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Don't Worry, Be Happy

Mark G. Yudof*

I once wrote to Justice Powell to complain that his opinion in a school desegregation case had compromised the organization of my co-authored book, *Educational Policy and the Law*;¹ I also have been known to grouse that the blurring of contract and tort duties and remedies by legislatures and courts is destroying the simple majesty of my first-year contracts course.² I never agreed to teach torts and will resist until the death of contract. For me, it is not so much a question of right or wrong, good law or bad, as it is a solipsistic insistence on civility in the treatment of abstractions. The intrusion of the “real world” (a phrase often intoned with hushed reverence in the classroom) constitutes a form of *lese majesty* or high treason. So it is with school finance reform. I prefer the 1970s and the heady days of *Private Wealth and Public Education*,³ *San Antonio Independent School District v. Rodriguez*,⁴ and *Serrano v. Priest*⁵ to the grinding, reification-destroying reality of the legislative process in the 1990s.

To recapitulate the classic argument, extensive reliance on local property taxes to finance elementary and secondary education creates an unjust allocation of resources because the level of educational expenditure on each student depends largely on the property wealth of his or her school district. Historically, tremendous disparities between poor and wealthy districts have co-existed within the same state, with some districts being hundreds of times more affluent than other districts. In addition, poor districts tend

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¹*Dean, University of Texas School of Law. B.A. 1965, LL.B. 1968, University of Pennsylvania.

²Yudof, *Contorts and the Muddled Quest for Bright Lines* (publication pending).


to exert higher tax efforts than affluent ones, only to raise far fewer dollars for education. The result is that children are favored or disfavored on the basis of geography.

This system, however, has two virtues: (1) property taxes provide school districts with a steady stream of revenue—often untapped by state governments—and (2) local communities can decide for themselves how much to tax and spend for public schools. The dilemma is this: How can legislatures cure the inequities without embracing a mindless form of equality of expenditure per child, perhaps leveling downward and destroying community control of public schools? The answer for the last twenty years has been to urge legislatures to reconstitute school finance systems, using state subsidies and other means, to guarantee that a penny of tax effort in any district in the state, no matter how poor, will yield the same number of dollars per student for education as in any other district. This concept is called fiscal neutrality. Once achieved, everyone (or perhaps almost everyone) is supposed to be happy. Every district, in effect, would draw on the wealth of the state as a whole, but each district can decide for itself how much to tax and spend for education. Differences in expenditures will depend on tastes and preferences, not on local property wealth. Taxpayers should be pleased because collectively they receive equal benefits for equal tax effort. And, assuming that voters and their elected representatives will be responsive to the educational needs of those in the district, students should be well served by such a system.

The crux of the political and fiscal problem, of course, is how to go about relandscape the educational terrain to achieve fiscal neutrality. For example, if one school district raises $10,000 per child at a tax rate of $1 per $100 of property value and another district raises only $1000 at the same rate, the state legislature needs to figure out a way to equalize the revenue between the two districts. But suppose that the state does not have sufficient funds to distribute to the poor district ($9000 a pop can add up) and, furthermore, suppose the state does not wish to level downward by placing a ceiling of $1000 per pupil (or some other number between $1000 and $10,000) on the wealthy district. Not to

worry, scholars have a solution: The state may "recapture" revenues from the affluent district and reallocate them to the poor district. Thus, to pursue my simple example, the first district may retain only $5500 per student of what it raises, and the state government will recapture the remaining $4500. The state will then reallocate the recaptured $4500 per student to the second district, thereby producing a total expenditure of $5500 ($4500 + $1000) per student. The two districts then will have equal expenditures at the same tax effort—exactly what would happen if, serendipitously, they had an identical number of students and exactly the same amount of property tax wealth.

According to the theory of school finance reform, this is the way school financing was supposed to work after a state supreme court had construed the education clause of its constitution to require fiscal neutrality. But my experience in advising the executive and legislative branches in Texas and in observing the process in other states is that political leaders have not been overly attentive to the mandates of theory. Perhaps they have read the script but they prefer improvisation, compromise, and political survival. In the absence of precise guidance from the courts—guidance that courts often are loathe to give (the judicial philosophy often is to assert authority in defining the wrong and to defer to legislative authority in fashioning the remedy)—the question asked by most legislators is a simple one: How can the basic structure of the educational system be maintained, with minimal changes, while still satisfying the state constitution? The obvious answer to this question is also simple: Spend more state money and leave the rest of the school finance system alone (si fractum non sit, noli id reficere). That is, raise the minimum floor for every district or guarantee the yield at each level of tax effort in the poor districts by adding state funds, while leaving the affluent districts free to continue to spend local property tax dollars. If there is a $9000


9. Translation from Latin: "If it ain't broke, don't fix it."
difference per pupil in expenditures between school districts at the same tax rate, raise the minimum expenditure to $5000, thereby reducing the gap, or make up the $9000 from general revenues, and everyone will be happy and have little cause to worry.

