

Research Report

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Building For The Future **A Look At School Facilities Funding In Texas**

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with

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About the Texas Public Policy Foundation

The Texas Public Policy Foundation is a 501(c)3 non-profit, non-partisan research institute guided by the core principles of limited government, free enterprise, private property rights and individual responsibility.

The Foundation's mission is to improve Texas government by generating academically sound research and data on state issues, and by recommending the findings to opinion leaders, policy makers, the media and general public. The work of the Foundation is conducted by academics across Texas and the nation, and is funded by hundreds of individuals, foundations and corporations.

Executive Summary

School facilities debt is a growing problem that is central to the challenge of funding public schools in ways that enhance the efficiency and effectiveness of state education dollars. As a part of the Texas Public Policy Foundation's school finance research initiative, district spending was examined to determine the extent of school facilities debt and identify how state policies influence district decision-making regarding debt. This research examines school facilities funding in Texas from a high-level, institutional perspective. It offers practical strategies for maximizing investments in facilities spending, decreasing school debt, and increasing local responsibility so that more educational dollars can be spent on instruction and improving student performance.

Findings

- Almost 70% of Texas school districts are burdened with facilities debt.
- Texas school districts owe close to \$50 billion for construction or renovation.
- Taxpayers pay twice for school facilities – local property taxes and state tax dollars.
- Districts receive over \$700 million state funds annually to offset facilities debt.
- State subsidies encourage districts to spend more – a district receiving the Instructional Facilities Allotment is automatically in \$7.4 million more debt.
- Robin Hood encourages districts to spend money on facilities instead of instruction because districts can keep dollars spent on facilities away from Robin Hood redistribution.
- Wealthy school districts are encouraged to finance expenditures with debt even when they could be financed with normal operating funds – a wealthy district under the Robin Hood system incurs \$6.4 million more debt.
- State subsidies encourage districts to spend extra on facilities design and size.
- The wealthier a district, the greater the debt it assumes – with each \$100,000 in total taxable wealth, on average a school district takes on an additional \$650 of debt.
- State subsidies for instructional facilities encourage districts to spend more money on non-instructional facilities.
- Nationally, low growth school districts generally spend as much as high growth districts.
- School districts add \$26,946.47 in facilities debt for each new student.

Recommendations

- Hold bond elections on standard election dates to encourage higher voter participation.
- Abolish the prevailing wage law to reduce renovating/construction costs.
- Eliminate the interest and sinking tax rate so districts pay off facilities bond from the same pool of tax dollars that underwrite operations.
- Disallow the Permanent School Fund bond guarantee program to be used for non-instructional facilities.
- Establish a maximum facilities subsidy for each student.
- Encourage districts to use money-saving facilities designs.
- Require schools to use best practices for school facilities finance.

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Previously, Dr. Schlomach was a researcher in the Office of the Texas Comptroller. There he conducted research into education and transportation, and was the principle author of a study examining the public school start dates.

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Introduction

The debate on school finance in Texas usually revolves around three main issues. First is the so-called Robin Hood system of school finance whereby relatively wealthy school districts must surrender part of their property tax revenues to relatively poor school districts. Second is the fact that many school districts are at or approaching a statutorily-determined property tax rate cap and are complaining of a need for more revenue. Third is the level of property taxation. Most agree that it is already too high and do not want home and business investment taxed any more than it is already.

Only the last of the three issues above concerns spending on school facilities despite the fact that sports stadiums and other school investments some consider unwise inevitably become part of any discussion on school finance. School facilities spending and taxes specifically raised to pay for facilities are not subject to the Robin Hood system's redistribution scheme.

Strictly speaking, school facilities taxes are not capped (see below). Because school facilities taxes are part of many taxpayers' total school property tax bill, the way that facilities are funded should be a fundamental part of comprehensive school finance reform. The growing investment of state tax dollars to help local school districts pay off facilities debt lends particular urgency to the need for state policymakers to establish standards, accountability, and controls for the debt that local school districts elect to incur and pass along to every taxpayer in the state.

This paper examines school facilities funding and spending from a high level statewide perspective. It looks at the state's role as well as local districts' role in facilities funding and the incentives inherent in the current system as it is now constructed. Finally, some recommendations are made with the purpose of reforming the system so as to alter incentives to bring about greater efficiency and to move more taxpayer resources to support instruction directly.

Local Facilities Funding in Texas

In fiscal year 2002, Texas public schools owed \$47.8 billion in principal and interest on bond issues.¹ This is more than the \$45 billion in principal and interest Iraq owed Arab countries by the end of the last Iraq war.²

Bonding authority was granted to school districts mainly for the purpose of purchasing real property – land and buildings – although some have used their bonding authority to finance the purchase of such things as computer equipment. Facilities financed with bonds include sports facilities and administration buildings as well as classroom space.

School property tax rates consist of two parts. Maintenance and operations (M&O) taxes are the bulk of a district's local tax revenues. M&O revenues are generally used for everyday operational expenses such as payroll and electricity. Interest and sinking (I&S)

taxes are restricted to paying for the interest and principal for bonds issued to finance large capital investments in a school district such as football stadiums and school buildings. Bonds can be issued to build new facilities or to repair and refurbish facilities, but they are not to be used for everyday operational expenses.

There are several differences between M&O taxes and I&S taxes in addition to what they fund. The Robin Hood school finance system redistributes only M&O property taxes. School districts that are property wealthy on a per-student basis must give up a portion of their M&O property tax revenue for redistribution by the state or they must partner with property poor districts, or pick another of the options available to them to essentially reduce their property wealth per student.³ I&S taxes are NOT redistributed under the Robin Hood school finance system.

Another difference between M&O and I&S taxes is in how they are levied. When a school district's board of trustees determines that a facility is required the board orders an election to have a bond issue approved by voters in the district in order to pay for the facility. M&O tax rates can be increased by a school board without voter approval. M&O tax rates are limited to \$1.50 per \$100 property valuation. I&S tax rates are limited, in total, to \$.50 per \$100 property valuation *at the time of a bond election*. If property values fall, however, there is no limit to which I&S tax rates can rise in most cases. According to Texas Bond Review Board data, only Carroll ISD in Tarrant County had an I&S rate that exceeded \$.50 per \$100 property valuation in fiscal 2002.

State Facilities Funding in Texas

In the decade of the 1990s much was made of the need for new and upgraded school facilities.⁴ As recently as 2002 the National Education Association stated that, "76 percent of [Texas] schools report a need to upgrade or repair buildings to good overall condition" and that "Texas faces an estimated \$13.7 billion cost for school modernization."⁵ Funds were appropriated in 1991 to help school districts with facilities. In 1993 a legislative proposal to issue \$750 million in state bonds to help with facilities was rejected by voters. In response to pressure for more school facilities spending and to an opinion expressed by the Texas Supreme Court that some kind of equalization of facilities funding would have to be instituted,⁶ the Facilities Assistance Grant program was created to assist school districts in financing facilities in 1995.⁷ It was replaced in law in 1997 with the Instructional Facilities Allotment.⁸

The Instructional Facilities Allotment is a state subsidy of I&S taxes of school districts with less than \$350,000 of property wealth per student. If a school district has only \$200,000 of property wealth per student, 1¢ of property tax yields \$20 for each student. Under the Instructional Facilities Allotment, the state would, in this example, subsidize each cent of local I&S property tax at the rate of \$15 per student. To extend the example, if this hypothetical district established an I&S tax rate of 12¢ it would be subsidized at a rate of \$180 (12 x \$15) per student.

The Instructional Facilities Allotment is intended to aid in funding school facilities where bond payments began with the 1997-98 school year. This aid is intended only for facilities that are used for instruction of the state's required curriculum (i.e., NOT sports facilities), so it is not open-ended with regard to what kinds of facilities it is supposed to help fund. Neither is it open-ended in terms of the total amount of facilities that it funds. The total amount of funds that can be used in the Instructional Facilities Allotment program in any given year is limited by the legislature's appropriation to the program. As a result, the Instructional Facilities Allotment has always been oversubscribed. More districts apply for the program with desired projects totaling more than can be subsidized by the Instructional Facilities Allotment.

The Instructional Facilities Allotment is also a long-term obligation on the part of the state. Once the state begins subsidizing a district's bond payments, the state is obligated to continue the subsidy until the debt is retired. In Fiscal 1998, the Legislature appropriated \$100 million to the Instructional Facilities Allotment.⁹ In Fiscal 2003, the Instructional Facilities Allotment cost the state \$282 million.¹⁰ This kind of growth in expenditure is natural given the long-term obligation and the tendency to add new obligations for the state every year.

By 1999, the Legislature was receiving complaints that districts with less property wealth than districts receiving Instructional Facilities Allotment assistance were making unsubsidized bond payments on debt issued prior to the Instructional Facilities Allotment's existence. Their complaint was a bit like the bargain hunter who considered a television purchase a good deal only to find out that his neighbor got the television for less on sale the next day. Another complaint was that districts with new buildings had to spend substantial sums on equipment such as desks in order to make the buildings functional and there was no state funding for such purposes.

