

Offering a Fair and Rational Strategy for Achieving Real Equity and Adequacy

A Proposal for Distributing New State Funding in a Way That Will Provide Adequate and Equalized Educational Funding for All Texas Children

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OVERVIEW

This proposal focuses on the way new state resources, when available, can be distributed so that all Texas children, over time, will have access to similar resources for their education. The method addresses the concern that, for reasons totally unrelated to differences in the costs of providing educational services, there are numerous specific areas in which the current system arbitrarily fails to fund some schools as well as it does others. *Ironically, every school district experiences the negative impact of one or more of the components of this phenomenon, although some districts are affected to a more significant degree.*

First priority – meeting the growing costs of the current system. The first priority for new public education funding would, of course, be to maintain the current system, including enrollment growth and other areas of increased cost to the state. Whatever new money is available after that would be divided into two equal portions for *adequacy* and *equity*.

Adequacy – increasing funding levels across the board. The first half of the remaining money would be distributed to all school districts through increases in the Equalized Wealth Level (EWL), Additional State Assistance (ASA), Basic Allotment (BA), and Guaranteed Yield Level (GL) in such a manner that any two districts with the same tax effort, *irrespective of wealth status*, would receive the same increase in revenue per Weighted Average Daily Attendance (WADA). ASA was enacted in 2001 as a means of including Gap districts in across-the-board funding increases.

This new funding would allow all districts to counter the impact of inflation and to meet new state mandates, higher accountability standards, and growing community expectations.

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Equity – eliminating funding disparities. The second half of the remaining new money would be used to move all districts to a common funding level by removing funding disparities in a way that would ensure that *every district would gain revenue, and those that have the least would gain the most.*

Proposals for Eliminating Existing Disparities

1. **Establish a uniform yield for all districts.** School districts receive the bulk of their Maintenance and Operations (M&O) funding based on a variety of levels of “yield” per WADA for each penny of tax effort. There is, in effect, a per-penny per-WADA yield for all of Tier 1 (except transportation and one-half of Cost of Education Index, or CEI), Tier 2 is a traditional “guaranteed yield” component, and Chapter 41 districts’ effective yields are reflected in the amount of the Equalized Wealth Level (EWL) – or, in some cases, a “hold-harmless” EWL. Every district should have access to a uniform yield that is at a high enough level to provide for quality education. Until such time as a better measure can be determined, that yield should be set at the average yield available to Chapter 41 districts. *That means that all Chapter 42 districts and more than two-thirds of Chapter 41 districts will benefit from this proposal.*
2. **Fully fund the Transportation Allotment for every Chapter 41 district.** The Transportation Allotment of every Chapter 42 district is fully funded. Chapter 41 districts obviously have transportation costs, but with a few exceptions their Transportation Allotments are not funded at all because of the way recapture is calculated. The Transportation Allotment of every district should be determined the same way and should be fully funded.
3. **Extend the full benefits of the CEI to Chapter 41 districts.** Chapter 42 districts receive the full benefit of the CEI adjustment in Tier 1 while Chapter 41 districts receive only half the benefit, again because of the way recapture is calculated. Chapter 41 districts should benefit from the CEI to the same extent that other districts do.
4. **Extend the Mid-size District Adjustment to Chapter 41 districts.** Chapter 41 districts are not eligible for the mid-size district adjustment, although they experience the same diseconomies of scale that Chapter 42 mid-size schools do. They should receive this funding.
5. **Equalize the impact of ASF Per Capita distributions.** Most Chapter 42 districts never see their Available School Fund (ASF) per capita money because the state uses it to help pay the *state’s share* of the district’s Tier 1 allotments. Chapter 41 districts, on the other hand, get all of their per capita funds – in addition to the amount of tax revenue they retain after recapture. Chapter 42 districts should be treated the same as Chapter 41 districts. Their per capita funds should be *in addition to – not included in –* their Tier 1 allotments.

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6. **Eliminate Set-Asides.** Chapter 42 districts lose part of their Tier 1 state aid to set-asides. Chapter 41 districts are not subject to set-asides, yet all Chapter 41 districts receive services financed by set-asides, and some receive grants for programs funded by set-asides. These services and programs should be funded through direct state appropriations, and set-asides should be eliminated so that each district receives its full allotments.

