SCHOOL DAYS AND LEGAL MAZE: CONSTITUTIONAL CHALLENGES TO PUBLIC SCHOOL FINANCE IN TEXAS

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On May 29, 2003, a majority of the Texas Supreme Court (seven justices, with another concurring in the judgment), in West Orange-Cove Consolidated I.S.D v. Alanis, 207 S.W. 3d 558 (Tex. 2003), reversed lower court decisions dismissing a claim brought by four plaintiff school districts, and remanded the case to the trial court for further proceedings. The majority ruled only that the allegations in the plaintiffs' petition were sufficient to state a claim that the state's system of funding public education in effect forced the districts to impose a state ad valorem tax, which is barred by the Texas Constitution. The decision did not rule on the constitutionality of the state's current system of public schools, instead remanding this issue for consideration in the trial court.

The issue concerned Article VII, Section 1, of the Texas Constitution, which provides that:

> A general diffusion of knowledge being essential to the preservation of the liberties and rights of the people, it shall be the duty of the legislature of the State to establish and make suitable provision for the support and maintenance of an efficient system of free public schools.

In 1989, in Edgewood Independent School District v. Kirby, 777 S.W.2d 391 (Tex. 1989), the Texas Supreme Court ruled that the state's public school finance system, with its heavy dependence on local property taxes, violated this provision of the state constitution. The system, held the court, resulted in wide disparities in the quality of public education between poorer and wealthier school districts. The Texas Legislature responded with legislation, which was subsequently challenged, resulting in a series of cases known as the Edgewood cases. In 1995, in Edgewood Independent School District v. Meno (Edgewood IV), 893 S.W.2d 450 (Tex. 1995), the court finally ruled that the revised system implemented by the Texas Legislature met constitutional muster. However, the court in that case warned that the new system, because of remaining funding disparities, could again become unconstitutional.

The warning in Edgewood IV concerned Article VIII, Section 1-e, of the Texas Constitution, which prohibits the levying of state ad valorem taxes. The funding system challenged in Edgewood IV created a two-tiered system:

- Tier 1 guarantees sufficient financing for all school districts to provide a basic program of education that meets accreditation and other legal standards. Under this tier, a school district that cannot generate revenue equal to a "basic allotment" through the minimum tax rate receives state funds to make up the difference.

- Tier 2 provides for partially state-supported local supplementation. Under this tier, for each penny a district raises the tax rate above the minimum, the state guarantees a certain yield per weighted student. The tax rate for maintenance and operations continues to be capped at $1.50, subject to various adjustments and exceptions. There is also some state funding for facilities, sometimes referred to as Tier 3 in the system.

The court in Edgewood IV ruled that this system did not impose an unconstitutional state ad valorem tax, because while it did set minimum and maximum tax rates, districts and their voters still had the discretion within these parameters to choose the tax rate and control the distribution of the proceeds. However, the court warned that if the cost of education rose to the point that a district was forced to tax at the maximum tax allowed under the bill just to meet minimum accreditation standards, the tax would in effect become an unconstitutional state-mandated ad valorem tax.

In West Orange-Cove Consolidated I.S.D, four school districts alleged that the court's warning had been confirmed, because they and other districts were now forced to tax at maximum rates set by statute in order to educate their students. These local taxes, they alleged, had now effectively become an unconstitutional state-mandated ad valorem tax. The district court dismissed the plaintiffs' complaint and the appellate court confirmed.

The state had argued in part that the plaintiffs' suit was not ripe because the system did not require all districts throughout the state to tax at the rate of $1.50, and therefore did not result in a statewide ad valorem tax. The majority rejected this argument, stating that the constitution prohibits state ad valorem taxes upon any property within this state. The issue, the majority said, is not the pervasiveness of the tax, but the state's control over it. An illegal state ad valorem tax is a tax imposed by the state, either directly or indirectly. Therefore, the majority asserted, a single district could make a claim that it is unconstitutionally constrained by the state to tax at a particular rate.

