

LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 79TH LEGISLATURE 2nd CALLED SESSION - 2005

July 22, 2005

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

FROM: John S. O'Brien, Deputy Director, Legislative Budget Board

IN RE: HB2 by Grusendorf (Relating to public education and public school finance matters; imposing criminal penalties.), **Committee Report 1st House, Substituted**

Estimated Two-year Net Impact to General Revenue Related Funds for HB2, Committee Report 1st House, Substituted: a negative impact of (\$8,130,284,249) through the biennium ending August 31, 2007.

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
2006	(\$3,139,458,900)
2007	(\$4,990,825,349)
2008	(\$5,443,509,848)
2009	(\$6,753,083,578)
2010	(\$7,054,051,161)

All Funds, Five-Year Impact:

Fiscal Year	Probable Savings/ (Cost) from <i>GENERAL REVENUE FUND 1</i>	Probable Savings/ (Cost) from <i>FOUNDATION SCHOOL FUND 193</i>	Probable Revenue Gain from <i>GENERAL REVENUE FUND 1</i>	Probable Revenue (Loss) from <i>School Districts</i>
2006	\$217,219,100	(\$3,364,900,000)	\$8,222,000	(\$2,638,800,000)
2007	\$107,262,651	(\$5,107,450,000)	\$9,362,000	(\$3,327,500,000)
2008	\$55,639,152	(\$5,509,350,000)	\$10,201,000	(\$3,163,600,000)
2009	\$48,133,422	(\$6,813,100,000)	\$11,883,000	(\$3,034,100,000)
2010	\$50,166,839	(\$7,118,200,000)	\$13,982,000	(\$2,830,200,000)

Fiscal Year	Change in Number of State Employees from FY 2005
2006	21.0
2007	21.0
2008	17.0
2009	17.0
2010	17.0

Fiscal Analysis

The bill would make substantive changes to the method of funding public education. The bill would amend current law regarding the calculation of entitlements under the Foundation School Program, would amend the method by which the state finances the Foundation School Program, and would make changes to various public education programs.

Article I of the bill relates to public school finance, including formula funding and property tax reduction.

The provisions of the bill are significantly different in fiscal year 2006 than in fiscal year 2007 and beyond.

In fiscal year 2006, school district tax rates are limited to a local fund assignment of \$1.25 with the state replacing the reduced local revenue with a commensurate level of state aid. Contingent on districts adopting the reduced rate, they are further entitled to an amount sufficient to increase school district employee compensation by \$2,000 for those individuals subject to the minimum salary schedule.

Beginning in fiscal year 2007, the provisions of the bill directing the calculation and distribution of state aid in the Foundation School Program shift significantly.

Effective fiscal year 2007, the local fund assignment is limited to \$1.20 with revised funding formulas providing increased state aid. The bill creates a single tier school finance system with a \$4600 Accreditation Allotment and a system of student and district weights and adjustments. The value of the weights and adjustments remain largely the same as under current law, save for the bilingual allotment, the Cost of Education Index, and the Small and Mid-Size District Adjustments. These adjustments increase relative to current law.

The current law Cost of Education Index values are phased out over a four-year period and replaced with the values found in the Teacher Fixed Effects CEI. The index values within Regional Education Service Centers are limited to the ratio that exists under current law, and districts are also guaranteed use of the higher of the current law or new value.

The adjustment for small and mid-size districts is increased over a three-year period.

School districts are held harmless to the 2006 per weighted pupil revenues plus 3%, total gains by districts over that 2006 amount are limited to 108% for 2007, 116% in 2008, and 124% in 2009. The bill stipulates that revenues created as a result of current law Chapter 41 wealth-sharing partnerships are to be recognized in the calculation of the hold harmless; due to data restrictions these costs are not included in this estimate.

Out of the formula entitlements described above, districts are directed to provide a \$2,500 compensation increase in fiscal year 2007 to school district employees subject to the minimum salary schedule.

Districts are authorized to levy an additional \$0.15 of enrichment tax effort, with access to enrichment limited to \$0.05 in 2007 and to \$0.10 in 2008 and 2009. The state guarantee on enrichment is \$39 in 2007, \$40 in 2008 and 2009, and equated to a specified percentile of wealth in 2010 and subsequent years.