Flush with another budget surplus, the 1999 Legislature created two more facilities funding programs in response to district officials' complaints that the Instructional Facilities Allotment was not adequately filling the needs of school districts. These programs were the Existing Debt Allotment and the New Instructional Facilities Allotment.¹¹

Like the Instructional Facilities Allotment, the Existing Debt Allotment subsidizes districts with less than \$350,000 of property wealth per student. The critical difference, though, is that the Existing Debt Allotment is used to subsidize school facilities debt that predated the program, and it subsidizes all debt, including that for non-instructional facilities. The Existing Debt Allotment, in fact, now represents a considerably greater sum of money than the Instructional Facilities Allotment. In Fiscal 2003, Existing Debt Allotment allotments amounted to \$487 million.¹²

The Existing Debt Allotment appears to be less of a commitment on the part of the state. There is no provision in the law, as there is with the Instructional Facilities Allotment, that school districts are entitled to state assistance as long as there is debt outstanding. In fact, apparently as part of the austerity measures that were instituted in 2003 in order to

deal with a large projected budget deficit, the legislature passed a provision whereby the commissioner of education could reduce the guaranteed wealth level in order to stay within the appropriated amount.¹³ This provision applies only to school districts most recently eligible, so there is certainly an effort to make sure that once a district is getting Existing Debt Allotment funding, that funding continues until the district's debt is completely satisfied.

The New Instructional Facilities Allotment grants to a district with a new building \$250 per student newly attending school in that building. The New Instructional Facilities Allotment applies for two years with the number of students for which the \$250 allotment is paid in the second year being adjusted downward to net out the number of students for which \$250 was granted in the first year.¹⁴ The New Instructional Facilities Allotment is designed to fill the equipment needs for districts with new buildings. Each year since its creation, \$25 million has been appropriated to the New Instructional Facilities Allotment. The Legislature put in place a formula whereby these funds are pro-rated across districts eligible for the program since it, too, is regularly oversubscribed.

Lessons from State Facilities Subsidy Programs

The development of the three facilities allotments are an excellent example of how the entire school finance system has developed and grown in complexity over the decades. Especially in the last decade, much has been made over the problem of funding equity for education. This is the reason for the existence of the Robin Hood funding program that so heavily shapes our funding system with respect to maintenance and operations taxes. It is a major reason the Instructional Facilities Allotment exists.

Every conceivable issue seems to require a separate funding element in education. One reason, already alluded to, for the creation of the facilities funding programs concerns the poor state of school facilities in Texas – a problem that apparently needs funding as if the M&O tax did not exist. On the operations side of school funding, there is an allotment for the teaching of gifted and talented students, another for technology (mainly computers), another for special education, another for bilingual education, and the list goes on. Each of these allotments has its own history. The point, though, is that the schools seem unable to educate any given student particularly well unless a specific allotment applies to that child. Why facilities should be in a state of disrepair given the ability of districts to pass bond issues with a separate tax rate to support them is a bit of a mystery.

Another phenomenon illustrated by recent developments in school facilities funding is that one funding program begets another. All of the various funding weights that exist in the current funding system on the operations side did not one day suddenly appear simultaneously. Each was created one at a time and every new weight carried with it some justification for creating another weight. Giving schools extra funding for one “problem” seems to simply encourage those in charge of schools to discover other “problems.”

Fairness plays a big role in school funding debates as well. The Existing Debt Allotment, which now outstrips the original facilities allotment, the Instructional Facilities Allotment, was created in no small part due to complaints regarding fairness, as noted above. On the operations side of school funding, there is a Cost of Education Index whose existence is entirely the result of school districts competing for funds and complaining of unfairness in the system. That index, created in 1990 and now some twelve years out of date, was created in an effort to account for regional cost variations across the state. Even though cost variations are largely reflected in wages and property values and, hence, tax revenues, the Cost of Education Index was instituted even before the Robin Hood system (which dampens such revenue differences).

According to the education lobby, no problem in education is solvable without more money, especially state money in the form of a subsidy. Consider the New Instructional Facilities Allotment. The demand for this program represents an admission by school district officials that they failed to sufficiently plan facilities expansion programs to take account of equipment needs. Apparently, poor planning on the part of school districts *does* represent an emergency, or at least an expense, on the part of the state taxpayer.

Another lesson taught by school facilities funding programs is that monetary incentives in addition to monies already expended seem necessary to get school districts to fulfill their basic missions. School facilities funding has been accomplished through the separate I&S fund and tax rate precisely because of the nature of capital investment – that the expenditures are large and the benefits of buildings accrue over a long period of time. Yet, the state seems to stay in a long-term, multi-year school facilities crisis.

The situation with school facilities is reminiscent of former Governor Bush's reading initiative. It separately funded the training and added bonuses of mentor teachers to teach reading to students and to teach other teachers how to teach reading. It is a fair bet that most taxpayers thought they were already paying for teachers to teach reading. There seems to be a requirement for taxpayers to pay twice when it comes to providing for the education of our children.

The State's Bond Guarantee

Texas taxpayers subsidize school facilities construction in another, more subtle way. Since 1985, the state's Permanent School Fund has guaranteed school bonds, allowing school districts to get the highest bond rating and, therefore, the lowest interest rates available. The Permanent School Fund, established in the state constitution, is composed of state-owned assets. These assets produce a substantial income which accrues to the Available School Fund. The Available School Fund, in turn, finances textbooks as well as a constitutionally-required per-student allotment to all schools.

One might think that reducing the cost of borrowing by using the Permanent School Fund to guarantee school bonds is a good idea for taxpayers, lowering the interest and sinking tax rate that they would otherwise pay. This is true for any given project. However, by

reducing the cost of borrowing, it is quite likely that the cost windfall is often being used to increase the size and overall cost of projects. Such cost increases may or may not contribute significantly to the overall education of Texas youth.

The Permanent School Fund is also used to guarantee more than just instructional facilities. All school bonds, regardless of the project for which they pay, are guaranteed. This includes bonds used to pay for football stadiums, indoor swimming pools, or performing arts centers.

One perverse effect of the Permanent School Fund guarantee is to insulate school district administrations from additional financial scrutiny that would otherwise occur. In general, many factors affect bond ratings. Bond rating companies mostly evaluate bond issuers on the basis of overall numbers such as already-existing debt, the total assets of the issuer, as well as other indicators of sound financial management. These evaluations are done in order to determine the ability of the bond issuer to pay back the bonds. Where risk is higher, bond ratings fall and higher interest is charged to the issuer. Where risk is lower, interest costs are lower. Because of the Permanent School Fund guarantee, however, outside scrutiny of districts' financial health is less necessary and districts are insulated from an alternative source of accountability when they borrow.

Local school bonds are being rated according to state assets rather than on the basis of local financial practices and conditions. In essence, state taxpayers as a whole are bearing the financial risk of local bond issues. This risk might not be great, but it does exist and this risk is being borne by taxpayers in addition to the cost of the state facilities subsidy programs outlined above.

The Texas Education Code, in Section 45.053(a), allows the Permanent School Fund to guarantee a total amount of bond principal equal to 2.5 times the value of the Fund, recently increased from 2 times the value in 2003. According to the State Auditor's Office, as of August 31, 2002, 63.6 percent of the old guarantee capacity had been used. The IRS, though, has a stricter limit, 76.5 percent of which had been used.¹⁵ Of course, this capacity waxes and wanes with market conditions and the value of the Permanent School Fund in addition to the amount of bonds being retired and issued from year to year.

Effects of Facilities Subsidies

Subsidies – all subsidies – make those who buy subsidized items pay twice. In addition, a subsidy encourages the production of the subsidized good or service beyond what is economically optimal. For example, dairy price supports (a type of subsidy) required the federal government to buy milk that consumers were unwilling to buy at the high price the government enforced in an otherwise free market. Technically, subsidies operate by reducing the price consumers pay for a product even as producers receive a relatively high price. The result is the same as with the milk example, though, in that too much of

the subsidized product is produced than can be economically justified by consumers' willingness to pay.

One might understandably wonder why, if school facilities are being subsidized by the state, there seems to be a facilities shortage. Is it not the case that statements like that of the NEA above refute the assertion that a facilities subsidy results in overproduction? Our problem appears to be too little in the way of facilities rather than too much. The answer lies in the fact that: 1) facilities are a durable good that take time to produce, and 2) school systems are not producers of school facilities; they are consumers of school facilities. Subsidies, because they have the effect of lowering the perceived price of a good for consumers, encourages consumers to buy more of a good than they otherwise would.

In the case of school facilities, the per-unit subsidy is known, but the state has not committed to fully funding the subsidy – i.e., the total appropriated for the facilities subsidy is less than school districts, in total, would like to have, given the size of the subsidy. Thus, the facilities programs are always oversubscribed. School district leaders have responded to the facilities funding programs the way any set of consumers would respond to a potential subsidy. They have spent or have tried to spend more than they otherwise would have. Since the state has not fully funded the subsidy, there is unsatisfied demand for it. Although there is a huge amount of facilities funding and more facilities construction than ever, there is a huge reservoir of perceived unmet need. It is rather like the cheese and butter giveaways by the federal government a few decades ago. When cheese and butter were passed out for free, there were always unsatisfied people standing in a long line waiting to get their share when the last packages were passed out.