The state made four other arguments which were rejected by the majority:

- The state asserted that the duty to provide an adequate public education belongs to the legislature, not local school districts. School districts, the state claimed, are not forced to tax at any rate, but instead choose to tax and educate at desired levels. The state is only encouraging certain choices, not compelling them. The majority said that the state was in effect arguing that nothing short of virtually absolute state control of ad valorem taxation violates the constitution. The constitutional prohibition, declared the majority, is violated whenever state control denies a taxing authority meaningful discretion. The legislature has a duty under the constitution to make suitable provision for a general diffusion of knowledge through free public schools. As long as the legislature establishes a suitable regime that provides for a general diffusion of knowledge, the legislature may decide whether the regime should be administered by a state agency, by the districts themselves, or by any other means. In fact, the legislature, through the Education Code, sets school accreditation standards and imposes sanctions for noncompliance. These provisions require school districts to provide an adequate education, and leave no meaningful discretion for districts to do otherwise. The majority reiterated its view that the current system can effectively deprive school districts of meaningful discretion and force them to tax at maximum rates.

- The state argued that the only requirement of school districts is that they provide an accredited education as defined by the legislature, and that the plaintiffs cannot allege in good faith that any district is forced to tax at the maximum rate just to meet this

requirement. On the contrary, the state asserted, districts taxing at maximum rates do so to provide enhanced educational opportunities and not merely to maintain accreditation. The majority rejected this argument, stating that accreditation standards are not the only requirements the state imposes on school districts. The state has chosen to rely heavily on school districts to discharge the duty to provide "a general diffusion of knowledge essential to the preservation of the liberties and rights of the people." The public school system the legislature has established, the majority held, requires that school districts provide both an accredited education and a general diffusion of knowledge. Because both requirements are binding on the districts, if a district is being forced to tax at a maximum rate in order to meet accreditation standards or to provide a general diffusion of knowledge, this in effect becomes an unconstitutional state ad valorem tax.

- The legislature has granted a partial homestead exemption from school district taxation, which a district may increase up to a certain amount at its option. The state argued that no school district that has opted for an increased homestead exemption can allege that it is forced to tax at maximum rates because it has the meaningful discretion to deny the increased exemption and tax at a lower rate. The majority disagreed, stating that to obtain dismissal of the plaintiffs' action based solely on the pleadings, the state must establish that the mere existence of local-option exemptions precludes as a matter of law the allegation that school districts are forced to tax at maximum rates. The state, the majority held, has not met this burden because the plaintiffs may be able to show that even without granting additional homestead exemptions, they could not provide an accredited education or a general diffusion of knowledge. Also, the majority noted, while school districts have discretion whether to increase homestead exemptions, it is far from obvious that this discretion is meaningful. By authorizing local-option homestead exemptions, knowing that some constituencies will insist on them, the legislature may actually have increased the pressure on school districts to tax at maximum rates. In any event, the majority ruled, the plaintiffs are entitled to attempt to show that homestead exemptions do not afford them meaningful discretion.

- The state argued that the plaintiffs cannot allege a violation of the constitution unless they tax at the applicable absolute maximum rate, not merely near that rate. The majority rejected this argument, responding that the constitutional issue remains the extent of the state's control. A district taxing a few cents below the maximum rate may no longer be able to provide an accredited education or a general diffusion of knowledge even by raising the rate to the maximum, and the majority held the district should not be forced to raise the rate to the maximum just to prove the point.

THE EDGEWOOD CASES: A BRIEF HISTORY

EDGEWOOD I:
EDGEWOOD INDEPENDENT SCHOOL DISTRICT V. KIRBY
777 S.W.2d 391 (Tex. 1989)

SUMMARY

The 1989 Edgewood ISD v. Kirby (Edgewood I) focused on Article VII, Section 1, of the Texas Constitution, which provides that:

> A general diffusion of knowledge being essential to the preservation of the liberties and rights of the people, it shall be the duty of the legislature of the State to establish and make suitable provision for the support and maintenance of an efficient system of free public schools.

