CHAPTER 6

OPTIONS FOR FUNDING FACILITIES

All interested parties agree that the state must become involved in a significant manner in the long-term financing of capital outlay and construction funding for school facilities.

Critical choices must be made in establishing a state government role in what has previously been a local government function. Six issues or elements have been identified for the purposes of this report to characterize the role the state will play, and each of these six areas require definition to fully describe the state role.

The six elements identified for this analysis are:

- The level of state control and influence over school district decisions and activities
- The level of local flexibility within and beyond a state support system
- The level of equity or fiscal neutrality to be met by the entire system of support
- The types of activities (debt service, repair, renovation, new construction) to be supported
- The data required to make decisions at the state level
- The impact on the Texas Education Agency and other state entities including staffing and administrative requirements for the state authority

There are a variety of alternatives available to channel funding for school facilities from the state to districts. Three basic options for meeting long-term needs include (1) a per capita allotment, (2) a guaranteed yield program, or (3) project or need based funding. In addition to these long term programs, complimentary programs can be used either to meet emergency needs, or to encourage new construction to improve school district efficiency.

As these basic options are examined in this chapter, the focus will be on how these options might address the needs which have been identified, and what consequences will likely result from a state program of support. Alternatives for the six elements characterizing the state's role under each option will be examined. A table which provides a summary of each financing option and its various attributes is provided at the end of this chapter.

Because school districts expend about $1 billion for debt each year along with $1 billion for capital outlay, the cost to the state of sharing responsibility for these costs could represent several hundred million dollars of expense. It is important to consider options for raising the necessary revenues for the state's participation.

Per Capita Funding

A per capita allotment would provide a fixed dollar amount of funding per pupil in weighted average daily attendance (WADA) to each school district. This is the funding mechanism which will be used to distribute the $50 million appropriated to the agency for the emergency facilities grants during the 1992-93 school year. Of the financing options to be presented here, this one offers the least amount of state control and is the least restrictive to school districts.

Under a per capita funding program, the state would establish a funding level, such as the $150 maximum per WADA used for the emergency grant program, and flow money to districts on the basis of the student population. Such a program has many attractive features, primarily due to the simplicity of administration. Very little data is needed to grant a continuing per capita sum of money, although the state can place restrictions on uses of the funds or eligibility for receipt which would complicate the grant process. Without the restrictions of eligibility criteria or limits on the use of grants, local control and flexibility are left virtually intact.

This option is the least equalizing of the three basic options presented. Under a pure per capita program, all districts are treated equally even though their needs and ability to meet those needs may differ greatly. There are methods through which this type of program could be modified to reflect differences in district needs, including requiring districts to demonstrate that, in fact, they have a debt service obligation or construction project in process, or by wealth testing district eligibility. More eligibility requirements place additional burdens on administration, increasing the likelihood that added staff would be needed.

Even with these types of modifications, a per capita program tends to favor large districts and put small districts at a disadvantage due to the small volume of cash provided. As an example, a district with 500 students would only receive $75,000 per year from a per capita allotment of $150 per student. This sum of money is sufficient to purchase less than two classrooms.

A per capita grant program is generally best suited to a system in which the funds have few restrictions other than reservation construction or debt service. There are few incentives inherent in a pure per capita grant program which would encourage fiscal restraint on the part of school districts with relatively few needs. An advantage to the state, however, is that cost can be more reliably identified and controlled.

Guaranteed Yield Funding

It has been the recommendation of the School Facilities Advisory Committee and a previous select committee that a guaranteed yield approach be applied to financing capital outlay and debt service in the Texas schools. Under a guaranteed yield system districts would be guaranteed a minimum rate of return for each penny of debt service tax rate per pupil. A guaranteed yield tier for facilities would function in the same manner as the current guaranteed yield system for operating funds.

While a guaranteed yield system leaves most of the control over how funds are spent with the local school district, this option provides the state with more control over the types of districts which receive funding than does a per capita approach. A guaranteed yield approach enables the state to direct funds at those low wealth districts which traditionally have had difficulty in raising funds for capital outlay. Because of the implied debt burden to local taxpayers which generates guaranteed yield funding, there are some higher assurances that school administrations will be more restrained in the projects undertaken, but the state cost of the support program is to some extent controlled by local district actions.

Concern has been expressed that in spite of its name, a guaranteed yield is not a true guarantee for funding, making bond counsels somewhat hesitant to support this type of program. In its recommendations, the 1988 Select Committee on Education addressed the issue of maintaining the integrity of funds allocated for school facilities. This is done in a fairly straightforward manner by requiring districts to deposit funds generated through a guaranteed yield program to their interest and sinking fund, to be used only for the payment of debt service and the construction of new facilities.

Districts without an I&S tax rate will not be able to receive funding under this program. This program therefore is restricted to supporting only debt service needs.

