school districts such as Zuni and Gallup-McKinley that are affected by a federal presence reducing ordinary bonding and taxing capacity are entitled to receive federal Impact Aid funding to offset this impact. The program allows states to take credit for the Impact Aid payments

by correspondingly reducing the amount of operational funding the state otherwise would provide the Impact Aid districts if the state can establish that state-provided operational funding for its school district is otherwise equalized. School districts are referred to as Local Educational Agencies or LEAs in the statute.

In October 1999, Zuni filed an objection to a certification made by the Department of Education that the state of New Mexico was equalized under 20 U.S.C. § 7709(b) and the corresponding regulations at 34 C.F.R. § 222.162. The certification allowed New Mexico to offset its contributions to local education agencies, including Zuni and Gallup, by a proportion of the federal Impact Aid payments made to those school districts. In November 1999, Gallup-McKinley filed a similar objection with the department, alleging that New Mexico had taken

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ZUNI PUBLIC SCHOOL DISTRICT  
NO. 89 ET AL. v. UNITED STATES  
DEPARTMENT OF EDUCATION ET AL.  
DOCKET NO. 05-1508

ARGUMENT DATE:  
JANUARY 10, 2007  
FROM: THE TENTH CIRCUIT

# Case at a Glance

Two New Mexico school districts sought judicial review of a decision by the secretary of the U.S. Department of Education certifying that New Mexico had an equalized program of state aid, thereby permitting New Mexico to factor in the receipt of federal Impact Aid funds when making its own distribution of educational aid to local public school districts. The districts claim they receive less revenue than they should have because the secretary used the wrong methodology in determining that New Mexico had equalized funding of public schools.

an inappropriate proportion of Impact Act funds into consideration when determining state aid, in violation of 20 U.S.C. § 7709(d)(1) and 34 C.F.R. § 222.163(a). The secretary denied the school districts' objections, and they appealed to the U.S. Court of Appeals for the Tenth Circuit.

Holding that Section 7709(b) was ambiguous, a three-judge panel of the U.S. Court of Appeals for the Tenth Circuit ruled that the secretary's construction of the statute was permissible and warranted judicial deference. The Tenth Circuit granted rehearing en banc before the full court. On rehearing en banc, the decision of the secretary was affirmed by an equally divided court. *Zuni Public School Dist. No. 89 v. U.S. Dept. of Education*, 437 F.3d 1289 (10th Cir. 2006). The U.S. Supreme Court granted the petitions of Zuni and Gallup-McKinley school districts for review. 127 S.Ct. 36 (2006).

## CASE ANALYSIS

Impact Aid is compensatory financial assistance paid by the United States to a school district whose ability to raise local revenues is limited either as the result of the real property within its boundaries being tax exempt due to the property's acquisition by the federal government or because the school district educates children residing on, or whose parents are employed on, federal property, including Indian lands.

Generally, states may not reduce state aid they provide to their school districts if the school districts receive Impact Aid. However, 20 U.S.C. § 7709(b) provides that if a state is certified by the Department of Education as having a program of state aid "that equalizes expenditures for free publication among local educational agen-

cies in the State," then the state is permitted to factor in the receipt of Impact Aid funds when making its own distributions of educational aid to the school districts.

The exception in Section 7709(b) first appeared in the Impact Aid laws in 1974. That statute (20 U.S.C. § 240(d)) used general language similar to that appearing in the current statute. However, instead of describing a disparity test, the 1974 statute expressly delegated to the secretary the power to define the term "equalize expenditures." As authorized by 20 U.S.C. § 240(d), in 1976 the secretary of education established an equalization formula by regulation outlining a disparity test. The regulations directed that a state would be deemed equalized if "the disparity in the amount of current expenditures of revenue per pupil for free public education among local educational agencies having similar grade levels in the state is no more than 25 per centum, as determined according to the procedures set forth in Appendix A to this subpart." Appendix A detailed the specific method by which to make the disparity determination. First, school districts were ranked by expenditures or revenues per pupil, and then those districts that fell "at the 95th and 5th percentiles of the total numbers of pupils in attendance in the schools of those [districts]" were eliminated. The 25 percent disparity comparison was then made between the remaining highest and lowest ranked school districts.

During the 1976 notice and comment process, the Department of Education responded to a question regarding whether the 95th and 5th percentiles were to be calculated based on the total number of pupils in the state or by school districts. The Department of Education stated:

The referenced percentiles are based on number of pupils. [The regulation] provides that in calculating the disparity standard according to the procedures set forth in Appendix A, the districts in a State will be ranked on the basis of current expenditures or revenue per pupil, and that those districts which fall above the 95th and below the 5th percentile of those agencies will be excluded for purposes of the calculation. The percentiles will be determined on the basis of numbers of pupils and not on the basis of numbers of school districts.

