

## Equity Center Testimony on the School Finance Commission Report

Presented to the House Public Education Committee

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First, we commend the Commission on the hard work and effort of members. The Commission was tasked with the difficult job of making recommendations that would move our school funding system forward toward one that is efficient, equitable and adequate for the task of providing the educational resources all our children need to become active and successful adults in a free and prosperous Texas. On the whole, what resulted is a compilation of recommendations that move our school funding system forward in a positive and necessary direction.

Our current system has become so inefficient and complex, there is no simple fix. It requires a massive overhaul and change of policy direction in order to meet Texas' future educational needs. To that end, the Commission Report proposes changes to the current system that will increase the efficiency of the way we fund public schools by putting the emphasis on creating a funding system based on known costs.

Moving to a system funded by current year values and collections is fundamental to ensuring state resources are delivered efficiently and directed at the known costs our system must address. This systemic shift changes our system of finance from one that is reliant on local fund assignments and outdated property values to one based on current tax collections—an accurate reflection of what districts can actually raise in a given year. This recommendation is a critical element necessary for any system to be efficient. Truly efficient use of the state's resources simply cannot be achieved as long as our system of funding remains based on data that is not current. That type of system will continue to reward some and punish others for no known cost-based reason, and the Commission was correct in recommending moving away from the inefficiencies (approximately \$1.8 billion) brought about by the use of prior year values.

The Commission correctly recommended the elimination of several other non-cost based elements of the current system (i.e. 1993 Wealth Hold-harmless, High School Allotment, differentiated Per Capita funding, etc.) The Commission also recommended additional imperatives to direct monies towards needs that will help us as we attempt to move resources to areas of greatest need and concern. Such recommendations as increased weighting for Compensatory Education, PreK-3<sup>rd</sup> grade funding for Compensatory and Bilingual/Dual Language students, and new funding to address issues for students with Dyslexia all work together to move our funding system in the right direction.

We appreciate the leadership, devotion of time and effort that Representatives Huberty, Bernal, and King, their staff and TEA staff have put into this endeavor.

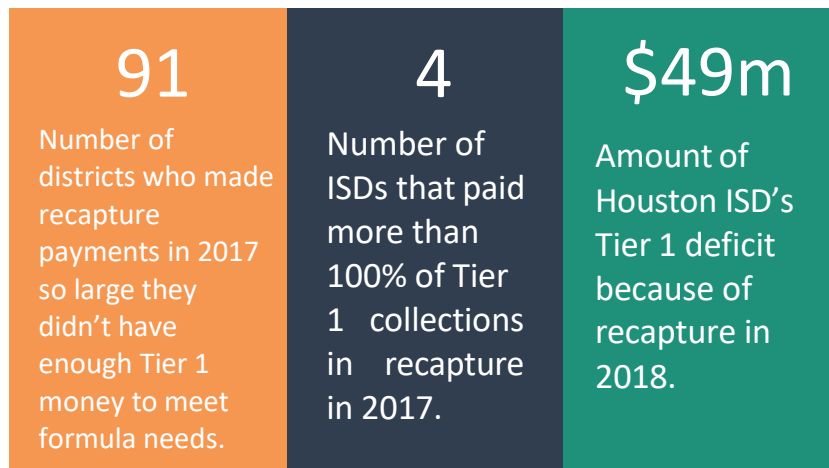
While as a whole, we feel very favorable toward the Commission's work and final report, there are some areas we think can still be improved to make the legislature's final work the best reflection possible of an efficient and equitable system.