But, alas, this is where things get sticky. A higher minimum expenditure per pupil, subsidized by the state, simply is not responsive to fiscal neutrality—unless it approaches the level of the highest-spending school districts. And the minimum, even if adequate in some educational sense, leaves unequal tax burdens in place with respect to local expenditures above the minimum. A rising tide may lift all ships, but generally not enough to satisfy fiscal neutrality. The plan will sink in a flood of criticism from less affluent school districts, and ultimately state supreme courts will declare that the remedy is inadequate.

Guaranteeing the yield as between the most impecunious school districts and the most wealthy is far more promising, but, if no limits are placed on the guarantee, the task is akin to subsidizing the income of the poor to bring them into parity with Ross Perot. Some districts have millions of dollars in property wealth per student (and usually few students), whereas others have a pittance of less than $30,000 per student. The total cost of equalizing the yield would be gargantuan, amounting to tens of billions of dollars in a state such as Texas. Even in boom times the task would be formidable. In an economic downturn, the task is near impossible—even if taxes were raised and funds for higher education, welfare, prisons, and social services were ransacked. And some of these services also are subject to court order.

The logic of the situation, from a legislative perspective, is to eschew perfection of fiscal neutrality and to reshape the objective to conform to political and fiscal realities. If the courts were to accept substantial fiscal neutrality or some not-too-close approximation of equal yield for equal tax effort in every part of the state, the cost of reform, while substantial, declines rapidly. The key is to write off the relatively few and small, wealthy districts at the tail of the wealth distribution. If the revenue guarantee in the poorest districts need only equal the yield of a district at the ninetieth or ninety-fifth percentile of property wealth in the state

10. See Yudof, supra note 8, at 501.
(substituting, as it were, a moderately well-paid business executive, lawyer, or physician for Ross Perot) and the reform is phased in over a number of years, then a more affordable plan will do the trick.

But minimalism in school finance reform, as in art, has its detractors. First, representatives of property-poor districts may bridle at compromise, and they may be able to block a new school finance package. Second, the judges may bridle, holding that their mandates are being ignored or watered down. Scorned judges and recalcitrant legislators do not mix well; indeed, in Texas the state supreme court rejected just such a remedy. Third, the ninety-five percent solution creates a dynamic for its own destruction. As the wealthy districts increase expenditures on education in future years, compensating for inflation, increasing personnel salaries and benefits, or funding new programs, the disparities will widen. Either the legislature must play catch up and spend more money in the poorer districts, or it must acquiesce in the gradual erosion of fiscal neutrality. Thus, the ninety-five percent solution is not a permanent one; the combatants will be compelled to re-engage on the field of battle on another day—both in the courts and the legislature.

If substantially equal access to resources is not the answer, and sufficient revenues are not available to achieve fiscal neutrality simply by enlarging the pie, then there is a limited range of choices. One possibility is to redistrict the state and to create school districts of roughly equal wealth per pupil—or at least districts with such a narrow range of disparity that they are more amenable to equalization through modest state subsidies. Indeed, if the state constitution would permit it, the whole state can be treated as one school district, there can be regional districts, or county districts might be employed. Apart from the possible loss of life during the counter-revolution (Saddam Hussein probably is more popular in Kuwait than school district consolidation is in Texas!), this approach threatens one of the pillars of the fiscal-neutrality solution—the preservation of local control of education. By degrees, larger districts will be less responsive to grass-roots

concerns within particular communities, and, indeed, even poor districts in Texas are resistant to losing their autonomy through consolidation with other school districts.

This brings us to the remedy of "recapture," a primary mechanism for school finance reform in the literature. Perhaps the most important point to understand about recapture is that it pits statewide elected officials against local officials. If school finance reform is achieved through a guaranteed-yield system—dependent on new state funds—then legislators will need to vote for additional taxes and take the accompanying political heat. This is even more true if existing taxes are thought to be near their limit, and new forms of taxation will need to be approved. For example, many Texas politicians are apprehensive about voting for a personal or corporate income tax and then standing for reelection. And some new taxes, for example a statewide property tax in Texas, may only be levied by amending the state constitution, for some state constitutions contain prohibitions on particular types of taxation.

