Texas Public School Finance Overview

TEXAS EDUCATION AGENCY

DECEMBER 2017

Presentation disclaimer

This presentation introduces and explains basic concepts of public school finance in Texas. It provides a high-level and simplified overview.

This presentation uses generalizations that are accurate for most school districts that have a compressed M&O tax rate of $1.00. More information about tax rate compression will be covered later in the presentation.

All formula calculations are based on fiscal year (FY) 2018 law. For any concept, there may be a significant exception in statute.

The descriptions, amounts, and formulas described in this presentation are derived from publicly available TEA documents, the General Appropriations Act, and the Texas Education Code (TEC) and are cited for reference.

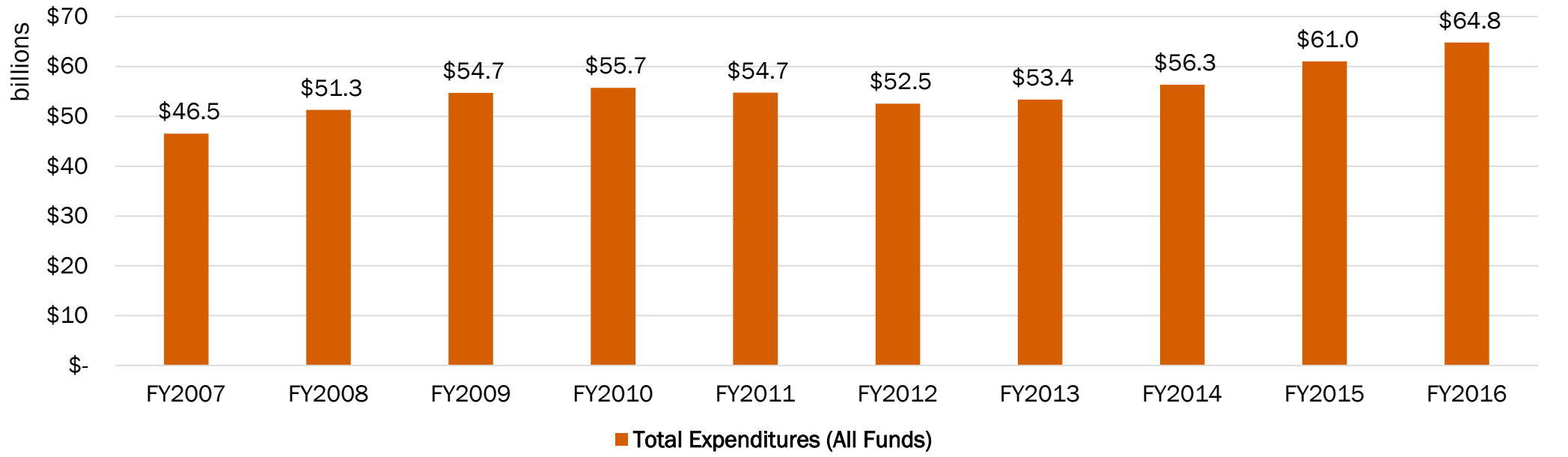
Agenda

- Public education expenditures
- Foundation School Program
  - Tier I and Tier II Funding
  - Facilities Funding
  - Charter School Funding
  - Wealth Equalization (Chapter 41)
- Special Topics
  - Districts with rapidly declining local property values
  - Financial Hardship Transition Program (HB21)
  - Appendix: Additional State Aid for Tax Reduction (ASATR)

Public education expenditures

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

Aggregate annual school district expenditures (all funds)

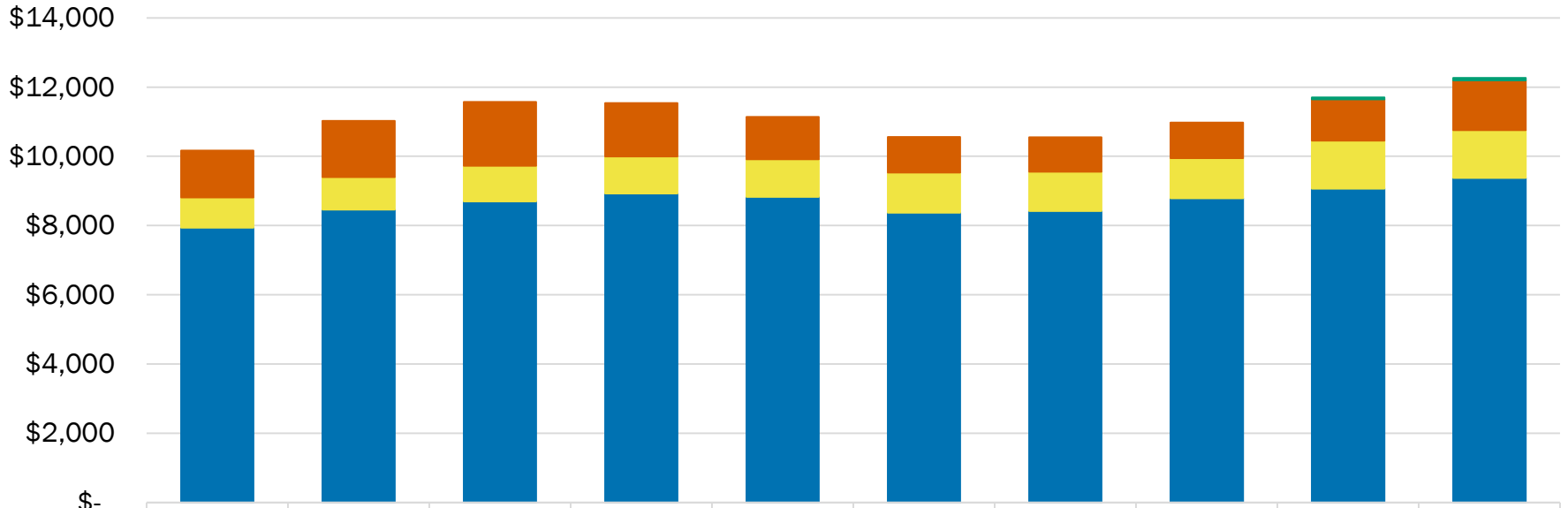


School district expenditures from state, local, and federal funds have increased by $18.3 billion annually, or 39.3% from $46.5 billion in FY2007 to $64.8 billion in FY2016.

All Funds generally includes all State, Local, Federal (including all Title programs and the Federal Free and Reduced Lunch Program), and Other Funds.
Expenditure Data taken from the TEA PEIMS online data and can be found at http://tea.texas.gov/financialstandardreports/.
Note: PEIMS Budgeted Financial Data reports do not include revenues or expenditures for education service centers (ESCs). They also exclude revenues, expenditures, and student counts for Texas Youth Commission schools.
Note: PEIMS Expenditure data includes Capital Outlay Expenditures

Average annual school district expenditures per student

All Funds per student expenditures have increased by $2,102 or 20.7% from $10,163 in FY2007 to $12,264 in FY2016.



	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016
Facilities Acquisition & Construction	$-	$-	$-	$-	$-	$-	$-	$-	$63	$69
Capital Outlay	$1,351	$1,625	$1,841	$1,543	$1,225	$1,024	$995	$1,026	$1,187	$1,440
I&S	$871	$936	$1,031	$1,076	$1,088	$1,167	$1,137	$1,159	$1,389	$1,382
M&O	$7,941	$8,463	$8,696	$8,922	$8,829	$8,366	$8,417	$8,787	$9,065	$9,373

All Funds generally includes all State, Local, Federal (including all Title programs and the Federal Free and Reduced Lunch Program), and Other Funds.
Expenditure Data taken from the TEA PEIMS online data and can be found at http://tea.texas.gov/financialstandardreports/.

Note: PEIMS Expenditure data includes Capital Outlay Expenditures as well.
Note: Prior to FY2015 Facilities Acquisition & Construction Costs were not disaggregated from total M&O expenditures

Texas Public Education Funds, 2016–2017 vs. 2018–2019 Biennium (in billions)

Public Ed Funding	2016–2017 Appropriated Biennium	2018–2019 Appropriated Biennium	Dollar Change 2016–2017 vs. 2018–2019	% Change 2016–2017 vs. 2018–2019
State Formula Funding	$42.33	$43.87	$1.54	3.60%
Local Formula Funding	$53.81	$59.49	$5.68	10.55%
Subtotal Formula Funding	**$96.14**	**$103.36**	**$7.22**	**7.54%**
State Non-Formula Funding / Interagency Contracts & Other	$1.94	$1.69	($0.25)	(13.03%)
Federal Program Funds	$10.11	$10.38	$0.27	2.70%
TEA Administration	$0.28	$0.29	$0.01	4.80%
Total Public Education Spending	**$108.47**	**$115.72**	**$7.25**	**6.68%**

Foundation School Program

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

Foundation School Program (FSP)

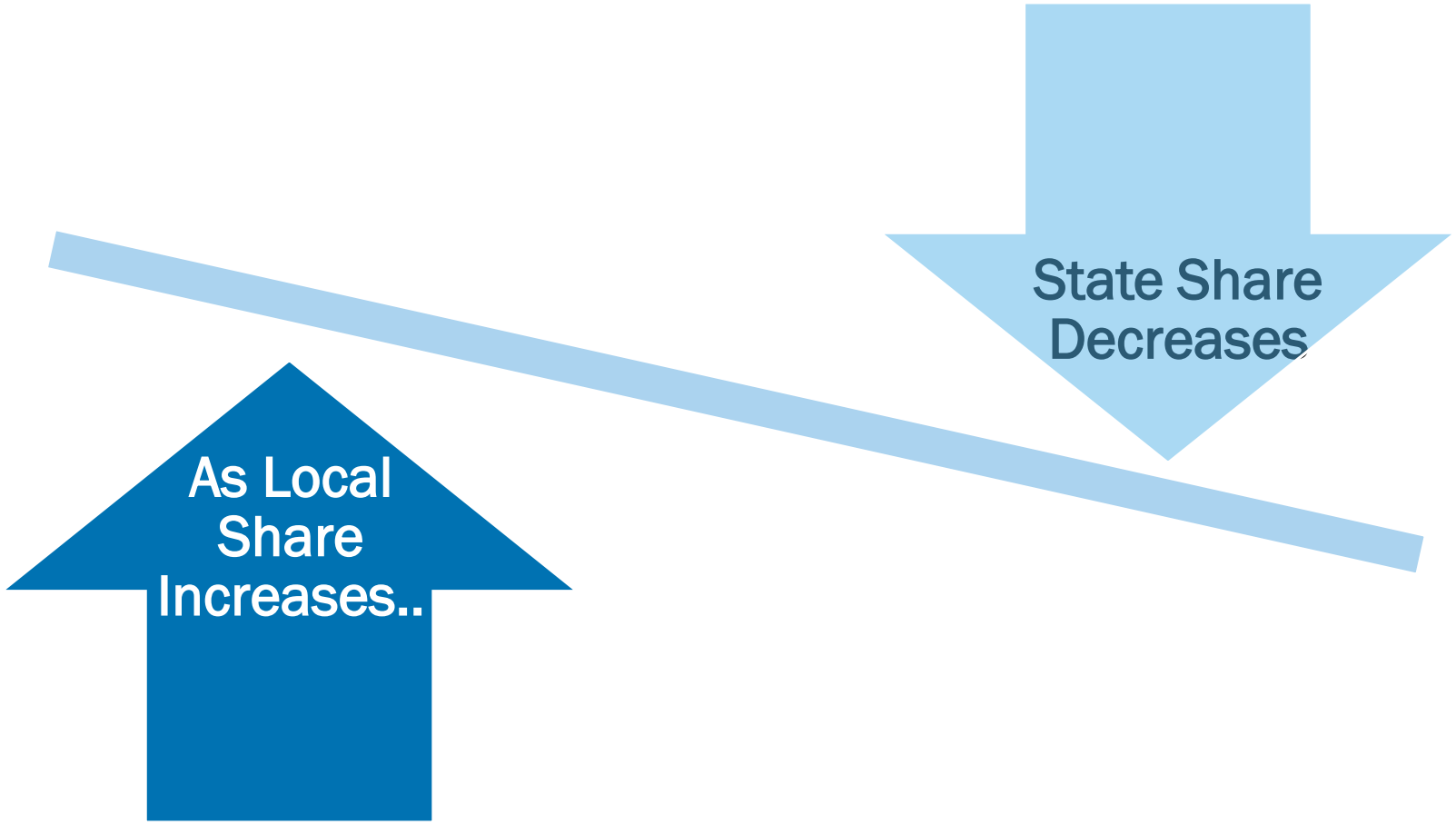
The FSP establishes how much state funding school districts and charter schools are entitled to receive.

Formulas are set in statute (Chapters 41, 42, and 46), and they consider both student and district characteristics including the number and type of students enrolled, district size and geographic factors, and local taxable property values and tax rates.

Generally, once entitlements are established, the formulas are used to determine how much a district can generate locally (local share) through property taxes before making up the difference with state funds (state share).

A balancing act:

State Share vs. Local Share



Total FSP Entitlement set in the GAA

Total FSP Entitlement = Tier I Entitlement + Tier II Entitlement + Facilities Funding

State Share for Tier I and Tier II is appropriated in the General Appropriations Act (GAA), TEA Strategy A.1.1. Equalized Operations

State Share of Facilities funding is appropriated in the GAA, TEA Strategy A.1.2. Equalized Facilities

ARTICLE III

EDUCATION

Sec. 1. The several sums of money herein specified, or so much thereby as may be necessary, are appropriated out of any funds in the State Treasury not otherwise appropriated, or out of special funds as indicated, for the support, maintenance, or improvement of the designated agencies and institutions of education.

