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SCHOOL FINANCE REFORM IN TEXAS: THE *EDGEWOOD* SAGA

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As one pessimist has opined, school finance reform is like a Russian novel: it's long, tedious, and everybody dies in the end. For that reason, among others, I will keep my remarks brief today. Besides, to paraphrase Samuel Johnson, there are some people who are not only dull themselves but they bring out dullness in others.

For more than fifty years, Texas has been in a more or less constant process of reforming its finance system for public education. Each reform has led to the infusion of more state dollars to guarantee a higher minimum expenditure per pupil and to narrow disparities between poor and affluent school districts. Every reform was followed by a period of relative complacency. However, during each complacent period, inflation, expanding enrollments, new state and federal mandates, and higher expenditures by richer districts caused the disparities to grow and fester, leading poorer districts and their allies to press for the next round of reforms. This process continued unabated even after the United States Supreme Court upheld the state's system in *San Antonio Independent School District v. Rodriguez* in 1973.¹ Lawsuits in this domain alter only the rules of engagement; they never settle the underlying dispute. Too much is at stake.

Sixteen years after *Rodriguez*, the Supreme Court of Texas entered the quagmire, holding in *Edgewood Independent School District v. Kirby (Edgewood I)*² that the state's school financing system violated the state constitution.³ While *Edgewood I* had enormous political, educational, and policy consequences for Texas, it was a genuinely unremarkable opinion when viewed against legal developments in other states. The Texas Supreme Court construed the constitutional mandate of efficiency in public education to require fiscal neutrality.⁴ Fiscal neutrality means

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¹ 411 U.S. 1 (1973).

² 777 S.W.2d 391 (Tex. 1989).

³ See TEX. CONST. art. VII, § 1.

⁴ *Edgewood I*, 777 S.W.2d at 397.

that expenditures on education must be a function of the wealth of the state as a whole and not of the wealth of each of the more than 1000 school districts in Texas.⁵ A property tax of one penny per \$100 of assessed value in a poor district must yield the same revenue as that rate would yield in a district with ten or even a hundred times its property wealth. This definition of equality—really taxpayer equity—echoes the plaintiffs' arguments in *Rodriguez* and is similar to supreme court decisions in other states. (Fiscal neutrality decisions are usually indistinguishable even to the kremlinologists of school finance reform.)

But there is one aspect of *Edgewood I* that was interesting and important—particularly from the vantage point of devising practical responses to the court's decision. The court drew back from requiring complete or perfect fiscal neutrality; rather, it stated that students in different districts must have "substantially" equal sums of money available for education.⁶ Those involved in the reform process—legislators, lawyers, educators, and the parties themselves—took this to mean that the state need not guarantee exactly the same yield per penny of tax effort in the poorer districts as in the very richest districts—those districts, often having few students, but with millions of dollars of property wealth per pupil. "Substantially equal" access does not mean "absolutely equal" access to education funds. While the parties and different policymakers disagreed about how high the level should be, whether ninety or ninety-five or ninety-eight percent of students or school districts should be within the fiscally neutral system, they did not disagree on the basic ground rules for reform.

As one would expect, the response to *Edgewood I* was formulated through a process of tough political bargaining, with the legislature convening for a regular session and number of special sessions, and the governor insisting upon no new taxes. The ultimate compromise, embodied in Senate Bill 1,⁷ involved a continuation of a multi-tiered financing system and the infusion of nearly \$1 billion in new state funds (and new taxes) and a phased-in, multi-year plan for satisfying the court's order. The "out years" of the plan were fuzzy, and the experts disagreed on what degree of equity would be achieved at full implemen-

⁵ *Id.*

⁶ *Id.*

⁷ Act of June 7, 1990, 71st Leg., 6th Called Sess., ch. 1, 1990 Tex. Gen. Laws 1 (codified in scattered sections of TEX. EDUC. CODE ANN. § 16 (Vernon 1991)).

tation. But the important point, for present purposes, is that Senate Bill 1 essentially exempted the wealthiest districts from the plan and used state funds to guarantee tax yields in the other districts. In other words, the Texas Legislature left out 132 of the richest school districts in Texas, districts with about 170,000 of the state's 3.3 million pupils.⁸ A penny of tax effort in the poorer districts would yield the same amount of money for education as a penny at the 95th percentile of wealth per pupil—but not the 100th percentile. The 100% solution would have required many tens of billions of dollars, a sum that probably would have exceeded the state's current total budget for all goods and services. The ninety-five percent solution was not cheap, but it was economically and politically feasible. The rallying cry was "95 in '95," the 95th percentile of equalization by the year 1995.

