LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 78TH LEGISLATIVE REGULAR SESSION

April 29, 2003

TO: Honorable Kent Grusendorf, Chair, House Committee on Public Education

FROM: John Keel, Director, Legislative Budget Board

IN RE: **HB3382** by Merritt (Relating to public school finance.), **As Introduced**

Estimated Two-year Net Impact to General Revenue Related Funds for HB3382, As Introduced: a negative impact of ($37,915,873,000) through the biennium ending August 31, 2005.

The bill would make no appropriation but could provide the legal basis for an appropriation of funds to implement the provisions of the bill.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2004	($7,932,066,000)
2005	($29,983,807,000)
2006	($30,461,722,000)
2007	($30,702,720,000)
2008	($31,039,052,000)

All Funds, Five-Year Impact:

Fiscal Year	Probable Savings/(Cost) from *FOUNDATION SCHOOL FUND* 193	Probable Revenue (Loss) from *School Districts*	Probable Revenue Gain/(Loss) from *GENERAL REVENUE FUND* 1	Probable Revenue Gain/(Loss) from *FOUNDATION SCHOOL FUND* 193
2004	$0	$0	($6,905,686,000)	($1,026,380,000)
2005	($17,550,000,000)	($13,000,000,000)	($11,034,805,000)	($1,399,002,000)
2006	($17,910,000,000)	($14,000,000,000)	($11,241,658,000)	($1,310,064,000)
2007	($17,680,000,000)	($15,000,000,000)	($11,707,374,000)	($1,315,346,000)
2008	($17,650,000,000)	($16,000,000,000)	($12,080,994,000)	($1,308,058,000)

Fiscal Year	Probable Revenue Gain/(Loss) from *Texas Great Teachers & Facilities Fund*	Probable Revenue Gain/(Loss) from *STATE HIGHWAY FUND* 6	Probable Revenue Gain/(Loss) from *Cities*	Probable Revenue Gain/(Loss) from *Transit Authorities*
2004	$11,347,844,000	$6,011,000	($64,825,000)	($23,539,000)
2005	$18,180,132,000	$10,681,000	($135,972,000)	($49,372,000)
2006	$18,514,471,000	$11,069,000	($139,750,000)	($50,744,000)
2007	$19,363,764,000	$11,587,000	($145,993,000)	($53,011,000)
2008	$20,069,357,000	$12,005,000	($152,482,000)	($55,367,000)

Fiscal Year	Probable Revenue Gain/(Loss) from *Counties/Special*

	Districts
2004	($7,999,000)
2005	($16,778,000)
2006	($17,244,000)
2007	($18,015,000)
2008	($18,815,000)

Fiscal Analysis

The bill creates a new system for funding public schools and significantly amends the tax structure in order to generate revenue to implement the provisions of the bill. This bill also acts as the enabling legislation for HJR 8.

Texas Great Teachers and Facilities Fund
The bill creates the Texas Great Teachers and Facilities Fund ("Fund"), dedicated to "the support of teaching, instruction, and the construction or maintenance of educational facilities in the public free schools." The Fund is created as a dedicated account in the general revenue fund. The Fund is comprised of various revenue sources as defined in HJR 8 and also includes existing balances from the foundation school fund, other tranfers and gifts.

Teaching and Instruction Allotment
The bill entitles each district to a "teaching and instruction allotment" from the Fund calculated as a defined salary target plus a defined benefits target times the district's average daily attendance. The allotment may only be used for teacher compensation and instructional spending. A waiver provision allows formerly Chapter 42 districts to spend the Allotment on non-instructional items. "Expected State Aid" (ESA) for each district is defined as the sum of the teaching and instruction allotment plus the facilities allotments to which they are entitled (see below).

Limitations on Local Taxation
For each school district a "Target Education Budget" (TEB) is calculated as 110% of the "Prior Education Budget" (PEB) which in turn is defined as the current law operations entitlement. To the extent that the TEB is less than the ESA, districts are directed to set their local ad valorem taxes to the extent necessary only to provide the revenue difference between the TEB and the ESA.

Once the reduction, if necessary, is made districts may levy an ad valorem tax subject to various thresholds of local voter approval depending on the tax rate. The absolute maximum tax rate is $1.25 per $100 of taxable property.