TEXAS EDUCATION AGENCY

	For the Years Ending August 31, 2018	August 31, 2019
Method of Financing:		
General Revenue Fund		
General Revenue Fund	$ 151,626,205	$ 149,626,204
Available School Fund No. 002, estimated	1,177,006,486	2,266,943,046
Instructional Materials Fund No. 003	1,091,110,514	12,270,954
Foundation School Fund No. 193, estimated	15,255,570,375	13,487,733,815
Certification and Assessment Fees (General Revenue Fund)	28,063,223	28,063,223
Lottery Proceeds, estimated	1,297,000,000	1,316,500,000
Subtotal, General Revenue Fund	$ 19,000,376,803	$ 17,261,137,242

Total Statewide FSP Entitlement in FY2018

5.04 million students in average daily attendance

and that number is projected to grow by more than 70,000 each year

$44.87 billion (state & local) for FSP M&O

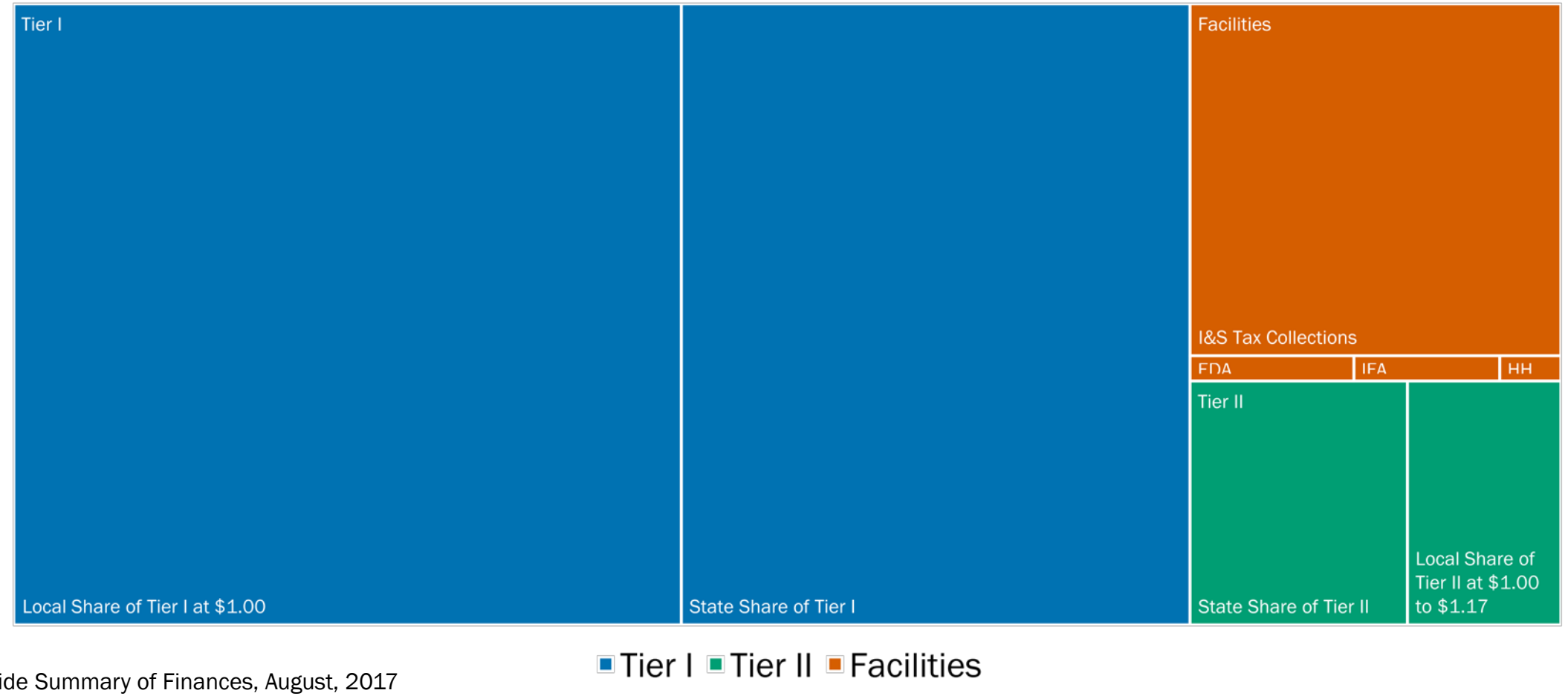
M&O = maintenance & operations -> salaries, utilities, etc.

$6.94 billion (state & local) for FSP I&S

I&S = interest & sinking -> debt service payments on bonds

TEA Statewide Summary of Finances, August, 2017

Total Statewide FSP Entitlement in FY2018



TEA Statewide Summary of Finances, August, 2017

FSP Key Concepts: M&O local property tax rate contribution to each Tier

Tier I

Compressed M&O Tax Rate ($1.00)

RECAPTURE

LEVEL 1

Tier II

LEVEL 1

Six Golden Pennies ($1.00 - $1.06)

NO RECAPTURE

Tier II

LEVEL 2

Copper Pennies ($1.06 - $1.17)

RECAPTURE

LEVEL 2

Maintenance and Operations Tiers

TIER I

Refers to the district's foundation entitlement.

The calculation is based upon:

- District characteristics.
- Student characteristics.
- Number of students in average daily attendance (ADA).
- **Basic allotment** per student in ADA, which is set in the General Appropriations Act ($5,140 in FY2018 and FY2019).
- School district tax rate (generally, $1.00 per $100 of local school district property value).

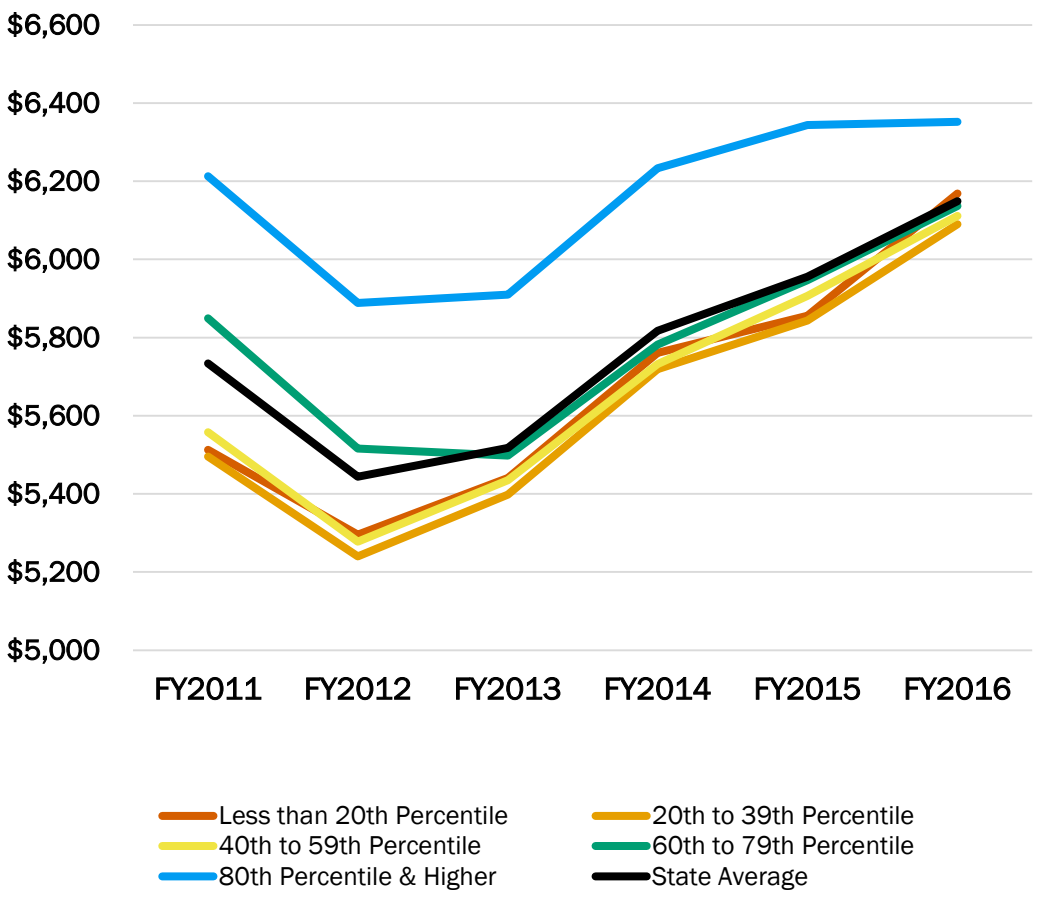
TIER II

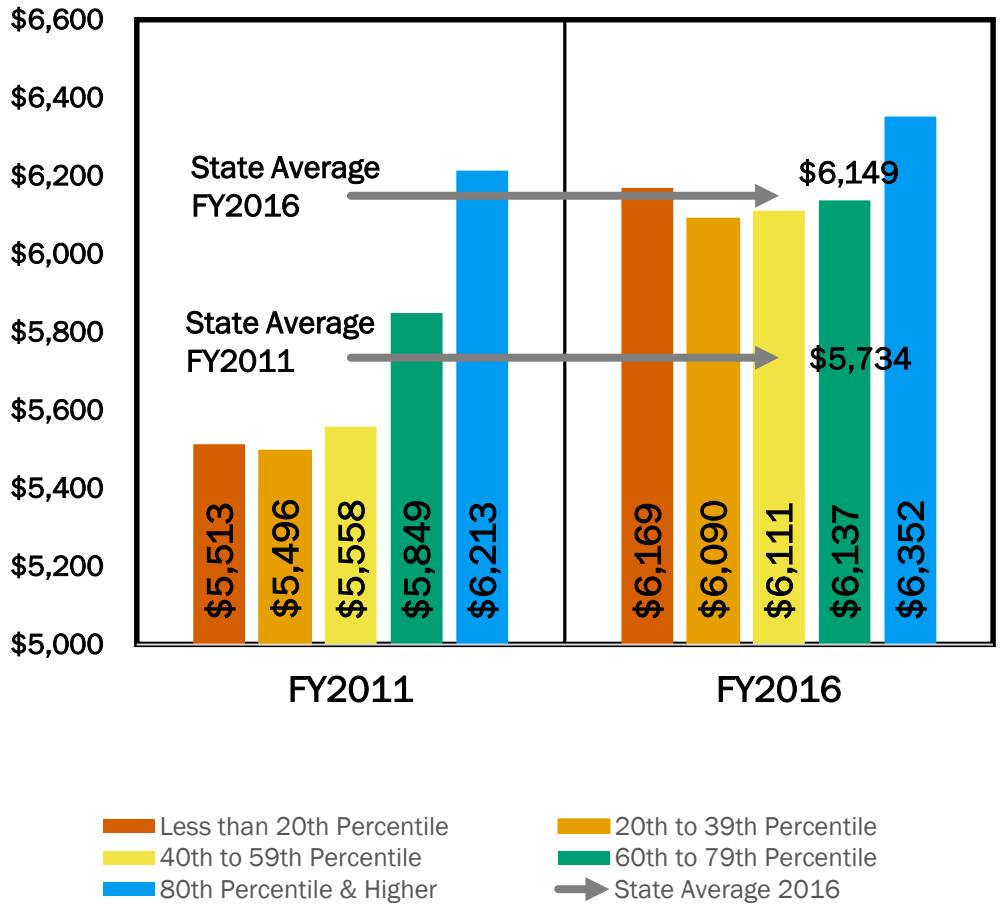
Refers to the district's "enrichment" entitlement.

The calculation is based upon:

- Number of students in weighted average daily attendance (WADA).
- Number of pennies of tax effort above $1.00.
- Guaranteed amounts for pennies of tax effort are set in statute and/or General Appropriations Act called the **Guaranteed Yield** Per Penny.
- School district tax rate (based on local decision to have optional tax rate between $1.00 and $1.17 per $100 of local school district property value).

FY2011 through FY2016 M&O Revenue per WADA by Wealth Percentiles





Source: Legislative Budget Board (Document ID: 3737)

Tier I Funding

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

How is Tier I funding determined?

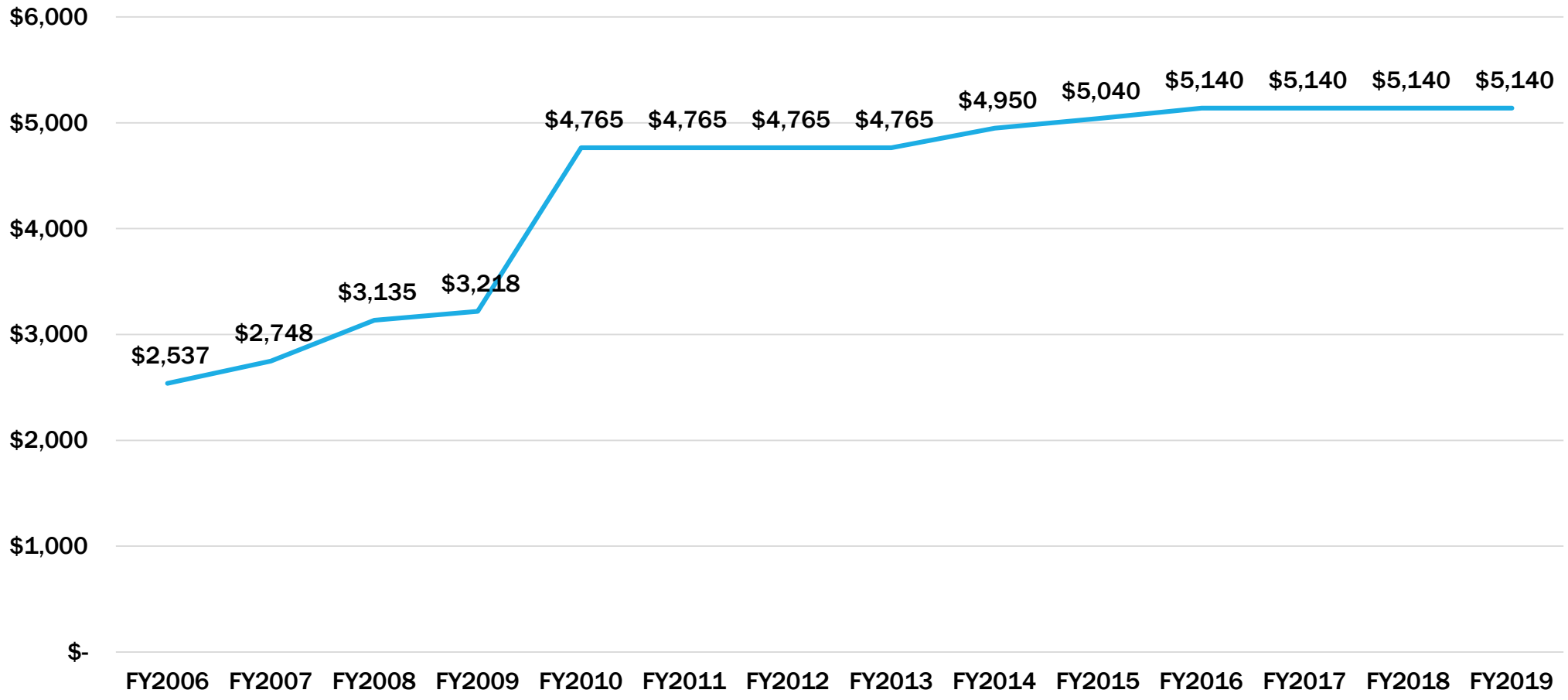
The Basic Allotment (BA) is $5,140 per student for the 2018–2019 biennium and is set in the General Appropriations Act (GAA).