In January 1991 the supreme court overturned Senate Bill 1 in the *Edgewood II* decision.⁹ That decision is genuinely remarkable. The court did not hold that the 95th percentile was too low, that the phase-in period was too long, or that the legislature's promises for the out years were illusory. Rather, the court held that the legislature's approach was conceptually flawed¹⁰ and that it need not even bother to review the evidence and the claims and counterclaims about what would be achieved by 1995.¹¹ "To be efficient, a funding system that is so dependent on local . . . property taxes must draw revenue from *all* property at a substantially similar rate."¹² This implies that a system must include every district in the state, no matter how rich or small, and anything short of that is per se unconstitutional. In short, "substantially" equal access meant perfectly equal access—with only minor differences in tax rates being acceptable.¹³

In the real world, perfection (or near perfection) is expensive. "Perfect" diamonds cost many times what merely good quality diamonds cost. A bottle of twenty-five-year-old scotch typically costs four times what one would spend for a twelve-year-old bottle. A BMW will sell for twice as much as a Honda. Perfection also brings conflict with other values and priorities. The

⁸ See *Edgewood Indep. School Dist. v. Kirby (Edgewood II)*, 34 Tex. Sup. Ct. J. 287, 290 (1991).

⁹ *Id.* at 287.

¹⁰ See *id.* at 289-90.

¹¹ *Id.* at 289.

¹² *Id.* at 290.

¹³ See *id.*

“perfect” or best health-care system may leave few resources for criminal justice or mental health. The public policy that would completely eliminate child abuse and neglect may undermine the autonomy and privacy of families. The best industrial policy for enhancing worker productivity may have a devastating impact on the environment or conditions of employment. As Voltaire once said, “the best is the enemy of the good.” The epiphenomena of perfection are highly imperfect.

The same is true in the domain of school financing. Under *Edgewood II*, every plan considered by the legislature in the spring of 1990, including those favored by the plaintiffs, is unconstitutional. Under a perfect fiscal neutrality regime, a property tax of a penny per \$100 of assessed value in a poor district with \$20,000 per pupil property value would yield two dollars per pupil. An equal tax effort in a wealthy district with \$5,000,000 per pupil property value would yield \$500 per pupil. It does not take a mathematical wizard to figure out that, unless some limits are established on the fundraising capacity of the wealthy district, Texas cannot establish fiscal neutrality between such districts without avoiding confiscatory taxes, bankruptcy, or the complete abandonment of other vital state services. When framed in these terms, there is no fiscal solution to the crisis. The whole education system must be restructured—and the supreme court indicated as much. State subsidies alone cannot do the job. Indeed, no state, other than perhaps California or Hawaii, currently would satisfy the standard of *Edgewood II*.

What might Texas do? There are a variety of approaches. First, the state might assume full responsibility for collecting the taxes for financing public education. The state would levy income, sales, property, or other taxes and distribute the revenues on a nondiscriminatory basis. (In Texas, an income or state property tax would require a constitutional amendment authorizing such taxes.)¹⁴ The result would be the abolition of the local property tax and the further centralization of educational policymaking at the state level. Local communities would no longer be involved in the financing of public education.

Second, Texas might consolidate school districts or tax bases of school districts. Regional districts, particularly if the lines were carefully gerrymandered, would diminish the disparities in wealth between districts. A uniform tax rate would be estab-

¹⁴ See TEX. CONST. art. VIII, § 1-e.

lished for the entire regional district, and poorer areas within the regional district would pay less in taxes than they received back from the regional governing authority. These large regional districts might follow county lines (although, generally speaking, cross-county districts would be better in terms of school finance reform) and they generally would not describe existing school districts or communities. Depending on the nature of the consolidation, there might be a diminution of authority at the local level, less grass-roots involvement of parents and voters in public schools, and educational districts with far larger geographic areas and student populations. Such "megadistricts" might produce some economies of scale (except in sparsely populated rural areas), but they also might exacerbate other problems. The trend in a number of large urban areas (including New York City, Chicago, and Los Angeles) has actually been toward decentralization of administrative authority as a means of blunting increased bureaucratization and promoting parental involvement.