There are attractive features about this financing option including the limited need for additional agency support, the high level of control which remains with the districts, and that a guaranteed yield system effectively lends itself to the criteria for equity established by the court.

Project Funding

A project funding approach is the most time consuming and administratively taxing of the options presented, and the one with the highest level of state control over state funds. This option would involve state review of each project, and funding would be provided for eligible portions of the construction. Under this option, funding could be based on pre-established standards for buildings or on state determined costs for various types of construction. State cost could be tightly controlled in the project approval process.

This option certainly increases state control of the kinds and costs of facilities which are constructed in local school districts. While the state would have more complete knowledge of how dollars for facilities are being spent, the administrative costs to the state are high due to the project review process. Administrative costs to school districts and the time to complete a project could also be lengthened by the review process. Some loss of local control should be expected, and decreased local flexibility to meet unique needs or preferences may result.

It is also unclear whether a project or needs based approach, unless it were to be wealth tested in some way, would meet the court requirement for equity. Under a project approach, districts with pending new construction or renovation needs would stand to benefit the most, but districts with outstanding debt obligations would receive no relief. Project funding could be a vehicle for targeting state funds to meet specific state-wide objectives, such as reducing portable building use.

Complementary Programs

In addition to the long-term programs presented to meet on-going district needs for funding for capital outlay and debt service, there are additional programs which can be used to meet emergency needs for facilities, or to provide incentives to districts to increase efficiency.

$50 Million Emergency Facility Grant Program

The 72nd Texas Legislature established an emergency grant program directed at helping property poor school districts meet their needs for safe buildings and adequate instructional space. Under rules adopted by the State Board of Education, school districts which qualify will receive $150 per pupil in weighted average daily attendance during the 1992-93 school year to be used for facilities repair or construction. Funds are distributed based on a formula which takes into account school district wealth, three year average tax effort, and growth in student population over a five year period.

Although the program is currently in place only for the 1992-93 school year, additional appropriations could extend the program, making it a supplementary allotment for districts with severe or emergency facility needs.

Incentive Programs for Increased Efficiency

Another option for programs which would be complementary to one of the long-term financing programs discussed above would be an incentive program for increased efficiency. Under such a program small school districts which elected to consolidate for the purpose of delivering services more efficiently could be provided with incentive funds to meet their needs for new construction.

The agency currently has an incentive program which provides districts with additional funds for up to ten years to districts which undergo consolidation. This program provides incentive aid payments to new districts with a minimum of 750 students in ADA. The amount of the aid is the difference between the new district's foundation aid and the sum of the foundation payments which would have been received had no consolidation occurred. A program for additional facilities funding could be established either as a part of the current program, or as a parallel program.

Combination Funding

Both the Select Committee on Education and the School Facilities Advisory Committee have recommended funding approaches that combine various aspects of the options presented above. The Select Committee proposed the use of both a capital depreciation grant for debt service along with an equalized funding program for new construction. Likewise, the School Facilities Advisory Committee has proposed both an interim, grant-based, financing program as well as a guaranteed yield program for meeting long-term needs.

None of the options presented above is intended to be mutually exclusive. By using two or more of these financing programs in combination, it would be possible to address a wide variety of needs at all levels of district wealth. Districts with emergency needs could obtain funding on an as needed basis through a grant program, while districts with long-term obligations for new construction and debt service would obtain funds through a facilities guaranteed yield as a part of the foundation program.

Sources of Revenue

State funding of grants to school districts for capital outlay and debt service will require substantial appropriations, probably increasing the overall appropriations for public education. As with any source of funds that is not the result of increased state revenues, additional funds directed towards school facilities must mean a decrease in funding for some other item.

Guaranteed Yield Under the Foundation School Program

Under the current Foundation School Program funding system, districts generate guaranteed yield funds from both the maintenance and operations (M&O) and the interest and sinking fund (I&S) tax rates. For the 1991-92 school year, districts could generate up to $21.50 in guaranteed yield funds for each penny of tax effort up to $0.45 above the required local fund assignment.

During the current year, districts generated $603 million in state guaranteed yield funds through the I&S tax rate. In general, most school districts appear to levy sufficient local taxes to meet I&S obligations rather leverage their local taxes through the existing guaranteed yield. Under current law, districts are not required to use state guaranteed yield funds generated by I&S taxes to finance debt service.

It is estimated that the state commitment to a facilities financing program would be between $300 and $500 million annually to meet current debt requirements through a separate debt service guaranteed yield. Were debt service to be placed in a separate facilities financing tier, the state cost of the current guaranteed yield would decrease by about $600 million. A separated guaranteed yield system for debt service could be essentially revenue neutral to the state. Some sort of phase-in period would be necessary to allow districts time to compensate for the loss of these funds from maintenance expenditures. In addition to the lost operating funds, allowances would need to be made for district reductions in tax rates which would result from additional state aid for debt service.