Recapture, on the other hand, is based on redistributing local property taxes. At least in theory, fiscal neutrality can be achieved without adding a nickel of new state funds. This may explain its popularity with some legislators, judges, and academicians. The problem, however, is that there is no fixed equilibrium point, for local taxation decisions will be critically influenced by the prospect of recapture. Affluent school districts, with low property tax rates, will be forced to choose between draconian cutbacks in programs and services versus substantially increased property tax rates. For example, a wealthy district, prior to school finance reform, might have raised $8000 per student for education at a rate of $.50 per $100 of appraised property value. Under a recapture plan, however, the district might need to raise $12,000, at a tax rate of $.75 per $100, in order to retain $8000 after turning over $4000 per student to the poor districts. The choice is between a reduction in current spending and a fifty percent increase in property tax rates (or a combination of reductions and tax increases).

If the school district opts to increase property taxes, the unpopularity of an already unpopular tax will be enhanced, and voters may well blame their higher tax burden on the local school board and superintendent. Similarly, a reduction in expenditures
may infuriate parents, students, and teachers. Inevitably, local officials will try to shift the blame to the legislature (or the courts), but they will fear being unsuccessful in assuring the voters that they are only pawns in a larger game. Pressure then will be put on the legislature to bail out the most adversely affected districts, but this only begins the cycle anew as elected representatives fear the political and economic consequences of new or higher state taxes. Thus, the pursuit of school finance reform inevitably becomes a struggle between state and local officials to avoid political accountability for tough and unpopular tax policies. The overarching goal is to win accolades for education reform while forcing some other level of government to endure the calumny for reckless taxation. This is the essence of modern local-state relations.

As if all this were not enough, recapture presents other problems. First, there is something graphic and unappealing about taking funds from one political subdivision and redistributing it to another. This often happens when taxing and spending decisions are separated, for only user fees produce an exact equivalence between burdens and benefits. For example, one county or school district may receive back from the state more or less than it pays in state taxes; a poor section of a city may receive back more in city services than it contributes to tax revenues. But, to a large extent, such redistributions are hidden from the voters. Education recapture plans are more explicit and crude, and they often inspire a hostile response from those who feel that they are victims of a Robin Hood experiment in social engineering. Moreover, the whole point of fiscal neutrality is that no school district is entitled to treat the property wealth in the district as wholly its own (any more than its sales receipts or income), but voters who have paid premium prices for residences and commercial property in chic areas often do not agree with such reasoning.

Second, recapture provisions may raise their own difficulties under state constitutions. In Texas, the state supreme court has held that funds raised for educational purposes in one school district may not be expended on students in another school district.12

12. Id. at 497.
There is considerable uncertainty about this; much may depend on what constitutes “a school district.” But the legislature, unless it is extremely careful, may be in the awkward position of having to enact a constitutional amendment, subject to voter approval, to remedy a constitutional violation of another provision of the state constitution. In addition, some have urged that recapture may be viewed as tantamount to a state property tax (forbidden by the Texas constitution), a position recently rejected by Judge McCown in the latest round of the Edgewood litigation.\textsuperscript{14}

Third, recapture plans may be subject to the charge that they level downward, establishing a de facto cap on education expenditures. At some point, even in the most pro-education districts, voters will rebel at taxing themselves at high rates only to lose the lion’s share of the benefits. This is akin to the problem of determining when a progressive income tax becomes so burdensome that taxpayers in the highest brackets are discouraged from earning additional income. But the school-finance situation is worsened by the fact that the redistribution of wealth is achieved by the mechanism of a tax on tax revenues. For example, if to sustain an $8000-per-pupil expenditure on education a school district must tax itself such that it raises twice or thrice that amount (retaining only a half or a third of total revenue), voters may throw in the towel, refuse to authorize higher taxes, and cut expenditures. Affluent parents may even opt to minimize taxes in order to free up income for tuition expenses at private schools. Under such circumstances, affected districts will urge that the state’s best (or at least most expensive) educational programs are being devastated by recapture plans. Conversely, poor districts will urge that it is not fair for only the wealthy districts to have the “lighthouse” programs. They may object to lids on spending, but they object even more to a system that allows only wealthy districts to spend freely on education.