By lowering the local costs of instructional facilities, the state subsidies free up funds for other kinds of facilities such as sports arenas and fine arts centers. Facilities can be constructed with higher-cost materials than are necessary. Expensive architectural features can be more easily afforded as well. In San Antonio, new high schools are or have been constructed that, in 2003 dollars, cost as much as \$132 per square foot. The median cost per square foot nationwide is \$122. For the region of the nation that includes Texas, the median cost per square foot is \$107.¹⁶ The median cost of a 2,200 square foot home (not necessarily brand new) in San Antonio is \$84.88 per square foot.¹⁷

One justification that can be put forth for the high cost of school buildings is that they are built to last and that higher-cost construction at present means lower maintenance costs in the future. There is a certain amount of truth to this. Generally, it would be expected that schools will cost more per square foot than a home. However, it is also reasonable to question the necessity and/or wisdom of constructing a school building to last 100 years given the fact that population patterns can and do change radically during such a long period of time.

In addition to the high cost of construction per square foot, school buildings are made more costly as a result of facilities standards required by the state. First put in place in the early 1990s by the State Board of Education, state law now requires the Commissioner of

Education to adopt such standards. No public funds, state or local, may be expended on new facilities that do not meet the standards.¹⁸ For example, elementary classrooms are supposed to have 36 square feet of space (a six-foot square) per child. There are standards for science and library space as well as classroom size standards for junior high and high school.¹⁹ These one-size-fits-all standards have recently been expanded and certainly result in greater construction expense.

These state standards, however, cannot be blamed for the expense of school construction on a cost per square foot basis. These standards have only to do with sizes of rooms and some safety equipment requirements for science classrooms. Except for what appear to be some very generous square footage requirements, the state standards, of themselves, do not have to add that greatly to the cost of facilities.

On an institutional basis, there is little incentive for school districts to be as efficient as they possibly can in any aspect of their operations, much less in their design and construction of facilities. Like all government agencies, school districts do not face the discipline of markets. There is no one to claim a residual (profit) so that there is little incentive to hold school management's feet to the fire in order to keep costs low. Taxpayers, whose interests would be served by greater efficiency, are too diffuse and have too little expertise to begin to make a difference in their own behalf.

The Robin Hood school system, to some extent, encourages facilities spending. The interest and sinking portion of the local property tax is not equalized. Raising that rate does not result in additional monies leaving a rich district like the same action does with the maintenance and operations portion of the property tax. Local school boards understandably look at facilities spending as a relatively easy way to please parents with children in school – one group of people in the district who are likely to vote.

Facilities Spending by the Numbers

The analysis above certainly seems to imply that facilities spending in school districts is likely excessive by some standard. However, such an assertion is difficult to prove. One reason for this is that different people evaluate the same expenditures differently. For some, it seems that virtually any expenditure on public schools is justified. For others, there is a tendency to want to see some evidence of results that make a given expenditure worthwhile.

The analysis, though, is less about whether or not enough is being spent than whether the current system encourages decision makers to allocate resources in an efficient manner. One way to test whether the system truly does produce the incentives and result in the kind of behavior described above is with the statistical technique of multi-variable linear regression. This is a statistical technique that not only allows a researcher to determine if two things are correlated but that also allows one to determine the degree of the relationship, taking into account other things that are correlated with something that the researcher would like to better understand and explain.

The issue at hand is facilities funding and therefore, school district debt. Specifically, what factors might explain school district debt? A readily available source of data regarding school debt resides with the Texas Bond Review Board. Each year, usually in April, the Texas Bond Review Board reports school district debt from the previous fiscal year. The latest data available as of this writing is from fiscal year 2002.²⁰

Conveniently, the Bond Review Board data contains more than just the amount of debt principal owed by each of 1,034 school districts in 2002. It also contains information on the amount of interest each district will pay, the number of students (average daily attendance) in each district, the change in the number of students over the previous five years, as well as total district wealth and other factors. All of this data is neatly contained in a downloadable Excel spreadsheet, making it convenient to calculate simple regressions using the statistical package available with Excel.

The results of a linear regression using the 2002 data and relating various factors to school district debt are reported in Table 1 (next page). The regression has a very good fit since only five factors explain over 86 percent of the variation in school debt among 1,033 school districts. This is demonstrated by the R^2 number reported at the bottom of the table.

All of the mathematical relationships of the five factors related to school district debt identified in the table are highly significant, statistically speaking. That is, there is a high likelihood that the relationship identified is a real relationship and not a spurious one. Four of the relationships identified are very highly significant. Normally, in a linear regression an intercept (like the “Y” intercept in the graph of a straight line) is reported. However, the intercept was statistically insignificant – i.e., it could not reliably be asserted that it was anything other than zero. Therefore, the regression was calculated with the intercept purposely equated to zero.

A linear regression calculates a coefficient (or multiplier) for each of the factors or variables (independent variables) that are being associated with the factor or variable that the researcher wants to explain (dependent variable). Each of the factors listed in Table 1 is *positively* associated with school district debt. For example, the first variable is district total average daily attendance. It simply says that, holding everything else constant, the larger a school district in student terms, the greater the debt. The size of the coefficient implies that if two districts are exactly alike except that one has 100 more students, the larger district will have \$250,465 (100 students x \$2,504.65) more debt.

The relationship (coefficient) between school district debt and district size is one which is very highly significant. It is not surprising that larger districts would have more debt than smaller ones. Larger districts have more buildings, more grounds, and more equipment. Even if they are not putting up new buildings they often need to perform heavy maintenance on existing ones or buy new equipment. For large districts these are large expenditures in the budget and it is natural that they would turn to bond issues to finance them.

Table 1. Factors Associated with School District Debt

Factor	Effect of an Incremental Change in the Factor (Coefficient)	Statistical Significance* (t-statistic)	Explanation
Average Daily Attendance	2,504.6543	9.86	Very highly likely a positive relationship
Total Wealth	0.0065	8.68	Very highly likely a positive relationship
Absolute Change in Average Daily Attendance (last 5 years)	26,946.4672	28.21	Very highly likely a positive relationship
Participant in the Instructional Facilities Allotment	7,349,181.0012	4.14	Very highly likely a positive relationship
Chap 41 (Rich) District	6,367,392.6216	2.07	Highly likely a positive relationship
R^2	86.25%		
Adjusted R^2	86.10%		
Standard Error	29,654,143.07		
F-statistic	1,290.94		
Number of observations (districts)	1,034		

*All coefficients are significant at the 99% level except that of the Chap 41 (Rich) District factor which is significant at the 95% level.

Source: Texas Bond Review Board and Texas Education Agency data, lead author's calculations

Whether it is appropriate that 100 more students should automatically result in another quarter of a million dollars in debt is a different issue, but it should be noted that a *growth* (as opposed to absolute size) factor is included separately in the regression. So, some further explanation seems necessary. Size of a school district's student body varies with the size of the district's electorate. It may be that the administrations of larger school districts are simply better able to convince those who vote in school elections to vote for proposed bond issues.

In Table 2 (next page), averages of various factors are reported for Texas school districts grouped in quartiles. That is, each quartile represents one-quarter of the school districts in the state. Under the percentage change in average daily attendance (ADA) school districts are arranged in order of percentage growth in ADA from highest to lowest so that the first quartile is the fastest-growing (in percentage terms) quarter of all school districts in the

state. The last quartile is the slowest growing districts. Quartiles by total ADA group the largest districts in the first quartile and the smallest in fourth quartile.

Table 2. Averages of Various Factors of School Districts Arranged by Quartiles

	Debt Principal Outstanding as of 8/31/02	2001 M&O† Tax Rate	2001 I&S‡ Tax Rate	2001 Total Tax Rate	Wealth Per ADA, 2002	Full-Year ADA, 2002
Quartiles by % Change in ADA*						
1st	\$56,374,418	\$1.3862	\$0.1495	\$1.5357	\$264,905	5,465.28
2nd	\$27,505,329	\$1.4072	\$0.1025	\$1.5097	\$241,218	4,542.73
3rd	\$12,724,856	\$1.3796	\$0.0741	\$1.4537	\$243,570	3,453.93
4th	\$5,011,464	\$1.3813	\$0.0507	\$1.4319	\$417,455	1,224.47
Quartiles by Total ADA*						
1st	\$92,997,398	\$1.4427	\$0.1579	\$1.6006	\$242,354	12,445.68
2nd	\$6,342,749	\$1.3889	\$0.1086	\$1.4975	\$210,190	1,466.89
3rd	\$1,776,486	\$1.3690	\$0.0768	\$1.4458	\$243,652	576.16
4th	\$405,986	\$1.3641	\$0.0346	\$1.3987	\$472,023	187.22

*ADA = Average Daily Attendance †M&O = Maintenance and Operations ‡I&S = Interest and Sinking

Source: Texas Bond Review Board, lead author's calculations

Note in Table 2 that there is far less variation in total school district debt among the percentage-growth quartiles as compared to the total ADA quartiles. Note also that the first quartile under percentage growth has a lower average interest and sinking (I&S) tax rate than does the first quartile under total ADA. Finally, note that there is a greater variation in maintenance and operations (M&O) tax rates among the total ADA quartiles than the percentage growth quartiles. All of these observations confirm the assertion that large districts tax at higher rates and spend more than necessary on facilities simply because they can. They are able to because their very size makes them less accountable to taxpayers.

Total wealth of a school district is another factor that is positively related, and very significantly so, to district debt. The wealth coefficient says that if nothing changes except that a district's wealth increases by \$1 million, the district will end up with an additional \$6,500 of debt. Now this is a puzzling result. There does not seem to be a particularly good reason for district wealth alone to result in greater district debt from a pure efficiency standpoint.