The Texas Supreme Court held that the school financing system, in which school districts provided 50 percent of public school revenues through local ad valorem and property taxes, resulted in vast discrepancies in school funding. Districts in property-poor areas had to impose higher property taxes, yet received smaller revenues, while wealthier districts could impose lower taxes and still obtain substantially higher revenues. The court ruled that under the state constitution, the legislature must establish and provide for an efficient system of public schools to diffuse general knowledge. The court found that the school finance system, with its vast disparities between school districts, was efficient neither financially nor in the general diffusion of knowledge, and therefore violated the Texas Constitution. However, the court declined to instruct the legislature as to what it must enact or order it to raise taxes; the legislature, stated the court, had the constitutional mandate to create an efficient system.

The court asserted that while the state's recent efforts to increase its contributions to the system might reduce some of the disparities, such efforts failed to reform the system itself and make it more efficient. While efficiency did not require a per capita distribution, the court ruled that districts must have substantially equal access to similar revenues per student at similar levels of tax effort, and children in poor districts and wealthy districts must be afforded a substantially equal opportunity to have access to educational funds. The court also rejected the argument that reforming school finance would eliminate local control, asserting that a more efficient system would allow for more local control, as poorer school districts would have access to economic resources not now available.

FACTS

The Edgewood Independent School District, joined by 67 other school districts and numerous students and their parents, filed suit alleging that the Texas public school finance system violated the state constitution. The trial court sided with the plaintiffs, but the appellate court reversed. The supreme court affirmed the trial court's decision, but modified the judgment, staying the lower court's injunction until May 1, 1990.

The state financed the education of approximately three million public school students through a combination of state and local revenue, providing about 42 percent of total education costs (school districts provided about 50 percent, the remainder coming from other sources, such as federal funds). The wide variations in the amount of taxable property wealth in each school district affected a school district's ability to raise revenue by increasing property taxes, because while wealthy districts could tax low and spend high, property-poor districts had to tax high to obtain relatively little revenue. The high tax rates in property-poor districts, stated the court, trap poor districts in poverty, discouraging new industry and development that would increase the tax base. The court found that the amount of money spent on each student had a significant impact on educational opportunities. Wealthier districts could attract and retain better teachers and administrators, offer a more extensive curricula and lower teacher-student ratios, provide programs to increase parental involvement and lower the drop-out rate, and finance better technical and educational facilities, while poorer districts could only offer a limited curricula; many poor districts were unable even to meet state-mandated standards for maximum class size.

EDGEWOOD II:
EDGEWOOD INDEPENDENT SCHOOL DISTRICT V. KIRBY
804 S.W.2d 491 (Tex. 1991)

SUMMARY

The injunction affirmed and modified by the supreme court in Edgewood I stopped the state from funding the public school system after September 1, 1989, unless the legislature repaired the constitutional defects in the system by that date. The district court extended the deadline. On June 7, 1990, S.B. 1 became law. The new legislation was challenged and, while the district court held that the system was still unconstitutional, it vacated the injunction. The supreme court noted that essentially S.B. 1 left intact the same funding system, with the same deficiencies, held to be unconstitutional by the court in Edgewood I:

- It did not change the basic system in which roughly half of all education funds came from local taxes, resulting in revenue disparities between rich and poor school districts;
- It failed to equalize access to funds among all districts, as it excluded the wealthiest school districts from its funding formula;
- To be efficient, a funding system so dependent on local property taxes must draw revenue from all property at a substantially similar rate. The system still insulated concentrated areas of property wealth from being taxed to support public schools, resulting in higher tax burdens on property holders in property-poor districts; and
- Vast inefficiencies remained in the system, resulting in duplicative administrative costs.

The court held that the public school finance system still continued to violate the efficiency standard set up by Article VII, Section 1. It overruled the lower court's judgment vacating the injunction, staying the effect of the injunction until April 1, 1991.

The court suggested that altering school district boundaries could make the system more efficient. It also discussed the consolidation of the tax base as another approach to efficiency. The lower court had rejected this approach as barred by the state constitution, based on the earlier supreme court decision in Love v. City of Dallas, 40 S.W.2d 20 (1931), in which the high court ruled that Article VII contemplated that school districts would levy taxes for the education of students within the districts. The supreme court held that the lower court had misinterpreted Love, ruling that the constitution did not prohibit the tax base consolidation and the creation of school districts along county lines for the purpose of collecting tax revenue and distributing it to other districts within their boundaries.