The $5,140 BA per student is increased for school characteristics:

- Increased for the school districts' cost of education index (CEI);
- Increased if the school district qualifies as small district or mid-size district

Once the BA has been increased for school characteristics, it is used in a series of formulas that take into account student characteristics.

The Basic Allotment has more than doubled since FY2006



Cost of Education Index (CEI)

The CEI is assigned to each district to adjust for the cost of educating students in the district's particular region of the state.

The CEI is based upon the principle that it is more expensive to provide education in some school districts than others.

Each school district was assigned a unique CEI in 1991. The CEI has not been updated since that time.

CEI values range from a low of 1.02 to a high of 1.20. The average CEI is 1.12.

The average funding increase produced is $620 for each student in ADA in each district, and the total formula amount produced for all school districts by the CEI is estimated to be $2.7 billion for FY2018.

Impact of different CEI values on the Basic Allotment

ABC ISD (CEI = 1.08)

ABA = BA × (((CEI – 1) × 0.71) + 1)

ABA = $5,140 × (((1.08 – 1) × 0.71) + 1)

Adjusted Basic Allotment (ABA) = $5,432 per student in average daily attendance

XYZ ISD (CEI = 1.17)

ABA = BA × (((CEI – 1) × 0.71) + 1)

ABA = $5,140 × (((1.17 – 1) × 0.71) + 1)

Adjusted Basic Allotment (ABA) = $5,760 per student in average daily attendance

Small district and mid-size district adjustments

The small district and mid-size district adjustment provide for additional funding for some school districts.

The small district adjustment (SDA) applies to districts with less than 1,600 students and has two formulas that provide differing levels of funding:

- **For districts < 300 square miles, $SDA^1 = (1 + ((1{,}600 - ADA) \times 0.00025)) \times$ Adjusted Basic Allotment**
- **For districts > 300 square miles, $SDA^2 = (1 + ((1{,}600 - ADA) \times 0.00040)) \times$ Adjusted Basic Allotment**

The mid-size district adjustment (MDA) applies to districts with less than 5,000 students.

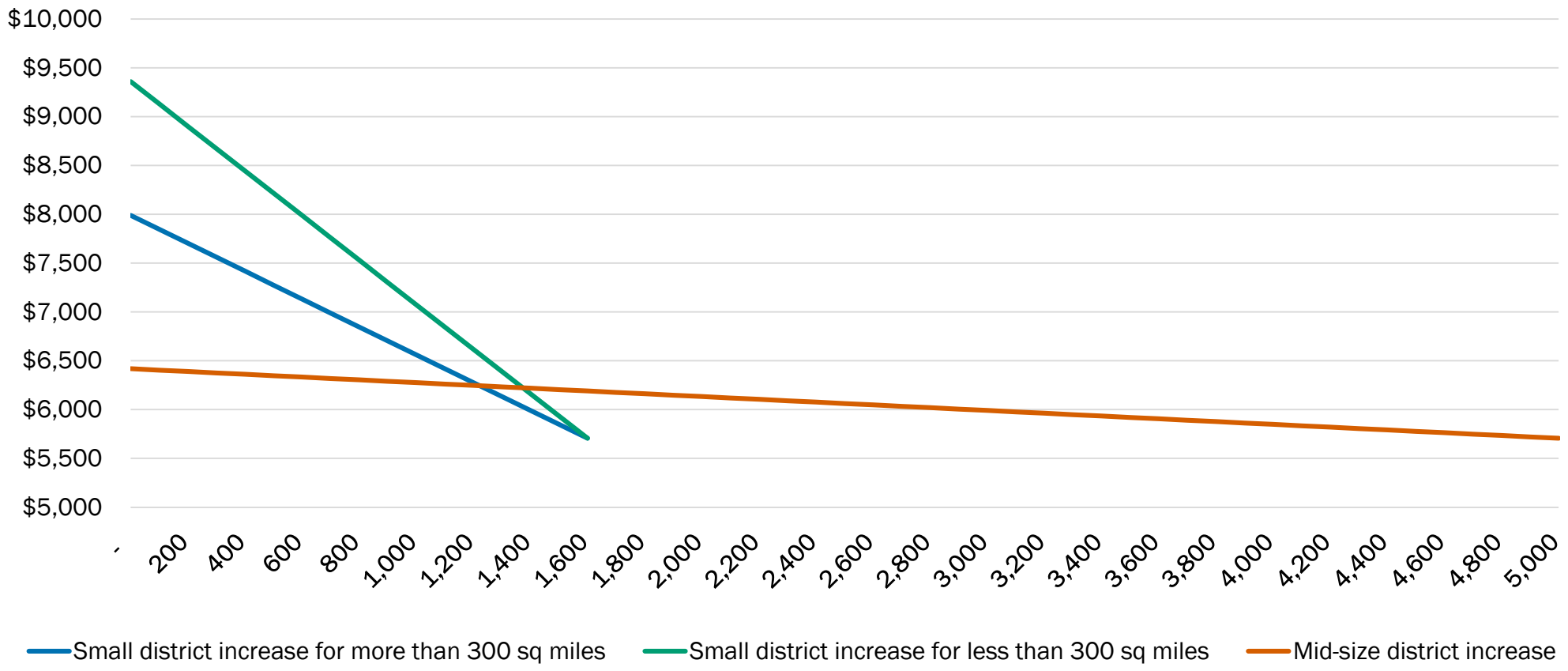
- **$MDA = (1 + ((5{,}000 - ADA) \times 0.000025)) \times$ Adjusted Basic Allotment**

Small district adjustment and HB 21

In 2017, House Bill 21 (85-1) created a six-year transition period to merge the two adjustments together. The transition period begins in FY2019 and by FY2024, there will only be one formula to govern all small-size districts, regardless of the number of square miles in the district. For districts with < 300 square miles, the adjustment factor will increase from 0.000025 (FY2018) to 0.00040 (FY2024).

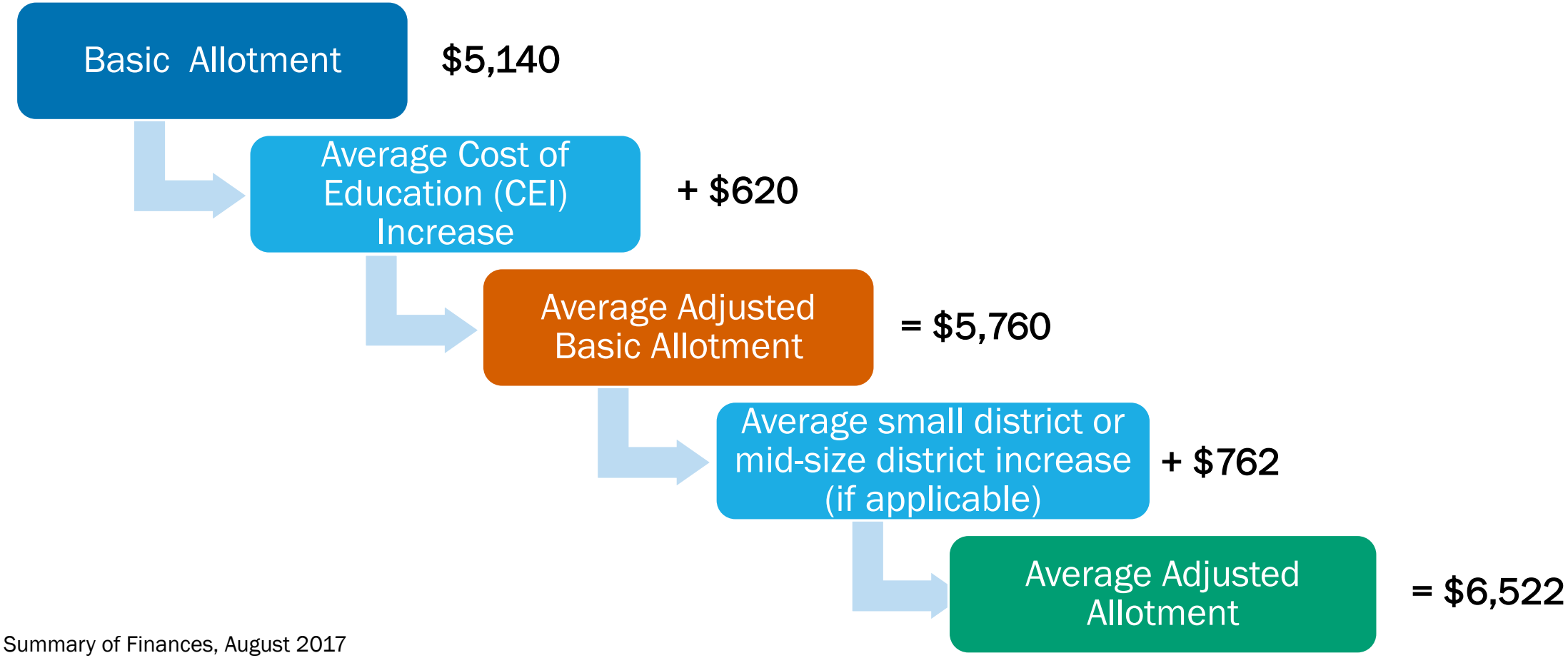
Fiscal Year	SDA Factor		Fiscal Year	SDA Factor
FY2019	0.000275		FY2022	0.000350
FY2020	0.000300		FY2023	0.000375
FY2021	0.000325		FY2024	0.000400

“Per student” funding generated by the SDA and MDA formulas decreases as enrollment increases



TEA Statewide Summary of Finances, August, 2017

In Summary: How the Basic Allotment becomes the Adjusted Allotment



TEA Statewide Summary of Finances, August 2017

Tier I includes funding weights to deliver additional funding for student characteristics

Program	Funding Weight
Regular Program	1.00
Special Education	various weights for each instructional setting
Career and Technology (CTE)	1.35
Advanced CTE	$50 per each eligible CTE course
Gifted & Talented	0.12 (capped at 5% of district ADA)
Compensatory Education	0.20
Pregnancy Related Services	2.41 (part of compensatory education)
Bilingual Education	0.10
Public Education Grant	0.10
New Instructional Facility Allotment	$1,000 per student in ADA in the new facility
High School Allotment	$275 per high school student in ADA

Tier I Bilingual / ESL Allotment example

In general, Tier I allotments are calculated by multiplying the number of students in each instructional setting by the applicable funding weight and by the district's adjusted allotment:

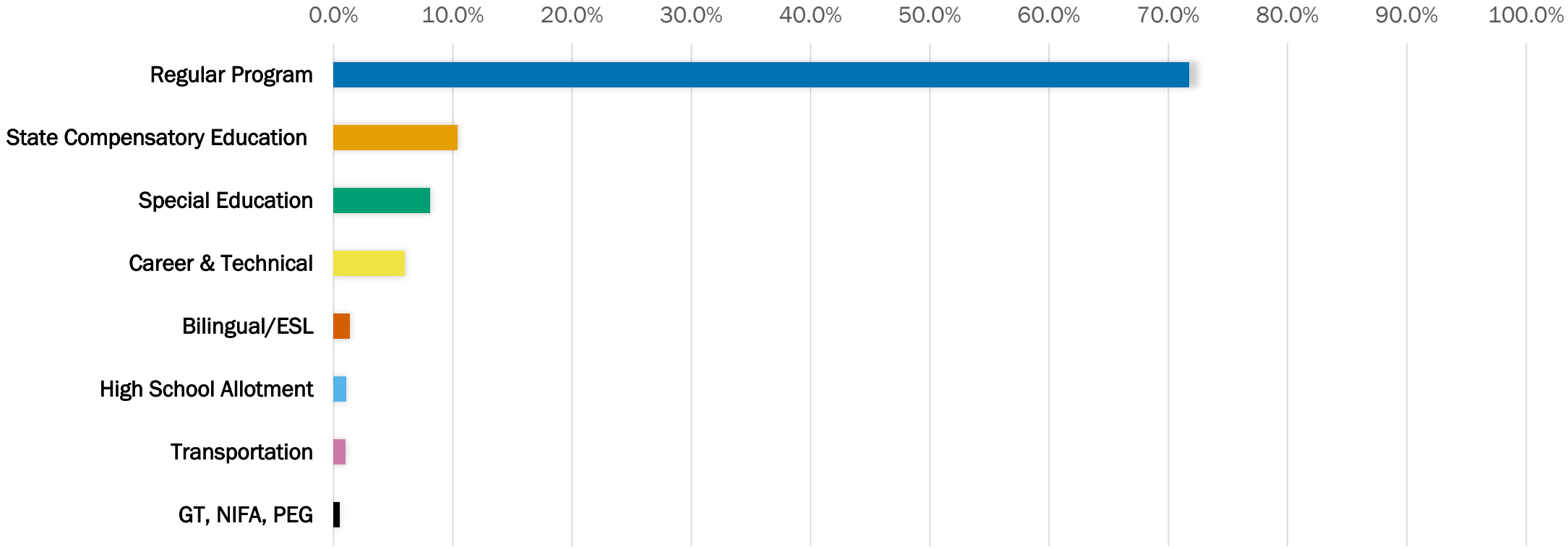
Bilingual/ESL ADA × Funding Weight × Adjusted Allotment

2,000 bilingual/ESL ADA × 0.10 × $6,522 = $1,304,400 in additional funding

Tier I formula amounts for a typical district

Program	Formula Amount	Percent of Total Tier I Funding
Regular Program Allotment	**$9,050,000**	**72.4%**
Special Education Adjusted Allotment	$880,000	7.0%
Career and Technology Allotment	$775,000	6.2%
Gifted & Talented Adjusted Allotment	$60,000	0.5%
Compensatory Education Allotment	$1,275,000	10.2%
Bilingual Education Allotment	$40,000	0.3%
Public Education Grant	$0	0.0%
New Instructional Facility Allotment	$0	0.0%
Transportation Allotment	$280,000	2.2%
High School Allotment	$140,000	1.1%
Total Cost of Tier I	**$12,500,000**	**100.0%**

The Regular Program Allotment comprises majority of Tier I funding ($26.6 billion out $37.1 billion)



	GT, NIFA, PEG	Transportation	High School Allotment	Bilingual/ESL	Career & Technical	Special Education	State Compensatory Education	Regular Program
Series1	0.5%	1.0%	1.1%	1.4%	6.0%	8.1%	10.4%	71.7%

Tier I: Local Share calculated at $1.00

Tier I

Compressed M&O Tax Rate ($1.00)

RECAPTURE

LEVEL 1

Tier I: Calculation of State Share

CHAPTER 42 DISTRICT

Tier I Total Cost	$12,500,000
Prior Tax Year District Property Value	$650,000,000
Local Share at $1.00 M&O tax rate	$6,500,000
State Share of Tier I	**$6,000,000**

CHAPTER 41 DISTRICT

Tier I Total Cost	$12,500,000
Prior Tax Year District Property Value	$1,350,000,000
Local Share at $1.00 M&O tax rate	$13,500,000
State Share of Tier I	**$0**

Tier II Funding

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

Tier II Overview

A district's Tier II allotment provides for enrichment funding which is intended to supplement the basic funding provided by Tier I funds.