Further Recommendations

- Finish moving the funding system to a single tier, single chapter system that funds all districts with the same formula for all pennies of tax effort. This eliminates the constant problems associated with funding for golden and copper pennies, transportation or not for chapter 41 districts, etc. It allows the legislature to create one formula that delivers the same known cost variables for every district regardless of wealth.
- Eliminate the current staff allotment and move the savings to the Basic Allotment or other cost-based elements—approximately \$140 million annually
- Change the current Local Option Homestead Exemption (LOHE) policy of funding 50% of the cost only for Chapter 41 districts with a LOHE to one that is consistent for both Chapter 41 and 42 districts with LOHEs. Either fund it for all districts or not at all, it is a “local option”—current non-cost based expenditure of approximately \$100 million annually
- Revisit and clarify Commission recommendations concerning the Small and Mid-size diseconomies of scale. If a diseconomy of scale exists, then it exists through all populations of students in that district. If it costs more because a district cannot fill each class in K-grade 4 with 22 students, then it follows that it also costs more to provide special education services, career and technology, etc., with smaller numbers of students.
- Reconsider the impact of the total elimination of the CEI as opposed to updating or moving to a newer recognition of those cost differentials
- Any successful attempt to effectively reduce local property tax rates must be governed by the following principles;
  - Effective and accurate tax compression requires the use of current year collections. The use of prior year values would leave tax compression subject to similar problems of inconsistency and inaccuracy that plague the current funding system.
  - Tax compression done correctly, must be on a statewide, not district by district basis. To do otherwise will over time, greatly increase taxpayer inequity.
  - Tax compression is most effective when applied to Interest and Sinking (I&S). Every dollar of additional state aid applied to I&S is automatic and sustained tax relief. Additionally, it is tax relief for fast growth districts that addresses the greatest cost they face, bonded debt acquired by building campuses to house new students.

## Conclusion

We have found that complexity, confusion, and inefficient funding elements preclude any systematic and meaningful determination of costs. The first step to addressing adequacy must be to eliminate all waste/inefficiency and simplify to the greatest extent possible. In other words, an adequate system is dependent upon an efficient system, based on state-identified costs and presented in an understandable manner.



The table above is from Governor Abbott's presentation title "Improving Student Outcomes and Maintaining Affordability through Comprehensive Education and Tax Reforms." There is some interesting information here, although, selective choices of data might be misleading.

For example, 2017 was a year in which property values for many districts rich in oil and gas either declined or did not grow as much as previous years. This would cause recapture to be uncharacteristically high and state aid to be low for school districts. This is not a recapture problem—it is the State's use of prior-year values and current year collections for determining local shares that create the problem.

To illustrate, let's look at 2018 data (the following year), the 91 recapture districts that "made recapture payments in 2017 so large they didn't have enough Tier 1 money to meet formula needs" drops to 37. That is because, again, this problem isn't caused by recapture. It is caused by the use of prior year values to calculate state aid and recapture.

In this same year, there were 275 low and mid-wealth districts *that were not recaptured at all in Tier 1* also received less money than their formula needs. Since these districts are not subject to recapture, changing recapture will do nothing to help these unfortunate districts. Again, recapture isn't the problem here. It is the use of prior year values and *it can affect any district, regardless of wealth.*

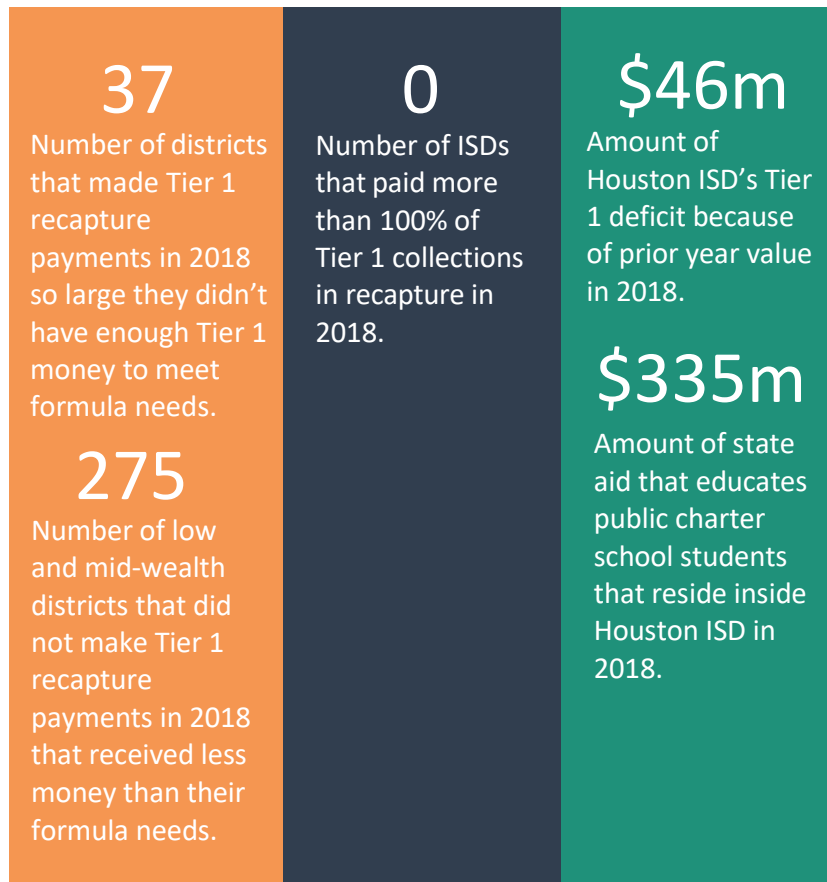
To further make the point, while there were 4 districts that paid more in recapture than they collected in Tier 1 taxes in 2017, but *ZERO* in 2018. This was due to the usage of prior year values to calculate state aid and recapture, as well as the volatility of oil and gas values. Something else not being told here is that these 4 districts, after recapture, all received *more funding* per WADA than 946 districts, averaging 42% more.