How the Distribution of Equity Funds Would Be Determined

A funding target would be established for each area of disparity, in most cases simply by using the best funding practices of the current state system. By comparing each district's level of funding with the target for that area, a per-WADA deficiency for that area can be determined. The total of these deficiencies for the individual areas would be the difference between where a district currently is funded and where it should be funded. The Equity portion of the new state funding would be dedicated to erasing this deficiency by distributing the money to the districts in proportion to the amount of their deficiency.

For example, a district with a \$1 million deficiency would get twice the benefit as a district with a \$500 thousand deficiency. This practice would send the most new money (per WADA per penny of tax effort) to the districts currently receiving the least. It will also ensure that *every* district has a stake in eradicating the disparities until true and complete equity is achieved.

By removing these funding disadvantages, Texas can move to a system that recognizes real costs and ensures that all districts have fair and equal access to the state's resources. And, the state can achieve this while allowing those districts currently funded at more advantageous levels to retain more of their M&O tax collections.

Summary

Funding for Adequacy: One-half of all new state funding in a given biennium (after the current system is maintained) should be dedicated to raising the Basic Allotment, Guaranteed Yield, and Equalized Wealth Level so that each district's increased benefit (per WADA and after allowing for disparities in tax effort) is the same.

Funding for Equity: The remaining half of new state funding should be dedicated to erasing the funding disparities, listed above, in a manner that would ensure that new money would go to all districts in proportion to the deficiencies in their current funding levels.

Notes:

1. There are a few Chapter 41 districts with very low M&O tax rates because their Equalized Wealth Levels (EWLs) are held harmless at a level substantially in excess of the standard EWL. We believe these districts are quite capable of increasing revenue on their own, without exhausting limited new resources. For that reason alone, this policy recommends that any Chapter 41 district which is funded at a level above the standard EWL *and* whose M&O tax rate is below \$1.20 not receive any additional benefit under this plan. Those districts that would currently be excluded from benefit are still listed in

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the accompanying report since their tax effort in the future cannot be determined at this time.

2. Texas must remain committed to current equity standards. In the unlikely event that the implementation of the above proposals results in failure to meet those standards, the proposals should be altered as needed to maintain the standards.
3. The state should also give consideration to eliminating certain discrepancies between current funding levels and the true cost of providing relevant services. The following proposals deal with some of the most serious cost discrepancies:

- a. **Correct known deficiencies in transportation and district size adjustments.** Since the transportation allotment is much less than it should be for virtually every district (determined by comparing a district's actual transportation expenditures to its transportation allotment), transportation allotments should be increased across-the board, pending the development of a fair and rational transportation formula. (For purposes of illustration the Equity Center has developed an impact model, in which transportation allotments are uniformly increased by 50%.)

The two district size adjustments (i.e., the small and mid-size adjustments) should be increased to levels indicated by generally accepted research findings. By correcting these adjustments in conjunction with updating the CEI (see 8, below), some of the reductions in funding caused by the new CEI might be offset by increases caused by the new size adjustments.

- b. **Update the CEI.** The state's CEI statistical model has not been updated since 1989. The Dana Center developed several versions of an updated CEI in preparation for the legislative session in 2001. The Legislature did not adopt any of the Center's alternatives. It is clear from the Dana Center's work that the current CEI no longer reflects the realities of uncontrollable geographic cost differences across the state. (For purposes of illustration, the Equity Center has developed an impact model which uses the Dana Center's Salary and Benefits Index (SBI)).

PROTECTING CHILDREN FROM STATE VALUES AND GETTING ALL PROPERTY ON THE ROLLS AT ITS TRUE VALUE

Equity Center Plan

Under the terms of the Equity Center's proposed legislation:

1. School districts are always assigned County Appraisal District (CAD) values, known as "local" values, for state funding purposes, regardless of the results of the annual Property Value Study (PVS) conducted by the Comptroller's Property Tax Division (CPTD). CPTD values are statistical estimates, called "state" values.