To receive Tier I funding, school districts generally must tax at $1.00 per each $100 of local district property value. However, districts have local discretion to set a tax rate that is between $1.00 and $1.17.

Tier II focuses on taxpayer equity by ensuring that school districts receive a guaranteed amount of funding for each penny of tax effort between $1.00 and $1.17 for each student in their weighted average daily attendance (WADA).

This guaranteed amount per WADA is called the **guaranteed yield.**

Tier II: Golden and Copper Pennies

Tier II

LEVEL 1

Golden Pennies: Local discretion to tax between $1.00 & $1.06

NO RECAPTURE

Tier II

LEVEL 2

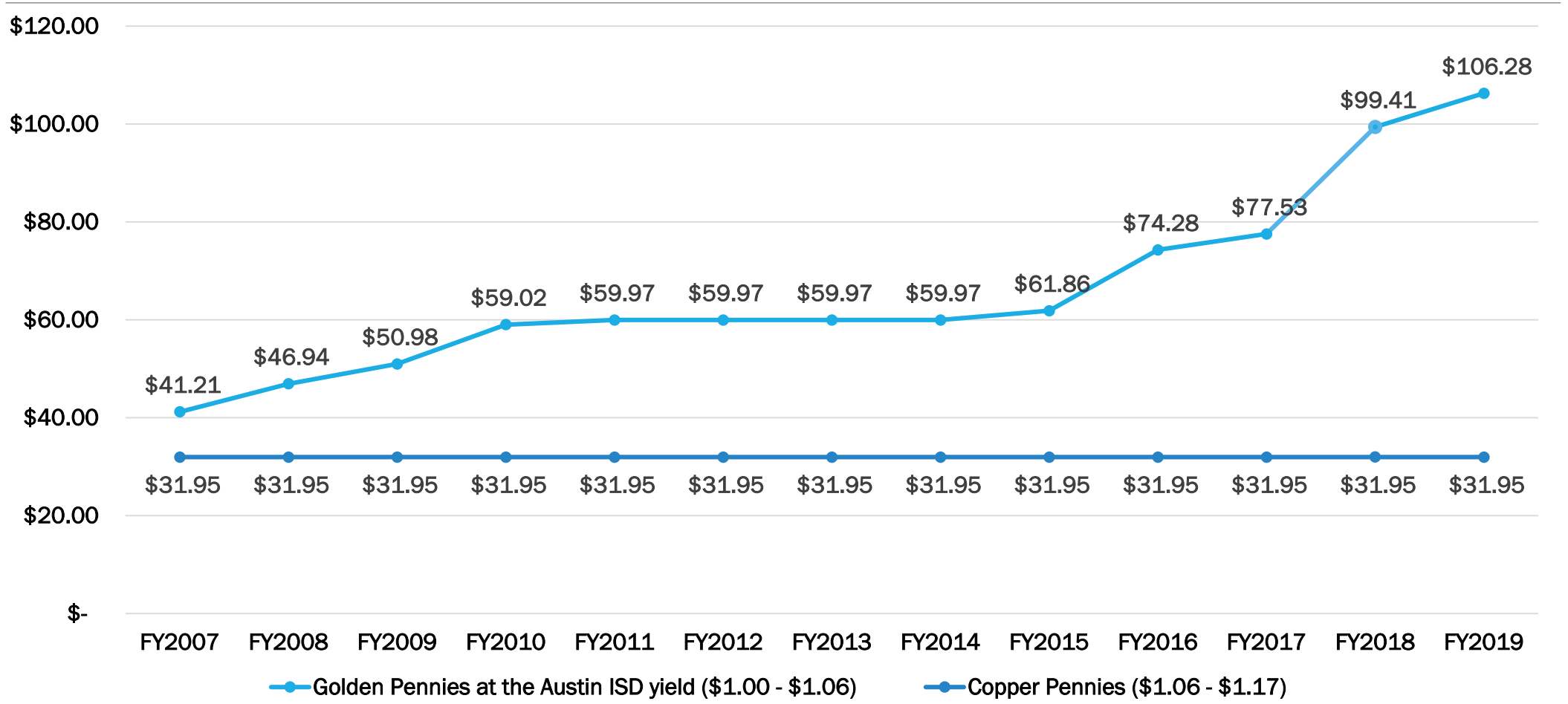
Copper Pennies: Local discretion to tax between $1.06 & $1.17

RECAPTURE

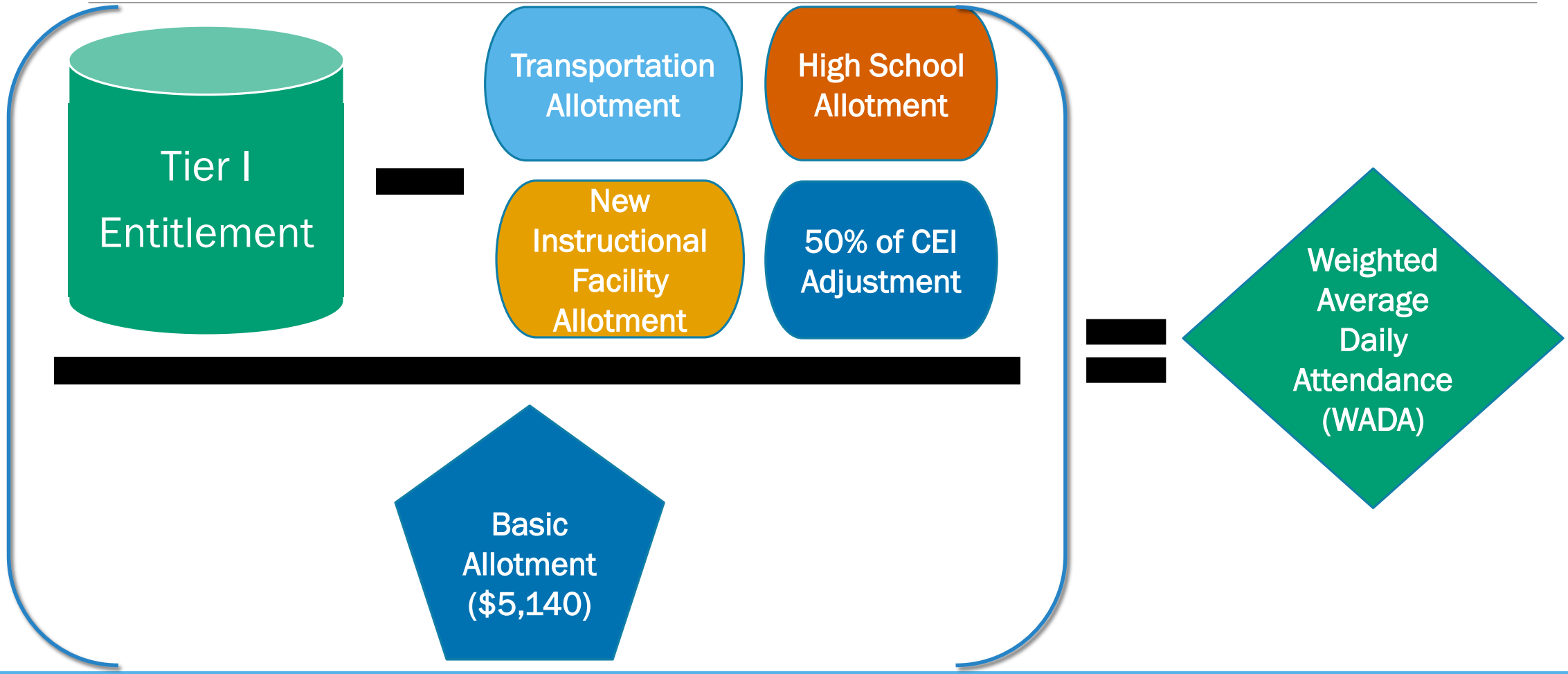
LEVEL 2

Voter Approval needed to tax above $1.04

Tier II Guaranteed Yield History



Tier II: How are the number of weighted students (WADA) in a district calculated?



The difference between ADA and WADA

AVERAGE DAILY ATTENDANCE (ADA)

The number of actual students in attendance on the average school day.

There are 5.04 million ADA in Texas but there are 6.84 million WADA.

There will always be less ADA than WADA.

Used to calculate Tier I allotments.

WEIGHTED AVERAGE DAILY ATTENDANCE (WADA)

Calculated using Tier I allotments (not the number of actual students in attendance).

Generally, districts with large populations of students with special characteristics (compensatory education students) will have more WADA.

Used to calculate Tier II allotments.