Basic Instructional Facilities Allotment
The bill entitles each district to a basic instructional facilities allotment calculated as $3500 times the quotient of average daily attendance divided by a defined income adjusted class size target. The target is a determination of the district's median household income. Certain districts defined as "growth" districts are eligible to receive an additional facilities allocation. Districts are entitled to the current law new instructional facilities allotment to subsidize the operations expenses associated with opening new facilities. It is assumed in this analysis that the facilities entitlement is entirely state-funded.

Changes to the Tax Code

The bill would amend Chapter 151 of the Tax Code to impose a sales tax at the rate of 2.8 percent of the sales price of taxable items sold in this state. This tax would be in addition to the current 6.25 percent sales tax. Revenue from the new tax would be dedicated solely to funding the TGTFP and would be delivered to the TGTFF. Revenue generated from the existing sales tax, in an amount equal to the tax at the rate of 3 percent of the sales price of total taxable items sold, would be dedicated and credited to the TGTFF.

Chapter 152 of the Tax Code would be amended to add an additional tax of 2.8 percent on the sale, rental, or use of a motor vehicle. Revenue from the new tax would be dedicated solely to funding the

TGTFP and would be delivered to the TGTFF. Revenue generated from the existing motor vehicle sales taxes, in an amount equal to the tax at the rate of 3 percent of the sales price of total taxable items, would be dedicated and credited to the TGTFF.

Tax Code Chapters 154 (Cigarette Tax), 155 (Cigar and Tobacco Products Tax), and 183 (Mixed Beverage Tax), and Alcoholic Beverage Code Chapters 201 (Liquor, Wine and Malt Liquor Taxes) and 203 (Beer Tax), would be amended to deposit the collections from these taxes into the TGTFF, instead of Fund 0001 or the FSF.

Chapter 182 (Miscellaneous Gross Receipts Taxes—Utilities Taxes) of the Tax Code would be amended to dedicate and credit gas, electric and water utility tax revenue to the TGTFF, instead of Fund 0001 and the FSF.

Chapters 181 (Cement Production Tax), 191 (Miscellaneous Occupation Taxes— Oil Well Service and Attorneys), 201 (Gas Production Tax), 202 (Oil Production Tax), and 203 (Sulphur Production Tax) of the Tax Code would be amended to deposit 25 percent of the cement production tax, oil well service tax, attorney occupation tax, gas production tax, and cement production tax in the TGTFF, instead of the FSF.

Chapter 466 of the Government Code would be amended to transfer all revenues currently swept by statute from GR Account—5025—Lottery to the TGTFF, instead of the FSF.

The bill would amend Article 4.12 of the Insurance Code to move the dedication of one-fourth of the insurance premium taxes collected under Article 1.14-1, Sections 11 and 12, and Articles 4.10. 4.11, and 4.11B to the TGTFF, instead of the FSF.

The bill would take effect January 1, 2004, but only if the constitutional amendment proposed by the 78th Legislature, Regular Session, relating to establishing a new 2.8 percent sales and motor vehicle tax dedicated to the Texas Great Teachers & Facilities Fund were approved by the voters. If the proposed constitutional amendment were not approved by the voters, the bill would have no effect.

Methodology

The repeal of Chapters 41, 42 and 46 results in a savings to the state of approximately $9 billion in 2005 increasing to an estimated $10.6 billion in 2008.

This analysis sought to approximate the data implied in the legislation in terms of educator salary and benefits; based on available Labor Department data and using the bill's methodology, the resulting "Teacher and Instruction Entitlement" is approximately $20 billion per year, or about $5,000 per ADA. The bill does not describe a provision for local cost sharing, leading to a completely state funded allotment.

Section 47.102 as added by the bill provides a guarantee to the level of revenue in the last year preceding the enactment of the new law. It is believed this is intended to be 2004 fiscal year. This analysis assumes the bill intends for the hold harmless to be calculated as an aggregate amount resulting in a likely cost of about $5.8 billion in 2005, increasing to $6 billion by 2008.

The facilities funding allocations include a $3500 per year for each adjusted class size target. The cost of the allotment is about $805 million in 2005, increasing to $900 million in 2008. In addition, there is a "fast growth" facilities supplement The cost of this supplemental amount is estimated to be about $50 million in all years.

The bill is silent with respect to open-enrollment charter funding, funding of military base districts, and other special entities. It is assumed that some form of the formulas would be applicable for each of those entities.