One explanation for the positive relationship between district debt and wealth might be that wealthy districts also face higher costs of property acquisition for schools. However, one of the other variables in the regression is one that identifies so-called Chapter 41 (wealthy) districts – the wealthiest districts of all. That variable is not as statistically

significant. In addition, greater wealth does not automatically imply student growth – the best reason for added debt due to the need for more space. Student growth is accounted for in the regression in absolute terms as a separate factor.

Another way to account for district wealth, and a more accurate one for the purpose of capturing the effects of variations in construction costs due to costs of living, would be to include wealth per student as an explanatory factor. In fact, this was attempted. Including the ratio of district wealth divided by average daily attendance yielded no statistical relationship between wealth per student and district debt.

A much more reasonable explanation for the positive relationship between debt and wealth is that greater wealth simply represents an opportunity for school officials to spend more money. Suppose the property value of a school district increases as a result of the sudden discovery of an oil or natural gas deposit. Automatically, the I&S tax rate is reduced because the rate is only allowed to cover the cost of servicing current debt. Suppose the I&S rate was 25¢ before the discovery but dropped to only 10¢ after the discovery. Most voters in the district, given that they were willing to pay the higher rate in the first place, are likely to vote for a rate higher than 10¢, regardless of whether the “needs” being funded are real or not. School officials are likely to respond accordingly with a new bond proposal.

The next factor in the table is the growth in average daily attendance (ADA) of school districts over the five years previous to 2002. When the absolute change in ADA is positive, it is certainly reasonable to expect that a school district’s debt will increase. Growth in the number of students brings with it for a district the necessity to provide space for those students to attend class. The relationship between school district debt and absolute growth in ADA identified in this regression indicates that one additional student results in a district incurring an additional \$26,946 of debt.

Even at \$132 per square foot (a high number for construction cost), and using the state’s required square footage for elementary school class space (36 square feet per student, which is more than for high school), \$27,000 should provide enough square footage for 5.7 students rather than just one. Of course, some debt pays to entirely replace old facilities. So, it is often not square footage just for new children for which facilities debt is paying. Another reason for the high cost of facilities for a new student might be that every building requires more than just classrooms. There are also hallways, bathroom facilities, and other areas to consider. On the other hand, this does seem like a lot of debt to be incurred for each new student given what is known about costs per square foot – that in the region including Texas, the median cost per square foot is \$107.

One growth factor that was considered for the regression but was not included is the percentage change in Average Daily Attendance in school districts from 1997 to 2002. The percentage change was provided in the Bond Review Board data. Regressions were estimated with this factor included but the coefficient estimated was statistically unreliable.

It would be expected that the greater the percentage increase in the number of students and Average Daily Attendance, the more likely school districts would need to increase facility capacity with new construction and, hence, new debt. Generally speaking, many school districts have some classroom capacity into which new students can fit. Greater facilities needs occur when the increase in students overwhelms this capacity, presumably when there is a large percentage change in the number of students.

Including the percentage change in Average Daily Attendance added almost nothing to the explanatory power of the regression. Also, statistical tests indicated that it was correlated to one or more other factors that do a far better job of explaining school district debt. It appears that the percentage of student population growth matters much less than increases in the total number of students. In other words, school districts have a tendency to react to any growth, large or small in relative terms, with an emphasis on new facilities rather than by considering ways to more fully utilize existing facilities.

One only has to witness a growing district building new schools and the fights that result over attendance zones to understand the truth of the statement above. Growth often brings with it geographic shifts in student populations. In order to make the fullest use of existing facilities attendance zones within a district have to be redrawn. This is a political process fraught with risk for elected district trustees. Parents are understandably impatient with long bus rides for their children. It is also very confusing for a child to have to ride a long distance to school when a campus with the appropriate grade is just a few blocks away. With the various conflicting demands made on them it is no wonder that school district officials might often choose to build their way out of dilemmas rather than make what are often much harder decisions regarding where children should attend school.

The last two factors affecting school district debt listed in Table 1 are what are referred to in regression analysis as “dummy variables.” In a data table each of these factors is represented by either a “1” (=true) or a “0” (=false). Either a school district is a participant in the Instructional Facilities Allotment program or it is not. Either a school district is a Chapter 41 (wealthy district from which equalization funds are taken) or it is not.

Most school districts that are in debt are either Instructional Facilities Allotment participants or are Chapter 41 districts. However, if all districts in debt were one of these, the dummy variables would simply substitute for the intercept that has not been calculated in this regression. This is not the case, however. A number of school districts carrying debt are neither Chapter 41 districts nor Instructional Facilities Allotment participants. A number of alternative regressions were run with and without the intercept and with and without either or both of the dummy variables. The results reported in Table 1 are the best results of the combinations computed.

If a school district is an Instructional Facilities Allotment participant, it is automatically in \$7.3 million more debt than otherwise. This is powerful confirmation of the analysis above – that a subsidy of school districts’ debt payments leads to more debt.

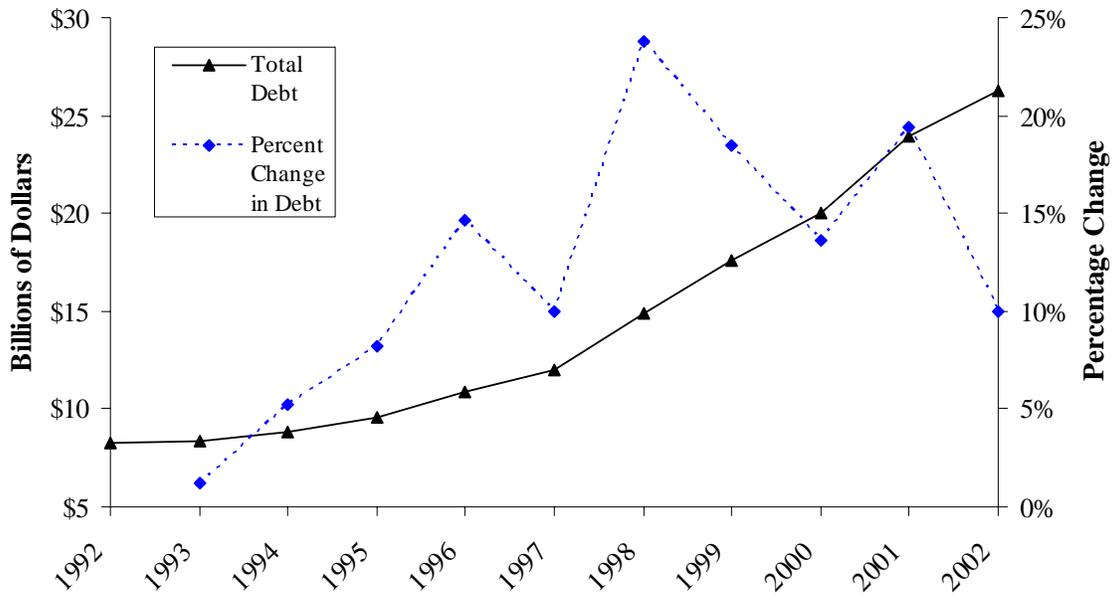
Of course, the legislature created the Instructional Facilities Allotment program specifically so that school districts could better afford facilities debt. Nevertheless, few legislators would readily admit that they voted for this program so that school districts could immerse themselves more deeply into debt. More likely the motivation was to help taxpayers better afford the facilities that districts were purported to already need and, presumably, for which local taxpayers were already willing to pay.

The result of the legislature instituting a state facilities debt subsidy can best be shown by data available from the Texas Bond Review Board. Figure 1 (next page) graphically illustrates total school district debt and its yearly change in Texas over the eleven year period, 1992 through 2002. Just from looking, even the casual observer can see that the rate at which school district debt was growing increased after 1995 slightly and then again, more markedly, after 1997. It was in each of these transition years, 1995 and 1997, that the legislature passed facilities subsidy programs.

The data from which Figure 1 is derived are contained in Table 3 (next page). Note the percentage changes in total school district debt. Once again, it is clear that school districts responded as soon as practicable to the legislature's facilities subsidy programs by going into debt at a faster rate than before. From 1992 to 1995 the yearly growth rate in debt barely exceeded eight percent in a single year. Then suddenly, from 1995 to 1996 debt shot up by over 14.6 percent. There was a brief fall-off in the growth in debt for one year. Then again, from 1997 to 1998 debt grew by nearly 24 percent! Since then, there has been a double-digit percentage increase in total school debt every single year.

Recall that the Instructional Facilities Grant program was created in 1995. School districts could only take advantage of it beginning in fiscal 1996. In 1997, the Instructional Facilities Allotment was first created. Again, there was a one-year lag before its effects could be seen. Clearly, school districts have responded to the facilities subsidies with a great deal more facilities spending and bond debt.

