

HB 3 by Huberty A True School Finance Overhaul

An extraordinary thing happened on the way to the 86th legislative session. Due to the creation of the Texas Commission on Public School Finance by the 85th Legislature, key members of the House and Senate Education Committees were appointed to the Commission and participated in an in-depth analysis of the inefficiencies in the state's school finance formulas and studied recommendations for improvements. Consequently, the Legislature began the legislative session with a comprehensive report listing fundamental improvements to the system and a strong will to implement those changes. And it just so happened that billions of dollars were sitting in budget riders specifically earmarked for that purpose.

Past commissions and select committees have gone through the motions, but produced reports that were largely ignored. However, under the excellent leadership of former Texas Supreme Court Justice Scott Brister, and the willing participation of his fellow commission members, THIS school finance commission met all day one to two times each month of 2018 and listened to endless hours of expert testimony regarding problems in the system and recommendations on how to address those problems. The Commission was focused on improving student performance, and the best methods by which to accomplish that. Their recommendations were presented to the Legislature in December 2018, and bills to implement them were filed by the chairs of the education committees in the House and Senate – Representative Dan Huberty (R-Houston) and Senator Larry Taylor (R-Friendswood).

The session began with a joint press conference during which Governor Abbott, Lt. Governor Patrick, and Speaker Bonnen proclaimed that school finance and property tax reform were their top priorities for the 86th legislative session. In addition, Governor Abbott put those issues at the top of his list of emergency items in his State of the State address. Speaker Bonnen made it clear that school finance reform was the number one priority of the House of Representatives and had cups printed for the House members' lounge that read, "School Finance Reform: The Time Is Now." So the push was on, and the whips were cracking to get it done.

The Senate's first education bill out of the gate was SB 3 by Nelson, which provided a \$5,000 salary increase to all classroom teachers and librarians, at a cost of \$4 billion for the

biennium – two-thirds of the \$6 billion increase allocated in the Senate budget for school finance, and 44% of the House budget's additional \$9 billion. Furthermore, the across-the-board pay raise was not in the House bill.



The House passed its bill, HB 3 by Huberty, two months later after multiple committee hearings. The bill infused \$6.3 billion in new money into the formulas to implement the majority of the Commission's recommendations, and reduced school district maintenance and operations tax rates by \$0.04 statewide at a cost of \$2.7 billion. It also reduced the amount that would be recaptured from school districts in the next biennium by \$3.0 billion. The bill passed the House 148-1 with Speaker Bonnen casting the first "Aye" vote.

When HB 3 was heard in the Senate, the \$5,000 pay raise was incorporated into its version. The Senate also incorporated other major changes that were not in the House bill, such as the use of current year values rather than prior year values in the school finance formulas and tax compression accomplished by using value growth above 2.5% in each individual district rather than on a statewide basis. The bill passed the Senate 26-3-2 and the two bills went to conference committee.

The conference committee report that emerged was a true compromise between the two versions of the bill, and passed both the House and Senate unanimously. The final version of HB 3 spends \$11.6 billion on public education and tax relief and checks every box that critics of the school finance system have long complained about:

- ✓ **"Property taxes are too high."** HB 3 allocates \$5.1 billion to lower school district tax rates by \$0.07-\$0.11 in the first year, with further reductions in year two.
- ✓ **"The state needs to put more money into public education."** HB 3 increases state funding by \$6.5 billion.
- ✓ **"Recapture is too high."** HB 3 reduces the amount that will be recaptured by \$3.6 billion, a 47% reduction.
- ✓ **"The state's share of public education funding is too low."** HB 3 increases the state's share of public education funding to 45% from 38%.

Tax Relief. A total of \$5.1 billion will be spent in the upcoming biennium for tax relief. The tax compression in the final bill is a hybrid of the statewide compression in the House bill, and individual district compression in the Senate bill. In the 2019-2020 school year, school district maintenance and operations (M&O) tax rates will be compressed by 7% (93% x district's tier one rate—the rate required to pay the district's share of formula entitlements), resulting in a \$0.07 reduction of M&O tax rates in school districts with \$1.00 tier one rate. Rates will be reduced an additional \$0.04 in school districts with M&O rates of \$1.17 (see Table 1). A district can maintain “enrichment pennies” that they currently levy above the compressed rate. In the 2019-2020 school year, school districts are prohibited from adopting an M&O tax rate higher than the compressed rate (including enrichment pennies) unless the district had a strategic plan in place to increase the rate before the bill passed. The current statutory M&O rate cap of \$1.17 will be lowered to \$1.10. This tax rate reduction will be reflected on tax bills mailed this October, and mortgage companies are required to adjust escrow accounts accordingly.