Tier II: Golden Pennies in FY2018

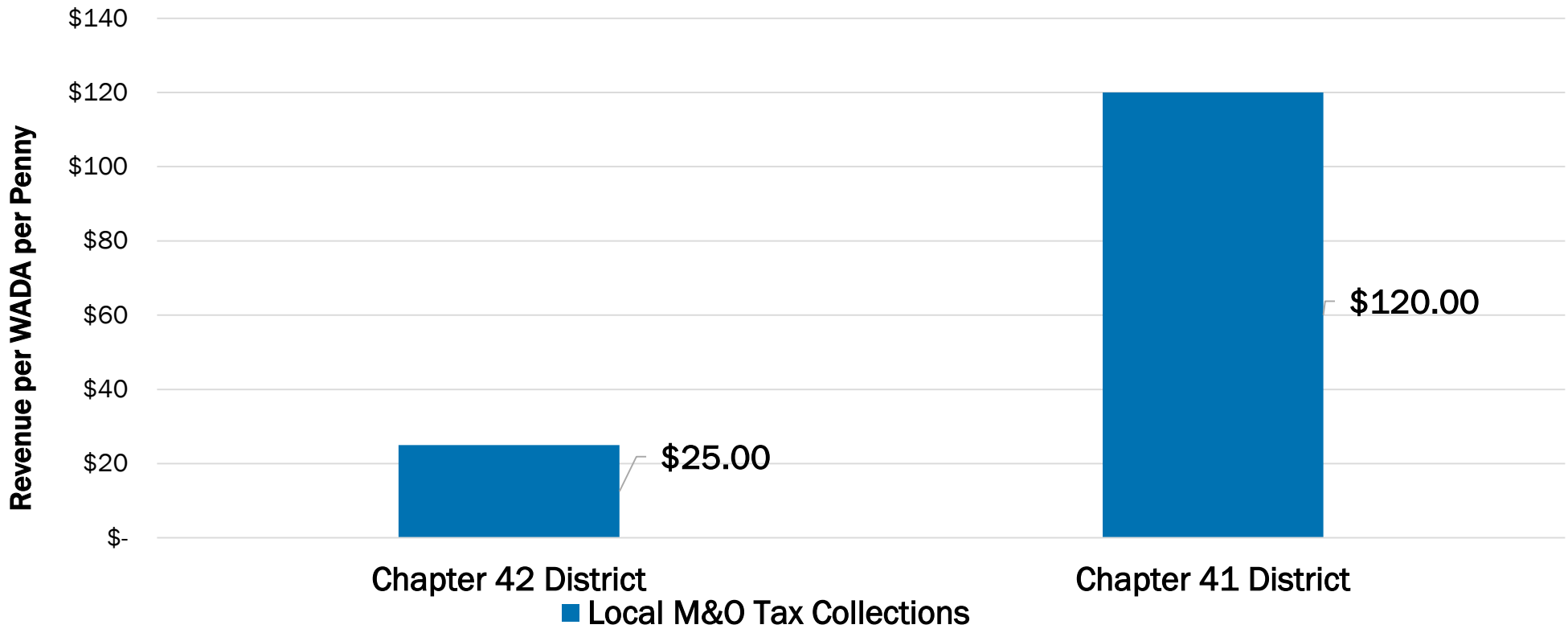
Tier II

LEVEL 1

Six Golden Pennies are equalized up to Austin ISD's wealth level of $99.41

NO RECAPTURE

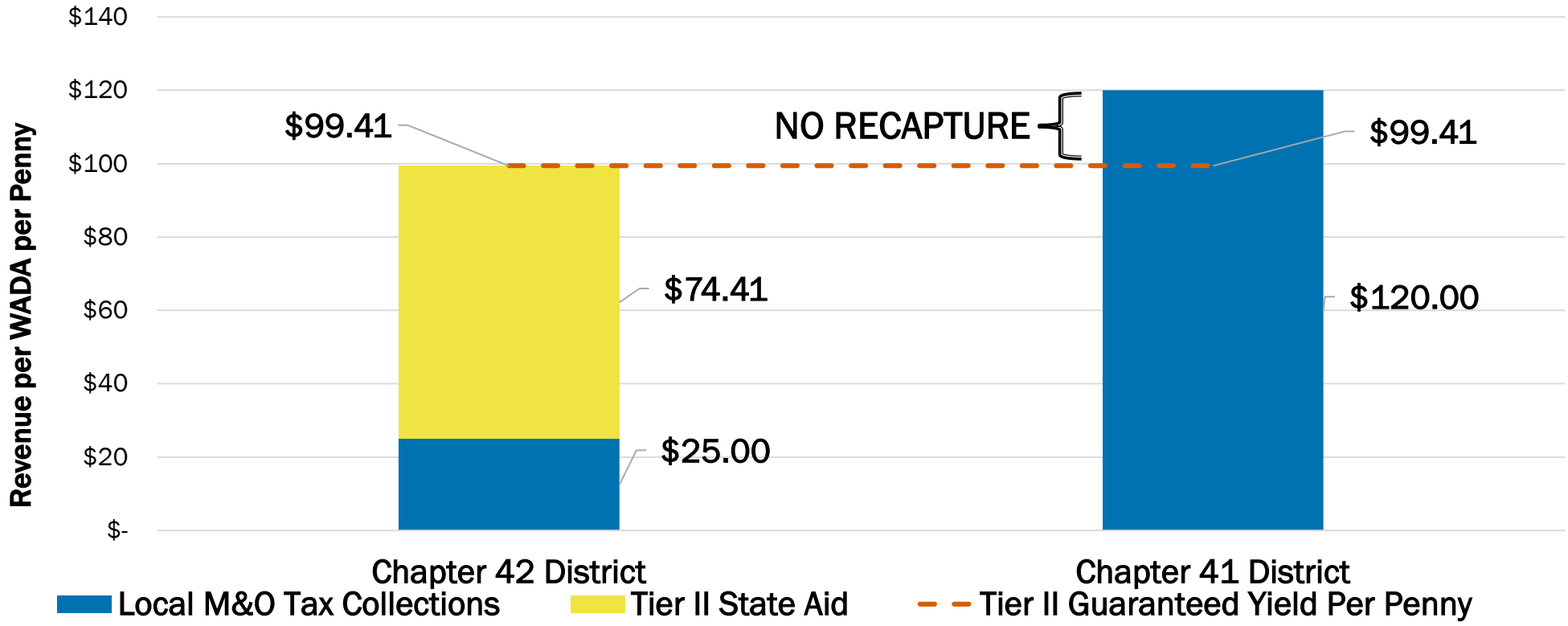
Revenue generated by a penny of tax effort can vary greatly between districts



Disparities in local taxable property values directly affect how much a penny of M&O tax effort can generate at the local level.

Tier II introduces the concept of the GUARANTEED YIELD (GY) formula on a "PER PENNY PER WADA" basis to help close the gap.

Chapter 42 districts are equalized up to AISD wealth level for the golden pennies



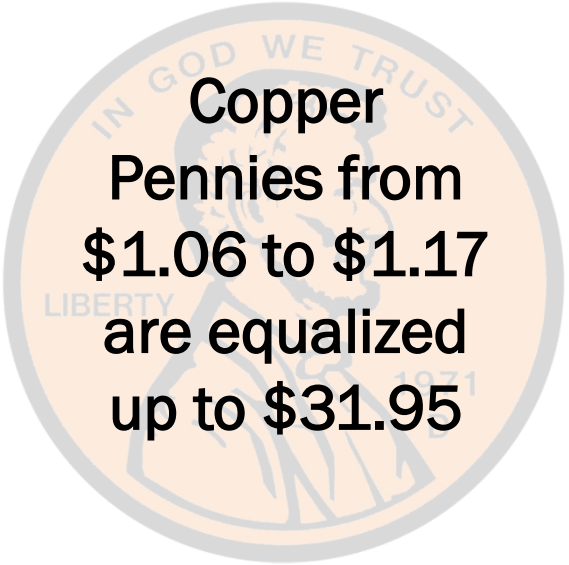
Golden Pennies equalized up to $99.41 per penny of tax effort per WADA (up to Austin ISD Wealth Level).

No recapture of M&O tax collections from districts that have a wealth per WADA greater than Austin ISD.

Tier II: Copper Pennies in FY2018

Tier II

LEVEL 2

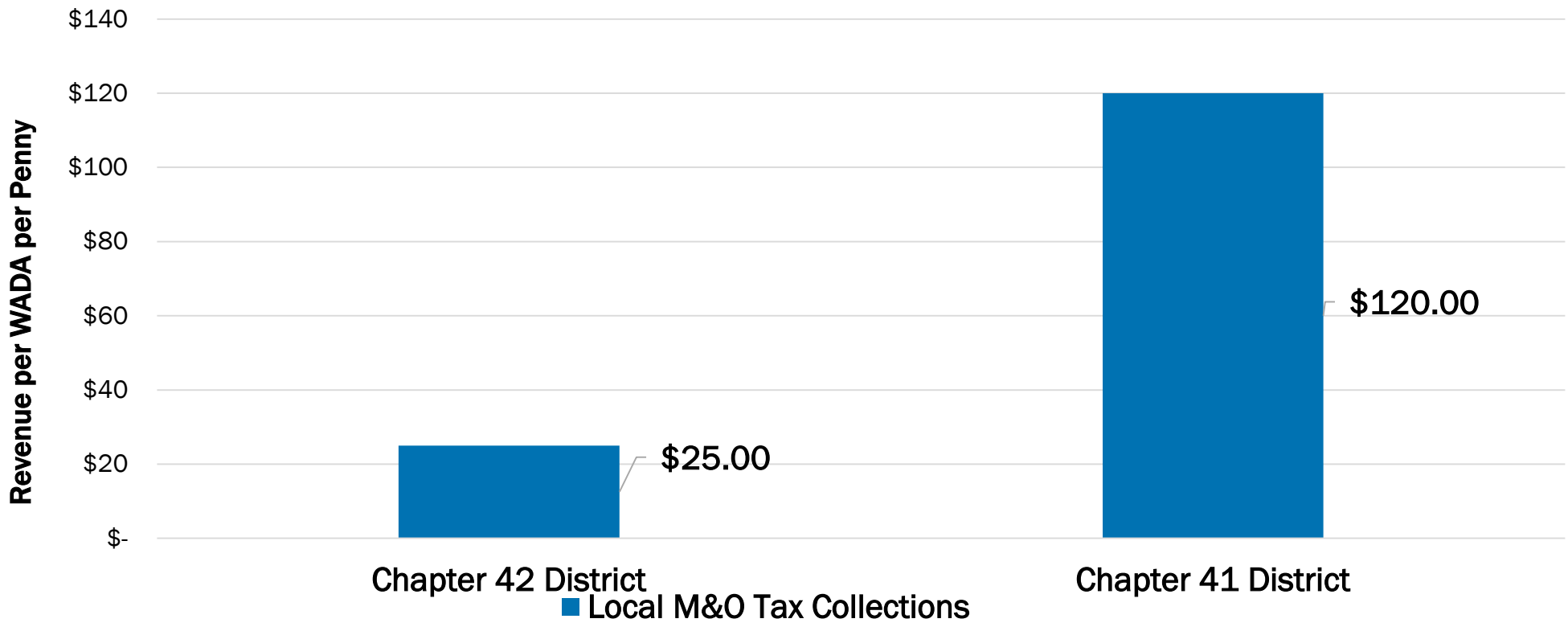


Copper Pennies from $1.06 to $1.17 are equalized up to $31.95

RECAPTURE

LEVEL 2

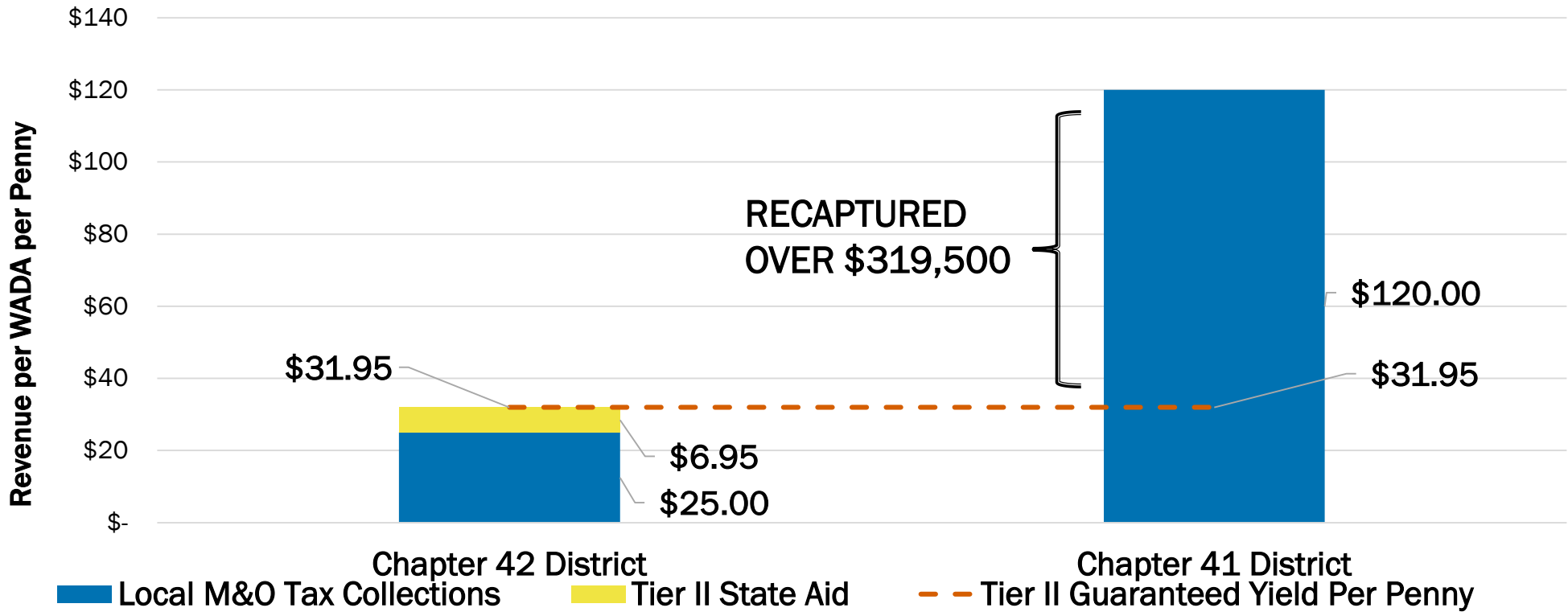
Revenue generated by a penny of tax effort can vary greatly between districts



Disparities in local taxable property values directly affect how much a penny of M&O tax effort can generate at the local level.

Tier II introduces the concept of the GUARANTEED YIELD (GY) formula on a "PER PENNY PER WADA" basis to help close the gap.

Chapter 42 districts are equalized up to $31.95 per WADA for the copper pennies



Copper pennies are equalized up to $31.95 per penny of tax effort for WADA

M&O tax collections from districts that generate more than $31.95 per penny per WADA are subject to recapture

Tier II Summary for FY2018

Six Golden Pennies guaranteed yield amount per WADA of $99.41

+

Copper Pennies guaranteed yield amount per WADA of $31.95

=

Total Tier II Entitlement

Golden Pennies

- Based on the six pennies above $1.00 ($1.00 to $1.06)
- Local election needed to tax above $1.04
- For Chapter 42 districts, the state will fund up to the Austin ISD yield per penny ($99.41) of tax effort per WADA
- **For property rich districts, there is no recapture on these six pennies**

Copper Pennies

- Based on pennies above $1.06 up to $1.17
- For Chapter 42, the state will fund up to the $31.95 yield per penny of tax effort per WADA
- Chapter 41 districts with tax effort in this zone will be recaptured at the $319,500 equalized wealth level

Tier II example of a district with an M&O tax rate of $1.12 and a local yield of $50

TIER II, LEVEL 1 (GOLDEN PENNIES)

WADA	1,000
Number of Golden Pennies	6
Guaranteed Yield	$99.41
Tier II, Level 1 Entitlement	$596,460
(Line 1 x Line 2 x Line 3)	
Local Share	$300,000
(Line 1 x Line 2 x $50)	
Tier II, Level 1 State Share	$296,460
(Line 4 – Line 5, floor of $0)	

TIER II, LEVEL 2 (COPPER PENNIES)

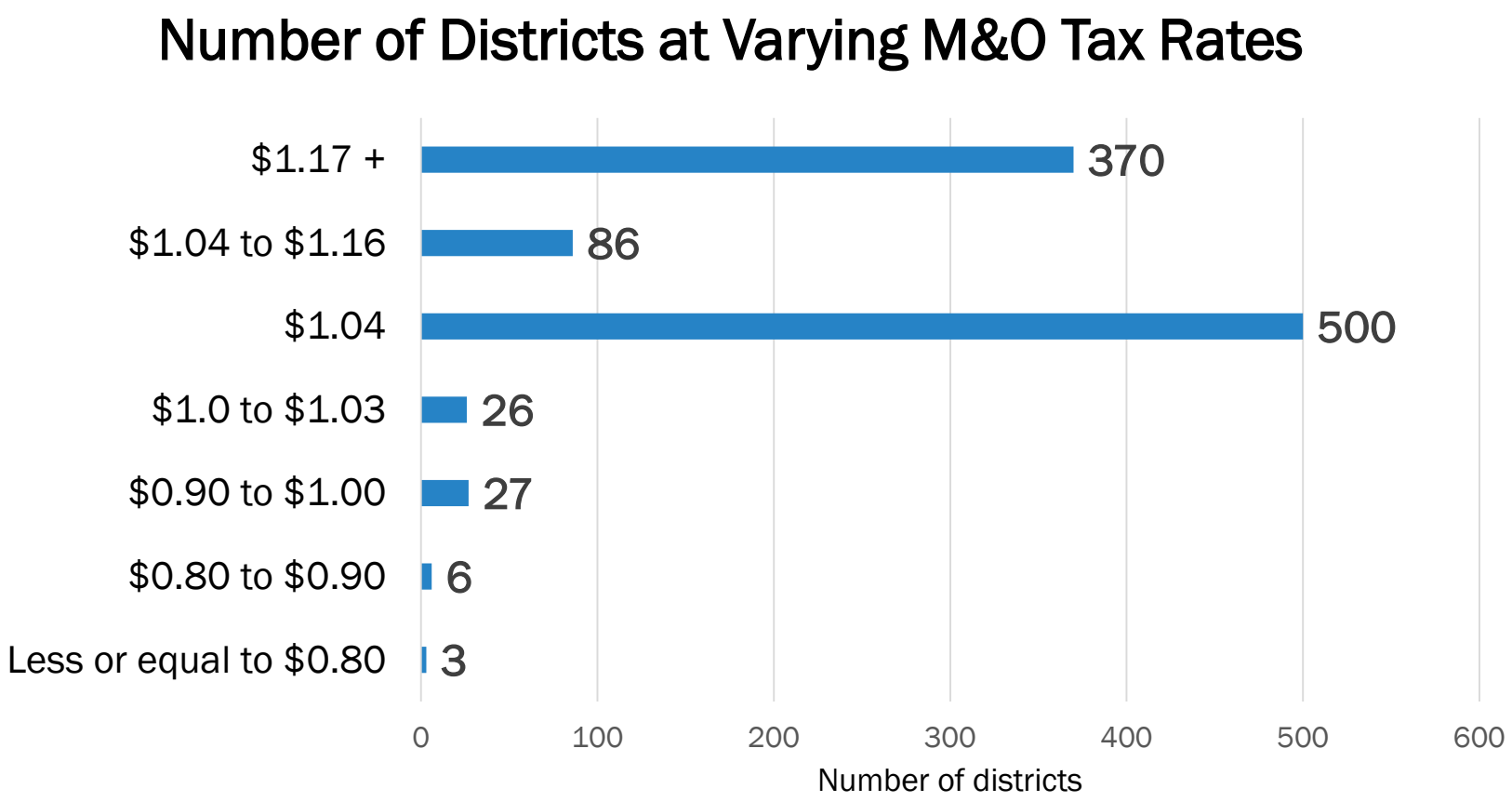
WADA	1,000
Number of Copper Pennies	6
Guaranteed Yield	$31.95
Tier II, Level 2 Entitlement	$191,700
(Line 1 x Line 2 x Line 3)	
Local Share	$300,000
(Line 1 x Line 2 x $50)	
Tier II, Level 1 State Share	$0
(Line 4 – Line 5, floor of $0)	