Figure 1. Trends in Total Texas School District Debt, 1992-2002



Source: Texas Bond Review Board

Table 3. Total School District Debt in Texas

Fiscal Year	Principal Outstanding	Yearly Percentage Change
1992	\$8,268,964,231	NA
1993	\$8,371,262,721	1.24%
1994	\$8,806,698,155	5.20%
1995	\$9,527,759,055	8.19%
1996	\$10,921,468,647	14.63%
1997	\$12,012,691,966	9.99%
1998	\$14,871,694,799	23.80%
1999	\$17,613,904,665	18.44%
2000	\$20,008,181,538	13.59%
2001	\$23,895,200,957	19.43%
2002	\$26,287,609,579	10.01%

Source: Texas Bond Review Board

Some would say that increased school district debt is fine, that school districts needed to spend more money on facilities. In addition, the state subsidies for facilities are limited to instructional space. Surely, the argument goes, everyone can agree that these are worthy programs when the money is only spent on classroom space.

The problem with the last argument is that just because, according to the books, the state funds are dedicated to instructional facilities, school districts are not precluded from spending more money on non-instructional facilities as a result of the subsidy. Suppose it is widely agreed in a school district that a new school with a \$10 million price tag is needed. In addition, though, there are those who would like to construct a new \$1 million sports facility. The district trustees do not believe taxpayers would stand for a tax rate to service more than \$10 million in debt. But, the state comes along and offers to help the district with a subsidy that will service \$2 million in debt. Now this is an opportunity! Suddenly, the trustees can fund the new school *plus* the sports facility *plus*, perhaps, a few bells and whistles *and* still have local taxpayers service *less* than \$10 million in debt.

Finally, the last factor identified as possibly having an effect on the level of debt school districts carry is whether or not a school district is wealthy enough to be classified a “Chapter 41” district. These are the school districts that are required to share their property tax revenues with other school districts under the state’s so-called Robin Hood law.

Once again, holding everything else constant, if a district is a Chapter 41, it is automatically \$6.4 million in more debt than it would be otherwise. There is less statistical certainty associated with this factor, meaning that the effect on district debt from being a Chapter 41 district is more likely to measure differently if other meaningful determining factors were identified and included in the regression. Nevertheless, the estimated statistical relationship is significant.

The relationship between school district debt and Chapter 41 status identified here seems to confirm what some have claimed. Since the interest and sinking (I&S) portion of the local property tax is not equalized for Chapter 41 districts, expenditures that would otherwise be financed by the maintenance and operations (M&O) tax are being financed through debt. For example, if computers are needed in several schools, a district can use its M&O capacity to fund their purchase instead of borrowing, even though computers can be justified as a capital expenditure. Chapter 41 districts, though, choose to borrow since 100 percent of I&S tax funds stay with the district whereas a portion of M&O funds are lost to the Robin Hood system’s redistribution scheme. Given the choice, it is rational that Chapter 41 districts would choose I&S over M&O funding wherever possible.

The current school finance system clearly encourages debt finance by school districts on each end of the wealth spectrum. Accordingly, it is not surprising that wealth per student, when included as a factor that might explain school debt, statistically showed no explanatory power. When it comes to the relative size of school districts’ debt, legislative policies play a big part. In fact, after growth in the number of students in a district,

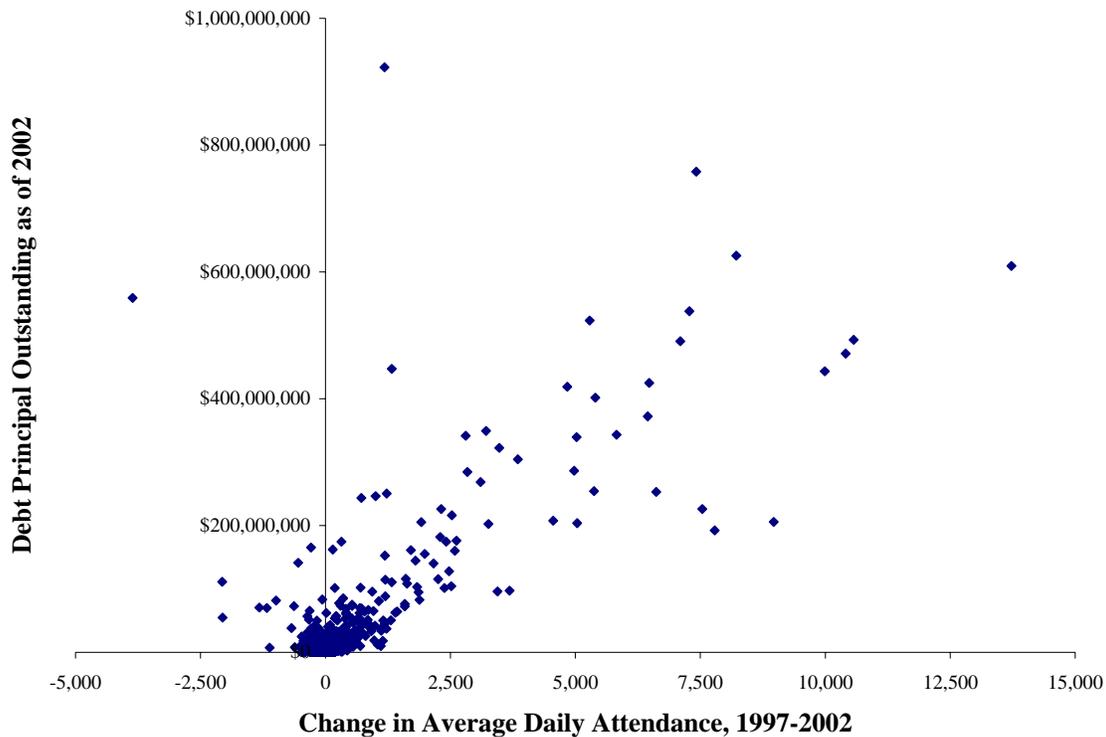
legislative policies seem to be the overriding factor in determining school district debt. Perhaps this is to be expected since the legislature created the system.

Given this last statement it might fairly be asked why participation in the Existing Debt Allotment was not included in the regression. It was not because it is a retroactive program. There is a great deal of uncertainty of whether the funds will be available for a district to participate in the Existing Debt Allotment. A district has to have issued bonds and made payments in order to participate in the Existing Debt Allotment as well. Therefore, the Existing Debt Allotment is less likely to encourage additional debt than the Instructional Facilities Allotment, which is a direct subsidy of new facilities and debt.

Facilities Costs and Growth

The cost of providing new school facilities for the nation’s growing number of pupils generally falls most squarely on the newer, faster growing communities in the suburbs. This is as true for Texas as in the nation as can be seen in Figure 2, which dramatically shows the positive relationship between school district debt and growth in students. Each dot in the graph represents a Texas school district. Clearly, the greater the student growth over the five-year period 1997 to 2002 in a school district, the greater the school district’s debt.

Figure 2. Texas School District Debt and Attendance Growth



Source: Texas Bond Review Board

The pattern illustrated in Figure 2 is often cited by the anti-sprawl (so-called smart growth) advocates as well as advocates for fast-growing school districts as evidence that suburban living is more expensive than central city living, especially with respect to the cost of government-provided infrastructure. The claim is that fast-growth areas are more expensive due to burgeoning demand and limited supply due to lagging development.

Data from the United States Department of Education,²¹ though, does not indicate that school costs are higher in faster growing areas (which are largely in outer ring suburbs or even exurbs) than the slower growing areas (which are often in central cities and inner ring suburbs). There is no doubt that a school district having to build new schools will spend more in capital expenditures and debt service than one that does not have to build new schools. But school districts in slower growing areas spent just as much as their faster growing cousins.

Examples of this phenomenon in Texas include Houston ISD, which grew by less than one percent from 1997 to 2002, but has the greatest amount of debt in the state at \$923 million. In the diagram above it's the lone dot (outlier) higher than all the others. Another outlier is San Antonio ISD. It's the dot to the left of the vertical axis that looks like a typo. This is a district that *lost* students yet it stands as the fifth most indebted school district in the state at \$559 million owed. Of the twenty most indebted school districts in the state, six grew by less than 10 percent. One of these, another outlier in the diagram above, is Austin ISD, which grew less than 2 percent. It is the dot sitting at about \$450 million with less than 2000 new students in average daily attendance (ADA).[†]

There are other outliers in the opposite direction – school districts in Texas that grew a lot but bucked the trend (in relative terms) on the amount of debt they carry. Cypress-Fairbanks ISD (the dot farthest to the right), which saw the largest increase in ADA with almost 14,000 new students, has \$600 million in debt, little more than San Antonio. Aldine ISD and United ISD are other examples of high-growth but relatively low-debt districts. They grew between 7,500 and 10,000 in ADA and had about \$200 million in debt.[‡]

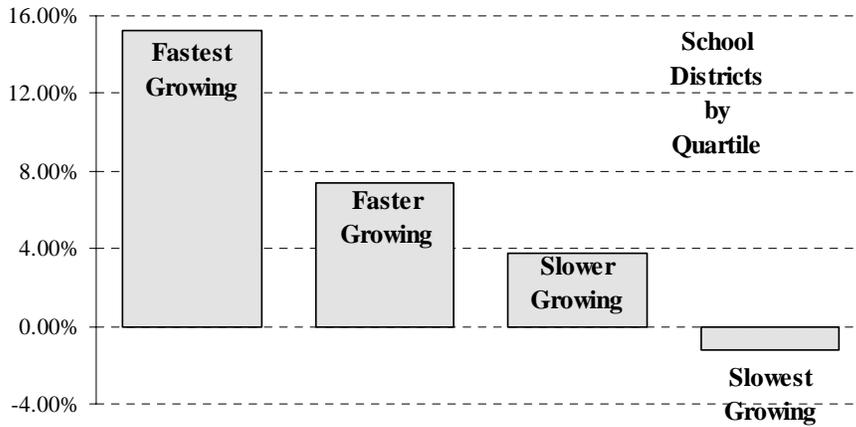
Fast growing school districts do face an inordinate burden in financing construction of new schools. As a result, it would be expected that spending per pupil would be higher in faster growing school districts. An analysis of data for school districts enrolling more than 15,000 students in 1997-1998 indicates that overall expenditures per pupil are actually lower than average (see Appendix):

- The fastest growing quartile (25 percent) of school districts experienced enrollment growth averaging 15.2 percent from 1995 to 1998, compared to an overall average increase of 6.3 percent (Figure 3, next page).

