

Confronting the Constitutional Challenges

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After a decade of relative calm, school finance is again at the top of the Texas legislative agenda. From 1989 through 1993, Texas policymakers were compelled to act by a series of legal challenges to the state school finance system that focused on considerations of *equity*, defined in terms of school districts' access to resources. Since that time, however, the increasing availability of data on student achievement has shifted the focus of litigation and policymaking in other states away from traditional considerations of equity and towards what is typically called *adequacy*, defined in terms of whether the financing of public education is sufficient to achieve the state's educational goals. Texas has not yet faced a serious adequacy challenge to its school finance system. However, a growing number of researchers, policymakers, and advocates for public education agree that the system could be vulnerable to such a challenge in the near future and therefore should be redesigned – or at least updated – so that it better complements the results that Texas public schools are expected to achieve.

One reason for concern about the adequacy of the Texas school finance system is that the state is in the process of substantially raising the bar for academic performance. Texas has begun to curb the practice of “social promotion” between certain grades and is entering the next phase of the testing and accountability system, including new high-school tests aligned with high-school curricular standards. The Recommended High School Program will become the default graduation plan for all students beginning with the class of 2008, and every Texas school will be accountable for closing achievement gaps among subpopulations of students as a result of *The No Child Left Behind Act of 2001*. Together, these policies will put a great deal of pressure on school districts whose fiscal capacity is already near the point of exhaustion. Already, nearly three-quarters of Texas public school students live in districts that levy property taxes at or near the statutory cap of \$1.50 per \$100 of valuation, meaning that their districts cannot draw down additional tax revenue or state aid. Experts agree that over time, the combination of higher standards and dwindling fiscal capacity will make the school finance system increasingly vulnerable to adequacy challenges. Therefore, the state might be better served to define, examine, and address educational adequacy *for itself*, rather than wait to have definitions and remedies foisted upon it by the courts.

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A desire to head off litigation provides only part of the motivation for school finance reform among Texas policymakers, however. In other states, traditional advocates for equity have pressed the question of adequacy, assuming that it would automatically entail considerably increased funding for public education. In Texas, however, it is *conservative* policymakers who have been the principal advocates for drawing a stronger connection between the financing and performance of public schools. As Senator Florence Shapiro (R-Plano), chair of the Senate Education Committee, argued last year:

A lack of resources should never be the reason school districts are not performing at the standards the Legislature sets. If it is, we are shortchanging our children.

This is an outcome none of us wants to see. A study to evaluate the components of a “thorough and efficient” system is an important first step in the school finance reform process. We already spend the equivalent of some states' entire budget on education. Don't we want to know how effective these dollars can be?¹

Traditional advocates for equity might be surprised to hear this argument from a leading conservative policymaker. The underlying idea, which is both novel and compelling, is that a school finance system linked to the state's educational goals might *not only* promote equity in terms of educational opportunities *but also* address a number of conservative concerns, ranging from doubts about the efficiency of the public education system, to opposition to the “leveling-down” mechanisms of “Robin Hood,” to a frustrating lack of evidence that large increases in funding for public education over the last several legislative sessions have produced commensurate gains in student achievement.

In this paper, I discuss the two major threats to the constitutionality of the current Texas school finance system and examine some of the implications of addressing these issues by constructing a system linked to the expected performance of the public schools. I begin with a brief overview of the current system, then discuss the challenges posed by dwindling fiscal capacity and a disconnection with the education goals of the state. I next provide a brief overview of the analyses required to estimate the costs of achieving the state's education goals. The approach I outline here would place Texas at the forefront among states that have tried to link the financing and performance of their public schools. It also poses new challenges, however, so I conclude by laying out some of the issues policymakers must grapple with as they design a results-based school finance system.

THE CURRENT SYSTEM

The current Texas school finance system is organized into three “tiers” of formulas that include adjustments and weights designed to offset additional costs of providing educational services in small and sparse school districts, in high-cost areas, and to

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students who require more intensive educational services. It also provides aid to help property-poor school districts service long-term debt for facilities. This system of formulas is called the Foundation School Program.

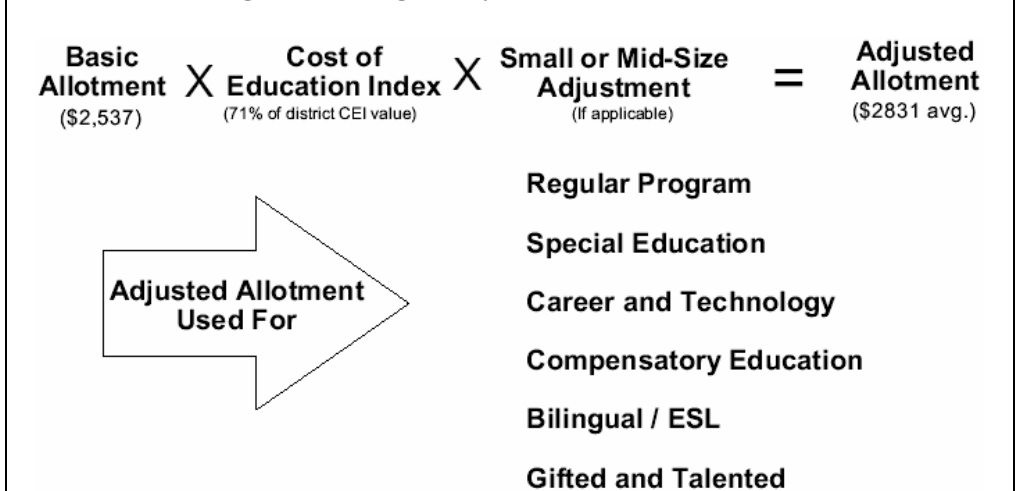
As Figure 1 illustrates, the calculation of districts' Tier 1 funding begins with the Basic Allotment, which is currently set at \$2,537 for \$.86 per \$100 of valuation of tax effort for school district maintenance and operations (M&O). The Basic Allotment is multiplied by the relevant weights and adjustments for each school district, such as the Cost of Education Index (CEI), the Small and Mid-Size District Allotments, the Sparsity Adjustment, and weights for students enrolled in special programs such as Special Education, Bilingual Education, and Gifted and Talented.