The report suggests Houston ISD had a Tier 1 deficit of \$49 million in 2018 due to recapture. The following information gives a more complete picture.

- First, the report shifts from 2017 data used for other comparisons to 2018. Actually, HISD did quite well in 2017. The reason for the deficit in 2018 is a once-in-a-lifetime, catastrophic flood that wiped out taxable value for the 2018 school year. Even so, this is not a recapture problem...it is a prior year value problem that could affect any school district, including those that are too poor to pay recapture.
- Second, this statement does not take into account the fact that HISD was given an adjusted ADA count that makes up for \$3,288,533.
- Third, this report does not mention the amount of state money that funds charter campuses inside Houston ISD boundaries. These public school campuses educate students who live in Houston ISD and whose parents pay Houston ISD taxes (that are being recaptured). The amount of state funding that goes to educate these students is about \$335 million. Any recapture paid by Houston ISD is coming back to educate students inside their borders, plus much more state aid.

- Fourth, while \$49 million sounds like a great deal of money, it is 3.4% of Houston’s Tier 1 allotment. Of all the districts in the state with a Tier 1 shortage, 23 have more than a 10% deficit. 13 of these are non-recapture districts. This is because the problem is not a recapture problem, it is a prior year problem.

Below is an updated chart with information to show more of a complete picture.



## **Making the Move from Prior Year Values to Current Year Collections:**

**Background:** The Foundation School Program was created to fund schools based on the best estimates of the cost of educating their students. The FSP is funded by a combination of what districts can raise locally and state aid. Historically, the state used prior year values because of technological limitations. Though we have the ability to use current data today, the current funding system still uses property values from the prior school year to estimate how much a district can raise locally, with state aid paying the remainder of that cost estimate. How much funding a district actually receives is a combination of that state aid and the amount they actually collect locally.

**Funding Guessing Game:** Using estimates based on prior year values creates a funding “guessing game.” When district values increase, the state overfunds the formula (entitlement) for the district and the district receives funding unrelated to its necessary costs. When district values decrease – or if a major taxpayer contests its values and withholds paying taxes – the state underfunds the formula entitlement and the district doesn’t have enough funding to meet basic needs. In both cases, no one really knows what their funding level will be from year to year. This makes budgeting and planning decisions difficult for districts and inefficient for the state. Estimates based on fluctuating property values – whether prior or current year – are just that: estimates. Moving to current year collections takes the guessing out of the equation. Districts will know with certainty the amount of funding they will receive – it will be exactly what they are entitled to through the formula system.

**Moving to Current Year Collections:** Districts build their budgets on projected tax collections. Districts use values received from the county appraisal district in the summer before the coming school year to project what their collections will be. With the use of current year collections, the need for the calculation of a district’s local fund assignment disappears. Therefore, the use of prior year values goes away. Using collections rather than values simplifies the budgeting process for districts and the state because funding is based on the district’s tax rate and actual collections for each year. Rather than the state putting billions of dollars toward unrecognized costs each biennium, they could better utilize those dollars by increasing the basic allotment, as is proposed by the Commission on Public School Finance.