2016 M&O Adopted Tax Rates

M&O tax rates range from **$0.70 cents to $1.24** (certain Harris county districts are able to tax above $1.17)

500 districts have adopted a $1.04 tax rate

370 districts have adopted the maximum 1.17 or above



Facilities Funding

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

Facilities Funding

In Texas, school districts can adopt interest & sinking (I&S) tax rates up to **$0.50** cents to generate revenue used to fund the annual debt service payments associated with bonds that are typically issued for the construction of facilities as well as for other legal, voter-approved purposes.

I&S tax collections are **not** used to pay directly for construction costs.

Facilities Funding: Instructional Facilities Allotment (IFA)

This program was enacted by House Bill 1 of the 75th Legislature (1997).

The IFA program provides assistance to school districts in making debt service payments on qualifying bonds.

Proceeds must be used for the construction or renovation of an instructional facility only.

The program operates through applications (**prior to bond issuance**) and has award cycles. The IFA is **NOT** used to pay directly for construction costs.

History of IFA awards

Round	Fiscal Year	Funding for Previous Awards (excluding new money)	Amount designated for new debt
1	FY1998	NA	Initial appropriation for all new debt
2	FY1999	NA	Initial appropriation for all new debt
3	FY2000	$124.9 million	$50 million
4	FY2001	$173.1 million	$50 million
5	FY2002	$202.3 million	$50 million
6	FY2003	$236.4 million	$50 million
-	FY2004	$272.4 million	NA
7	FY2005	$263.7 million	$20 million
-	FY2006	$269.6 million	NA
8	FY2007	$252.9 million	$50 million
-	FY2008	$281.1 million	NA
9	FY2009	$237.4 million	$87.5 million
-	FY2010	$285.3 million	NA
10	FY2011	$225.8 million	$75 million
-	FY2012	$300.3 million	NA
-	FY2013	$290.9 million	NA
-	FY2014	$276.7 million	NA
-	FY2015	$255.9 million	NA
-	FY2016	$224.2 million	NA
11	FY2017	$185.2 million	$55.5 million

Source: Texas Education Agency, Summary of Finances

Facilities Funding: Existing Debt Allotment (EDA)

Created by the Texas Legislature in 1999, and the roll-forward provision was made permanent in 2009 (HB 3646).

House Bill 21 (2017, First Called Session) increased the EDA guaranteed yield from $35 to the *lesser of* $40 per ADA per penny on interest and sinking fund (I&S) taxes levied by school districts to pay the principal of and interest on eligible bonds, *or* an amount that would result in a $60 million increase in state aid from the previous yield of $35. The yield for the 2017–2018 school year is estimated to be less than $37.

EDA can be used to help pay for debt on both instructional and non-instructional facilities. EDA is **NOT** used to pay directly for construction costs.

The program operates without applications and has no award cycles but, **to be eligible, payment of existing bonds must have been made during the final year of the previous biennium.**

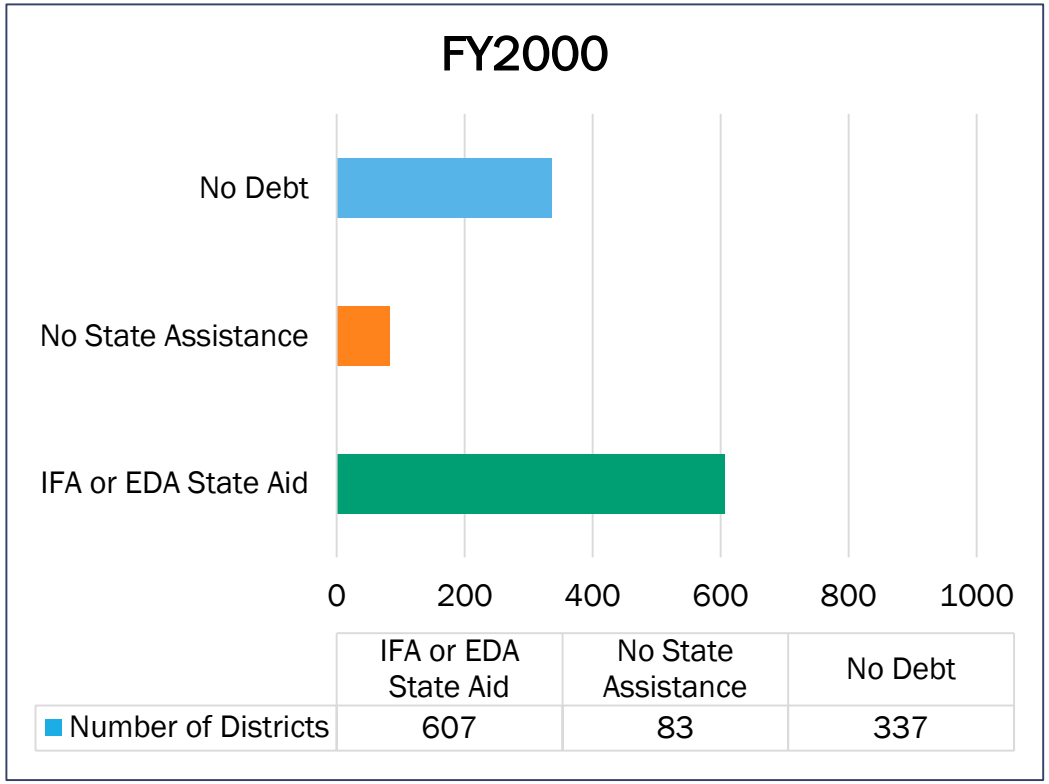
Eligibility, guaranteed yields, and limits on IFA and EDA

Funding formulas for facilities are similar to Tier II because they work on a **guaranteed yield per penny of tax effort per student.** However, facilities funding formulas use ADA instead of the WADA used in Tier II.

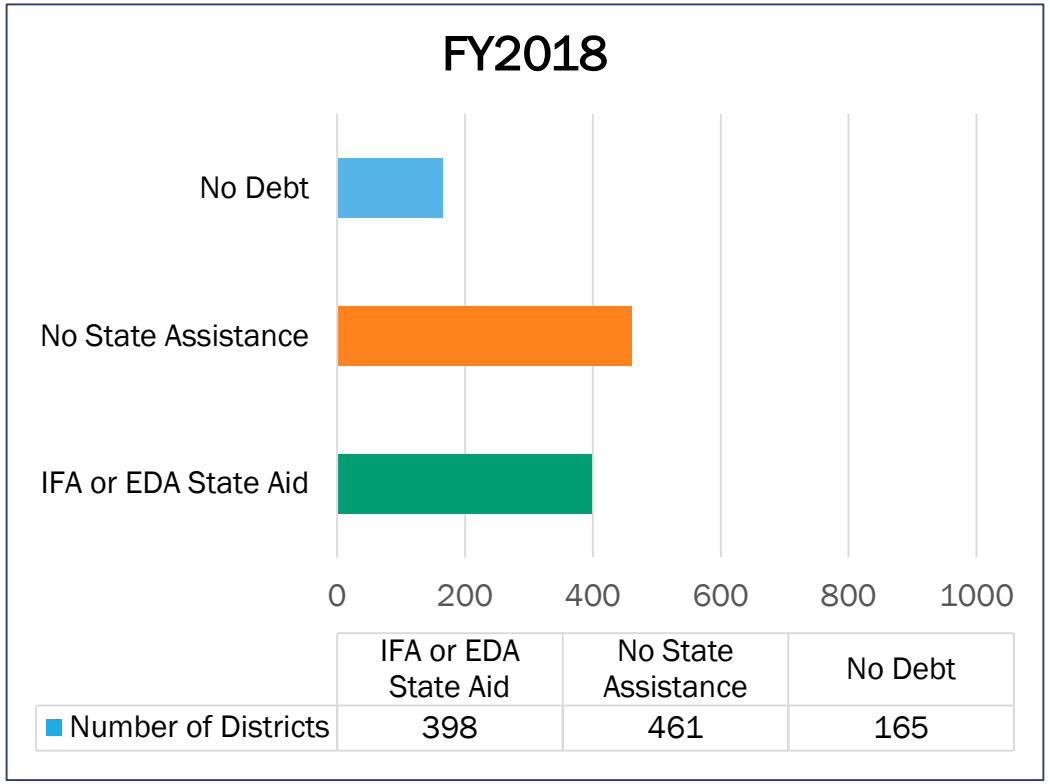
IFA has a guaranteed yield of $35 per student in ADA per penny of tax effort, while EDA has a floating guaranteed yield, currently estimated to be approximately $37, and EDA funding is currently limited to $0.29 cents of tax effort.

How many districts receive IFA and EDA?

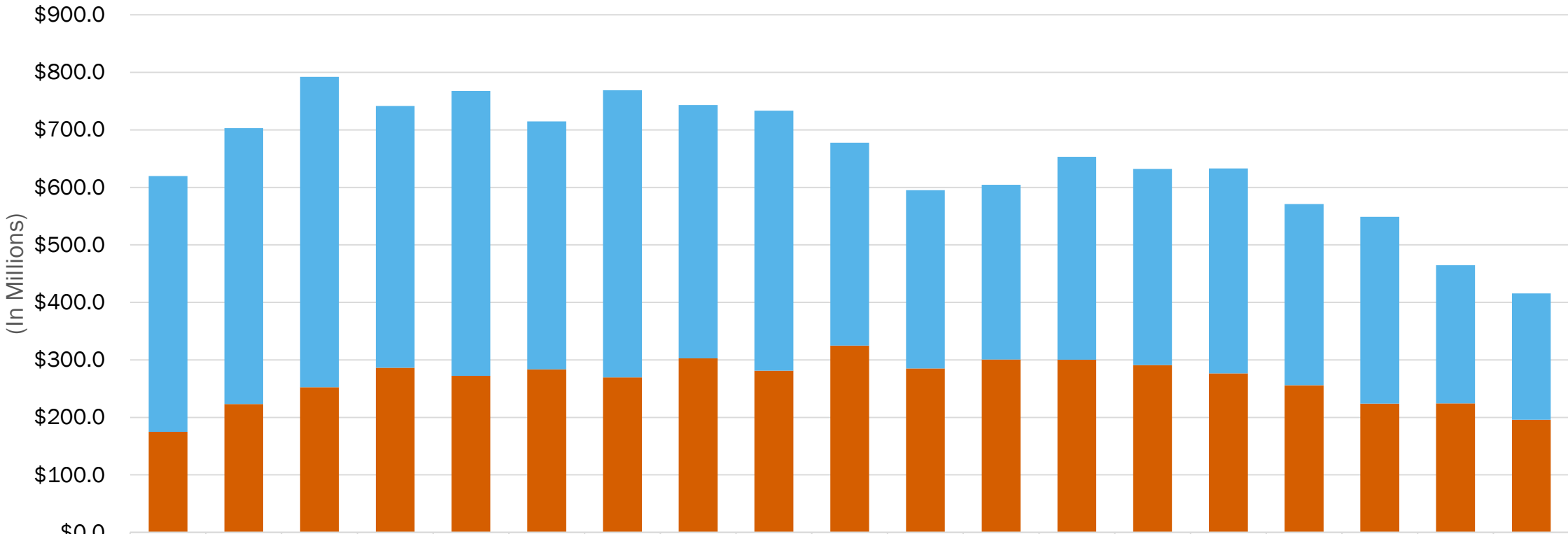
IN FY2000, 607, OR 59% OF SCHOOL DISTRICTS RECEIVED EITHER IFA OR EDA.



IN FY2018, 398, OR 39% OF SCHOOL DISTRICTS RECEIVED EITHER IFA OR EDA.



The state has contributed nearly $12.4 billion to public school facilities funding since the inception of IFA and EDA.



	FY2000	FY2001	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016	FY2017	FY2018
EDA	$444.7	$479.9	$539.8	$455.2	$495.1	$430.9	$499.3	$440.2	$452.4	$352.6	$309.7	$303.7	$352.7	$341.4	$356.3	$315.2	$324.5	$240.5	$219.8
IFA	$174.9	$223.1	$252.3	$286.4	$272.4	$283.7	$269.6	$302.9	$281.1	$324.9	$285.3	$300.8	$300.3	$290.9	$276.7	$255.9	$224.2	$224.4	$195.9

Charter School Funding

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

Charter school funding

Charter schools are entitled to Tier I and Tier II state aid, but, because they do not have the ability to generate the local share through a property tax base, the state funds 100% of the entitlements.