Figure 1.
Calculation of Tier 1 Funding

$$\begin{array}{r}
 \text{Tier 1 Allotments} \\
 \text{-Transportation} \\
 \text{-50\% of CEI} \\
 \hline
 \text{Adjusted Tier 1} \\
 \div \$2,537 \\
 \hline
 \text{Weighted ADA}
 \end{array}$$

Tier 2 funding, which pertains to districts' M&O tax effort beyond the first \$.86 per \$100 of valuation, is based on the number of students in Weighted Average Daily Attendance (WADA). WADA is calculated on the basis of a school district's Tier 1 allotments, as illustrated in Figure 2.²

Figure 2.
Calculation of Weighted Average Daily Attendance



The state currently guarantees districts a minimum yield on M&O tax effort beyond \$.86, up to a statutory limit of \$1.50, of \$27.14 per penny of tax effort per WADA. The third tier of the system, which pertains to tax effort for debt service (called I&S, for Interest and Sinking), does not interact with Tier 1 and Tier 2. Eligible school districts are guaranteed a yield of \$35 per penny of I&S tax effort, per student in unweighted average daily attendance (ADA). Not every district receives aid for debt service, however. The state sorts school districts by property wealth, then distributes aid starting with the poorest districts until funds appropriated for Tier 3 aid are exhausted.

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As in many states, the primary driver behind the creation of the system outlined above was litigation. Article VII, Section 1, of the Texas Constitution lays out the key terms in which the legal battles about Texas school finance have been fought over the last two decades.

A general diffusion of knowledge being essential to the preservation of the liberties and rights of the people, it shall be the duty of the Legislature of the State to establish and make suitable provision for the support and maintenance of an efficient system of public free schools.

The courts have consistently acknowledged that the Legislature has broad discretion to define the “general diffusion of knowledge,” while being more prescriptive about what it means to “make suitable provision for... an efficient system.”³ In ordinary usage, “efficiency” refers to a relationship between inputs and outputs, such as educational resources and student achievement. In school finance litigation, however, discussions of efficiency have focused almost entirely on the problem posed by the fact that Texas school districts have such widely varying tax bases, from less than \$12,000 per pupil in Boles ISD to more than \$3 million per pupil in Kenedy County Wide CSD. The Texas Supreme Court found in *Edgewood I* that an efficient school finance system requires “a direct and close correlation” between school districts’ tax effort and the educational resources available to them, up to the point that all districts have “substantially equal access to similar revenues per pupil at similar levels of tax effort.”⁴ In *Edgewood II*, the court determined that an efficient system need not be *absolutely* equal and that districts should be permitted to supplement their funding through local tax effort.⁵ Nevertheless, these two decisions suggest that districts’ access to revenues – at least to whatever point is necessary to achieve the constitutional mandate of a general diffusion of knowledge – must be substantially equal.⁶ That is to say, every school district must have more or less equal access to the resources required to provide some fundamental level of education.

The current system achieves “substantially equal access to similar revenues” by “leveling up” via the system of guaranteed yield on tax effort described above and by “leveling down” via a system of recapture. The Foundation School Program effectively guarantees every school district, regardless of the actual value of its local property tax base, access to revenues as if the value of its tax base were no less than \$295,000 per weighted student for the first \$.86 of M&O tax effort and \$271,400 for the next \$.64 of M&O tax effort. School districts whose local tax bases are valued at more than \$305,000 per weighted student, called the “Equalized Wealth Level,” are required to exercise one of five recapture options with regard to their M&O tax effort, which are outlined in Figure 3 on the next page. These options, often collectively referred to as “Robin Hood,” are described in Chapter 41 of the Education Code, so the approximately 134 school districts to which they apply are sometimes called “Chapter 41” districts.

Most Chapter 41 districts choose option 3 or option 4, which means that they share a portion of their M&O tax revenues with other school districts or with the state. The system provides incentives for districts to enter into agreements with Chapter 41 districts

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choosing option 4, which enables the districts to receive slightly more funds than they otherwise would receive. In recent years, many Chapter 41 districts have devised intricate methods of gaming this feature of the system, by requiring receiving districts to send some portion of the additional funds they receive to education service centers, juvenile justice programs, or even appraisal districts that serve the sending districts.⁷

On their face, options 3 and 4 of the Robin Hood system appear to violate a standard set in 1931 in *Love v. City of Dallas*, in which the Texas Supreme Court ruled that school districts may not be compelled to use local tax revenues to educate students who reside outside of their district boundaries.⁸ However, in *Edgewood IV* the court found that the Robin Hood system does not violate the standard set by *Love*, because while voters may choose to pay to educate students in other districts, albeit grudgingly, they are not strictly required to choose those options.⁹

It is important to note that the “Robin Hood” system only applies to part of school districts’ tax revenues. Specifically, recapture applies only to M&O tax revenue; it does not apply to tax revenue for debt service, or I&S, which means that property wealthy districts can have substantially more access to revenue for debt service. For example, Highland Park ISD in Dallas County has a tax base of more than \$1.1 million per pupil. For districts eligible to receive Tier 3 aid, however, the state guarantees the equivalent of a tax base of about \$350,000 per pupil for I&S tax effort up to \$.50 per \$100 of valuation. This sort of inequity notwithstanding, school finance experts agree that the combination of the guaranteed yield system and the “Robin Hood” system of recapture have made the Texas school finance system one of the most equitable

Figure 3. **Recapture Options**

Option 1: *Consolidation by Agreement.* School boards of two or more districts may agree to consolidate into a new district in which per-pupil property wealth is less than \$305,000.

Option 2: *Detachment and Annexation by Agreement.* School boards of two or more districts may agree to detach taxable property from one district and attach it to one or more other school districts, provided that the per-pupil property wealth for each of the districts involved, after the detachment and annexation, is less than \$305,000.

Option 3: *Purchase of Attendance Credits.* District may purchase “attendance credits” from the state to reduce their per-pupil property wealth below \$305,000.