[†] San Antonio is an Instructional Facilities Allotment participant. Austin is a Chapter 41 district. Houston is neither of these.

[‡] Cypress-Fairbanks is neither an Instructional Facilities Allotment participant nor a Chapter 41 district. Aldine and United are both Instructional Facilities Allotment participants.

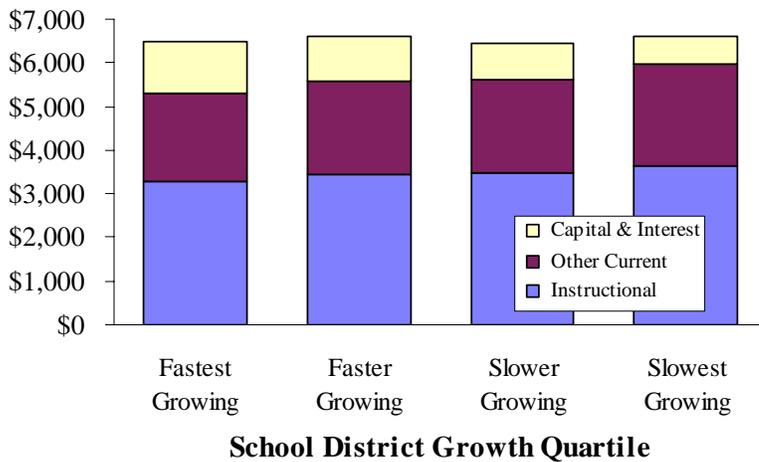
Figure 3. School Enrollment Growth, 1995-1998 (U.S.)



Source: See Appendix

- As would be expected, capital expenditures and interest (including the cost of new school construction) were higher in the fastest growing quartile, at \$1,189 per pupil, 28 percent more than the \$928 average and nearly double the \$640 spent by the slowest growing school districts.
- However, overall expenditures were second lowest in the fastest growing quintile (the “slower” growing quintile was lowest, 0.2 percent below the fastest growing quintile). The highest growth quartile spent \$6,477 per pupil in 1998, one percent less than the \$6,543 average (Figure 4). Fastest growing quintile school districts spent two percent less per pupil than in the slowest growing school districts.

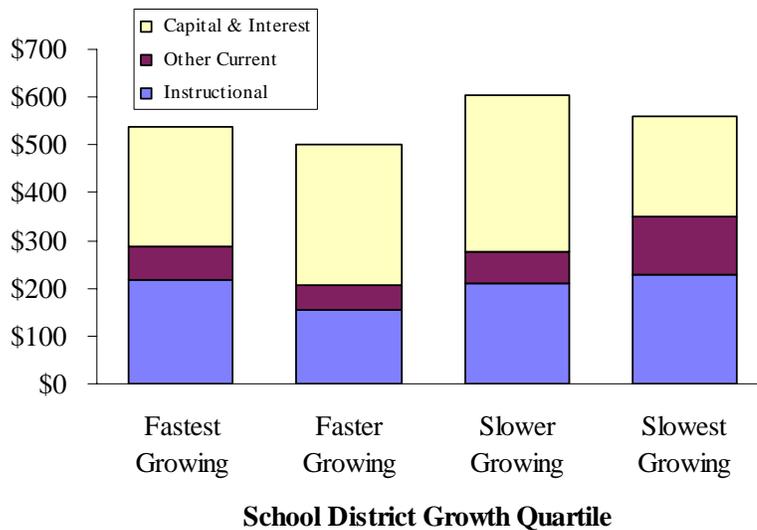
Figure 4. Spending per Pupil in 1998 (U.S)



Source: See Appendix

- Overall expenditure growth was less in the fastest growing quartile. The fastest growing quartile experienced expenditure increases averaging 9.1 percent from 1995 to 1998, compared to the 9.2 percent average (Figure 5).

Figure 5. Change in Spending per Pupil, 1995-1998 (U.S.)



Source: See Appendix

What is most significant, however, is not the rather modest expenditure differentials between school districts in fast growing areas and those in slower growing areas. It is rather that there is so little difference. All of the quartiles, from the fastest growing to the slowest growing, had expenditures within 1.5 percent of the average. Referring back to Table 2, it is worth noting that Texas school districts show less tax rate variation when compared on a percentage growth basis.

There is, however, one difference in the national data worth noting. It is often suggested that education costs would be lower if people moved into the slower growing central cities and the older infrastructure there was put to greater use, rather than having enrollment growth continue to occur in the faster growing suburbs. If the faster growing district construction and debt service costs were imposed in the slower growing districts, it could be expected that costs would be approximately 10 percent higher. And that does not take into consideration the complications that can make building in already intensely developed areas more expensive. This casts serious doubt on the potential for reducing educational expenditures through “brownfield” or “infill” residential development.²²

The higher costs attributable to new school construction in the fastest growing school districts appear to be more than offset by higher spending on instruction and administration in the average school district. This may be an indication of what might be called “bureaucratic entrenchment” – a reflection of greater control in the older, slower growing districts by entrenched interests, such as teachers unions and older, larger bureaucracies.

Recommendations

Hold Bond Elections on Standard Election Dates

Although more limited in the date they choose than they have been in decades past, school districts are not limited to standard May and November election dates to which people have become accustomed. There is quite a bit of latitude for them to determine dates on which bond elections will be held. Common practice is to hold them on Saturdays.

Although school districts are required to publicize bond elections, these elections suffer from relatively modest voter turnout because of the nonstandard election dates. The result is that those with the biggest interest in seeing the bond proposal pass – teachers, school administrators, and parents – often turn out, while the average taxpayer who foots the bill is trying to enjoy free time on the weekend.

Greater turnout on standard election dates is widely considered to constitute a higher hurdle for proposed bond issues by school officials. Many voters who would otherwise not vote in a bond election, they believe, will vote against the bond. What this reform would mean is that school officials will have to build greater consensus and knowledge in their communities. They are also likely to face tougher questions regarding the size and scope of their designs, necessitating a more efficient use of resources.

Although school district boundaries often do not coincide with other political subdivision boundaries, it is reasonable to expect, with the current technologies available, that school district elections could be held simultaneously with other general elections. They should be, and taxpayers certainly deserve the convenience.

Abolish the Interest and Sinking Tax Rate

A fundamental reform that would bring real discipline to school facilities investment would be to allow school districts to have only one tax rate. Instead of having two tax rates, one designated “maintenance and operations” (M&O) and another designated “interest and sinking” (I&S), there should only be a single rate and a single cap. If bonds need to be issued, the current policies and procedures could stay in place, but taxes necessary to pay off bonds would have to be derived from the same potential pool of tax monies as taxes that support everyday operations.

Under current policy, there is no tradeoff that has to be made or can be made between facilities funding and operations funding. School districts are put in the awkward position where they literally cannot spend any more money on academic programs due to M&O tax limitations and funding formula limitations. On the other hand, they can spend I&S funds on facilities made fancier and larger than they need to be, including facilities that are not academic in nature at all.

School districts have too little opportunity to make the most efficient decisions regarding tradeoffs between capital and non-capital (including labor) expenditures. Under current policy, especially for poor districts and rich districts, state policy makers have effectively encouraged school districts to over-invest in facilities. As a rich district, spending on facilities does not result in funds being confiscated. As a poor district, spending on facilities is subsidized. All of this occurs because of the existence of the I&S tax.

Currently, some school districts are already funding some capital investments from their M&O tax rate. A survey by the Texas Senate Education Committee yielded a list of school districts that have pledged a portion of their M&O taxes to pay off loans for such things as mold remediation, computer purchases, repair and rehabilitation of facilities, school buses, stadium seating, portable buildings, a gym, an athletic stadium, school building construction, and a host of other projects. The list of districts and projects runs for seven pages. Another thirteen pages of districts and projects reflect loans and leases which are long-term contractual obligations almost like bond debt.

In order to adopt this recommendation, current debt obligations would have to be honored under current law. The M&O and I&S limits would have to be combined. Current and future rates would have to stay within this new limit in order to prevent tax increases.

No doubt the bond market would not like it if this recommendation were adopted. However, it seems unlikely that if the Permanent School Fund guarantee for voted debt was maintained, that the cost of borrowing would increase.