Charters are funded using state average funding variables for Tier I, Tier II, and EDA (covered next).

Charter schools are not eligible for facilities funding under IFA but do qualify for NIFA as part of the Tier I calculation and will qualify for EDA beginning in FY2019 due to the passage of HB21 (2017).

Charter school funding – Tiers I & II

Charter schools' Tier I allotments are calculated using the **state average** adjusted allotment ($6,522 in FY2018).

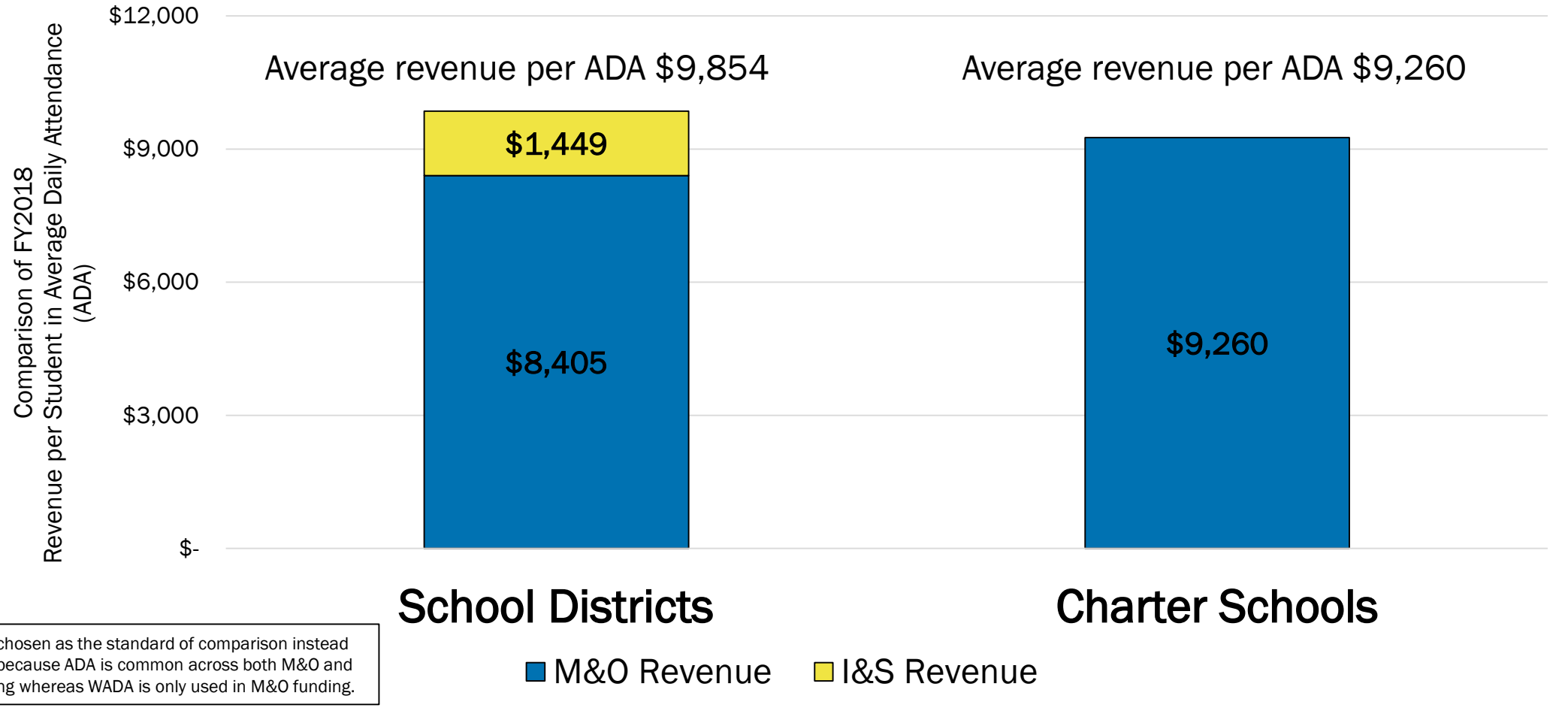
This average allotment is higher than that of many school districts because the **small district and mid-size district funding increases are already factored in** when the average is computed.

Charter schools' Tier II allotments are calculated using the state average M&O tax rates for the golden and copper pennies ($0.0568 and $0.0445, respectively in FY2018). **Charters benefit as more districts hold elections to increase their M&O tax rates above $1.04.**

Charter school funding - EDA

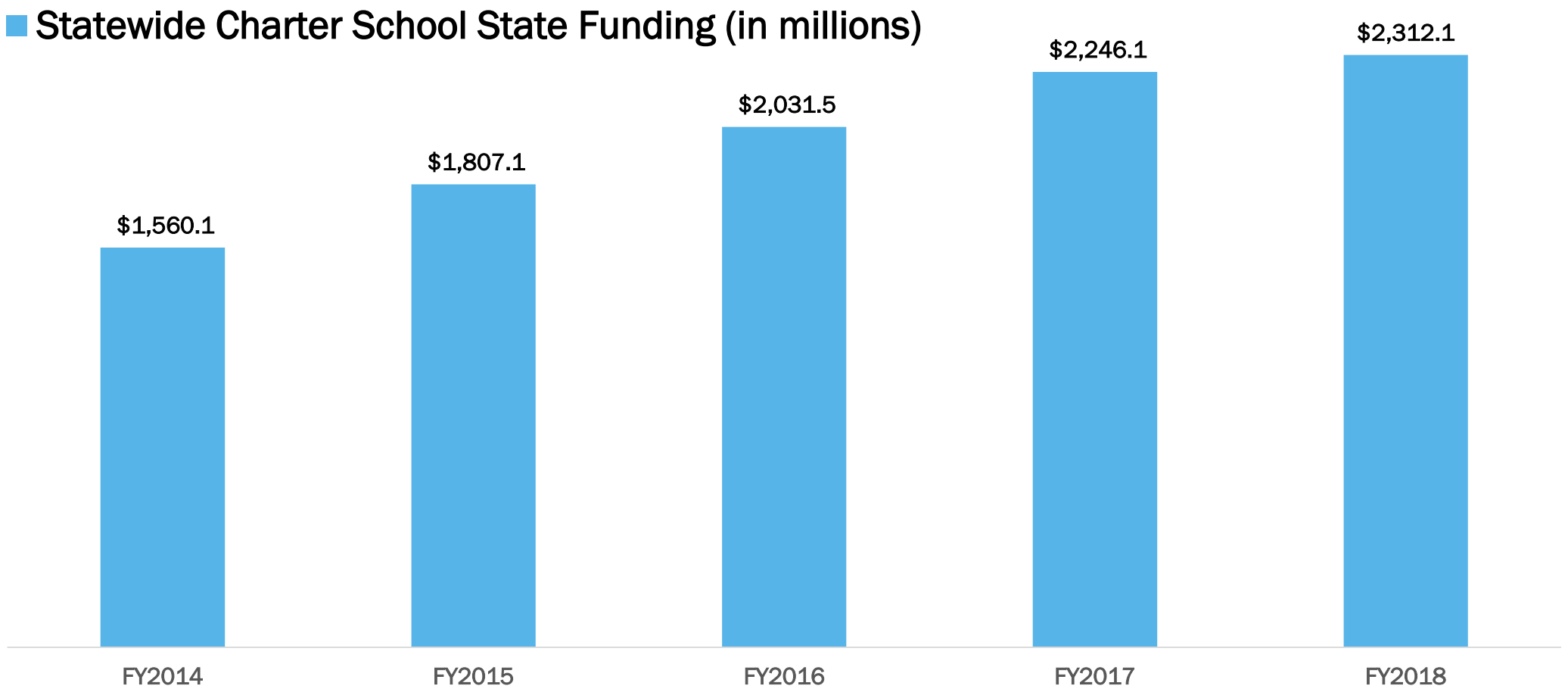
Beginning in FY2019, certain charter schools will be eligible to receive an EDA allotment calculated using the state average debt service tax rate for school districts (estimated at 19.9 cents) or a rate which will deliver $60 million in additional funding (6.9 cents) multiplied by the estimated EDA guaranteed yield (~$37) multiplied by the charter school's ADA.

In FY2018, charter schools will receive ~$594 less per student than school districts (overall), but they will receive $855 more per student in M&O funding.



ADA was chosen as the standard of comparison instead of WADA because ADA is common across both M&O and I&S funding whereas WADA is only used in M&O funding.

Increasing enrollment has increased charter school funding by 148% in the last five years



Wealth Equalization (Chapter 41)

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

What is a Chapter 41 district? Recapture?

Recapture ensures that a district's property wealth per student does not exceed certain levels, known as equalized wealth levels.

A district that is subject to recapture is often referred to as a Chapter 41 district because the provisions governing recapture are found in Chapter 41 of the Texas Education Code (TEC). Districts not subject to recapture are called Chapter 42 districts.

Districts subject to the provisions of recapture must choose a method to reduce their wealth per WADA below the equalized wealth level.

How does a district reduce its wealth down to the equalized wealth level?

A district has five options available to reduce its property wealth per WADA (pay recapture):

- Consolidation with another district (TEC, §41.031)
- Detachment and annexation of property (TEC, §41.061)
- **Purchase attendance credits from the state (TEC, §41.091) ← This is 100% of recapture.**
- Education of nonresident students from a partner district (TEC, §41.121)
- Tax base consolidation with another district (TEC, §41.151)

If a district fails or refuses to exercise Option 1, 3, 4 or 5, the commissioner is required to achieve wealth equalization through detachment and annexation or consolidation (Option 2).

Why do we have recapture?

The Texas Supreme Court has held that:

- at similar tax rates, Chapter 41 school districts should not have significantly more money per student in weighted average daily attendance (WADA) than Chapter 42 school districts, and
- recapture is constitutional noting that recapture helps to fund the amount of money available to equalize revenue per WADA for school districts across the state taxing at similar levels.

What are the equalized wealth levels (EWLs)?

The first EWL is equal to the maximum school district property wealth per WADA provided by the basic allotment. This level applies to the tax effort up to a school district's compressed tax rate (CTR) and is currently $514,000, which is tied to the basic allotment ($5,140, which is **set in the General Appropriations Act (GAA)**).

The second EWL is determined by the funding provided to Chapter 42 school districts for their tax effort that exceeds the CTR, up to six golden pennies (which there is no recapture on) that are used in Tier II. This EWL is tied to the Austin Independent School District's yield per WADA per penny ($99.41 in FY2018, **also set in the GAA).**

The third EWL is set in **statute** at $319,500 per WADA, and it applies to any tax effort that exceeds the "CTR plus six cents" and is tied to the copper pennies that are also used in Tier II.

Equalized wealth levels (EWLs) per penny of tax effort

Tier I

Basic Allotment of $5,140 & EWL of $514,000

RECAPTURE

LEVEL 1

Tier II

LEVEL 1

Six Golden Pennies at Austin ISD guaranteed yield of $99.41

NO RECAPTURE

Tier II

LEVEL 2

Copper Pennies at $31.95 guaranteed yield and EWL of $319,500

RECAPTURE

LEVEL 2

How is recapture calculated? Below is a simplified example

Description	Recapture at $1.00
1. District Property Value (Prior Tax Year)	$1,350,000,000
2. Number of Weighted Students in Average Daily Attendance (WADA)	2,500
3. District Wealth per WADA (Line 1 ÷ Line 2)	$540,000
4. State's Equalized Wealth Level (EWL) per WADA	$514,000
5. Excess Wealth per WADA (Line 3 – Line 4)	$26,000
6. Excess Property Value (Line 5 × Line 2)	$65,000,000
7. Recapture Percentage (Line 6 ÷ Line 1)	4.8%
8. M&O Tax Collections at Compressed M&O Tax Rate ($1.00)	$13,500,000
9. Recapture before discounts (Line 8 × Line 7)	$650,000

Top payers of recapture in FY2018 vs what they paid in FY2009 (in millions)

District	FY2009	FY2018 (estimated)	Percent Change
Austin ISD	$174.4	$513.6	194%
Houston ISD	-	$228.9	-%
Plano ISD	$89.3	$149.4	67%
Highland Park ISD	$71.9	$99.0	38%
Eanes ISD	$57.9	$93.4	61%
Spring Branch ISD	$5.1	$81.4	1,473%
Lake Travis ISD	$30.5	$43.6	43%
Grapevine-Colleyville ISD	$35.0	$42.1	20%

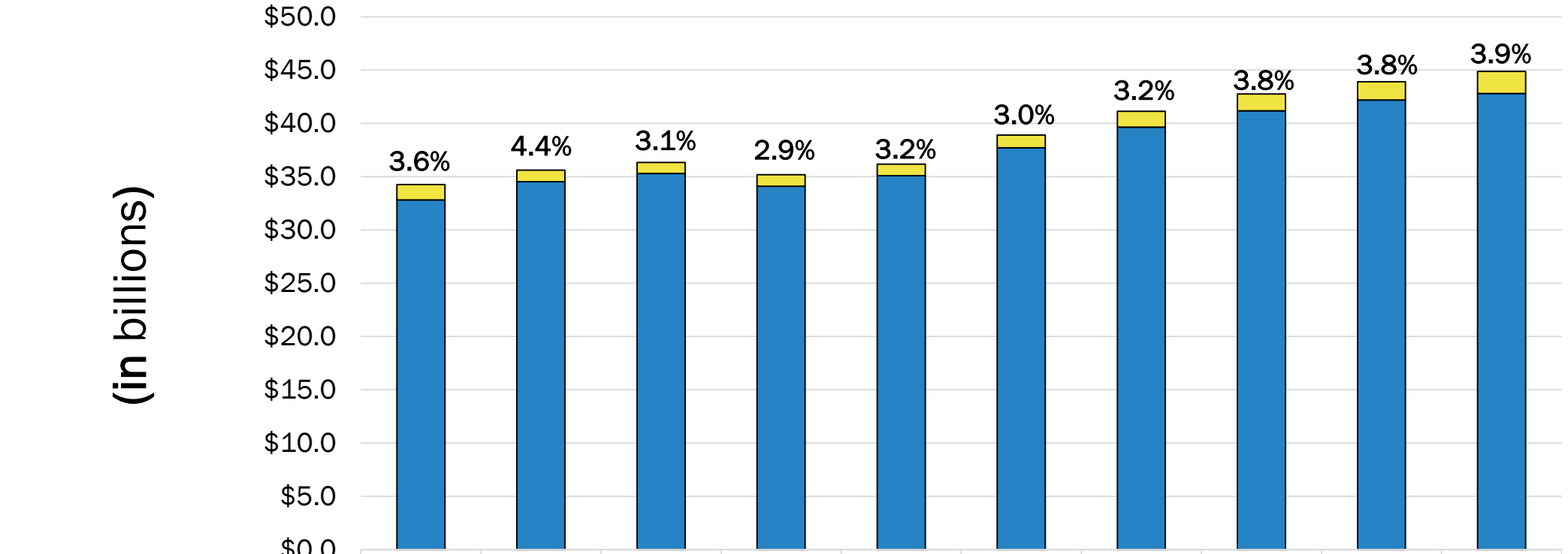
How does the state use recapture revenue?