Issuance Of State General Obligation Bonds

Another option for generating new funds for school facilities is the issuance of state general obligation bonds. Unlike the revenue bonds authorized under the Public School Facilities Funding Act (see below), general obligation bonds carry the full faith and credit of the state, and are the first item in line to be paid from state funds. Receipts from the issuance of debt could be used to support any of the options identified above.

While these bonds would provide the state with additional monies to provide to school districts, the state would be responsible for finding the funds to repay the principal and interest on the debt. These funds would come either from increases in state revenues or redistribution of funds away from existing uses. However, depending on the amount of bonded indebtedness incurred, and prevailing interest rates, the use of general obligation debt could be a more economically effective approach to providing funding for facilities.

Redirecting Other State Funds

The state currently provides approximately $6.5 billion in direct education related appropriations, not including the employer's share of teacher retirement. These funds come from general revenue tax sources, tax receipts of the Foundation School Fund, and the Available School Fund. To fund the state share of capital outlay or debt service, some current state appropriations could be redirected to meet the needs of a guaranteed yield or other grant system.

As an example, approximately $1 billion is provided annually to school districts through the Available School Fund (ASF). The ASF derives its income from dividends on Permanent School Fund (PSF) investments and other revenues. Because the PSF is a long-term capital asset, it may be logical to use the proceeds from it as a means to secure additional long-term assets for public education. Currently the ASF funds are distributed on a per capita basis and may be used for any legal purpose. It is possible that the ASF could also be used to provide the state share of the cost of debt service and capital outlay, or as a revenue source to guarantee state bonds to provide facilities funding to districts.

Alternative uses for the ASF will not add to the total revenues available for appropriation. If the ASF supports a separated debt service guaranteed yield program, the impact to the overall state appropriation requirements could be minimal, assuming some reduction in the maintenance guaranteed yield costs. As a revenue source to back additional state debt to be channeled to capital outlay, alternative uses of current state appropriations may actually extend the financial support the state can provide to districts.

Use of the Public School Facilities Fund[1]

In 1989 the 71st Texas Legislature authorized the State Bond Review Board to sell up to $750 million in revenue bonds in order to provide low interest rate loans to school districts for the purpose of either refunding existing debt or constructing new facilities. To date, no bonds have been sold under the program, however discussions as to how these funds might be used to finance some or all of the state's share of a facilities program are underway. One option which is under consideration as a potential piece of legislation is the modification of the Public School Facilities Funding Act to allow the state to issue these bonds as general obligation bond to meet its share of a facilities funding program.

1. Public School Facilities Funding Act, Article 717t, Vernon's Texas Civil Statutes, 1992.

SUMMARY OF OPTIONS FOR FACILITIES FINANCING

POLICY OPTION	LEVEL OF STATE CONTROL	LEVEL OF LOCAL FLEXIBILITY/ CONTROL	LEVEL OF EQUITY	DEBT SERVICE OR NEW FACILITIES	DATA REQUIREMENTS	AGENCY CONSEQUENCES
Per Capita (WADA) This is the system used to distribute the $50 million emergency grants. This option would provide a fixed dollar amount per pupil in weighted average daily attendance to each district.	This option provides the lowest level of state control, unless separate specific restraints are built into the system. While being the least restrictive policy option presented, it is also the least discriminating. In a pure system, every district would receive funds regardless of need. This could result in funds being provided to districts that would not use them. To avoid potentially wasting funds in this way, it would be possible to establish wealth or need tests for such an allotment.	This option provides the greatest level of local flexibility or control. In a per capita system, districts are provided with a grant to meet their facilities needs as they see fit. State restrictions could be imposed to limit uses of funds. Districts will be required to comply with State Board of Education standards for new construction.	The level of equity in a pure per capita system is very low because this type of funding mechanism does not discriminate either on the basis of district need or ability to pay. Equity could be improved if the allotment were wealth tested.	Monies provided to districts under this option could be used either to meet existing debt service obligations or to provide financing for new construction.	This option would not require the collection of any new or additional data. Information on district populations and district wealth (should a wealth test be applied) are currently available at the agency.	This option would have very limited consequences for the agency. There would be no additional administrative or data collection requirements in order to provide funding to districts on a per capital basis.