In the 2020-2021 school year, the bill provides an average of \$0.13 rate reduction using statewide property value growth in excess of 2.5% to compress tier 1 tax rates. The compression percentage will be the lower of 93% or the newly calculated percentage. In addition, school districts with value growth above the statewide average will be required to use revenue from the district's value growth in excess of 2.5% to compress their tier 1 tax rate. This will result in varying M&O rate caps, with each school district being subject to an M&O tax rate cap equal to the district's maximum compressed rate plus \$0.17. TEA will calculate and make available all maximum compressed rates, and if a school district has a maximum compressed tax rate that is less than 90% of any other district's rate, the Commissioner will recompute the lower rate until it is within the 90% range.

Tax Ratification Elections. A tax ratification election will be required if a school board adopts a tax rate that exceeds its compressed M&O rate (including enrichment pennies) plus the district's debt rate. In the 2020 tax year, the rollback rate, or “voter approval rate”, is increased by \$0.01, but school boards must unanimously adopt the tax rate in order

to access the \$0.01 without an election. Tax ratification elections must be held on a uniform election date that allows sufficient time to comply with the requirements of other laws, and a school district must conduct an efficiency audit before holding an election. The requirement for an efficiency audit is waived for two years if the school district is located in a disaster area.

“Golden” and “Copper” Pennies. Our school finance formulas divide enrichment pennies (pennies above the tier one rate) into two types – “golden” pennies which are currently the first six pennies above the tier one rate (commonly \$1.01-\$1.06) and not recaptured, and “copper” pennies which are currently all pennies between the golden pennies and the \$1.17 M&O tax rate cap (commonly \$1.07-\$1.17) which are subject to recapture.

HB 3 adds two more “golden pennies” for a total of 8 (the first 8 pennies above the compressed rate). The bill also delinks the guaranteed yield on the golden pennies from the yield per penny of Austin ISD (\$126.88) and links it to the greater of (1) 0.016 x the basic allotment (\$98.56) or (2) the yield per penny for each student in a school district at the 96th percentile of wealth.

HB 3 also increases the guaranteed yield of “copper pennies” by 54% to \$49.28 and ties the guaranteed yield to 0.008 x the basic allotment (\$49.28). A district must compress these pennies to the number of pennies that would raise the same amount of revenue per weighted student as in the previous year. This amounts to an additional \$0.04 M&O tax rate compression in districts that are currently levying a \$1.17 M&O tax rate.

Recapture. HB 3 changes the calculation of recapture to the amount of revenue above its tier 1 entitlement raised by a district's tier 1 tax rate. Recapture payments will no longer be based on property wealth per WADA (weighted average daily attendance). School districts can remit their recapture obligation in one payment not later than August 15 rather than in monthly payments from February 15 to August 15. It is estimated that changes made by HB 3 will reduce recapture for the next biennium by \$3.6 billion, a 47% drop.

Table 1
Maintenance and Operations (M&O) Tax Rate Reduction
2019-2020 School Year

Current M&O Tax Rate	HB 3 M&O Tax Rate 2019-2020	M&O Tax Rate Reduction
\$0.70	\$0.65	-\$0.05
\$0.90	\$0.84	-\$0.06
\$1.04	\$0.97	-\$0.07
\$1.10	\$1.02	-\$0.08
\$1.17	\$1.06	-\$0.11

Repealed Formula Elements. The bill repeals outdated formula elements as well as provisions that flow funds to all school districts outside of the formulas, and redistributes that revenue. Repealed elements include:

1. **Cost of Education Index (CEI)**, a multiplier assigned to each school district that was calculated using 1991 data to provide funds to help the district adjust for factors outside of its control. The data was so out of date that the adjustment was no longer serving its intended purpose. The revenue savings is used to increase the basic allotment.
2. **Hold harmless for property wealthy school districts** that was “temporarily” put in place in 1993 and renewed several times before being made permanent is phased out over 5 years.
3. **Early agreement credit** for property wealthy school districts that agree to pay the amount owed to the state.
4. **Gifted and talented weight** which increased funding for up to 5% of a school district’s students identified as gifted and talented. Because all school districts identified at least 5% of students, funds flowing through this weight were incorporated into the basic allotment. School districts are required to maintain their gifted and talented programs, or funds will be withheld from the district, and they must report to the Commissioner of Education regarding their use of funds on gifted and talented programs. The revenue that flowed through the weight is now flowing through the basic allotment.
5. **High school allotment** of \$275 per student in average daily attendance in grades 9-12. All school districts received this allotment outside of the formulas, so the revenue has been incorporated into the basic allotment.
6. **Staff salary allotment** for non-professional staff. Districts receive \$500 for each full-time non-professional employee and \$250 for each part-time non-professional employee outside of the formulas. These funds are incorporated into the basic allotment.
7. **Hold harmless for 2015 homestead exemption increase.** This hold harmless guaranteed 2015 funding levels, and is no longer necessary.