Option 4: *Contract for Education of Nonresident Students.* Districts with per-pupil property wealth above \$305,000 may enter into agreements with other districts to pay the costs of educating students in that district. To provide incentives to districts to enter into such agreements, the state deducts the *average* entitlement from the receiving district’s state aid, and districts are permitted to keep any excess funds.

Option 5: *Tax Base Consolidation.* School boards of two or more districts may agree to conduct an election to create a consolidated taxing district for M&O of the relevant school districts that has a per-pupil property wealth below \$305,000.

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in the nation, particularly in terms of targeting funds towards property-poor districts.¹⁰ Although certain elements of the system have been adjusted, it has been relatively stable since it was enacted in 1993 and has survived multiple legal challenges.

Two major threats to the constitutionality of the system are imminent, however. Either of these challenges has potential to cast the state back into the uncertainty and expense associated with having the school finance system thrown out by the courts. In the next two sections, I will outline these two threats and offer a few suggestions for how the state might stave them off.

THE FIRST THREAT: DWINDLING FISCAL CAPACITY

The Texas school finance system is highly leveraged on local property values, because the vast majority of revenues for public education in Texas come from local school district taxes on residential and business property. In the current biennium, the state is expected to provide slightly more than 40 percent of revenues for public education, versus well over 50 percent from local property taxes.¹¹ State tax revenues for education include sales taxes, franchise taxes, lottery proceeds, fuel taxes, gas and oil taxes, “sin” taxes, insurance taxes, utility taxes, and the Available School Fund. Recapture funds from districts that elect to send property tax revenues directly to the state are also treated as state revenues. However, the state is prohibited from levying a state property tax by Article VIII, Section 1-e of the state constitution.

The issue of state versus local shares of revenues for public education has sometimes received a great deal of public attention. Discussions of this issue often neglect the major factors that affect the local/state ratio, however, implying that the state has simply failed to spend enough. For example, it is rarely noted that the current school finance system is structured so that the state must generally bear the increased costs associated with growth in student populations, because the state guarantees districts a minimum funding level per student, based on local tax effort. The cost of enrollment growth is substantial, because the Texas public education system adds approximately 70,000 students every year. Other things being equal, the school finance system needs about \$700 million each biennium in additional funds just to keep pace with enrollment growth.

Inflation has also affected the state share of spending for public education, although more indirectly than enrollment growth. In most sectors of the state economy, inflation has been modest in recent years. Nevertheless, many school districts have had difficulty keeping pace, particularly with the rising costs of health insurance. Over time, the state will increasingly be forced to confront the health insurance issue, due to the teacher health insurance program created by the Legislature in 2001. In general, local school districts, rather than the state, must bear cost pressures associated with inflation, however. The Foundation School Program contains no adjustment for inflation, and the formulas are rarely updated to reflect actual costs. Therefore, to deal with inflation, districts must cut spending or raise taxes and hope for additional appropriations – which Legislatures have tended to dedicate to particular programs or couple with new mandates.

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From 1995 through 2001, substantial increases in local property values allowed the Legislature to address these cost pressures by shifting an increasing share of the burden of paying for public education to local taxpayers. Given the structure of the Foundation School Program, increases in property values result in savings to the state, because less money is required to make up differences between guaranteed yields and local tax revenues, and because more recaptured funds are available to help underwrite the system. Since 1995, the property tax base in Texas has risen steadily at a rate sufficient to carry increased appropriations for public education, and legislators have become accustomed to counting on value growth to offset increased costs. As property value growth has slowed, however, the Legislature no longer has that luxury. A sharp decline in the total property tax base could be disastrous for the state budget.

The state economy seems to be improving steadily. Nevertheless, given the extent of program cuts required to address a nearly \$10 billion budget shortfall without major tax increases, a large infusion of state funds into the school finance system in the near future is unlikely – and could potentially be disastrous for the state if property values were to decline sharply, given the structure of the current system. Despite the severity of the budget situation, the 78th Legislature did manage to allocate \$1.2 billion in new funds to school districts, enough to ensure that every school district will receive \$110 per WADA in each year of the current biennium. In an important departure from recent practice, these funds were not earmarked for particular programs or for employee compensation. Nevertheless, while this infusion of funds will help keep the current system afloat for the short term, most districts are not well positioned for the long term. As mentioned above, the system implicitly relies on districts to cut costs or raise taxes. So it should come as no surprise that a majority of districts already tax at or near the statutory cap of \$1.50 and are unable to draw down additional state aid by increasing their M&O tax effort. This phenomenon is worrisome, because the Texas Supreme Court warned in *Edgewood IV* that if school districts were compelled to tax at the maximum M&O rate of \$1.50 to ensure a general diffusion of knowledge, the Legislature effectively would have set an unconstitutional state property tax.

However, if the cost of providing for a general diffusion of knowledge continues to rise, as it surely will, the minimum rate at which a district must tax will also rise. Eventually, some districts may be forced to tax at the section 20.09 rate of \$1.50 maximum allowable rate just to provide a general diffusion of knowledge. If the \$1.50 cap on tax rates were to become in effect a floor as well as a ceiling, the conclusion that the Legislature had set a statewide ad valorem tax would appear to be unavoidable because the districts would then have lost all meaningful discretion in setting the tax rate.¹²

To restate: even if the school finance system is both equitable in terms of ensuring substantially equal access to revenues and sufficient to ensure a general diffusion of knowledge, local school districts must have meaningful discretion to set property tax rates. Otherwise, the system is unconstitutional.

It is tempting to read this passage from *Edgewood IV* to imply that districts will have lost “meaningful discretion” to set tax rates when, *on the whole*, the \$1.50 cap has become a

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floor as well as a ceiling. In that case, a loss of meaningful discretion would be evidenced by large numbers of districts being forced to levy M&O taxes at \$1.50. This interpretation was suggested by the district court in *West Orange-Cove Consolidated Independent School District v. Alanis*, which noted that only 12 percent of school districts tax at \$1.50 for M&O without granting local option tax exemptions. However, the Texas Supreme Court recently disagreed with this interpretation, embracing a much more rigorous position, according to which the system would be unconstitutional if even *one* district were compelled to tax at the statutory cap.¹³ Given that large numbers of districts levy M&O taxes at the \$1.50 cap, the court's position raises serious questions about the constitutionality of the current system. Several of the largest Texas school districts have recently joined the *West Orange-Cove* litigation to press this argument.