FACTS

Under S.B. 1, there was to be a wide variety of biennial studies to detect deviations in funding between school districts; using this information, the state could biennially adjust state funding to narrow such gaps. This bill also imposed a two-tiered finance structure known as the Foundation School Program (FSP):

- The first tier was a basic allotment designed to enable all school districts to provide a basic education. Each district taxing itself at or above a minimum level was guaranteed a base level of funding composed of state and local revenue per student in average daily attendance (because some students, such as those needing bilingual or special education, are more expensive to educate, most of the revenue was to be distributed according to formulas assigning "weights" to students with different needs).

- The second tier was a guaranteed yield or equalized enrichment tier. At this tier, all districts would receive a guaranteed revenue per weighted student for each cent of local tax effort above the first tier's level. The state would fund the difference between the guaranteed revenue and the amount each cent of local tax revenue generated. If a district was so wealthy that each cent of tax effort generated more than the guaranteed revenue per weighted student, that district would receive no state revenue.

The plaintiffs returned to the district court, arguing that the finance system was still unconstitutional and seeking to enforce the original injunction. The district court agreed that the system was still unconstitutional, but vacated the injunction and refused to hear any requests for further relief until it became apparent that the legislature would not implement a constitutional school finance system by September 1, 1991. The plaintiffs appealed, as did the state, which challenged the finding that the system was still unconstitutional.

MOTION FOR REHEARING

In a motion for rehearing, certain plaintiffs asked the supreme court to expressly overrule Love and allow statewide recapture of local ad valorem revenues for the purposes of equalizing school revenues. Chief Justice Phillips declined to overrule Love. In Love, the court had held that the City of Dallas could not be compelled to educate students residing outside of the city's school districts, on the grounds that the state constitution only contemplated that such districts would be organized and taxes levied for the education of students within those districts. Judge Phillips stated that while under the Texas Constitution the legislature may authorize local school districts to levy additional ad valorem taxes, those taxes are expressly reserved for the maintenance of public schools within those districts. Therefore, local tax revenue could not be recaptured by the state.

Four justices, while supporting the decision to deny the motion, challenged the Chief Justice's decision to write an opinion, asserting that it was not a true opinion generated in response to the question before the court, but was an unwarranted advisory opinion.

EDGEWOOD III:
CARROLLTON-FARMERS BRANCH INDEPENDENT SCHOOL DISTRICT V. EDGEWOOD INDEPENDENT SCHOOL DISTRICT
826 S.W.2d 489 (Tex. 1992)

SUMMARY

S.B. 351, enacted by the legislature in 1991 in response to Edgewood II, created a two-tier system for equalization of the state's contributions to the school finance system. The bill created county education districts (CEDs), whose only purpose was to levy and collect ad valorem taxes at a rate mandated by the state and distribute the proceeds as prescribed by the state. The court ruled that S.B. 351 was unconstitutional on two grounds:

- It violated Article VIII, Section 1-e, of the Texas Constitution, which prohibits the levying of state ad valorem taxes upon property within Texas. Because the state mandated the levying of ad valorem taxes by the CEDs, set the rate, and controlled the distribution of the proceeds, the court held that the tax was in effect a state tax; and

- The ad valorem tax was levied without prior voter approval in violation of the state constitution, which requires that the electorate approve any such tax.

The court did find that the creation of the CEDs was constitutional, as the constitution grants the legislature the power to create and regulate school districts. The constitutional bar against local or special laws did not apply because the bill affected the entire state.

The court declined to apply its decision retroactively, as this would disrupt the education of Texas' children, instead giving the state until June 1, 1993, to remedy the system.

FACTS

S.B. 351 implemented a two-tier program:

- The first tier entitled each school district to a basic per student allotment for each student. This basic allotment, which was intended to provide sufficient funding to allow all districts to provide a basic education, was subject to adjustment and supplementation for matters ranging from a district's local cost of education to special education. Each district was to raise an assigned local share through CEDs, which would levy, collect, and distribute property taxes, but perform no educational duties. This local share was the product of a tax rate specified by statute and the taxable value of property within the CEDs. The CEDs could not refuse to levy the mandated tax. The Commissioner of Education (commissioner) was to notify each CED of the amount due each component school district and set the schedule for distribution.