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2. CADs are required to reappraise all property at least once every two years. Similar to the training requirements for school board members and administrators, CAD board members and chief appraisers are required to attend annual training as prescribed by the Board of Tax Professional Examiners.
3. CPTD continues to conduct its annual PVS, but the study covers *all* categories of property, and the same degree of accuracy is required for all categories. The CPTD is provided the additional resources needed to achieve those results. The study continues to recognize that a school district's state value falls within a range (as opposed to being absolute) by establishing a fair and appropriate margin of error.
4. *Although the school district is always assigned local values for school funding purposes, if the local value for the same school district (after the CAD appeals the state value for the district) falls below the margin of error for two years in a row, the CAD board of directors is required to appoint a master from a group of appraisers certified for this purpose by either the Texas Association of Appraisal Districts or the Board of Tax Professional Examiners, whichever is deemed appropriate. Resulting costs are borne by the appraisal district. (Section 5.102(c) of the tax code already authorizes the Comptroller to appoint a "special master" in cases where noncompliance with generally accepted appraisal standards and practices continues to occur.) Under this scenario, the CAD has the same right to appeal an adverse study finding to district court as does the school district under present law.*
5. The master remains in charge of the CAD until the tax roll is certified in the year that follows the first time the CPTD assigns local values for all districts. During the time the master is in control of the CAD:
 - a. The CAD's board of directors and chief appraiser remain in place in an advisory capacity.
 - b. The master is authorized to set and control an operating budget of up to 2% of the prior year's combined levies of all entities served by the appraisal district. The budget may exceed 2%, but only with a majority vote of the board of directors. Each taxing entity in the county is assessed for its share of the cost in proportion to its share of total tax collections.
 - c. Current appeals processes remain in effect, except as modified by item 8, below.
6. Confidential sales disclosure is mandatory for all real estate transactions. The disclosure is certified by all parties to a sale and includes all information needed to determine whether the sale is an arms-length transaction. The original certified disclosure is filed with the deed in the County Clerk's office, and copies are forwarded to the appropriate CAD and to the CPTD.
7. If an industrial or commercial taxpayer chooses not to render all or some of its personal property by April 15, the taxpayer retains the right to appeal the value assigned by the CAD but is denied attorney's fees arising from an appeal in district court. CADs are given audit authority to verify taxpayers' renditions, similar to the power the Comptroller has to audit business records for sales tax purposes.

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Background/Discussion

Under current law, school districts and other taxing entities levy taxes on values that have been appraised by their CADs.

All property within a CAD must be reappraised at least once every three years. The CAD's proposed appraised values are generally mailed to taxpayers in May and, following an appeals process, the CAD certifies the appraisal roll, generally by July 25th. The CPTD then conducts its PVS within each school district to determine whether the values set by the CAD are in compliance with state law.

Simply stated, the PVS is a statistical analysis based on a random sample of sales, supplemented when necessary by CPTD appraisals. The resulting state value is then compared with the CAD's local value. If the local value falls within a "margin of error" of plus or minus 5% of the state value, the school district is assigned local value for school finance purposes. If the local value lies outside the 5% margin of error, the district is assigned state value.

Every superintendent is acutely aware that if state value is assigned, and if it is greater than local value, the school district loses state funds (or its recapture increases) – even though the values set by the CAD are largely beyond the control of the school district.

Unfortunately, because of cost factors and inadequate data, the Comptroller's PVS does not include all categories of property, and it does not provide equally accurate estimates for the categories that are included. For Industrial Real and Industrial Personal property, the CPTD simply accepts local values. As to Commercial Personal property, for example, the state's weak rendition requirements and the lack of local and state audit powers make it virtually impossible for either the CADs or the CPTD to determine the true value of that property.

In addition, the lack of mandatory sales disclosure in Texas limits the accuracy of both CAD appraisals and CPTD estimates of the value of residential and commercial real estate. The predictable and typical result of these kinds of shortcomings in the system is that substantial amounts of taxable value are not reflected in CAD appraised values.

SIMPLIFYING & IMPROVING FACILITIES FUNDING

Proposed Enhancements and Refinements of Facilities Funding:

1. Do not reduce or eliminate Instructional Facilities Allotment (IFA) funding until and unless Existing Debt Allotment (EDA) is revised to guarantee the same or greater benefits to the lowest wealth districts.
2. Automatically roll EDA forward. This is necessary so districts can honestly inform taxpayers what their Interest & Sinking (I&S) tax rate for proposed new debt will be. The delay of state participation until the following biennium (biennium lag) can be handled by structuring a district's repayment schedule so as to minimize the

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amount due in the current biennium. (If this proposal is adopted by the Legislature, but 5, below is not, the Equity Center will publish a guide to assist member districts in setting I&S tax rates in the second year of a biennium so as to maximize state EDA assistance in the next biennium.)