Some advocates of the current system insist that the fiscal capacity problem could be addressed easily if only the state would put more money into the system. Substantial increases in state spending, they argue, would not only shift the responsibility for funding public education back towards the state but also renew the school finance system's fiscal capacity, especially if a large portion of the new funds were dedicated to forcing down local property tax rates. Tax compression could apply to all districts, or only to districts with some minimum level of tax effort. In any case, the strategy would be to provide districts with a higher guaranteed yield – or, for Chapter 41 districts, to allow them to keep larger proportions of local M&O tax revenues – on condition that they lower M&O tax rates by some specified amount. If the Legislature used the 1999 approach as a model, the level of this new guaranteed yield would most likely be set so that not all of the new state funds would be dedicated to tax relief, to give districts some relief from rising costs. In principle, such a strategy would enable districts to come out ahead in terms of available revenues, with lower tax rates.

Two caveats about tax compression: first, it is very difficult to engineer, because it requires a deep understanding of the school finance system, a sophisticated awareness of the cost pressures school districts face, and accurate predictions about school districts' taxing behavior. When the Legislature attempted to compress school districts' property tax rates in 1999, about a third of the districts ultimately adopted higher M&O tax rates. Second, even in the best-case scenario, compression provides limited relief to taxpayers, because most taxpayers will still pay higher property taxes due to increased valuation. In principle, compression means that the local tax burden will not increase as rapidly as it otherwise might have, because districts will lower or at least refrain from increasing tax rates. However, this idea provides limited consolation to taxpayers frustrated by high property tax bills. The Legislature could try to make it more difficult for districts to raise property tax rates – for instance, by requiring local elections – but this approach would not really resolve the core issue, which is that *the school finance system is increasingly funded by local property taxes levied at the statutory cap*. To provide substantial relief to taxpayers while adding capacity to the system to account for future cost increases, the Legislature would have to combine tax compression and high hurdles for raising tax rates with an enormous infusion of state funds. The current state tax system simply cannot generate the billions of dollars that would be required, however, given the current outlook for the state economy.

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Another possible approach, although admittedly one with less immediate power, would involve the creation of incentives for efficient school and district management. As I have discussed elsewhere, the fact that school districts tend to follow established traditions when allocating additional resources is a major obstacle to innovation.¹⁴ To counter this basic entropy in the system, the Legislature could establish incentives for schools and districts to adopt proven, research-based educational programs, to limit non-instructional spending, and especially, to experiment with more efficient compensation strategies, including performance-based compensation. At the state level, policymakers could also make the administration of public education more efficient by terminating ineffective and duplicative programs and by limiting major investments to proven, cost-effective programs. For the long term, for example, the Legislature might add evaluation requirements for statewide educational programs and initiatives similar to the “Sunset” requirements for state agencies. Every educational program in which the state invests, including teacher preparation programs, could be required to have clear, measurable goals linked to student achievement, to demonstrate progress towards meeting those goals, and to be evaluated periodically in terms of the return-on-investment to the state. Ideally, these evaluations would be conducted by a third party, would be subjected to external review, and would yield recommendations to the Commissioner of Education and to the Legislature for improving or terminating programs.

Suppose that, despite legislative efforts to force tax rates down and encourage efficiency, school districts continue to raise M&O tax rates, so that almost every district levies M&O taxes at or near the \$1.50 cap. Will the scenario that the Texas Supreme Court warned of in *Edgewood IV* have come to pass?

Not necessarily. On this point, two cases are especially worth noting. First, in *Edgewood IV*, the court did not precisely find that school districts levying taxes at the \$1.50 cap would make the school finance system unconstitutional. Rather, it found that “a floor as well as a ceiling” of \$1.50 *just to provide a general diffusion of knowledge* would be tantamount to a statewide property tax. This point was emphasized by the district court in its ruling against the plaintiffs in *West Orange-Cove*. In particular, the court implied that the Legislature has neither directly nor indirectly compelled districts to tax at the statutory cap.

The school districts are under no legal obligation to fund what they may believe necessary in their hearts for a general diffusion of knowledge. The school districts are only legally obligated to fund what the Legislature has determined in the accreditation standards is required for a general diffusion of knowledge.¹⁵

The district court’s ruling in *West Orange-Cove* was affirmed by the Third Court of Appeals, which emphasized that the core issue is not the number of school districts at or near the \$1.50 cap, but rather whether any district *must* tax at the cap. Although the state supreme court ultimately remanded the case to the district court, it made a point of stating

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that the responsibility for defining the requirements of “a general diffusion of knowledge” rests primarily with the Legislature. While districts are free to maximize their local M&O tax effort to provide educational opportunities beyond those required for a general diffusion of knowledge (i.e., state requirements), the state is not strictly obligated to facilitate local district officials’ or even local taxpayers’ preferences. It remains to be seen whether the *West Orange-Cove* plaintiffs can either demonstrate that any school district must tax at the cap merely to provide the level of education that the state requires or persuade the court that the Legislature’s specification of a general diffusion of knowledge is set too low to be constitutional under Article VII, Section 1. This second idea points to a second threat to the constitutionality of the current school finance system, which is its disconnection with the state’s educational goals.

THE SECOND THREAT: DISCONNECTION WITH THE EDUCATIONAL GOALS OF THE STATE

Like most states, Texas has not drawn a formal connection between its school finance system and the results its public schools are expected to produce. The current school finance system has worked reasonably well thus far in terms of ensuring that districts have equitable access to revenue at similar levels of tax effort, and Texas has made remarkable gains in student achievement in certain areas over the last decade. Nevertheless, it is unclear whether the system is sufficiently funded, alone distributed appropriately, to sustain the next round of education reform. As Texas continues to ask more from its public schools, discussions about school finance will increasingly focus on the fundamental question of what it means to make “suitable provision” for the general diffusion of knowledge. In this section, I outline two ways that the state might address this question.