In 1994, Section 7709 was passed, repealing and replacing Section 240(d). Section 7709 specifically spells out the 25 percent disparity test and includes language setting out the basic parameters of the required 95th and 5th percentile determinations contained in the earlier regulations and appendix. The new language largely reiterated the disparity test and percentile determinations laid out in the earlier regulations and appendix. However, the percentile language in the 1994 statute differs from that in the earlier regulations. While the former appendix directed that the 95th and 5th percentiles should be calculated by "the total number of pupils in attendance in the schools to determine which LEAs to eliminate, the 1994 statute dictates that school districts "with per-pupil expenditure or revenues above the 95th percentile or below the 5th percentile of such expenditures or revenues in the State" should be disregarded. The legislative history of the 1994 legislation noted that the statute "prohibits a State from taking Impact Aid payments into account in determining the amount of State aid to be paid to LEAs that receive Impact Aid, unless that State has an equalization plan

approved by the secretary and describes the standard which state plans must meet.”

After the passage of 20 U.S.C. § 7709, the department enacted new regulations in 1994 replacing the 1976 regulations. The new disparity calculation language closely mirrors the language of Section 7709. 34 C.F.R. § 222.162(a). However, the regulation goes on to state in fashion similar to the 1976 regulations that “[t]he method of calculating the percentage disparity in a State is in the appendix to this subpart.” The appendix contains the same per-pupil expenditure ranking method that was outlined in earlier appendices, and it details the same specific methodology for calculating the 25 percent disparity test. The appendix directs that the determination of disparity be made by “[i]dentifying those LEAs in each ranking that fall at the 95th and 5th percentiles of the total number of pupils in attendance in the schools of those LEAs.”

The history accompanying the new regulation notes that the regulation outlines the single statutory standard for determining whether a state is equalized and “specifies the method the Secretary will employ to measure the statutory disparity standard.” In essence, the department has adhered since 1976 to a rule dictating that when disregarding school districts to determine whether a state is equalized, the 95th and 5th percentiles should be calculated by the total number of students in the state rather than by the number of school districts.

In determining whether New Mexico qualified in fiscal year 2000 (July 1, 1999, to June 30, 2000) as an equalized state under Section 7709, the Department of Education followed the methodology provided in the appendix to 34 C.F.R. § 22.162 to

decide whether school districts fell within the 95th and 5th percentiles of “the total number of pupils in attendance in the schools of those districts.” Applying this methodology to New Mexico, which has predominantly small school districts among its 89 public school districts, the department eliminated the 18 highest ranking and the seven lowest ranking before ascertaining that the newly top-ranked school district received only 14.43 percent more state funding than the newly bottom-ranked school district. The department concluded that New Mexico’s public school funding was substantially equal.

Zuni and Gallup-McKinley argue that they are entitled to receive federal Impact Aid payments without offset against their state operational funding because the state of New Mexico does not qualify for the Impact Aid exemption. They assert that the secretary’s methodology directly conflicts with the statutory language of 20 U.S.C. § 7709(b). The districts read the section as requiring the department to eliminate school districts on the basis of school district percentiles rather than by student population percentiles.

According to the school districts, the legislative and regulatory history shows how two Impact Aid formulas emerged—one authorized by the secretary and one authorized by Congress. Asserting that Congress changed the system in 1996, the districts say the 1996 changes eliminated the secretary’s authority to establish the equalization formula by creating a new and different equalization formula.

The districts contend that the 1996 legislation requires the secretary to disregard local educational agencies with per-pupil expenditures or revenues above the 95th percentile or below the 5th percentile. The school

districts argue that as a result of the 1996 legislation, the total number of students is irrelevant in determining percentiles of per-pupil expenditures.

It is the districts’ position that the two Impact Aid formulas are radically different. The districts reason that the statute requires exclusion of school districts whose per-pupil expenditures or revenues are above the 95th percentile and below the 5th percentile of per-pupil expenditures or revenues in the state. Declaring that there are established standard methods for making a percentile calculation, the districts assert that, when the objective is to calculate where the 95th and 5th percentiles fall along the area of school districts ranked by their per-pupil revenues, no consideration can be given to other factors such as pupil attendance numbers. Thus, the districts say the secretary’s injection of a pupil attendance factor into the calculation is plainly at odds with the statute. The districts suggest that the secretary arguably could have acted by regulation to require use of a particular one of the established standard percentile calculation methods, so long as the regulation did not require or permit the use of any data or factor beyond each school district’s per-pupil revenues in the calculation.