Reform the Permanent School Fund Bond Guarantee Program

In order to encourage districts to place their highest spending priority on academic instruction, the Permanent School Fund should only guarantee bonds issued for the purpose of constructing instructional facilities. In addition, each district should face a limit in how much in bonds the Permanent School Fund will guarantee. As much as possible, limits should be placed on subsidies of school facilities to only those facilities that are necessary for schools' central mission – to provide for a “general diffusion of knowledge.”²³

A formula should be established to determine a maximum amount of bonds for any district to have guaranteed by the Permanent School Fund. The formula should be weighted for the age of a district's standing facilities and the growth of the district's student body in absolute and percentage terms. The formula should build in a limit on the amount of square footage per student the district may possess and still benefit from the

bond guarantee program. Finally, the per-square-foot cost of a new facility should be limited for guarantee purposes, and indexed to inflation.

Subsidize Only a Maximum Expenditure Per Student for Facilities

The legislature should consider establishing a maximum allowable expenditure per student for new facilities. Based on the number of students that will occupy facilities, the legislature should consider establishing a maximum amount that it will subsidize under the Instructional Facilities Allotment and Existing Debt Allotment programs.

School districts would have to search for ways to achieve greater efficiency in their facilities plans if subsidies were limited to some level of necessity as defined by the legislature. The legislature could encourage further efficiencies by providing incentives within the facilities subsidy programs.

One incentive the legislature could build into the subsidy programs might be to provide for greater subsidies in percentage terms when school districts enter into cost-saving public/private partnerships. For example, school districts should be encouraged to use design-build contracting, and to partner with private and/or public organizations to construct facilities with dual uses. There is evidence that considerable savings are possible through various partnership methods.²⁴

Build a State Database of School District Holdings

Ideally, in a comprehensive analysis of school district facilities spending it would be very good to know, with some specificity, just exactly what school districts have in their facilities inventory. In addition, it would be useful to know when various facilities were constructed, how many children use the facilities, the purpose for which they were originally built, and the purpose for which they are currently used.

Some years ago, there was an effort to determine just how much property school districts owned in the state. Apparently, the data was considered to be of little use. In fact, the state keeps no systematic records on the amount of property owned by school districts and, therefore, there is no way for the state to set up a system to determine real facilities needs in school districts. The legislature has nothing but the testimony of school officials as information on school facilities needs in the state.

The state should have more information regarding school facilities, especially when the state is helping to fund those facilities. The state gathers a great deal of data on what maintenance and operations are supposed to fund by gathering data on student achievement. Something similar needs to occur with respect to facilities. The Texas Bond Review Board has some information about current debt, but little information on the facilities being financed. The privately-run Municipal Advisory Council has far more information about what current debt is funding, but details on square footage and other relevant information is nonexistent.

The state should have a database of existing facilities as well as facilities scheduled to be constructed and for which debt is owed. In addition to the information already mentioned above, the database should contain information on the value of various properties owned by a district and square footage devoted to instruction, athletics, administration, and entertainment. A clear distinction should be made between information regarding administrative versus instructional facilities.

Armed with a comprehensive database, the state would be in a better position to determine the best facilities-funding policies. In addition, researchers would have a rich database available to them to help determine optimal facilities usage.

Encourage Money-Saving Facilities Designs

A simple and obvious fact is that people move more readily than buildings do. Populations move. Concentrations of school-age children vary geographically over time. In other words, a school ideally located today may be far away from most children in a city fifty years from now.

Most school buildings constructed today are clearly intended to last for a very long time, as long as 100 years. Given the fact that populations vary so greatly over time within any given geographic region, it is worth questioning whether school buildings should be built to such lasting specifications.

The state should explore the possibilities for school building designs that are functional, safe, attractive, and save money. Local conditions must always be of primary importance, but investment in some state guidelines to help school administrators and school boards who have little expertise in building design would be wise. The existence of such guidelines might help a district save a great deal of money on any given construction project.

Local officials are at a distinct disadvantage in expertise and knowledge compared to architects and contractors who have good reason to maximize the size of any given project. It might even be advisable to limit architect fees in some way in order to encourage school districts to make use of existing designs. Dallas ISD, for example, spent over \$3 million in fiscal year 2003 on architect and engineering fees for new facilities. Local conditions require some expenditure on such services regardless of whether a new school is of a previously-used design. But, greater standardization of school designs should save taxpayer funds at least on design services.

Repeal the Prevailing Wage Law

Chapter 2258 of the Texas Government Code is the state's prevailing wage law. Though not mentioned elsewhere in this paper, it is a contributor to the cost of every public works project in this state, including the construction of school buildings. The law requires that contractors building a public work paid for by public funds (i.e., tax money) must pay the "prevailing wage."

Determination of a prevailing wage is not easy. What the law requires is an onerous task for a local government. For every craft that will be required in a project, the local authority would have to determine the average wage paid in the region within which the project is to be constructed. The region would have to be defined, data gathered and computed, and then the computed wages would have to be enforced.

The easiest method by which to avoid much of the administrative cost just described is to use the relatively straightforward method, provided for in state law, of simply using federal prevailing wage data available from the Department of Labor. The Department of Labor, using its own shortcut, uses union-determined wages as the prevailing wage. The effect of this onerous law is to increase the cost of labor for government projects and thereby increase costs to taxpayers.

Barring other reforms, it seems clear from the analysis above that school districts would use whatever savings might result from repealing the prevailing wage law to expand their facilities projects with no real savings to taxpayers. Nevertheless, by repealing Chapter 2258 of the Texas Government Code, the legislature would not only create the potential to save state and local taxpayer money on school projects, but on highway projects, and other public works projects all over the state.

A Few Best Practices for Fiscally Responsible School Districts

In a 2002 publication of the Mackinac Center for Public Policy entitled *The Six Habits of Fiscally Responsible School Districts*,²⁵ a dozen principles for debt finance are outlined. Not all of these principles will be restated here, but it is worth considering several in the context of school facilities funding in Texas. The legislature should consider enacting these into law.

The first principle is that **long-term debt should not be used to finance current operations or to capitalize expenses**. As has been noted above, it is quite possible that Chapter 41 districts are following just the opposite of this recommended practice. They certainly have an incentive to do so. Although some current operations expenditures can be easily justified as capital expenditures, computers, for example, should not be paid out with bonds that mature over decades. This same practice violates the second principle in the Mackinac publication which is that **long-term debt should be used only for capital projects that cannot be financed from current revenue sources**.

Due to Michigan law, **total district indebtedness should not exceed 15 percent of the district taxable valuation for any given year**. Perhaps Texas should consider such a limitation. In Texas, one school district (Boles ISD in Hunt county) has indebtedness that represents almost 67 percent of its assessed valuation. Eleven Texas school districts exceed the 15 percent ratio.

Another recommendation in the Mackinac publication is to **avoid capital leases, certificates of participation, or similar instruments for the acquisition or use of**

facilities or equipment. As has already been seen, it is common practice for school districts in the state to obligate themselves in this way. No long-term debt obligation should be allowed without a vote of the local taxpayers who must fund such an obligation.

What is perhaps the most violated principle listed in the Mackinac paper is that **public funds, property and resources should not be used, directly or indirectly, to influence the outcome of ballot questions.** School districts regularly publish what can best be described as promotional literature for bond issues. In these publications, past bond issues are described and praised, usually in the form of an interview of a district trustee. The superintendent usually presents a case for the need for new facilities, also often in the form of an interview. No countervailing point of view is presented in these publications. Although there is never a statement specifically urging anyone to vote for a bond issue, there is always a statement simply urging everyone to vote.

Conclusion

School facilities funding should be a key component of public school finance reform. Today almost 70 percent of school districts are in bond debt and districts owe close to \$50 billion. Over the past decade, the state has assumed greater responsibility for facilities debt incurred by local school districts, and today, the state helps districts pay off debt and provides the Permanent School Fund as a guarantee for additional debt. In effect, local facilities debt has become state debt and the consequences of local district facilities decisions are passed out of the district to the pockets of every taxpayer in the state. Most taxpayers have little ability to participate in the financial decisions or to hold the districts accountable.

State subsidies for school district facilities have sparked a spending boom. As debt mounts, school districts channel funds away from student instruction and mortgage the academic future of children for decades.

A statistical analysis of school district debt reveals that districts often go into debt simply because they can. There is no good reason for a district to be in more debt simply because its property wealth is greater. Yet, that is the case. It is also difficult to understand why district size and district growth lead to such large increases in debt as indicated by the statistical analysis.

The existence of the Instructional Facilities Allotment clearly encourages greater debt. The current school finance system also clearly encourages wealthy districts to finance more expenditures with debt.

Perhaps every penny of school district debt is justified. There is nothing that has been presented here that directly disputes such a claim. However, there is no evidence to support such a claim, either. The fact is that at the state level there is no real oversight of facilities spending and debt. The legislature appears eager to funnel the funds but not so ready to get the information it needs to protect taxpayers.

School finance reform offers an ideal opportunity for state policymakers to address the growing problem of school district facilities debt. Growing state responsibility for local financial decisions and mounting debt urgently argues that strong standards and accountability must be established. Perverse incentives in the current system must be eliminated. Districts should be encouraged to make more efficient use of resources, and to guide resources directly to instruction rather than to edifices. With a focus on incentives and obtaining relevant information, the legislature can make better, more informed decisions regarding facilities funding in the future.