Before we can connect the financing of schools to the results they are expected to achieve, we must specify the level of education that the state is required to provide. Given that the Legislature has broad discretion to define the general diffusion of knowledge, as well as the power to assign the administration of public education to entities like the State Board of Education, the Texas Education Agency, and local school districts, statutory law should arguably serve as the primary authority on this matter.¹⁶

A general articulation of the state’s educational goals may be found in the opening sentence of Section 4.001, Subtitle A, Title 2 of the Education Code, which specifies some of the liberties and rights alluded to in Section 1, Article VII of the constitution.

The mission of the public education system of this state is to ensure that all Texas children have access to a quality education that enables them to achieve their potential and fully participate now and in the future in the social, economic, and educational opportunities of our state and nation.

Chapter 4 goes on to define nine objectives for public education, which begin to link this

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general mission to particular means for enabling Texas children to achieve their potential to pursue social, economic, and educational opportunities.

- OBJECTIVE 1: Parents will be full partners with educators in the education of their children.
- OBJECTIVE 2: Students will be encouraged and challenged to meet their full educational potential.
- OBJECTIVE 3: Through enhanced dropout prevention efforts, all students will remain in school until they obtain a high school diploma.
- OBJECTIVE 4: A well-balanced and appropriate curriculum will be provided to all students.
- OBJECTIVE 5: Qualified and highly effective personnel will be recruited, developed, and retained.
- OBJECTIVE 6: The state's students will demonstrate exemplary performance in comparison to national and international standards.
- OBJECTIVE 7: School campuses will maintain a safe and disciplined environment conducive to student learning.
- OBJECTIVE 8: Educators will keep abreast of the development of creative and innovative techniques in instruction and administration using those techniques as appropriate to improve student learning.
- OBJECTIVE 9: Technology will be implemented and used to increase the effectiveness of student learning, instructional management, staff development, and administration.

These objectives are abstract and hortatory, and for the most part only introduce issues to be addressed later in the Education Code. It is not clear, for instance, which personnel should count as "qualified and highly effective," nor is it obvious what it means to demonstrate "exemplary performance in comparison to national and international standards." Section 4.002 begins to describe the purposes of public education in more concrete terms, however, by laying out four goals that invoke the accreditation standards defined in Section 39.072.

- GOAL 1: The students in the public education system will demonstrate exemplary performance in the reading and writing of the English language.
- GOAL 2: The students in the public education system will demonstrate exemplary performance in the understanding of mathematics.
- GOAL 3: The students in the public education system will demonstrate exemplary performance in the understanding of science.

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GOAL 4: The students in the public education system will demonstrate exemplary performance in the understanding of social studies.

These goals suggest a high standard. If “exemplary performance” is defined in terms of state accreditation standards, then less than 29 percent of Texas schools met this standard in 2002.¹⁷ These four goals also raise the uncomfortable possibility of a reduction of the state’s educational goals to standardized test scores in four subject areas. Of course, the state constitution does not refer to competence in particular subject areas, but rather to the broader purposes of ensuring that Texas students are able to pursue “social, economic, and educational opportunities.” This tension between the state’s reliance on standardized testing and the general purposes outlined in the constitution is worrisome, because as critics of the state accountability system rightly argue, test scores by themselves are poor proxies for individual opportunity and democratic citizenship.

The Texas Supreme Court seems to agree that it could be inappropriate to reduce the state’s educational goals to test scores, if the tests in question were poor measures of a general diffusion of knowledge. In *Edgewood IV*, for example, the court warned:

This is not to say that the Legislature may define what constitutes a general diffusion of knowledge so low as to avoid its obligation to make suitable provision imposed by article VIII, section 1. While the Legislature certainly has broad discretion to make the myriad policy decisions concerning education, that discretion is not without bounds.¹⁸

So while the Legislature has considerable freedom to specify the educational goals of the state, its discretion is not so broad that it could set standards that are too low to enable Texas students to pursue social, economic, and educational opportunities, *regardless of how equitable the system was*. That is to say, even if every school had equitable access to the resources necessary to provide every student with some basic level of education, the system could *still* be unconstitutional.¹⁹ The public education system as a whole must also meet a certain threshold of suitability. The court reinforced this position in *West Orange-Cove*, adding that the state’s obligation to make suitable provision extends not only to districts’ ability to provide an accredited education as defined by the Legislature, but also to districts’ ability to ensure a general diffusion of knowledge – two binding requirements which could, but might not be, aligned. The authority to determine when either or both of these requirements has been satisfied rests with the courts.

In many respects, the Legislature, working with the State Board of Education, the Texas Education Agency, and local school districts, has arguably stepped up to the challenge of defining and administering a suitable public education system. Consider the following:

- The Texas state curriculum, the Texas Essential Knowledge and Skills, which was adopted by the State Board of Education in 1996, is considerably more rigorous

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than its predecessors, to the point that state standards in certain subjects (e.g. advanced mathematics courses), are aligned with Advanced Placement standards.

- The new state test, the Texas Assessment of Knowledge and Skills, is better aligned with the state curriculum and will test a broader range of objectives and grade levels than the Texas Assessment of Academic Skills. Field test scores indicate that TAKS will be considerably more challenging than TAAS.
- In 2002, the state began to issue “Gold Performance Acknowledgements” to schools that met higher performance standards, including measures of how many students performed to higher levels than simply “passing” state tests.
- In 2002-03, Texas will begin to implement curbs on social promotion, starting with third graders and eventually including fifth and eighth graders.
- Beginning with the entering class of high school freshmen in 2004, the default high school graduation plan will be the State Board of Education’s Recommended High School Program.
- The state has implemented statewide initiatives that include advanced training for teachers in reading and mathematics, which this year will be expanded to include science.

In practice, each of these elements has certain limitations and could stand to be improved. For example, the state curricular standards are admittedly weak in certain areas, such as computer science, and both the TAAS and the TAKS have justifiably been criticized for not measuring the depth of students’ knowledge so that parents and teachers could know whether their children are ready for advanced work. These issues notwithstanding, it is striking that policy discussions about public education in Texas tend to be more about the *specification and implementation* of these elements than about the principles on which they are based. This consensus is remarkable and, given the stable history of education reform in Texas over the last two decades, easy for Texans to take for granted. As noted above, however, drawing a direct connection between school finance and what schools are expected to achieve will require policymakers, educators, and the general public to revisit fundamental questions about the sort of education required for a general diffusion of knowledge. Ideally, the outcome of these deliberations will be clearer specifications of the end goals for public education, in other words, of what Texas expects its public schools to accomplish.