3. Set the yield for IFA and EDA (currently \$35/ADA) at a level at which at least 85% of all students (ADA) will be in the equalized system. This is already the equity standard adopted by the state for M&O purposes (the Guaranteed Yield Level for Tier 2 is set so that 85% of all WADA are included in Tier 2). It appears the \$35/ADA level currently captures about 85% of ADA, so adhering to the 85% standard for facilities will not (at this time) increase state cost.
4. Set the equalized tax rate for EDA at not less than 29 cents, and do not make any part of the rate subject to the availability of surplus funds.
5. Calculate the state's share of EDA each year based on the actual bond payments due, rather than on the amount of I&S tax collections in the second year of the prior biennium. Because operating costs are not fixed amounts, the state uses prior M&O tax collections for appropriations purposes simply as a method of controlling the state's share of operating costs. Unlike operating costs, bond payments are fixed amounts which the state can ascertain and use for appropriations purposes without concern about controlling for unknown factors.
6. Determine the state's share of an IFA or EDA independent of the source(s) of a district's local share, so that once the state's share is determined, the state sends that amount to the district and the state's responsibility (and involvement) ends. The district may then choose any state-authorized local funding source(s) for its share and will not be penalized for being a good steward of the public trust by being efficient with the public's money.
7. Authorize a district to use for its local share of an IFA or EDA the following sources, in addition to the sources already authorized: interest on investments, penalty and interest on delinquent taxes, and excess I&S collections from *any* prior year (i.e., not just 1999-2000 and after, as in current law).
8. Allow a special I&S tax for maintenance/renovation projects with *one-time* voter approval. Districts should be allowed to incur *ongoing* debt – under EDA, with an annual payment not to exceed \$350 per ADA (which is what a 10¢ I&S tax rate for Tier 3 districts at the current \$35/ADA yield). The bond proceeds could be used for maintenance/renovation expenses such as re-roofing, replacement of floor covering, and asbestos removal, as well as equipment related to heating, air conditioning, water, sanitation, and electricity.
9. Adjust IFA and EDA formulas to ensure that a decline in a district's ADA does not cause an increase in the district's I&S tax rate. That rate should not change from year to year except to reflect increases or decreases in actual debt payments. The

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ADA adjustment under Section 42.005 is rationally related to operating expenses because operating expenses can be adjusted downward following repeated ADA declines. Debt payments, on the other hand, are fixed amounts that cannot be reduced when ADA declines. Section 42.005 therefore does not provide an appropriate adjustment for IFA and EDA purposes, especially when a district's ADA declines continuously over a number of years.

10. Extend to EDAs the same first claim on state funding for schools that IFAs already have. This will assure continuation and reliability for state facilities funding throughout the life of districts' financing issues.
11. Authorize the Commissioner of Education, possibly subject to consultation with legislative leaders, to resolve adverse unintended consequences of new law until the Legislature meets again.

Background/Situation

Over the past several years, the legislature has made significant progress in helping Texas school districts fund facility construction and renovation. Aside from two rather limited grant programs in 1991 and 1995, all state participation in school district debt for facilities prior to 1997-98 was limited to that portion of a district's debt service that could fit within the \$1.50 maximum effective tax rate for state funding in Tiers 1 and 2. The full burden of a district's additional bond payments fell upon the local taxpayer.

Beginning with the 1997-98 school year, in a significant shift in policy from awarding one-time grants to funding long-term debt obligations, the state established the IFA. The IFA covers both voted bonds and lease-purchase agreements.

Beginning with the 1999-00 school year, the state began equalizing old (existing) bonded indebtedness (other than IFA) by means of the EDA. This program, like the IFA program, guarantees districts a yield of \$35 per ADA. The EDA is not applicable to lease purchase agreements and will not provide state assistance for any debt for which taxes were first levied after 2000-01 unless the legislature rolls the EDA forward when it meets in 2003.

There is some anticipation that the legislature will continue to roll forward the EDA each regular session to cover new debt. But there is no guarantee. Thus, a district cannot know whether its new debt will be covered by EDA. If the new debt is not covered, and the district does not qualify for IFA funds, the district must be ready and able to fund its new debt with additional I&S taxes outside the equalized debt system, or with state Tier 1 funds, which would then not be available for M&O purposes.