Additional Funding. The additional \$6.5 billion sent to school districts through the new and improved formulas will increase the state share of public education funding to 45% (from 38%), and lower recapture by \$3.6 billion, or 47% in the next biennium. Testimony before the Texas Commission on Public School Finance highlighted that only 36% of low-income 3rd grade students and 24% that are English language learners are proficient in reading. Therefore, new formula elements are targeted to assist those students as well as others that have disabilities that hamper their ability to read. Changes and additions to the school finance formulas include:

Basic allotment, the amount guaranteed per student, is increased by 19.8% to \$6,160 from \$5,140, an increase of \$1,020 per student.

Current year values rather than prior year values will be used in formula calculations to provide greater equity among the different types of school districts.

Compensatory education funding increase for low-income students is based on student needs, using a weighted sliding scale of 0.225-0.275 (currently a flat 0.20). The revenue will be distributed based on “economic census blocks” using median household income, average educational attainment, percentage of single-parent households, and rate of homeownership. Funding will no longer be distributed solely based on a student’s qualification for free and reduced price lunch.

Career & technology allotment is expanded to include courses in grades 7 -12 from 9-12.

Special education mainstream weight is increased to 1.15 (from 1.10) and requires the Commissioner of Education to distribute funding to school districts for special education students in the amount necessary to comply with federal requirements for maintenance of state financial support. Additionally, the Commissioner of Education is directed to appoint a Special Education Allotment Committee to make recommendations on special education funding.

Small and mid-size district adjustment is converted from a formula adjustment to a stand-alone allotment, but it is maintained as a formula multiplier for special education students.

Bilingual weight of 0.10 is maintained.

Transportation allotment is calculated per mile per student instead of by linear miles.

Full-day prekindergarten for eligible 4-year-olds is mandated. Districts can receive a waiver from this requirement for lack of facilities but only after seeking partnerships to provide the services.

“Formula transition grants” will be provided to school districts for five years so that all school districts and charter schools will receive at least the lesser of (1) 103% of the amount they would have received under current law or (2) 128% of the statewide average amount of M&O revenue that would have been provided for the 2019-20 school year under current law. A special hold harmless is provided for the 10 school districts that are the only one in a county and have less than 300 ADA.

Interest payments will be included in a reimbursement to a school district caused by litigation that lowered the school district’s value.

Revenue protection payments for Chapter 313 agreements will be calculated based on prior year values.

Early education allotment is added for economically disadvantaged and bilingual students in grades K-3 at a weight of 0.10.

Dual language allotment is added at a weight of 0.15 for bilingual students in a dual language program, or 0.05 if the student is English proficient.

Dyslexia allotment is added for each student identified as having dyslexia or a related disorder at a weight of 0.10.

Dropout recovery school and residential placement facility allotment of \$275 per student is added for students attending a dropout recovery school or residing in a residential placement facility.

Fast growth allotment is added for each student in a school district with enrollment growth in the top quartile over the past three years, at a weight of 0.04.

Mentor program allotment is added to provide school districts with funds to pay stipends to mentor teachers.

College, career, and military readiness outcomes bonus is added at \$5,000 for economically disadvantaged students, \$3,000 for non-economically disadvantaged students, and \$2,000 for special education students in the top 25th percentile of performance on the SAT and ACT test, and other indicators established by the Commissioner.

Extended year incentive program is added for school districts that provide an additional 30 days (1/2 day) instruction for students in Pre-K through 5th grade.

Blended learning grant program will be created by the Commissioner of Education to assist districts in combining classroom and online instruction.

Kindergarten-Third Grade Reading Standards. Each school district and charter school is required to provide a phonics curriculum that uses systematic direct instruction in kindergarten through third grade to ensure all students obtain necessary early literacy skills and K-3 teachers and principals must attend a literacy achievement academy. School districts will administer a reading diagnostic instrument to all kindergarten students.

Early Childhood Literacy and Mathematics Proficiency Plans. Each school district must adopt and post on the district's website early childhood literacy and mathematics proficiency plans that set specific annual goals for the following five school years to reach quantifiable targets for student performance in reading and mathematics at each campus. An annual report of progress must be reviewed by the school board and posted on the district's website.

Teacher Salaries. The \$5,000 across-the-board salary increase was replaced with a directive to school districts to spend 30% of their revenue gain on employee salary increases with emphasis on classroom teachers that have more than 5 years of experience. Districts can choose to apply for a new teacher incentive allotment that provides funds for pay increases to effective teachers who teach at high needs campuses, rural campuses, or in areas experiencing a critical teacher shortage. Teachers designated as master, exemplary, or recognized by the district and who teach at campuses with the greatest needs can receive a bonus of up to \$32,000. Each school district is required to submit a report to the Legislature on salary and wage increases by December 1, 2020. HB 3 also requires the Commissioner of Education to create a "Do Not Hire" registry for education employees.

HB 3 truly is a Herculean accomplishment by the 86th Legislature. Chairmen Dan Huberty and Larry Taylor and every other legislator that worked on the bill should be commended. In addition, Governor Abbott, Lt. Governor Patrick and Speaker Bonnen should be applauded for their steady leadership, guidance and support for the effort throughout the session.

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