What then are the options? The most viable approach is a hybrid one: Enact a law that achieves a high degree of fiscal neutrality while ensuring that the opponents of increased state taxes, redistricting, and recapture do not lose too much in the new

\textsuperscript{14} Graves, Judge Upholds School Tax Reforms, Austin Am.-Statesman, Aug. 8, 1991, at A1, A17.
reform measure. The result is likely to be complex and not particularly pretty. It is also more the product of political bargaining than grand principles or designs. And the solution may not be a stable one.

The Texas legislature recently embraced such a hybrid approach in Senate Bill 351. It finessed the recapture problem by creating 188 consolidated tax districts, largely following county lines. These consolidated districts are empowered only to set a tax rate (at or above a minimum determined by the legislature) and to levy and collect a property tax across the entire district. The revenues then are allocated back to individual school districts within the consolidated unit on a per pupil basis. The idea is that poor school districts within the consolidated unit will receive back far more than they contribute in taxes, and the reverse will be true of affluent districts. In essence, this is a form of recapture, but one that is not quite so obvious on its face. And this approach attempts to avoid the charges that community control of schools has been decimated and that funds raised within a district are spent in another. The proponents of the plan argue that the consolidated district is the relevant entity for taxation purposes; the original school districts are the relevant entities for voter control. To be sure, local school districts lose part of their power to set tax rates, but they retain all of their other governance powers. The district court in the Edgewood case recently upheld this form of recapture.6 District courts in other parts of the state also have denied preliminary relief in similar cases brought by adversely affected school districts.7

By creating consolidated tax districts and setting the minimum tax for them, the Texas legislature greatly reduced disparities in wealth among taxing jurisdictions, and it thereby significantly reduced the need to infuse new state funds into the system. Above the minimum tax, the legislature guaranteed a revenue yield to every district in the state for each additional penny of tax effort, up to a specified maximum tax rate and yield. But what is the price of the package in terms of the cumulative impact of increases

17. Id.
in state and local taxes? The state's contribution to elementary and secondary education will increase by about $600 million in 1991-92, reaching a total of $6.3 billion.\textsuperscript{18} Overall state funding for the 1991-93 biennium will be $1.67 billion higher than for the previous biennium.\textsuperscript{19} While this is a substantial commitment of resources, the magnitude is such that lawmakers were able to avoid the enactment of an income tax or major increases in existing state taxes.

The calculations, however, are more speculative in coming up with reliable numbers for projected increases in local property taxes. One must predict how each affected district will respond to the choice between budget cuts and higher taxes, and policymakers have sharply disagreed in their estimates of property tax rates and revenues in local school districts over the next two years. Preliminary estimates, however, indicate that far more than half of the costs of school finance reform in Texas will be borne by local ratepayers. In 1991-92 alone the local contribution to elementary and secondary education will rise to $7.2 billion, up from $5.74 billion in 1990-91.\textsuperscript{20} Thus, for the first year in the implementation of Senate Bill 351, the expenditure of new local funds (about $1.5 billion) is more than twice the allocation of new state funds (about $600 million). And the percentage of state support of total expenditures for elementary and secondary education (excluding federal funds) declined from about fifty percent in 1990-91 to less than forty-seven percent in 1991-92.

Proponents of fiscal neutrality in Texas have won a substantial victory. The big losers are wealthy districts with low rates of property taxation. The minimum tax for consolidated districts and the guaranteed-yield tier of the new law will create geometric increases in property taxes in affluent districts virtually overnight—unless substantial budgetary reductions are implemented. The conference committee of the state house and senate omitted hold-harmless clauses for wealthy districts when it became clear that such devices would significantly increase the tab for school-


\textsuperscript{19} Rugeley, \textit{supra} note 18.

\textsuperscript{20} Graves, \textit{supra} note 18.
finance reform. The legislature did provide for some local enrichment on an unequalized basis (that is, not subject to the fiscal neutrality principle), but the amount is small and subject to a "floating" cap on overall expenditures.\(^2\) Conversely, tax rates will remain relatively steady or decline in poor districts, but expenditures per pupil will increase substantially.

Perhaps a few examples would be helpful. The Highland Park Independent School District, a small and affluent district in Dallas with a reputation for excellence, lost $16 million in state revenues, and its tax rate will double in 1991-92.\(^2\) Even more dramatically, the Glen Rose district (home of the $9 billion Comanche Peak nuclear power plant) will see its property tax rate increase from $.25 per $100 of value in 1990-91 to $.79 in 1991-92, a more than two hundred percent increase.\(^2\) By 1994-95, it is estimated that Glen Rose will have a tax rate of $1.10.\(^2\) Conversely, North Forest, a poor district, will levy the same tax rate ($1.55) in 1991-92 as in 1990-91, and it is estimated that the rate will be identical in 1994-95. But over the five-year period, expenditures per pupil will grow from $4117 to $5801.25.\(^2\)

Caught between the extremes are large urban districts like Houston, Dallas, and Austin. By statewide standards these districts have significantly higher than average property tax wealth per student, but they are not among the most affluent districts in the state. They will lose substantial state funding, and they are compelled to choose between raising tax rates and cutting budgets. They also have large concentrations of poor and minority children, many of whom are in need of specialized (and expensive) educational services.