Furthermore, there are two features of current law that force a district to choose between either losing state facilities funds or imposing a higher I&S tax rate than is actually needed. In both cases, certain local funds that can legally be used to pay debt are not taken into account by the state when it calculates the state's share of an IFA or EDA. In the first case, the state disqualifies the other local funds involved from being considered

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part of the district's local share of an IFA or EDA. In the second case, the state recognizes the relevant other local funds as local share, but disqualifies those funds from being considered in the determination of the limit of state EDA assistance in the coming biennium. In either case, the prudent approach for the district is to impose whatever I&S tax rate it takes to earn the full state share of the district's debt, even though the rate could be lower if other legally applicable funds were used to meet all or part of the district's local share. The resulting excess I&S tax rates are unfortunate by-products of current law.

All things considered, under the current state system, revenue available to districts for construction or renovation varies widely. Access is very limited for those districts not eligible for IFA and with tax bases too limited to support new debt without assurance of EDA coverage. At the other extreme, the richest Chapter 41 districts have access to virtually unlimited facilities funds, since I&S taxes are no longer subject to recapture (due to a special exception the Legislature granted in 1997).

GUARANTEEING THE GUARANTEED YIELD PROTECTING AGAINST DECLINING TAXABLE PROPERTY VALUE

Proposed Legislative Action:

Due to the extraordinary potential damage to affected school districts in the absence of corrective action, the Legislature should enact the following provisions without delay:

1. If a district that has experienced a decline in value from the prior year sets its M&O tax rate at the legal maximum for the district, and does not grant a local option homestead exemption, the district's DPV, as determined under Subsection 42.252(a) of the Education Code, is adjusted by an amount sufficient to ensure that:
 - a. the district's current total state and local M&O revenue is not less than it would be if the district had not experienced a value decline, and
 - b. the district's maximum DTR, as determined under Subsection 42.253(e) of the Education Code, is not less in the following biennium than it would be if the district had not experienced a value decline.

2. The value decline adjustment is made during the settle-up process under Section 42.253 of the Education Code, i.e., the adjustment is not limited by a sum-certain appropriation and is not contingent on the availability of surplus funds.

As a matter of good public policy, the legislature should also enact the following at the earliest possible time:

The amount of taxable property value used to determine the state's share of a school district's allotments under Chapters 42 and 46 of this code, or the amount of a district's wealth in excess of the Equalized Wealth Level or the Adjusted Wealth Per Student under Chapter 41 of this Code, may not exceed the amount of value on which the district can impose taxes for the current school year.

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Background/Discussion:

Every district with declining taxable property value, regardless of which wealth category the district falls in, is penalized under current school finance law. The reason is simple. The state holds the district responsible for more taxable value than what the district can actually tax.

If, for example, a district's value declines from \$500 million in the prior year to \$480 million in the current year, the state calculates the district's state aid or recapture for the current year based on \$500 million. But the district can tax only \$480 million. The result is a penalty in the form of either a state aid deficiency or excess recapture.

This practice prompts the question: If a taxpayer's income declined from last year to this year due to company cost-cutting measures, would it be acceptable for the IRS to calculate his taxes based on last year's income?

There are only three ways a district can make up for the M&O penalty. Raise the M&O tax rate, dip into the fund balance, or cut programs. There are only two ways when it comes to the I&S penalty under Chapter 46 – raise the I&S rate or use excess bond reserve funds, if any.

The state provides no relief whatsoever for value declines up to 4%. If the value decline exceeds 4%, the state may – or may not – adjust for the excess decline. Unlike most school funding elements, the value decline adjustment is *not* guaranteed through the settle-up process. It is subject to a sum-certain appropriation to begin with, and is then contingent on the availability of surplus funds in the education budget.

The most harmful consequences of value declines under current law are suffered by districts that are at or so close to their M&O tax rate cap (generally \$1.50) that they cannot raise the rate sufficiently, if at all, to (1) offset the value decline penalty or (2) to achieve their maximum tax effort (DTR) for Tier 2 funding in the following biennium.

TREATING THE ADA DECLINE ADJUSTMENT LIKE SIMILAR COST FACTORS

Proposed Legislative Action

Fully fund the ADA decline adjustment, using the well-established, standard settle-up procedure in the event the actual statewide decline exceeds the estimate used for appropriations.

