LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 79TH LEGISLATURE 3rd CALLED SESSION - 2006

April 19, 2006

TO: Honorable Jim Keffer, Chair, House Committee on Ways & Means

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

IN RE: **HB1** by Chisum (Relating to public school finance and property tax rate compression; making an appropriation.), **As Introduced**

Estimated Two-year Net Impact to General Revenue Related Funds for HB1, As Introduced: a negative impact of ($2,385,800,000) through the biennium ending August 31, 2007.

The bill contains language to make an appropriation to support the provisions of this bill, but does not specify an amount.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2007	($2,385,800,000)
2008	($2,542,800,000)
2009	($2,652,200,000)
2010	($2,804,700,000)
2011	($2,903,900,000)

All Funds, Five-Year Impact:

Fiscal Year	Probable Savings/(Cost) from *FOUNDATION SCHOOL FUND* 193	Probable Revenue Gain/(Loss) from *School Districts*
2007	($2,385,800,000)	($1,673,200,000)
2008	($2,542,800,000)	($1,366,300,000)
2009	($2,652,200,000)	($1,041,100,000)
2010	($2,804,700,000)	($680,300,000)
2011	($2,903,900,000)	($280,300,000)

Fiscal Analysis

The bill requires school districts, starting in the 2006 tax year (2006-07 school year), to reduce their nominal maintenance and operations (M&O) tax rate to the lesser of $1.33 per $100 of valuation, or 88.67 percent of the M&O rate adopted for the 2005 tax year - hereafter referred to as the "buydown" rate. The bill then entitles districts to state aid sufficient to guarantee state and local revenue per student in weighted average daily attendance (WADA) in an amount equal to the greater of (1) what the district would be entitled to in the 2006-07 school year under current law, or (2) 2006 revenue per WADA, including state aid districts received for property value decline and wealth-sharing arrangements. For a district subject to recapture, the additional revenue it is entitled to receive to maintain this revenue target may be received as an downward adjustment to its recapture payment.

Beginning in the 2006 tax year (2006-07 school year), districts have the ability to levy pennies of tax effort above the buydown rate. For the 2006 tax year, for districts "bought down" below $1.33, the district may levy up to 6 pennies above the buydown rate, but not to exceed a total M&O rate of $1.33, without a rollback election. For any district (excepting districts who are allowed under current law to tax above the $1.50 cap), accessing pennies above $1.33 requires a rollback election. For the 2006 tax year, districts may levy up to $1.38 with a simple majority approval by voters, and up to $1.48 with a 2/3 majority. For the 2007 and 2008 tax years, districts may levy up to $1.43 with a simple majority, and $1.48 with a 2/3 majority. For the 2009 and 2010 tax years, districts may levy up to $1.48 with a simple majority, and $1.50 with a 2/3 majority.

These pennies remain part of Tier 2 in the Foundation School Program, and thus eligible to the same guaranteed yield of $27.14 per penny per WADA. However, for districts subject to Chapter 41 recapture, the bill excludes M&O tax revenue generated on pennies above $1.33 from the calculation of their recapture payments.

The bill provides to the Texas School for the Blind and Visually Impaired and the Texas School for the Deaf state aid in an amount that would hold them harmless against the loss in local district tax revenue. The bill also requires districts participating in Tax Increment Financing (TIF) agreements to pay the same amount into a TIF fund as if the tax rate were the amount levied in 2005, and directs the Comptroller to deduct for this marginal TIF payment from the district's recognized taxable value.

The bill makes an appropriation of an unspecified amount to the Texas Education Agency for distribution to school districts to satisfy the requirements of the bill.

Methodology

In fiscal year 2007, this bill results in a total net state cost estimated to be $2,372 million. Of this amount, approximately $2,148 million represents the equivalent of a dollar-for-dollar replacement of state aid for local revenue in the school finance system. Since the Foundation School Program's funding formulas are unchanged by the bill, the portion of a district's entitlement not flowing through the formulas is delivered as a "hold harmless" payment. Other provisions in the calculation of a district's revenue target -- guaranteeing the higher of 2007 current law revenue or 2006 revenue per WADA, allowing districts to include revenue gained in excess of entitlement from wealth-sharing arrangements, and including revenue for property value decline -- add approximately $65 million in state costs in 2007.

The provision allowing districts to access pennies above their buydown rate results in additional local revenue and state costs. For fiscal year 2007, it is assumed that districts, on a statewide average basis, access the equivalent of four pennies above their buydown rate. The state guaranteed yield on these four pennies results in a state cost of $159 million, and an increase to retained local revenue of $474 million.

The bill's reduction in district local revenue, combined with the effect of netting out a district's recapture payments against its hold harmless revenue guarantee, reduces recapture payments statewide from an estimated $1.8 billion to approximately $1.2 billion in 2007.

After fiscal year 2007, net state costs of the bill increase, driven by the increasing cost to the state to replace the recapture revenue that is eliminated by the bill, and by districts accessing additional pennies above their buydown rate. The total net state cost of the bill increases by $100-$150 million in each year after fiscal year 2007, with a net state cost in 2011 estimated to be $2,877 million. State aid increases in the out years are enhanced by a revenue benefit certain districts gain by using 2006 revenue per WADA as their revenue target, but are somewhat offset by the bill's revenue target calculation which limits the revenue benefit certain districts otherwise would receive from property value increases.

The remaining out-year state cost increases are due to the assumption of increasing tax effort above districts' buydown rate. On top of the assumption of a statewide average of four pennies in 2007, it is assumed that districts will add another 3 pennies of tax effort in each year of 2008 to 2011. The Tier 2 state cost impact of these additional pennies is limited by the projection that districts will begin hitting the effective tax rate cap of $1.50 in increasing numbers in the years after 2007, and by the state fiscal benefit due to increase in recapture collected on additional pennies levied by recapture districts that fall below $1.33.

The state cost to hold the School for the Blind and Visually Impaired and the School for the Deaf harmless for the loss of school district revenue is estimated to be approximately $200,000 annually. The state aid increase due to the recognition of district payments into a TIF fund as required by the bill are estimated to be $14 million in 2007, increasing by roughly 17 percent each year thereafter.

Technology

The bill is not expected to have a significant technology impact to the Texas Education Agency.

Local Government Impact

School districts would see a decrease in local revenue due to the bill's tax rate reduction and an increase to state aid due to the bill's revenue guarantee provision.

Districts' local revenue loss from an 11.33 percent tax rate reduction is estimated to be $2,148 million in 2007, increasing by 4-5 percent each year thereafter. However, for the purposes of the fiscal note it is assumed that districts would access, on a statewide average basis, the equivalent of four pennies above their buydown rate in 2007, which would generate an estimated $474 million in retained local revenue, resulting in a net local revenue loss of approximately $1,673 million. These pennies also would generate an estimated $159 million in state aid. In fiscal year 2008, under the assumption of seven additional pennies over the buydown rate (the four levied in 2007 and another 3 in 2008), the local revenue loss prior to enrichment of $2,333 million would be offset by a gain of $867 million in retained local revenue on those seven pennies. For 2009 to 2011, it is assumed that districts would add an average of three pennies each year, with corresponding impacts to local revenue and state aid.

Source Agencies: 304 Comptroller of Public Accounts

LBB Staff: JOB, SD, JGM