Once the state has settled on an appropriate specification of the general diffusion of knowledge, there are two basic strategies for connecting school funding to the state’s educational goals. The first would involve the creation of a system of direct financial incentives for improving student achievement.

Choosing the right performance standard is the first of two essential steps towards financial incentives for student achievement. Arguably, this standard should be *value-*

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added, to reflect aspects of student performance that cannot be explained away by the characteristics of the students served. We are rightly more impressed by exemplary schools that serve large numbers of poor students than by exemplary schools in which most of the students come from wealthy families. It is also important that performance awards not serve as disincentives to teach disadvantaged students. Finally, performance standards for schools and districts should include analyses of their relative efficiency. Schools and districts that are better able to transform resources into gains in student achievement should be rewarded for doing so. I will return to this issue below.

The second step towards effective performance incentives is to identify the appropriate target: districts, schools, principals, teachers, or perhaps even students. Policy discussions of performance incentives in education generally focus on schools, principals, or teachers. School-based performance rewards, for example, have the advantage of encouraging teamwork. Awards to principals recognize the importance of good leadership. Awards to teachers are attractive as a strategy for overcoming the traditional disconnection between teacher compensation and teacher quality, and are bolstered by compelling research indicating that in general, no single factor matters more to student achievement than effective teaching.

Given the problems inherent in identifying high-performing individuals on the basis of a limited set of outcome measures, a two-level approach to performance incentives may be more appropriate. Instead of a statewide system of performance incentives for teachers, principals, or perhaps even schools, the state might provide grants to districts to develop and implement performance incentive systems that include a few key components. For example, the state might provide matching funds to districts to encourage them to dedicate a substantial portion of any funds for salary increases to performance incentives. This approach would maintain local control and encourage innovation while still allowing the state to control costs and set some broad parameters for implementation. For instance, districts could be required to submit data on their local performance awards systems, and TEA could be required to compile and distribute information about effective practices.

A statewide system of incentives would be more appropriate for school districts. Again, these incentives should be based on a value-added measure, as opposed to the current system of accountability ratings. Some “exemplary” schools and districts achieve that status without adding as much value as schools and districts rated “acceptable.” Performance awards for school districts should also be based at least in part on analyses of their relative efficiency. For example, each year the state could publish a predicted per student expenditure level for providing a level of education consistent with the state’s educational goals. These predicted spending levels could be based on analyses of three-year averages of every school district’s expenditures and results in terms of student performance, coupled with analyses of the expected costs of new requirements. At the end of each school year, districts that met or exceeded performance expectations while spending less than expected levels could then receive a financial award equivalent to some portion – perhaps 50 percent – of the difference between projected and actual expenditures, as a reward for efficiency. Texas is one of the only states with sufficiently

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rich data on the financing and performance of its schools to enact such a system. Although it would admittedly require technical expertise to establish, the results would be easy to communicate to the public. And, best of all in tight budget years, such a system of incentives would actually *save* the state money.

In the next section, I describe a more long-term strategy for linking the financing and performance of Texas public schools, by aligning the formulas with the educational goals of the state. This realignment would require a thorough analysis of schools' and districts' performance to identify "best practices," which could then be used to construct formulas that would ensure sufficient levels of funding.

ESTIMATING THE COSTS OF PUBLIC EDUCATION

School finance experts have attempted to link the financing and performance of states' public schools using four approaches, each of which offers a different perspective. These approaches are described in Figure 4.

Figure 4. **Methods of Evaluating Education Cost**

- *The statistical or econometric approach.* This approach uses statistical analyses of data on school and/or district spending and performance to infer the cost of producing certain results. It can include statistical controls for the characteristics of students and districts and can be used to generate data about school district efficiency. It is similar to the approach used to construct the Texas cost-of-education index and was applied in part in the Dana Center's study of methods for adjusting district funding to reflect uncontrollable cost variations.²⁰
- *The successful schools approach.* This approach starts by defining a level of performance, such as accountability ratings of "exemplary," then examines the average expenditures of schools or districts achieving the desired results.
- *The professional judgment approach.* This approach relies on focus groups of educators to design model schools or districts that incorporate "best practices" with regard to management and instruction. Prices of the various elements of the model schools and districts are then estimated using statistical approaches, including adjustments for student and district characteristics.
- *The comprehensive school reform or effective practice approach.* This approach examines the level of resources expended by schools and districts either to implement whole school reform models, such as Success for All/Roots and Wings, or in more recent iterations, to implement various research-based practices. The price of producing certain levels of student achievement is inferred to be equal to the price of implementing programs that have been proven to improve student achievement.

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Researchers can use any of these approaches alone or in combination to estimate the costs of producing results that reflect the educational goals of the state. In most states, “adequacy studies” have used the successful schools approach or the professional judgment approach. For example, in 1995 in Ohio, John Augenblick and John Myers applied the successful schools approach to estimate the basic costs of public education – before any cost adjustments were applied – at \$3,930 per student. This approach has since been applied in Illinois, Mississippi, New Hampshire, Maryland, and Kansas. In 1997 in Wyoming, James Guthrie and Richard Rothstein used the professional judgment model to estimate the resources needed to run prototypical elementary, middle and high schools. Per student costs for the model elementary school were estimated at \$6,165 per student. This approach has since been applied in Wisconsin, Oregon, Minnesota, South Carolina, Maryland, and Kansas. Statistical approaches have been used more in academic research than in legislative reports, with the exception of the cost-function analysis in the Dana Center’s study of uncontrollable cost variations in Texas.