Background/Discussion:

In 2001 the Legislature, at the urging of a coalition of school districts and the Equity Center, enacted an adjustment to help cover the residual costs associated with declining student population. Subsection 42.005(b)(2) of the Education Code provides that “A school district that experiences a decline of two percent or more in ADA shall be funded on the basis of... an ADA not to exceed 98 percent of the actual ADA of the preceding school year...” While an adjustment to 98 percent may not always fully cover the costs of

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an ADA decline, this provision represents a major step forward in recognition of those costs.

Nonetheless, the ADA decline adjustment is not yet treated like similar cost factors, such as ADA growth, in the sense that the actual adjustment is subject to a sum-certain appropriation that may turn out to be insufficient, in which case the adjustment would be less than 98 percent. By contrast, ADA growth is fully funded through the settle-up process (Section 42.253, Education Code) in the event the Legislature has underestimated the cost of ADA growth during the appropriations process.

The use of a sum-certain appropriation may have been justified by some degree of uncertainty as to the potential cost of the adjustment. However, the ability of the state to estimate statewide ADA decline in the future is not significantly different from its ability to estimate statewide ADA growth, as well as other factors which, under current law, are estimated for appropriations purposes and finalized during settle-up.

ELIMINATING THE BIENNIUM LAG IN THE TIER 2 GUARANTEED YIELD

Proposed Legislative Action:

Eliminate the biennium lag in state recognition of increased tax effort in Tier 2. The additional state assistance should begin in the year in which a school district increases its tax effort.

Background/Discussion:

Prior to the 1993-94 school year, an increase in a school district's M&O tax effort triggered an immediate increase in state Tier 2 funding. Since then, an increase in tax effort in either year of a current biennium has generated new local revenue only. Hence, the less wealthy a district is, the less money per weighted student the district realizes as a result of its increased tax effort.

The last school year of a biennium is called the Tier 2 base year because, as a district establishes its tax effort for that year, it also establishes its maximum DTR for both years of the next biennium. Any increase in effort during the base year, to the extent the district maintains that effort in the following biennium, generates an increase in the district's Tier 2 state aid beginning with the first year of the following biennium. This delay in state response until the next biennium is called the "biennium lag." In contrast, for each penny of additional tax effort Chapter 41 and gap districts not only gain more in local revenue alone than Tier 2 districts gain in state and local revenue combined, they get all of theirs immediately.

The biennium lag and the current settle-up process were enacted in SB 7 (1993) to limit state costs and to end years of proration. Simply stated, the delay in state response until the next biennium limits state Tier 2 costs during the current biennium. It also eliminates the politically unpopular proration that would otherwise occur in the event districts collectively increased tax effort more than anticipated by the state.

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The biennium lag is a *student equity and adequacy problem* because a Tier 2 district cannot access increased funds at the Guaranteed Yield Level (GL) until at least one year later in the next biennium. In the event the district's rate increase occurs in the first year of a biennium, the district cannot access additional funds at the GL until *two* years later. The biennium lag is a *taxpayer equity problem* because taxpayers in a Tier 2 district must suffer a higher tax rate than a wealthier district in order to meet comparable current needs – and – must suffer a higher than currently-needed tax rate in order to qualify for increased funding to meet anticipated future needs.

Elimination of the biennium lag will allow a local district to set the tax rate and adopt a budget based on current needs. The school board will be able to increase the tax rate only when actual needs arise, rather than in anticipation of future needs. This has the potential to eliminate most unnecessary tax rate increases.

Arguments that districts will use this latitude to maximize state funding each year are weak. Clearly, most districts so inclined would have already increased or maximized their Tier 2 funding by adopting higher rates over the seven years the biennium lag has been state policy.

Further, ***the lag is no longer needed to avoid proration***. There was a time when the state had no idea what district tax response would be during an upcoming biennium. Plus, there was no settle-up process. We now have over 15 years of experience with tax response, and the state can now estimate it much more accurately. Should any shortfalls occur, however, they can be handled the same way other shortfalls are currently handled – *via* the settle-up process in the next year.

PROTECTING COMPENSATORY EDUCATION

Funding for At-Risk Children

Texas schools receive about \$1.2 billion each year to fund state compensatory education (SCE) programs. These programs are designed to provide academic services to students in danger of dropping out of school. Since the beginning of state funding for compensatory education, rules regarding allowable expenditures have grown increasingly complex and increasing amounts of Tier 1 state aid (mostly from SCE allotments) have been retained by TEA to fund other programs. We recommend the following improvements.