The most commonly chosen method of paying recapture is Option 3 (paying directly to the state). **This option represents 100% of recapture.**

Payments are made in seven equal installments from February through August of every fiscal year.

Funds received by the state from recapture, which will total $2.08 billion in FY2018, are appropriated in the General Appropriations Act as a method of finance to help pay for the Foundation School Program (FSP).

Recapture as a percentage of total M&O state/local revenue over the last decade

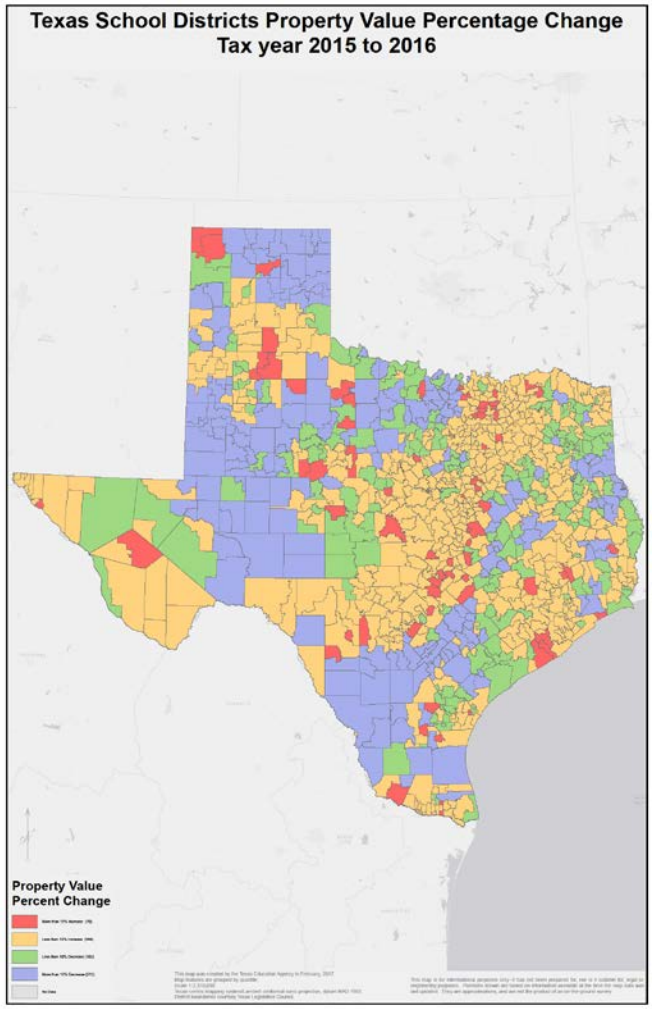


	FY2009	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016	FY2017	FY2018
Chapter 41 Recapture	$1.4	$1.1	$1.0	$1.1	$1.1	$1.2	$1.5	$1.6	$1.7	$2.1
Total M&O Rev State/Local	$32.8	$34.5	$35.3	$34.1	$35.1	$37.7	$39.7	$41.2	$42.2	$42.8

Special Topic: Districts with rapidly declining local property values

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

Districts with rapidly declining property values: a statewide perspective



- Districts marked in blue and green have declining property values
- Districts marked in red and orange still have increasing values and include the major urban areas of the state
- Overall the state still has increasing property value

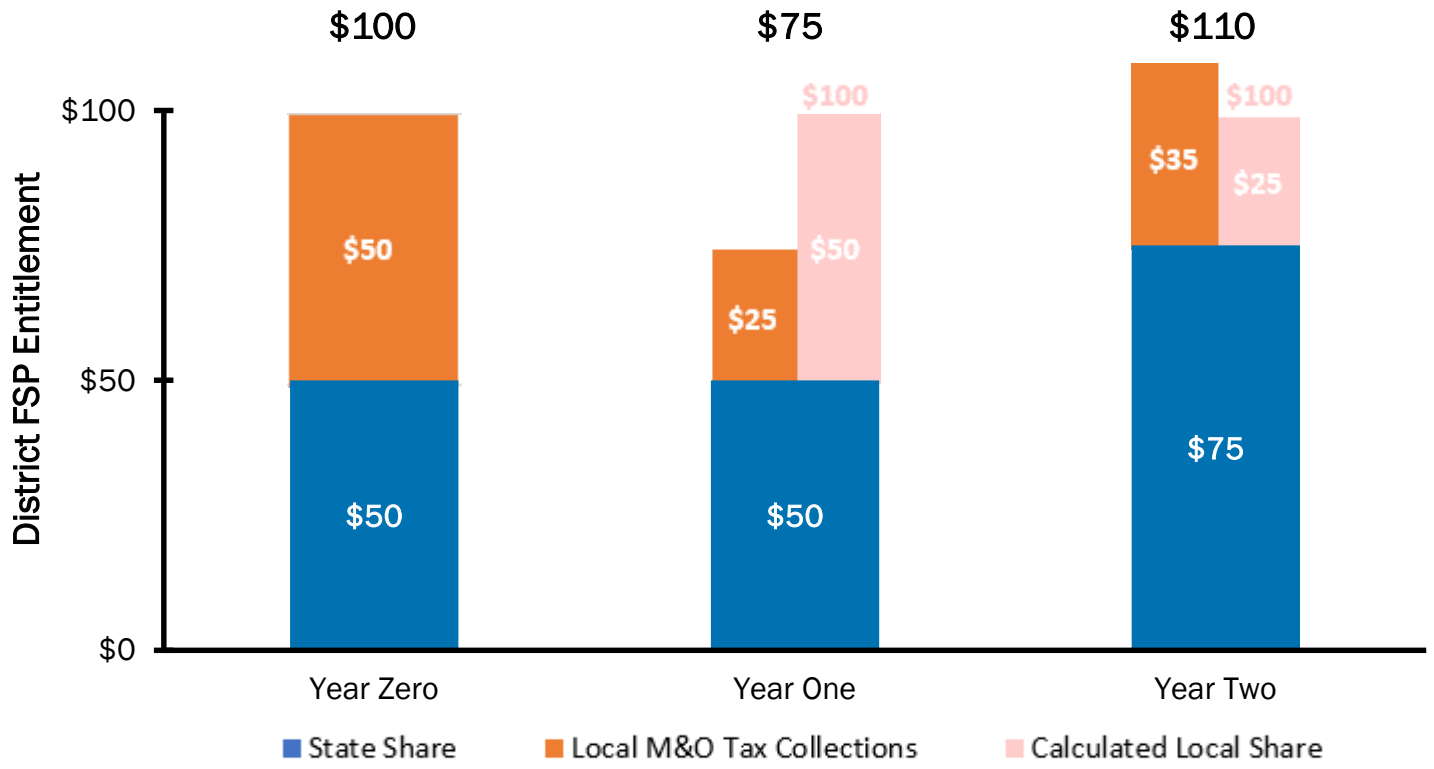
Hardships caused by decreasing values

1. Districts with declining values are disadvantaged because **the state uses prior year property values in calculating the local share of the FSP (see next slide).** In these cases, prior year values don't fully reflect the decline and exaggerate the district's ability to raise local tax revenue.

2. When making payments to districts during the fiscal year, **the state is required to assume the same estimated percentage increase** in property values for all districts.

3. **Districts with declining values therefore experience significant under-payments** which can negatively impact cash flow and overall funding levels.

Fluctuations in local property values impact FSP funding (because *local share* calculation uses prior year values)



Funding Adjustments for school districts with rapidly declining property values

The 85th Legislature appropriated $75 million in the 2018-2019 biennium to be spent on providing funding for school districts with rapidly declining property values.

Districts with declines in excess of four percent will be eligible to receive funding adjustments.

$50 million in adjustments were made as part of “near-final” settle-up for the 2016-2017 school year in September 2017.

$25 million in adjustments will be made as part of “near-final” settle-up for the 2017-2018 school year in September 2018.

Special Topic:
Financial Hardship Transition Program

"HARDSHIP GRANTS" UNDER HOUSE BILL 21

(85TH LEGISLATURE, 1ST CALLED SESSION)

Hardship Grants (HB 21)

Creates a two-year hardship grant program to provide transitional aid for districts experiencing a loss of M&O revenue relative to statute in place for FY2017

Transition grants available for FY2018 and FY2019

All eligible districts under the legislation will receive a grant award. Therefore, districts do not need to apply to TEA to receive a grant.

Grants were awarded in October 2017.

Grant program limited to $100 million in FY2018 and $50 million in FY2019

Contact information

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Appendix:
Additional State Aid for Tax Reduction

TEXAS PUBLIC SCHOOL FINANCE OVERVIEW

What was ASATR?

In 2006, the legislature compressed (reduced) local M&O tax rates by 1/3. This reduced most local M&O tax rates down from $1.50 to $1.00 resulting in school districts having 1/3 less local tax revenue to fund their local share.

To ensure districts did not lose funding as a result of the tax compression, the legislature increased the basic allotment to help offset some of the loss.

In addition, the Legislature created Additional State Aid for Tax Reduction (ASATR). Under ASATR, a "target revenue" amount per WADA was established for each school district, ensuring districts had as much funding in 2007 as they did in 2006, prior to the tax rate compression.

What was ASATR?

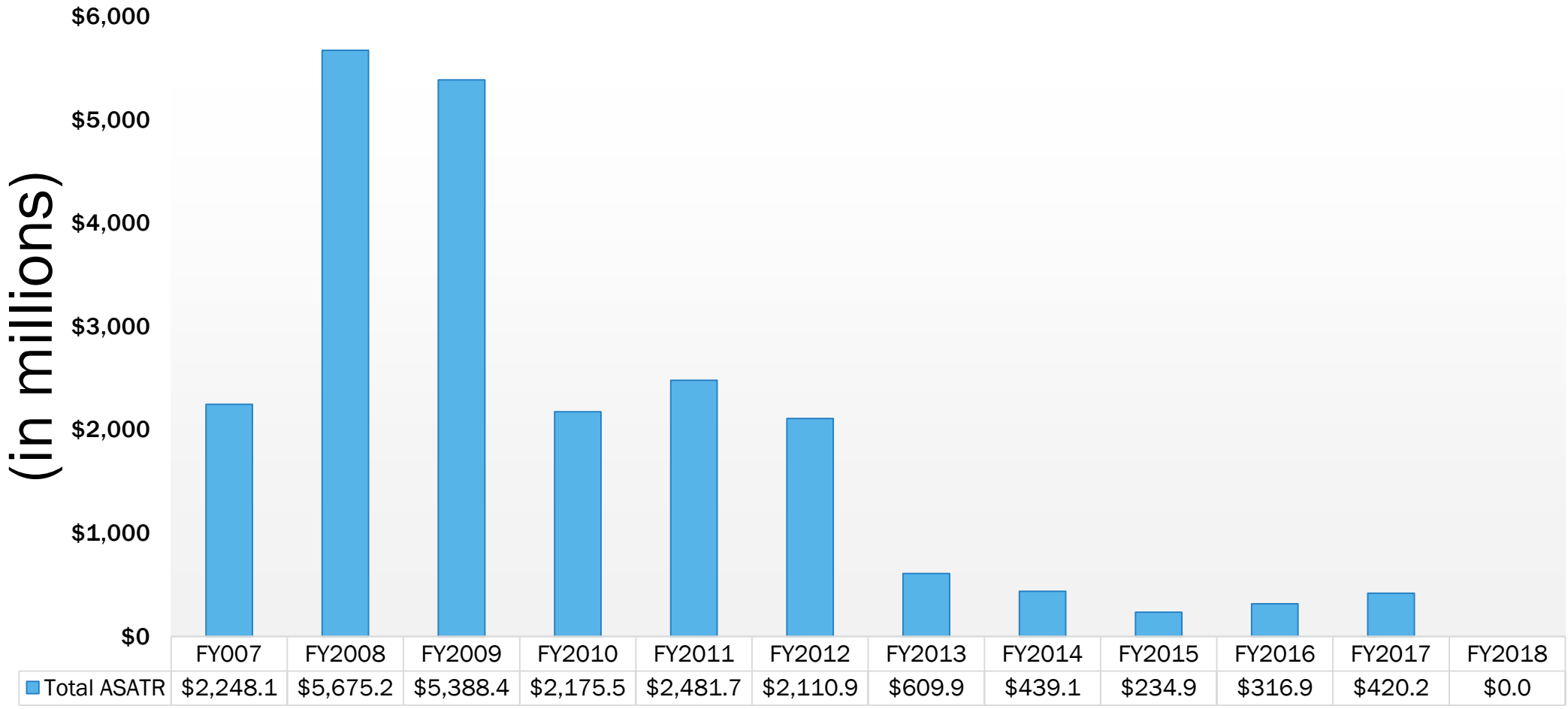
SB 1 (2011) set an expiration date for ASATR of August 31, 2017.

Over time, as the basic allotment and local property values increased, school districts began receiving more money through the Tier I FSP formulas, thus needing less ASATR funding.

However, in FY2017 (the last year before the expiration of ASATR) there were still approximately 267 districts receiving approximately $420.2 million in ASATR.

Districts that received ASATR generally had high target revenue amounts, and have more funding available than other comparable school districts (on a per WADA basis).

History of ASATR funding



	FY007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016	FY2017	FY2018
Total ASATR	$2,248.1	$5,675.2	$5,388.4	$2,175.5	$2,481.7	$2,110.9	$609.9	$439.1	$234.9	$316.9	$420.2	$0.0