The state can manage the change to current year collections in the same manner it handles student counts. The state already estimates school funding at the start of a year, and when the exact numbers are known at the end of the year, they use a process called “settle up” to adjust funding accordingly. District administrators already create budgets based on projected collections and will have good knowledge of what collections are out and what are expected to come in. Districts will know their funding level based on what the formulas guarantee them and the state makes up the difference when collections fall short, and when collections occur, the state recovers their money.

**Efficiency in Funding, Certainty in Budgeting:** The current system of funding based on prior year values guarantees certainty at the school district level only on state aid. Districts are never really certain what their funding will be. Moving to a system based on current year collections guarantees certainty on exactly what every district will receive – their formula entitlements – through the combination of state aid and local collections. Total funding will be based on recognized costs, not an arbitrary change in local property values. The only remaining uncertainty is the number of students, which will continue to be handled through settle-up when final counts are known.

Not only is moving to current year collections something the state is now able to do, it is something the state should do as it is a much more efficient way to determine district funding and a much more reliable way for districts to plan and budget accordingly each year.

**Fiscal Impact to the State:** Making the change to Current Year Collections allows the state to make a one-time adjustment of \$1.8 billion to put into the Basic Allotment, according to the Commission on Public School Finance report.

### Why Moving to Tax Collections rather than Prior or Current Year Values Works

Funding schools based on local tax collections results in great improvements in the funding system by:

- Eliminating the uncertainties that using property values -- either current or prior -- cause, creating the absolute certainty that every district will receive its formula entitlement: no more and no less
- Greatly improving the simplicity of funding formula
- Making the local district budgeting process dependent on tax rate and entitlement of funding through a single formula system for all
  - Tier 2 funding is already based upon current year collections
- Eliminating the budgeting and financing problems created by funding formulas based upon year old property values and the up and down relationship they pose with actual revenues available to the district in any given year
- Allowing districts to maintain consistent overall funding, even when major taxpayers contest their taxes and the district is unable to collect those taxes until subsequent years
- Dramatically increasing the overall efficiency of the state funding system every single year by allowing state revenues to flow to districts in the exact amount needed to fulfill formula funding entitlements for that year
- Avoiding the current funding problems caused for the state and local districts because of loss of access to funding entitlements because of declining property values and/or smaller rates of growth
- Allowing the state to consistently use the increased efficiencies to direct funding to address specific areas of need as determined by the state
- Eliminating the need for a local fund assignment in the formula
- Changing the funding formulas so they can focus on needed reform, not property values
- Relegating the use of prior year property values to an outside the formula practice employed by the Comptroller to fulfill its original purpose—the maintenance of a system of valuing property across the state that assures fair and consistent valuation practices among the various County Appraisal Districts for all local jurisdictions, not just school districts.
- Allowing any form of tax compression or statewide property tax reduction to work easily and seamlessly for all taxing jurisdictions. If we are to have legitimate tax compression, funding schools on year old data instead of current year collections, will work in direct conflict with the current ideas of reducing property taxes and will complicate and do harm to the budgeting and funding cycles for public schools.

**Relevant Timeline – District, County and Comptroller Property Tax & Budget Cycle**

**School District Cycle**

**January 2018**

**Spring 2018** - budget planning  
2018-2019 school year

**Summer 2018** – receive CAD  
values, project collections &  
student counts

Set budget

Set tax rate

**October 2018 – August 2019** –  
collect 2018 taxes

**September 2019** – TEA Settle-up

**County Appraisal District Cycle**

**Leading up to January 2018 and  
after** – set values

**Spring 2018** – sends out value  
statements, begins protest  
hearings

**Summer 2018** – delivers 2018  
tax roll to school districts

**October 2018 – August 2019**

**September 2019**

**Comptroller PTAD Cycle**

**January 2018**

**Spring 2018**

**Summer 2018**

**January 2019** – certifies  
preliminary 2018 results

**March-July 2019** – hears  
protests

**August 2019** – certifies final  
2018 PTAD values