- The second tier provided all districts with substantially equal access to additional funds by guaranteeing each district a specified amount per student for each cent of tax effort over that already assigned to the CED. This state guarantee extended only to a set amount of tax effort, and the bill also capped each district's "enrichment and facilities tax rate" (DTR). If a district's local revenue exceeded the set amount per student for each cent of the DTR, the district received nothing more from the state.

Numerous school districts and private citizens asserted that S.B. 351 violated the Texas Constitution by:

- levying a state ad valorem tax in violation of Article VIII, Section 1-e;

- levying this tax without voter approval; and

- creating the CEDs.

CONCURRENCE AND DISSENT

Justices Cornyn and Gammage concurred with the majority opinion that S.B. 351 was unconstitutional and the decision was properly applied prospectively. However, Justice Cornyn declined to join that portion of the decision delaying its effect until 1993. Similarly, Justice Gammage stated that he would withhold the effect of the decision only until June 1, 1992. Justices Doggett and Mauzy dissented.

EDGEWOOD IV:
EDGEWOOD INDEPENDENT SCHOOL DISTRICT V. MENO
893 S.W.2d 450 (Tex. 1995)

SUMMARY

S.B. 7, enacted in 1993 by the 73rd Legislature, created a two-tiered system. School districts implementing a statutory tax rate were guaranteed a basic allotment to meet state accreditation standards, as well as additional funds for tax efforts exceeding the statutory minimum, up to a set cap. A cap was imposed on a district's taxable property at a level of $280,000 per student. Any district exceeding this $280,000 cap could elect one of five options to bring its taxable property within this cap. If a district failed to exercise one of these options, the commissioner was to detach property from the district and annex it to another. If this failed to reduce the district's taxable property, the commissioner was to consolidate the district with another district or districts.

Numerous school districts, both rich and poor, and individuals brought a wide-range of challenges against the new legislation. Most of the challenges brought by the property-poor districts asserted that the system was still unconstitutionally inefficient, with significant revenue and tax disparities between property-poor and property-rich districts.

Five justices held that S.B. 7 was constitutional. The court stated that under the state constitution a public school finance system must be efficient both financially and in providing for the general diffusion of knowledge. An efficient system does not require equality of access to revenue at all levels or preclude school districts from generating local taxes to supplement an efficient system, as long as districts have substantially equal access to a level of funding that would achieve a general diffusion of knowledge. The court found that S.B. 7 achieved this constitutional level of efficiency by providing students in both property-poor and property-rich school districts with substantially equal access to a level of funds necessary to provide for an education meeting the state's accreditation standards. The evidence, held the court, established that all districts could generate the funds necessary for the general diffusion of knowledge, although property-poor districts had to do so at a slightly higher rate, and S.B. 7 dramatically reduced the disparity in tax rates for 85 percent of the students in the state. The remaining tax and revenue disparities between the poor and wealthy districts were not so great as to render S.B. 7 unconstitutional.

Many of the challenges brought by property-rich districts concerned the cap on a district's taxable property and the procedures for reducing the wealth of a district that exceeded this cap, and these all were rejected by the court. Also, the court ruled that S.B. 7 did not impose an unconstitutional state ad valorem tax, because while it did set minimum and maximum tax rates, districts and their voters still had the discretion within these parameters to chose the tax rate and control the distribution of the proceeds.

However, the decision carried several caveats:

- While districts might be able to generate revenues to supplement an efficient system, supplementation cannot become so great that it destroys the efficiency of the system;

- If the cost of education rose to the point that a district was forced to tax at the maximum tax allowed under the bill just to meet minimum accreditation standards, the tax would in effect become an unconstitutional state-mandated ad valorem tax; and

- Because the bill lacked a separate component for funding school facilities, if educational costs rose to the point that a school district was unable to meet its operations and facilities needs within the program established by S.B. 7, the state will once again have failed to fulfill its constitutional obligation to provide an efficient education system.

Another challenge was that the present system, by failing to provide for vouchers to private schools, did not provide a constitutionally suitable and efficient education. The court declined to order vouchers, reiterating that the constitution gives the legislature the primary responsibility to decide how best to achieve an efficient system. The court also ruled on the abolishing of the CEDs and the redistribution of CEDs funds and taxes.