Each of these approaches has certain strengths and limitations. In some cases, decisions about which approaches to use have been driven by the availability of data. In Wyoming, for example, the professional judgment approach was deemed to be the only available option because of limited data on the financing and performance of the state’s public schools. These decisions can also be more principled, however. Advocates for the successful schools approach, for example, argue that averages of existing patterns of school or district expenditures are preferable because they are easier for policymakers and the general public to grasp. Similarly, advocates for the professional judgment approach and the comprehensive school reform/effective practices approach argue that they provide a clearer picture of what district officials could buy with the funds they receive. It is important to note, however, that these approaches generally achieve transparency by avoiding questions about how various uncontrollable factors, such as regional cost differences and differences in the students served, influence the costs of education. In the case of the successful schools approach, for example, the use of averages masks the extent to which a state’s current finance formulas influence school and district spending. To compensate, researchers who apply this approach typically include adjustments derived in other studies in their recommendations, although doing so arguably compromises the putative transparency of the approach.

In Texas, rich data on the financing and performance of public schools enables researchers to use more sophisticated approaches to test standard hypotheses about the connections between school finance and student achievement – analyses that would be impossible in most states. These analyses can then be used to create a new school finance system that is sensitive to a wide range of factors that are beyond the control of school district officials, including geographic cost differences, differences in students served, and variations in population density. Besides offering the advantage of Texas-specific analyses of cost differentials, this approach allows researchers to examine the relative efficiency of schools and districts. This would be a major advance. To date, none of the adequacy studies conducted in other states have included estimations of the efficiency

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and productivity of schools and districts. In Texas, policymakers could for the first time draw on analyses of the *cost-effectiveness* of schools and districts.

Besides providing information about how to align the school finance formulas with the educational goals of the state, analyses that examine schools' and districts' efficiency and productivity could be useful in two respects. First, the findings could be used to establish financial incentives for districts as described above. Second, an examination of the budgeting and resource allocation practices of these schools and districts would help researchers identify and describe cost-effective practices for addressing particular challenges, such as dropout reduction or increasing the number and diversity of students completing advanced courses, such as those required for the Recommended High School Program. Regardless of the approach used to determine adequate levels of funding for Texas schools and districts, however, it is important to note that *different conceptions of the general diffusion of knowledge will most likely result in different cost estimates*. It is advisable for policymakers to request analyses using several different specifications of the state's educational goals. A collection of such analyses could provide information about the marginal costs of producing higher levels of achievement on different kinds of outcome measures, and together could provide information about the potential costs of raising standards.

LOOKING TO THE FUTURE OF TEXAS SCHOOL FINANCE

Texas school districts serve an incredible diversity of students in an extraordinary range of circumstances. One strength of the current system is that it incorporates adjustments for many of these uncontrollable factors, from differences in the prices that districts must pay for teachers, to the effects of district size, to variations in the intensity with which schools must use their resources to serve students in different kinds of programs. A statistical/econometric analysis like the one described in the previous section would provide policymakers with detailed information about how to include cost adjustments for factors like these in the next school finance system. For example, like the current system, although not necessarily via a system of weighted students, the next Texas school finance system should account for variations in the costs associated with educating different kinds of students to levels of performance that are consistent with the educational goals of the state. In particular, students who live in poverty, who need accelerated programs, who have limited proficiency in English, or who are in special education programs tend to be more expensive to educate than other students, and the school finance system should account for these costs. Adjustments for inflation and for advanced high school courses might also be warranted and should be examined. In the end, which adjustments are included and in what manner will depend on how the state's educational goals are specified in statute and reflected in practice. But regardless of the adjustments included, it is important to recognize that *the system that the analyses would recommend would not necessarily be more or less complex than the current formulas*. The complexity of the next Texas school finance system is ultimately more of a policy decision than a technical matter. From a structural standpoint, the next system might even strongly resemble the current system, although hopefully with more accurate cost adjustments, as well as mechanisms for keeping the formulas up to date.

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Regardless of its structure, a school finance system based on analyses like the ones described above will require a new set of criteria for evaluating its integrity. As discussed above, the primary driver for school finance reform in Texas over the last two decades has been successful litigation focused on considerations of equity defined in terms of the availability of resources. Therefore, the tests that experts standardly use to evaluate the system have focused on six equity measures, collectively known as the “safe harbor.” As usually described, these measures are listed in Figure 5.

The first three indicators, which purport to capture the key features of the system at the time that it withstood the plaintiffs’ challenge in *Edgewood IV*, are regarded as the principal equity measures and are included in the Legislative Budget Board’s equity analyses. The next three are based on the court’s recommendations in *Edgewood IV*. The fourth measure was substantially addressed in 1999 by Senate Bill 4 (76th Legislature), which added the third tier for districts’ I&S tax effort. The fifth was discussed above. The sixth measure refers to the court’s warning that the system would be unconstitutional if the cost of providing a general diffusion of knowledge were to rise to the point that a district could not meet its operational and facilities needs within the equalized program.²²

Figure 5. The Safe Harbor

1. 85 percent of the students in the equalized system (i.e. in districts eligible for Tier II aid).
2. \$600 maximum per-pupil revenue gap between the wealthiest and the poorest districts at \$1.50 tax rate for M&O.²¹
3. 98 percent of the revenue in the system equalized.
4. Debt service for facilities included in the system.
5. School districts retain meaningful discretion to set local property tax rates.
6. Sufficient funds available to districts to meet Chapter 39 accountability requirements.

In principle, a school finance system linked more directly to the educational goals of the state would shift the primary focus away from traditional equity considerations like these and toward considerations of whether the system provides sufficient resources to ensure a general diffusion of knowledge. As the district court recently found in *West Orange-Cove*, school districts are only legally obligated to fund what the Legislature has rightly determined as being required for a general diffusion of knowledge. And from the state Supreme Court’s point of view, it appears that the Legislature’s obligation to ensure that districts have substantially equal access to revenues extends only up to the point necessary to achieve the constitutional mandate of a general diffusion of knowledge.

It is important not to underestimate the significance of this shift in perspectives. Equity in terms of access to resources can be described *more or less independently* of the results that schools are expected to achieve. In contrast, a results-based system starts from a

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description of the state's educational goals, then identifies levels of resources required to achieve them. An absolutely equitable system might not be adequate to achieve the state's educational goals; likewise, a school finance system sufficient to ensure the general diffusion of knowledge might not be equitable. Depending on how they are framed, considerations of equity and adequacy may complement each other, but in principle, *neither is a necessary condition of the other*.