Proposal #1

The State should not retain (i.e. “set aside”) any of a district’s SCE allotment to defray the cost to the state of funding other state programs and initiatives. These set-asides should be eliminated, and programs currently funded through set-asides should be funded by other means. Failing this, wealthy districts should at least pay a share of the compensatory education set-asides since they receive benefits from them.

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Rationale: The funding level of any program, including SCE, is ostensibly based on the actual cost of accomplishing the goals of the program. Withholding a portion of SCE funds the state has determined are needed by a district to serve its at-risk students undermines the ability of that district to accomplish the goals of the program.

Set-Aside Facts (*Based on 2000-01 Data*):

1. Chapter 42 SCE allotments totaled approximately \$1.1 billion. This amount includes the local share (i.e., the amount of Tier 1 costs that is assigned to each district as its local share).
2. More than \$147 million in Tier 1 state aid was withheld from Chapter 42 districts. Seven Chapter 42 districts lost *more than 100%* of their compensatory education funding (actually had a negative number for compensatory education after set-asides were subtracted from their Tier 1 funding!). Twenty-eight (28) districts lost more than 50% of their SCE allotment, 170 districts lost more than 20%, and 499 districts lost more than 10%.
3. \$0 was withheld from wealthy districts. However, they received \$9 million in grants and services paid for with set-asides withheld from property-poor and mid-wealth districts (\$5.8 million in grants, plus an estimated \$3.2 million for TAAS administration).
4. This means that wealthy districts received over 6% of the SCE funding that was withheld from poor and mid-wealth districts in addition to being allowed to retain (after recapture) sufficient revenue to fully fund their own SCE allotments.

Proposal #2

The compensatory education audit should be eliminated. Failing this, an annual audit should not be required for districts whose 2002-03 audit reports show they are spending SCE funds appropriately or whose at-risk children are performing on the state assessment at a level above the statewide average for at-risk children.

Rationale: The cost of the compensatory education audit is, in effect, an unfunded mandate that further erodes a district's ability to serve at-risk children.

Proposal #3

Any campus with 40% or more children eligible for the free or reduced lunch program should be able to conduct a campus-wide [or district-wide?] compensatory education program.

Rationale: The current standard is 50% or more children eligible for free or reduced lunches. The federal Title I threshold for a school-wide program is 40% of children eligible for free or reduced lunches. This new criteria would make SCE guidelines consistent with Title I.

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Proposal #4

Districts should be allowed to use their SCE allotments to serve any child they have determined to be at risk.

Rationale: In addition to serving students included in the definition of at-risk children contained in Chapter 29 of the Texas Education Code, districts are already allowed to use local criteria to identify additional students who are at risk. However, the number of students served using local criteria is limited to 10% of the number of students who were identified and served the prior school year under state criteria.

Educational considerations.

1. Districts are held accountable for student performance. They should have the authority to determine how funds are spent.
2. Local educators are best suited to determine which students are at risk. As Texas increases the accountability standards, it becomes paramount that local educators be given significantly more discretion in how these funds are spent and which children districts are permitted to serve.
3. Statewide, one-size-fits-all regulations impede educators who are dealing with problems unique to a particular district. Example: Districts are preparing students to pass a tougher test. Children not considered at risk under state criteria because they consistently passed the TAAS with low passing scores are obviously in danger of failing the new test. If the number of children in a particular district in this category exceeds the state's 10% limit, then funds may not be expended for them – even though these children could fail the new test as a result of this lack of intervention.

Financial considerations. Adding a full 10% to the prior year's number translates to allowing the local district to spend about 9% of its SCE allotment on at risk children not identified by the state ($10\% \div 110\% = 9.1\%$). This percentage is probably overstated because it assumes an equal cost in providing services to the additional children. In many cases there is no additional cost. For example, serving an extra child may be as simple as an after-school teacher having 5 children to work with instead of just 4.

Ironically, in 2000-01, at the same time districts were, in effect, prohibited from spending more than 9.1% of their allotments on locally-identified at-risk children, the state withheld more than 9.1% of the compensatory education allotment in 537 Chapter 42 districts – *all for other programs!*