Third, the state might adopt a "recapture" plan. Without going into the gory details of such an approach, let me note that rich school districts would be permitted to use their substantial property wealth for education, but would not be permitted to keep all of the funds that they were able to raise. Thus, to return to my earlier example, the rich district might be permitted to retain only \$251 of the \$500 it is able to raise with a tax of a penny per \$100 of assessed value. The remaining \$249 would be sent to the poor district that raised only two dollars at the same tax rate, thereby guaranteeing equal revenues of \$251 to both districts. The net effect is to equalize the tax bases of districts by means of revenue transfers.

The recapture approach has some appeal to state officials because it enables them to say they achieved fiscal neutrality, without raising state taxes. The problem is that it is likely to result in higher local property taxes, as affluent districts seek to preserve their programs with lower yields for their tax effort. It also places a de facto cap on local expenditures. At some point, rich districts will keep so little of what they raised that they will not tax themselves at a higher rate—even if programs suffer. In addition, it may be hard for many voters to swallow the idea that they are obliged to pay for public schools in other districts (although this obligation is frequently accepted with respect to other state-wide services and taxes). Furthermore, it appears

that the Texas Constitution may represent an insurmountable obstacle to recapture.¹⁵

Finally, the state can combine one or more of the other approaches with a system of state subsidies. For example, the state might establish countywide districts and use state funds to guarantee a uniform yield between rich and poor counties. The likely cost of achieving fiscal neutrality would be much lower because variations in county property wealth per pupil are much narrower than the variations in wealth among the more than 1000 school districts. The size of the subsidies would generally be in an inverse relationship to the size of the regional districts; i.e., the smaller the district, the larger the state subsidy that would be required. If the state were divided into six large regions of nearly identical wealth, state expenditures to guarantee yields would be quite modest.

In the midst of the legislature's deliberations over the politically unappealing avenues to achieving perfect fiscal neutrality, five justices on the supreme court recanted. In *Edgewood III*, in the context of a motion for reconsideration, the court held that perfect fiscal neutrality was not required once an "efficient" system had been established.¹⁶ What is an efficient system? Apparently, it is one that includes all of the property in the state in the plan, that allows poor districts some access to the wealth of more affluent districts (by establishment of consolidated tax districts), and that still provides substantially (but not perfectly) equal access to resources.¹⁷ Thus, some unequalized local enrichment clearly is permissible.¹⁸ But in returning to the *Edgewood I* formulation, the court declined to identify the precise point at which too much local enrichment would tip the balance against fiscal neutrality and in favor of unconstitutionality.

Edgewood III was greeted with a mixture of consternation and relief. The state house and senate approved conceptually similar but conflicting bills.¹⁹ The conference committee of the two bodies then approved a complex measure that would combine consolidated county tax districts (with some modifications), recapture, and guaranteed yields to achieve compliance with the

¹⁵ *Edgewood Indep. School Dist. v. Kirby (Edgewood III)*, 34 Tex. Sup. Ct. J. 368, 368 (1991) (citing TEX. CONST. art. VIII, § 1-e, art. VII, § 3).

¹⁶ *Id.*

¹⁷ *See id.* at 368 n.2.

¹⁸ *Id.* at 368-69.

¹⁹ S.B. 351, 72d Leg., Regular Sess. (1991).

court's mandate.²⁰ The bill passed in the senate and failed in the house. Some legislators questioned the constitutionality of the recapture and enrichment provisions. Some opponents of the bill perceived that the enactment of the measure would have produced less local control, higher property taxes, and a levelling down in terms of the quality of educational programs. Others argued that the proposed system was still too dependent on local property taxes and allowed too much unequalized enrichment by wealthy districts. Still others feared that many of the large urban districts (Houston, Dallas, Austin, Fort Worth) would be big losers. In terms of the state as a whole, the large urban districts are relatively wealthy (often having nearly twice the average property wealth per student as the state as a whole). As a result, the bill probably would have required those districts to transfer some tax revenue, despite the fact that they have large populations of poor and minority students with costly educational needs.

What is likely to happen? Even Nostradamus would be out of his depth in predicting the future of school finance reform in Texas. The supreme court has not spoken with great clarity; the picture would be far less confusing if *Edgewood II* and *III* had never been decided. The deadline imposed by the courts, April 1, 1991, has passed. The legislature is deeply divided. Some members of the legislature are acting in a statesman-like manner; others do not understand the complex issues; still others vote in accordance with how the school districts in their house and senatorial districts will fare. The only certainty is that the process of action and reaction between the courts and the legislature is likely to be long and tedious. The story is beginning to resemble *War and Peace*, though it is likely to be less amusing. One can only hope that its conclusion will be less catastrophic.

²⁰ *Id.*