The bill would direct the Legislative Budget Board to conduct a number of annual and biennial analyses on public education funding, including expenditures, the formula funding elements, special education, facilities, and the cost of education index.

Article II of the bill relates to various education programs, educator incentives, and instructional materials. Significant fiscal implications of these provisions are discussed in the methodology section.

Article III of the bill contains conforming amendments, Article IV relates to charter schools, Articles V and VI are reserved for expansion, Article VII relates to the State Board for Educator Certification, and Article VIII contains repealers.

Methodology

Article I

The school finance provisions of the bill result in a net revenue increase to local school districts and a cost to the state.

In fiscal year 2006, the net state cost of the formula provisions described above is \$3.4 billion, including funds for the \$2,000 educator pay increase. Depending on actual implementation of the tax rate-setting provisions, state costs could increase in both 2006 and in each year thereafter.

In fiscal year 2007, the net state cost of the single-tier provisions described above is \$4.6 billion, of which \$1.1 billion represents an increase in total revenue to school districts.

Due to the provisions of the bill that shift over time, including the phase-in of the new Cost of Education Index, phase-in of the new small and mid-size district adjustment, and the gradual elimination of restrictions on net gain, the costs in the out years are expected to increase by about \$500 million per year, with 2010 reflecting net state cost of \$6.1 billion.

The bill makes provision for wealth equalization. The state implication of those provisions is included in the costs above. However, if applicable school districts set tax rates at the allowable floor under the provisions, state costs could increase by \$90 million starting in 2007 over the costs identified above.

The provisions for equalized enrichment also result in increased state cost and local revenue generation over time. In 2007, the state aid per penny of equalized enrichment is \$116 million. By 2010, that cost per penny is \$135 million. If all districts eligible accessed the maximum amount of enrichment allowable, state cost in 2010 would be in excess of \$2 billion.

Due to the significant increase in state aid associated with this legislation, each monthly Foundation School Program payment to school districts will be relatively larger than under current law. As a result, the current law system of deferring what would otherwise be the August payment to September will result in a reduction in appropriations demand to implement the provisions of the bill.

It is estimated that completing the funding formula analyses required of the Legislative Budget Board would cost \$750,000 each biennium. The study of school facilities is estimated to cost \$500,000 in 2006.

State costs for providing 50 percent of district social security contributions, phased in over three years beginning in fiscal year 2007, is estimated to be \$11 million in 2007, \$24 million in fiscal year 2008, \$38 million in 2009, and increasing gradually each year thereafter.

Article II

Increases in public education salaries have an impact on the state's contribution to TRS. Additional TRS contributions related to the salary provisions for school district employees in the bill are estimated at \$17 million in fiscal year 2006 and \$27 million in fiscal year 2007. Additional state aid associated with salary provisions is included in the formula amounts given above.

2A.16 would amend the health care compensation supplement (pass-through) program under Subchapter D, Chapter 22, Education Code as added by Senate Bill 1691, Acts of the 79th Legislature, Regular Session, 2005. Instead of receiving a state-funded compensation supplement, eligible public education employees would be permitted to elect deferral of a portion of compensation for the purpose of contributing to a cafeteria health plan or participating in health care premium conversion. This provision would produce a savings to the state of \$273 million in fiscal year 2006 and \$275 million in fiscal year 2007 in General Revenue. This provision would also reduce the increased state TRS

contribution related to the salary provisions of the bill. These savings are already included in the TRS amounts discussed elsewhere in this document.

For the mentoring program, in 2006 there will be an estimated 40,200 teachers with less than two years experience. Under the assumptions of one mentor per three teachers, and a cost of \$1,500 annually, this would give an initial cost of \$20.1 million annually. However, it is estimated that federal funds available for this purpose could be used to defray the cost to general revenue, lowering the annual cost to \$14.1 million, increasing slightly each year with teacher growth.

Based on submitted proposals from vendors, development of the electronic student records system is estimated to incur a one-time development cost to the Texas Education Agency of \$2 million in 2006, with ongoing maintenance costs of \$300,000 each year thereafter

The Comptroller estimates a gain in state tax revenue ranging from \$8.2 million in fiscal year 2006 to \$14.0 million in fiscal year 2010 associated with the compression of the school year required under the provisions of the bill.