Thus far, the large urban districts have responded in different ways to Senate Bill 351. Austin cut $8.1 million from its budget and raised its tax rate from $1.26 to $1.47 per $100, a sixteen and six-tenth percent increase.\(^2\) Houston, under the leadership of a

\(^{21}\) See Tex. S.B. 351, supra note 15.


\(^{23}\) Graves, supra note 20, at B4.

\(^{24}\) Id.

\(^{25}\) Id.

new superintendent, closed four schools and eliminated 357 non-teaching positions. In this fashion it was able to cope with school finance reform with only a five percent tax increase. In Dallas, all hell broke loose. Dallas lost at least $47 million in state aid, and it fired 245 of its 8400 teachers. It also approved a seventeen percent increase in property taxes. In the early fall of 1991, 3000 students boycotted classes—chanting, shouting, and singing in front of the administration building—to protest the dismissals. While generally peaceful, five students were arrested for throwing rocks and bottles at police officers during a brief melee. Teacher groups supported the student protest and filed suit to enjoin the dismissals. As one knowledgeable observer stated, “the Dallas school system is in chaos, with students and teachers taking to the streets . . . to protest mass teacher layoffs.”

The district responded by hiring back some of the teachers, but the board refused to raise taxes enough to hire them all back. Finally, amid some allegations that the criticisms of Superintendent Marvin Edwards were racially inspired (he is an African American), the board approved recommendations from the superintendent to make budgetary cuts and to rehire all of the dismissed teachers. The teachers' groups promised to forego sick days to help pay for the package and administrators promised to leave some administrative positions unfilled and not to fill others when vacancies arose. On September 13, 1991, the front page of The Dallas Morning News had a huge headline announcing the accord along with a photograph showing the superintendent and board members Rene Castilla and Thomas Jones holding their hands over their heads “to symbolize the board’s unity.”

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27. Id. at A4.
28. Id. at A1.
34. Lewis, supra note 32, at 1A, 20A.
35. Id. at 1A (photograph caption).
What will happen next is difficult to predict. On the legal side, a district court has upheld the constitutionality of Senate Bill 351, but an ultimate appeal to the Texas Supreme Court is virtually inevitable. On the political side, the situation is volatile. The recent lawsuits filed by forty affluent school districts and the magnitude of property tax increases in many districts may be precursors of a taxpayer revolt across Texas. The reaction in Houston to Senate Bill 351 may indicate that some substantial cuts in educational spending will occur—even in large urban districts with large populations of poor and minority children. And the example of Dallas may presage a particularly ugly form of political infighting, with various racial and ethnic groups, teachers, students, taxpayers and others engaged in a struggle to protect their interests during the implementation process. Finally, the politically optimistic may contend that the reforms will create a dynamic for increasing expenditures in both rich and poor school districts. That is, tax rates may be kept down and budget cuts may be avoided by relatively affluent districts only if they join forces in the legislature with the poorer districts to raise the state’s total financial commitment to public education.

In terms of policymaking, we can learn a great deal from the recent history of school finance reform in Texas and elsewhere. As two eminent social scientists have noted, policymakers

always have a choice between trying to find “solutions” . . . by arranging to have a given problem frontally assaulted by persons who think it through to a solution, or by arranging to set in motion interaction [political bargaining, reciprocity, mutual adjustment] that will, with the help of analysis adapted to the interaction, eventuate in a solution or preferred outcome.

Given the passions, entrenched bureaucracies, scarcity of resources, and conflicting interests, informed political horse-trading and not rational models have and will continue to carry the day in education finance.

Perhaps this is as it should be, and there is no need for fear or worry. Freud was fond of saying that “theory is good, but it

doesn't prevent things from being true." But among the sons and daughters of the Enlightenment, naively professing in the classrooms of universities, it is not surprising that many wistfully yearn for the simplicity of unencumbered reason and abstraction, for the days before school finance reform was held hostage to political realities, "computer runs," and tax policy.