This idea has two critical implications for Texas policymakers. First, it will be important to specify the standards by which the new system will be evaluated. I would argue that there should be two sets of measures, based on the notion that the system should be *suitable* and *efficient*.

- *Suitability*, in this context, implies that the system must ensure that districts have sufficient funding to meet Legislative mandates in terms of educational results. When the state raises standards, policymakers should derive accurate cost estimates and fund the schools accordingly. Unfunded mandates are directly counter to the spirit of a system that makes suitable provision for a general diffusion of knowledge.
- *Efficiency* refers to the equity standards established in the *Edgewood* cases. Assuming the current methods of finance for the school finance system are maintained, then at least up to the point required for a general diffusion of knowledge, the Legislature must ensure that districts have substantially equal access to similar revenues at similar levels of tax effort. Furthermore, the Legislature must take care to ensure that substantial amounts of property are not insulated from taxation. These principles suggest that to the extent that the system is funded via local property taxes, some combination of guaranteed yield and recapture might be inevitable, at least up to the point that districts can achieve the educational results required by the state.

What should happen beyond the point of tax effort required to provide the level of education required by the state? This question points to a second critical implication of the shift towards aiming at a suitable and efficient school finance system, which is that beyond the level of funding required for a general diffusion of knowledge, equity becomes more a policy matter than a constitutional question. In other words, *beyond a certain point, decisions about equity properly shift from the courts to the Legislature*.

For the short term, this idea implies that the process of designing a school finance system designed around the state's educational goals will most likely exacerbate rather than eliminate tensions evidenced in policy discussions about the Robin Hood recapture system. As I noted above, the Robin Hood system is primarily a mechanism for "leveling down" spending, the primary beneficiary of which is not property-poor districts but the state. Beyond whatever point is required to ensure that districts have substantially equal access to the resources required for a general diffusion of knowledge, the recapture system primarily functions as a method of finance for the school finance system. The court's ruling in *Edgewood IV* notwithstanding, it is conceivable that some future court

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would reject the notion that the state is permitted to require a small number of property-wealthy school districts to underwrite a substantial part of the public education system. At some point, an argument to this effect will probably be made, framed in terms of whether an extended system of recapture in the context of a results-based school finance system violates the standard established in *Love*.

Policy deliberations about how to resolve these issues will raise deep questions about fairness and opportunity, and their outcome will be of critical importance to the future of Texas. Traditional advocates for equity will argue that access to revenues should approach absolute equality. Advocates for property-wealthy districts will argue that they should not be hobbled in their ability to spend, nor should they be compelled to underwrite so much of the costs of the system. But in the end, the right question for policymakers to ask is clearly not how little the state can constitutionally get away with, but rather to what extent the accident of geography should determine the educational opportunities available to the children of Texas.

ENDNOTES

¹ Senator Florence Shapiro, “The \$26 billion question? The true cost of education,” *Austin American Statesman*, November 1, 2002.

² WADA = Tier 1 allotments, minus the Transportation Allotment and 50 percent of the effects of the CEI, divided by the Basic Allotment (see Figure 2).

³ On this issue, see *Mumme v. Marrs*, 40 S.W. 2d 31, *Edgewood Independent School District v. Meno*, 917 S.W. 2d 717 (Edgewood IV), and most recently, *West Orange Cove Consolidated Independent School District v. Alanis*. The Legislature’s discretion is not without bounds, however. See *Edgewood IV* at 463n8 and 470.

⁴ *Edgewood Independent School District v. Kirby*, 777 S.W.2d 391 (Edgewood I) at 397.

⁵ *Edgewood Independent School District v. Kirby*, 804 S.W. 2d 491 (Edgewood II) at 500.

⁶ *Edgewood IV* at 464.

⁷ See J. Jacobs, “Richer School Districts Find Ways to Share Less,” *Austin American-Statesman*, Thursday, March 7, 2002. See also the Legislative Budget Board’s report, “Regional Education Service Centers and Wealth Equalization ‘Option 4’ Arrangements,” available at http://www.lbb.state.tx.us/Education/Public/ESC_Report_0402.pdf.

⁸ *Love v. City of Dallas*, 40 S.W. 2d 20.

⁹ *Edgewood IV* at 472.

¹⁰ On this issue, see “The Funding Gap: Low-Income and Minority Students Receive Fewer Dollars,” The Education Trust, August 2002.

¹¹ The federal government provides approximately 9 percent of funding for Texas public education.

¹² *Edgewood IV* at 471.

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¹³ See 107 SW3d at 578, 579.

¹⁴ “Advancing Teacher Quality Through Performance Pay,” paper and presentation to the Lone Star Foundation, *Public Education Reform in Texas: A Comprehensive Progress Report*, Austin, Texas, December 7, 2000. Available online at <http://www.utdanacenter.org/bios/hkeller.html>.

¹⁵ *West Orange-Cove Consolidated Independent School District v. Alanis*, 2002 WL 534582.

¹⁶ *Edgewood IV* at 463n8 clearly states that the Legislature has broad discretion to establish a suitable regime for ensuring the provision of a general diffusion of knowledge.

¹⁷ Article III of the General Appropriations Act incorporates similar goals into the standards of achievement for the Texas Education Agency.

¹⁸ *Edgewood IV* at 463n8.

¹⁹ On a related note, Justice Cornyn explicitly warned in *Edgewood IV* that the state would be vulnerable to future legal challenges if districts were not able to provide a general diffusion of knowledge – as reflected in the academic accountability system – within the equalized school finance system. This idea opens the door wide to considerations of adequacy.

²⁰ See C. Alexander, et al., *A Study of Uncontrollable Cost Variations in the Costs of Texas Public Education*, November 1, 2000. Available online at www.utdanacenter.org.

²¹ On this point, advocates for property-wealthy school districts argue that the *Edgewood IV* court actually rejected the \$600 gap standard in favor of a standard based on tax rates necessary to provide the general diffusion of knowledge. That point notwithstanding, the \$600 gap is still used as a standard equity test.

²² *Edgewood Independent School District v. Meno*, 917 S.W. 2d 717, 1995.