State At-Risk Incentive Program. The bill would limit the cost of the state incentive program for improving student performance on at-risk campuses to \$100 million annually, beginning with fiscal year 2007. It is assumed that this full amount would be utilized each year.

In 2007, the replacement of the \$30 per ADA technology allotment with a \$100 per ADA instructional materials and technology allotment is estimated to cost \$300 million. Beginning in 2008, the \$150 per ADA allotment is estimated to cost the state \$523 million in 2008 and \$534 million in 2009, increasing each year thereafter with student growth. However, given that the state would have appropriated funds for instructional materials in the 2008-09 biennium – estimated to be \$515 million for the biennium – the net increase in state costs for the 2008-09 biennium is \$542 million.

Technology grants: For the purposes of this fiscal note, it is assumed that funding available for technology grants under this section will be limited to non-General Revenue sources.

Dual language pilot program. Expenditures in 2007 are limited to \$130,000 for planning grants, and biennial expenditures for this project starting in the 2008-09 are limited to \$13 million.

Texas Governor's Schools. The schools would be supported by grants, limited to \$750,000 each, made from funds appropriated for that purpose. The commissioner would be granted rulemaking authority. Assuming 2 schools are approved each year, the annual cost is estimated to be \$1.5 million.

It is estimated that TEA would require additional staff to implement certain provisions of the bill. Beginning in 2006, the agency estimates the need for 3 full-time equivalents (FTEs) to review local plans under the educator excellence incentive program, 8 FTEs (decreasing to 4 FTEs in 2008 and beyond) for the biannual instructional materials review process, and 10 subject area experts to oversee the development of computer-adaptive assessment tools.

Article IV

For the facilities allotment for charters, the agency estimates that the charters that have been rated exemplary or recognized and meet the other requirements of the section represent approximately 6,000 students in ADA. At \$1,000 per ADA, the annual cost of this allotment is estimated to be \$6 million.

The estimated cost of providing additional state aid to qualifying charter schools for the stipulated salary increases assumes that all employees are appropriately certified. Data on certification status of charter school employees is not available. Under this assumption, the estimated cost to the state is \$8.6 million in fiscal year 2006 and \$2 million in each subsequent year. Increased TRS contributions associated with these provisions are estimated to be \$340,000 in fiscal year 2006 and \$504,000 in fiscal year 2007.

Article 7 of the bill would abolish the State Board for Educator Certification (SBEC) and transfer its duties to the Texas Education Agency. Since SBEC functions are supported entirely with fee revenue under current law, no cost or savings is anticipated with this transfer.

Technology

The bill would have a technology impact for the Texas Education Agency, including the development and maintenance of a student records system and a best practices clearinghouse, and the transfer of responsibility for district textbook orders.

Local Government Impact

School districts would see a decrease in local revenue and an increase to state aid commensurate with the funding formula changes described above. Out of these funds, school districts would be directed to fund the salary increases to employees subject to the minimum salary schedule stipulated in the bill. These costs are estimated at \$626 million in fiscal year 2006 and \$796 million in fiscal year 2007 statewide.

The bill would require school districts to use an amount equal to at least 1% of the districts' total professional staff payroll, estimated to be approximately \$200 million annually, to provide incentive payments to employees who demonstrate success in adding value to student achievement.

School districts would generally benefit fiscally from the state cost provisions identified above. Significant programmatic sources of revenue would include:

A mentor program would provide teachers across the state approximately \$14 million annually, and a new facilities program would provide certain high-performing charter districts \$1,000 per student.

School districts would receive additional funding for state at-risk incentive programs. Funding would be expected to total \$100.0 million annually, starting in 2007.

The bill would provide an instructional materials and technology allotment, which would provide districts an additional \$300 million for 2007 and \$524 million in 2008, increasing with student growth each year thereafter. Beginning in 2008, districts would be required to use these funds to purchase any needed instructional materials.

Source Agencies:

LBB Staff: JOB, CT, SD, JGM, UP