Endnotes

- ¹ Texas Bond Review Board, *FY2002 Texas Independent School District Debt Outstanding*, Excel spreadsheet, <http://www.brb.state.tx.us/brbpages/Pub/local/02ISDvaMOrvLP.xls>.
- ² “Iraq’s Shrinking Debt,” Review & Outlook, *Wall Street Journal*, January 23, 2004. The figure includes reparations owed to Kuwait for the first Iraq war.
- ³ See Texas Education Code, Section 41.003 for a list of all options.
- ⁴ For one example from 1998, see “Billions Needed For Texas Schools, Says A&M Prof,” <http://www.tamu.edu/univrel/aggiedaily/news/stories/archive/100598-1.html>. See also, Texas Comptroller of Public Accounts, *Current and Future Facilities Needs of Texas Public School Districts*, ©1998, internet document, http://www.window.state.tx.us/tpr/tspr/facilities/exec_sum.htm.
- ⁵ National Education Association, “School Modernization Facts: Texas,” October 11, 2002, <http://www.nea.org/lac/modfacts/TXfacts.html>.
- ⁶ *Edgewood I.S.D., et.al. v. Meno et. al.*, 917 S.W.2d 717 (Tex. 1995). Justice Cornyn states that “the challenge to the school finance law based on inadequate provision for facilities fails only because of an evidentiary void,” and that, “These components of an efficient system—instruction and facilities—are inseparable.” Justice Cornyn goes on to point out, however, that “Debt service taxes in the property-poor districts, however, generate far more revenue than required for actual debt service allocations” and that “the undisputed evidence is that all districts can presently meet their operations and facilities needs with funding provided by Tier 2.” While the court is clearly concerned about facilities funding as well as operations funding, the system for funding facilities was considered adequate to provide for a general diffusion of knowledge given the available evidence.
- ⁷ Texas Comptroller of Public Accounts, *Current and Future Facilities Needs of Texas Public School Districts*, ©1998, internet document, http://www.window.state.tx.us/tpr/tspr/facilities/exec_sum.htm.
- ⁸ Texas Education Agency, *School Law Bulletin, 2004*, West, 2004, p. 428. Texas Education Code, Section 46.001.
- ⁹ General Appropriations Act, 1998-1999 Biennium, State of Texas, http://www.lbb.state.tx.us/The_LBB/Access/AppBills_LBEs.htm#Archive.
- ¹⁰ Texas Education Agency, *IFA State & Local Shares, 2002-2003*, Excel Spreadsheet, http://www.tea.state.tx.us/school.finance/facilities/ifa/shares03_r1.xls.
- ¹¹ Texas Education Agency, *School Law Bulletin, 2004*, West, 2004, pp. 365 & 434. For the Existing Debt Allotment, see Texas Education Code, Section 46.031. For the New Instructional Facilities Allotment, see Texas Education Code, Section 42.158.
- ¹² Texas Education Agency, Excel Spreadsheet, http://www.tea.state.tx.us/school.finance/funding/eda_pmts_0203.xls.
- ¹³ Texas Education Code, Section 46.034(d).
- ¹⁴ Texas Education Code, Section 42.158.
- ¹⁵ Alwin, Lawrence F., *An Audit Report on Certification of the Permanent School Fund’s Bond Guarantee Program*, SAO Report No. 03-032, State Auditor’s Office, April 28, 2003.
- ¹⁶ Adler, Karen, “New Schools Offer Economics Lesson,” *San Antonio Express News*, Metro Edition, October 19, 2003, pp. 1A, 18A.
- ¹⁷ “Most Expensive Housing Markets: See How Yours Stacks Up,” *CNNmoney*, website, October 24, 2003, http://money.cnn.com/pf/features/lists/hpci_data/index.html, author’s calculation.
- ¹⁸ Texas Education Code, Section 46.008.
- ¹⁹ Texas Administrative Code, Title 19, Sections 61.1033 and 61.1039.
- ²⁰ Texas Bond Review Board, *FY2002 Texas Independent School District Debt Outstanding*, Excel spreadsheet, <http://www.brb.state.tx.us/brbpages/Pub/local/02ISDvaMOrvLP.xls>.
- ²¹ Digest of Education Statistics, 2002, U.S. Department of Education, Office of Education Research and Improvement, Washington DC, Table 93.- Revenues and expenditures of public school districts enrolling more than 15,000 students, by state: 1997-98.
- ²² There is also the reluctance of households to place their children in central city public schools due to real or perceived educational performance deficiencies.
- ²³ Texas Constitution, Article 7, Section 1.

²⁴ Guhse, David, *Innovative and Workable Ideas for Building Schools: Public/Private Partnerships: A New Way to Fund and Build Schools*, The Thomas Jefferson Institute for Public Policy, Springfield, VA, October 2001.

²⁵ Johnson, Kirk A., and Elizabeth H. Moser, *The Six Habits of Fiscally Responsible Public School Districts*, Mackinac Center for Public Policy, Midland, MI, December 2002.

Appendix

School Districts with More than 15,000 Students: Nominal Analysis Quartiles Based Upon Growth In Student Population 1995-1998

Subject	Quartile	1	2	3	4	All
		Fastest Growing	Faster Growing	Slower Growing	Slowest Growing	
	Cases	106	107	107	106	426
Growth In Pupils	Mean	15.20%	7.40%	3.80%	-1.20%	6.30%
	High	71.00%	9.40%	5.40%	2.00%	71.00%
	Low	9.50%	5.40%	2.10%	-6.40%	-6.40%
1998 Revenue Distribution	Federal	4.90%	5.80%	7.20%	8.80%	6.70%
	State	51.60%	49.80%	55.80%	50.30%	51.90%
	Local	43.50%	44.40%	37.00%	40.80%	41.40%
	Total	100.00%	100.00%	100.00%	100.00%	100.00%
1995 Revenue Distribution	Federal	5.00%	5.90%	7.20%	8.70%	6.80%
	State	47.30%	46.60%	54.10%	49.20%	49.80%
	Local	47.70%	47.40%	38.70%	42.10%	43.40%
	Total	100.00%	100.00%	100.00%	100.00%	100.00%
Percentage Point Change	Federal	-0.10%	-0.20%	0.00%	0.10%	-0.10%
	State	4.30%	3.10%	1.70%	1.20%	2.10%
	Local	-4.30%	-3.00%	-1.60%	-1.30%	-2.00%
1998 Expenditures/Pupil	Total	\$6,477	\$6,616	\$6,463	\$6,616	\$6,543
	Current	\$5,288	\$5,593	\$5,605	\$5,976	\$5,615
	Instructional	\$3,274	\$3,432	\$3,491	\$3,620	\$3,455
	Other Current	\$2,014	\$2,160	\$2,113	\$2,356	\$2,161
	Capital & Interest	\$1,189	\$1,023	\$858	\$640	\$928
1995 Expenditures/Pupil 1998\$	Total	\$5,938	\$6,116	\$5,858	\$6,054	\$5,991
	Current	\$5,001	\$5,385	\$5,327	\$5,627	\$5,335
	Instructional	\$3,056	\$3,276	\$3,283	\$3,392	\$3,252
	Other Current	\$1,944	\$2,109	\$2,044	\$2,234	\$2,083
	Capital & Interest	\$938	\$730	\$531	\$427	\$656
Change	Total	\$538	\$500	\$605	\$562	\$551
	Current	\$287	\$207	\$278	\$350	\$280
	Instructional	\$218	\$156	\$209	\$228	\$203
	Other Current	\$69	\$51	\$69	\$121	\$78
	Capital & Interest	\$252	\$293	\$327	\$212	\$271
Percentage Change 1998\$	Total	9.10%	8.20%	10.30%	9.30%	9.20%
	Current	5.70%	3.80%	5.20%	6.20%	5.30%
	Instructional	7.10%	4.80%	6.40%	6.70%	6.20%
	Other Current	3.60%	2.40%	3.40%	5.40%	3.70%
	Capital & Interest	26.80%	40.10%	61.50%	49.70%	41.30%
1998 Revenues/Pupil	Total	\$6,444	\$6,688	\$6,564	\$6,789	\$6,621
	Federal	\$321	\$389	\$469	\$595	\$443
	State	\$3,310	\$3,291	\$3,664	\$3,404	\$3,418
	Local	\$2,813	\$3,007	\$2,431	\$2,790	\$2,760
	State & Local	\$6,123	\$6,299	\$6,096	\$6,194	\$6,178
1995 Revenues/Pupil 1998\$	Total	\$5,923	\$6,273	\$6,046	\$6,272	\$6,129
	Federal	\$296	\$372	\$436	\$546	\$413
	State	\$2,800	\$2,926	\$3,273	\$3,084	\$3,021
	Local	\$2,826	\$2,975	\$2,337	\$2,643	\$2,695
	State & Local	\$5,627	\$5,901	\$5,610	\$5,726	\$5,716
Change	Total	\$521	\$415	\$518	\$516	\$492
	Federal	\$25	\$17	\$33	\$49	\$31
	State	\$510	\$366	\$391	\$320	\$396
	Local	(\$13)	\$33	\$94	\$148	\$65
	State & Local	\$496	\$398	\$485	\$468	\$462
Change In %	Total	8.80%	6.60%	8.60%	8.20%	8.00%
	Federal	8.30%	4.40%	7.50%	8.90%	7.40%
	State	18.20%	12.50%	11.90%	10.40%	13.10%
	Local	-0.50%	1.10%	4.00%	5.60%	2.40%
	State & Local	8.80%	6.80%	8.60%	8.20%	8.10%

Data from US Department of Education. Some items calculated by author.



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