The districts contend that the first step in the secretary’s formula correctly ranks the school districts by per-pupil revenues. However, the districts contend the secretary improperly proceeds to eliminate school districts from the final field by excluding districts whose cumulative pupil attendance numbers are below the 5th percentile or above the 95th percentile of total pupil attendance numbers. By using a formula that eliminates school districts based on percentages of pupils instead of eliminating districts

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whose per-pupil revenues fall above the 95th percentile or below the 5th percentile (based on per-pupil revenues) the districts assert that the secretary excludes many New Mexico school districts whose per-pupil revenues fall between the 95th and the 5th percentiles of those school districts when ranked by per-pupil revenues. The districts conclude that the secretary's formula excluded 13 more school districts from the final list as to which the disparity test was applied, reducing that field to 66 from the 79 school districts as required by the statutory formula.

According to the districts, when Congress decided by statute in 1994 to establish the equalization formula, it rejected the Secretary's 1976 equalization formula. Had Congress wanted to capture the secretary's formula in the new statute, the districts say "the language was there for the taking." Instead, the districts assert that Congress took a different course. The districts say that the legislative history demonstrates that Congress chose to require the secretary to stop eliminating school districts based on pupil attendance numbers in making the equalization calculation and instead to eliminate school districts based on per-pupil revenues as specified in the statute. The districts claim that the secretary's method is not an interpretation of the statutory method.

Zuni and Gallup-McKinley argue that the secretary has no authority to substitute the secretary's policy choices regarding the proper impact and formula for those of Congress. They say that which method is deemed the most appropriate ultimately reduces to a policy choice about which anomalies and inequities are the most tolerable. The districts assert that Congress could have delegated this call to the secretary, but did not.

It is the districts' position that the secretary's 1995 Impact Aid formula was not promulgated as a regulation intended to have the force of law. They point out that, when the secretary promulgated the proposed regulations, the secretary announced a "Waiver of Proposed Rulemaking" and exempted the process from public notice and comment requirements. The districts note that the secretary said the new regulations "merely reflect statutory changes, remove unnecessary and obsolete regulatory provisions, reorganize and clarify the language of the regulations, and make minor revisions." Thus, the districts contend that the regulations do not establish or affect substantive policy.

The districts claim that the controlling rules on statutory construction forbid use of the secretary's formula. According to the districts, Congress has directly spoken by requiring use of a different formula. Because Congress's formula is clear, the districts say this should be the end of the matter. The districts argue that the plain meaning of the 1994 statute requires use of the statutory formula rather than the secretary's formula.

When a court reviews an administrative agency's construction of the statute it administers, the Supreme Court has ruled that if the intent of Congress is clear, that is the end of the matter. *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). If a court determines Congress has not directly addressed the precise question at issue and the statute is silent or ambiguous with respect to the specific issue, then the question for the court under *Chevron* is whether the administrative agency's answer is based on a permissible construction of the statute.

It is the districts' position that the secretary's formula is not entitled to *Chevron* deference. The districts explain that administrative implementation of a particular statutory provision qualifies for *Chevron* when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority. The districts stress that deference is not accorded merely because the statute is ambiguous and an administrative official is involved. The districts claim Congress did not give the secretary express authority to adopt a different formula. It also says the secretary has no implied authority to adopt a different formula.

Since the secretary's formula was not issued in exercise of rule-making authority, the districts conclude it is not entitled to *Chevron* deference. Furthermore, claiming the secretary's formula is inconsistent with the statutory formula, the districts say it cannot be a permissible administrative interpretation of the statute.

According to the respondents, the statute is ambiguous. They assert that when a law entrusted to an agency's administration is ambiguous, or when Congress implicitly or explicitly left a gap in the law to be filled in by the agency through the formulation of policy or rules, the courts must accept the agency's position so long as it reflects a permissible construction of the language in question. Because the statute mandates that expenditures or revenues be examined on a per-pupil basis, the respondents contend that the department's method of determining the 95th and 5th percentiles based on the total student enrollment in the state is a permissible construction.

## SIGNIFICANCE

If Zuni and Gallup-McKinley prevail in this proceeding, they and other similarly situated public school districts that receive Impact Aid may receive more revenue than they would under the secretary's formula. If the respondents prevail, public school districts that receive Impact Aid may receive less revenue. However, such a ruling may result in states having more funds available for distribution to all school districts—including those that do not receive Impact Aid.

Of broader significance is how the Court with its new membership will deal with the question of deference to administrative agency application of statutes. The Supreme Court has devoted considerable attention in the last five years in considering the varying degrees of deference deserved by agency pronouncements. See, e.g., *United States v. Mead Corp.*, 533 U.S. 218 (2001); *Christensen v. Harris County*, 529 U.S. 576 (2000); *General Dynamics Land Systems, Inc. v. Cline*, 540 U.S. 581 (2004); *National Cable & Telecommunications Ass'n v. Brand X Internet Services*, 545 U.S. 967 (2005); *Gonzales v. Oregon*, 126 S.Ct. 904 (2006).

## ATTORNEYS FOR THE PARTIES

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