The level of assistance with facilities appears to fall short short of the amount needed to service debt that already exists in school districts. According to the Texas Eduction Agency, the amounts provided in this legislation are approximately $1.4 billion less than the amount needed annually to maintain current debt service obligations. The calculation of the hold harmless apparently does not distinguish debt service tax authorizations from maintenance tax authorizations. The rollback limitation also does not seem to make the distinction. It is unclear whether districts would retain the authority to tax for debt service based on the tax reduction requirements in this bill.

The Texas Education Agency estimates that revamping the programs that calculate state aid (specifically, the web based application in current use) would have a significant impact on the operation of the Texas Education Agency necessitating $500,000 for system modifications.

The fiscal implications of imposing the additional 2.8 percent sales tax and crediting revenue from the existing sales tax at a rate of 3 percent to the TGTFF were estimated using current state sales and use tax revenue projections. The higher sales tax also would raise revenue collections from the sale of the motor lubricants, which are deposited into the State Highway Fund 0006, as required by the constitution. The fiscal 2004 impacts reflect an effective date of January 1, 2004. Local sales tax losses, attributable to the higher after-tax prices faced by consumers, were estimated proportionately.

With respect to motor vehicle sales and rental taxes, the fiscal implications of imposing the additional 2.8 percent tax and crediting revenue from the existing tax at a rate of 3 percent to the TGTFF were estimated using current state sales and use tax revenue projections. The fiscal 2004 impacts reflect an effective date of January 1, 2004. However, the bill is drafted in such a way that 3 percent of the tax on motor vehicle rentals, which is not collected by a county tax assessor-collector, would not be credited to the TGTFF, as presumably intended. If this were corrected, the TGTFF would receive an additional $211 million in the 2004-05 biennium; and Fund 0001 would lose the equivalent amount.

For the other revenue sources affected by this bill, future collections would be diverted from Fund 0001 and/or the FSF to the TGTFF on the bill's effective date. The fiscal 2004 impacts reflect an effective date of January 1, 2004.

The bill would divert 100 percent of mixed beverage tax collections to the TGTFF. The quarterly allocations to counties and cities from the mixed beverage tax would continue as that statutory authorization remains, but they would be funded by general revenue not related to mixed beverage tax collections.

Note: The bill refers to Tax Code Chapter 172, which neither exists in current law nor would be created by this bill.

Note: Negative dynamic fiscal impacts would result from the increases in the sales and motor vehicle tax rates. However, the bill also would result in lower school property tax rates. As the net impact of these changes cannot be determined, the dynamic fiscal impacts have not been estimated.

Note: Although the bill would create the Texas Great Teachers and Facilities Fund as an account in Fund 0001, the proposed constitutional amendment in the accompanying House Joint Resolution would establish the fund as a permanent fund.

Note: This legislation would do one or more of the following: create or recreate a dedicated account in the General Revenue Fund, create or recreate a special or trust fund either with or outside of the Treasury, or create a dedicated revenue source. Legislative policy, implemented as Government Code 403.094, consolidated special funds (except those affected by constitutional, federal, or other restrictions) into the General Revenue Fund as of August 31, 1993 and eliminated all applicable statutory revenue dedications as of August 31, 1995. Each subsequent Legislature has reviewed bills that affect funds consolidation. The fund, account, or revenue dedication included in this bill would be subject to funds consolidation review by the current Legislature.

Local Government Impact

The fisacl impact to local school districts and other local governments is reflected above. The local school district impact relative to property tax reduction does not include an estimation of local enrichment as allowed in the legislation as such determinations would be highly speculative.

The bill guarantees that school districts will receive at least as much total revenue as they received in the "last full year before enactment of this Act" which is assumed to be fiscal year 2004.

The bill stipulates that the Teaching and Instruction Allotment may only be used for costs directly associated with teacher compensation and instruction. Under the language of the bill, costs associated with school district expenditures, including those for non-instructional support staff, administration, transportation, and extra-curricular activities would be paid from the local ad valorem tax provisions; however, the ad valorem tax provisions of the bill are strictly limited.

The provision of funding for textbooks is not stipulated in this bill. Language in the Texas Education relating to textbooks is not amended in this bill, but the HJR 8 dedication of the Available School Fund to the Texas Great Teachers and Facilities Fund raises questions about the state provision for textbook funding.

Source Agencies: 304 Comptroller of Public Accounts, 701 Central Education Agency
LBB Staff: JK, WP, CT, SM, UP