FACTS

Following Edgewood III, the Texas Legislature proposed a constitutional amendment authorizing the creation of CEDs with limited authority to levy, collect, and distribute ad valorem taxes. When the electorate rejected this amendment, the legislature enacted S.B. 7. This bill created a two-tiered system to school finance system:

- The first tier guaranteed sufficient funding for school districts to provide a basic education program meeting accreditation and other legal standards. For each student in average daily attendance, a district was entitled to a basic $2,300 allotment (students were "weighted," with allotments being subject to adjustment to reflect actual education costs). To take part, a district had to raise its local share of funding, defined as the amount produced when an effective tax rate of $0.86 per $100 valuation was applied to the taxable value of property within the district for the prior tax year. If the district could not produce its allotment by such tax rate, the state funded the difference.

- The second tier gave each district an opportunity to supplement the basic level of education. For every cent of additional tax effort over the first tier's $0.86, the state guaranteed a yield of $20.55 per weighted student. To the extent that an additional cent of tax effort failed to yield this amount from the district's tax base, the state would make up the difference. However this guaranteed yield was capped, in that no second tier funds were available for effective tax rates exceeding $1.50.

S.B. 7 also imposed a cap on a district's taxable property at a level of $280,000 per student, which was phased in over three years. Any district exceeding this $280,000 cap could elect one of five options to bring its taxable property within this cap:

- consolidation with another district;

- detachment of territory;

- purchase of average daily attendance credit;
- contracting for the education of nonresident students; or
- tax base consolidation with another district.

If a district failed to successfully exercise one of these options, the commissioner was to detach district property and annex it to another. If this failed to reduce the district's taxable property, the commissioner would consolidate the district with another district or districts.

The legislation also established a system of student assessment and school district accreditation. Districts which chronically failed to meet accreditation standards were subject to penalties, including dissolution and annexation to another district.

DISSENT

Four of the justices dissented, arguing that S.B. 7 was indeed unconstitutional:

- Although Justice Enoch agreed that S.B. 7 was constitutionally efficient, he asserted that the state, by relying on local property taxes to fund public schools, violated its constitutional duty to make suitable provision for public schools. He also argued that the state's reliance on local taxes imposed an unconstitutional state ad valorem tax;
- Justice Hecht, joined by Justice Owen, agreed that S.B. 7 was an unconstitutional state ad valorem tax. He also asserted that the wealth-sharing provisions violated the constitutional provision, as construed by the court in Love, which restricts the use of a school district's tax revenues to the schools within that district; and
- Justice Spector argued that the majority had changed the test for efficiency under Edgewood I, in which the court held that districts must have substantially equal access to similar revenues per pupil at similar levels of tax effort. She asserted that the majority opinion now recast this standard, redefining the state's duty as providing districts with substantially equal access to revenue as necessary for a general diffusion of knowledge. The state, she argued, could set accreditation standards so low that any school district, no matter how poor, would be able to meet them. Poorer districts would have no practical means of improvement, as the state would have to supply only the most minimal level of funding, yet wealthier districts would still have access to enormous revenues at only the slightest marginal tax effort. She also attacked the fact that poorer school districts still had to impose higher tax rates to meet accreditation requirements. The failure to include any provisions for facilities exacerbated this unfairness, as poor districts with limited ability to raise revenues would have to choose between funding current operations or paying for capital improvements.

SCHOOL FINANCE DECISIONS IN OTHER STATES

In Edgewood I, the court noted that courts in Arkansas, California, Connecticut, Kentucky, Montana, New Jersey, Washington, West Virginia, and Wyoming, which all had finance systems similar to that in Texas, had held that those systems were unconstitutional, for varying reasons. Since then, almost every state has faced legal challenges to its means of financing its public schools. State supreme courts in Alaska, Alabama, Arizona, Idaho, Kansas, Maryland, Massachusetts, New Hampshire, Ohio, South Carolina, Tennessee, and Vermont have upheld challenges to their states' school finance systems on constitutional grounds or have found that the state constitution required the legislature to provide some form of an adequate education. In 2002, such challenges were filed in Colorado and Iowa.