SUMMARY OF OPTIONS FOR FACILITIES FINANCING

POLICY OPTION	LEVEL OF STATE CONTROL	LEVEL OF LOCAL FLEXIBILITY/ CONTROL	LEVEL OF EQUITY	DEBT SERVICE OR NEW FACILITIES	DATA REQUIREMENTS	AGENCY CONSEQUENCES
Guaranteed Yield This option would operate in the same manner as the current guaranteed yield system for operating funds to provide a guaranteed return for each penny of debt service tax rate per pupil for qualifying districts. This option has been proposed previously as a separate tier, but has not been passed.	This option provides some level of state control through the financing levels established. Under this option all districts below a specified level of wealth would receive a guaranteed return on a fixed level of interest and sinking fund (I&S) tax rate. The state would not control the types of projects for which funds are spent.	This option provides a significant level of local control for districts which qualify for funding. Districts which receive funding will be able to use the funds to meet their needs as they see fit. State restrictions could be imposed to limit the uses of funds. Districts will be required to comply with State Board of Education standards for new construction.	A guaranteed yield system of funding school facilities would meet the equity test laid out by the courts. Under such a system the amount of funding available for financing capital outlay and debt service is not a function of local district wealth.	Under this option the level of funding would be tied to the district's debt service tax rate, however, districts would be able to use funds to meet existing debt obligations or to finance new construction.	This option would not require the collection of any new or additional data. Information on district wealth and debt service tax rates are currently available to the agency.	This option would have very limited consequences for the agency. There would be no additional data collection requirements and few administrative changes necessary in order to provide funding to districts on a guaranteed yield basis.

SUMMARY OF OPTIONS FOR FACILITIES FINANCING

POLICY OPTION	LEVEL OF STATE CONTROL	LEVEL OF LOCAL FLEXIBILITY/ CONTROL	LEVEL OF EQUITY	DEBT SERVICE OR NEW FACILITIES	DATA REQUIREMENTS	AGENCY CONSEQUENCES
Per Project This option would involved state review of each project, and funding would be provided for some or all of the construction. Under this option funding could be based on pre-set standards for buildings or on state determined allowable costs.	This option provides the greatest level of state control. Under a per project funding option, districts would be required to submit project information and funding needs to the state for review prior to receiving any monies. Although this option provides significant state control, it does come with a high state cost. The up-front cost of this program includes both the provision of state funds, and the commitment of state resources for plan review (see Agency Consequences).	This option provides local districts with the least flexibility and control. Under this option districts would be required to seek prior approval for a project in order to receive state funding. In addition to limiting control, this option also requires the district to budget extra time for the review process.	A per project system could be made equitable provided that the percentage of state and local funds assigned to the project reflected local school district wealth. Another option for increasing equity would be to have the entire cost of the project funded by the state and make no allowanced for local funds or improvements.	This option provides funding only for new facilities. Under this option districts with completed construction projects and outstanding debt obligations would not be eligible for funds.	A per project funding option would require data in addition to the information currently available at the agency. Districts would be required to submit additional information as a part of the application process.	This option would impose significant new demands on agency resources. Currently there are two individuals in the Division of State Funding and School Facilities working on implementation of the facilities program. However, this is insufficient staff for review of project plans. In states with project review programs, staff size ranges from 10 to more than 70 persons working in this area.

SUMMARY OF OPTIONS FOR FACILITIES FINANCING

POLICY OPTION	LEVEL OF STATE CONTROL	LEVEL OF LOCAL FLEXIBILITY/ CONTROL	LEVEL OF EQUITY	DEBT SERVICE OR NEW FACILITIES	DATA REQUIREMENTS	AGENCY CONSEQUENCES
Complementary Programs						
$50 Million Emergency Grant During the 1992-93 school year, $50 million in emergency facilities funds will be distributed to school districts on the basis of local property wealth, tax effort and growth in student population. Grants will be in the amount of $150 per student in weighted average daily attendance.	The level of state control associated with this program is minimal. The funds are provided to the districts as a grant, and districts will determine what constitutes an emergency.	This program provides those districts receiving funds with significant flexibility. Although districts are encouraged to use the funds to meet health and safety needs first, funds may be used to address any kind of need for instructional space.	This program is equalized by wealth and tax effort. Under the formula used to allocate funds, 55% of the determination is based on district wealth and 30% of the determination is based on tax effort.	This option is directed at meeting needs for renovation or new construction, but may be used to address debt service needs.	This program did not present a need for any new or additional data.	As a result of this new program, the agency has developed rules for the distribution of funds, and has hired two architects to work in the Division of State Funding and School Facilities and administer the program.
Incentive Programs for Increased Efficiency This program would provide incentive funding for districts to consolidate and build new facilities in order to increase district efficiency.	The level of state control under this option would be relatively low. Once districts had made a decision to consolidated and build a new facility, funds would be awarded for district use.	The level of local control under this option would be relatively high. Districts would be free to make decisions about consolidation, and the only construction requirements would be those contained in the agency standards.	N/A	This option provides funding only for new construction or the renovation of facilities. Districts would not be able to use this option to meet outstanding debt obligations.	This option would require no new data to be collected by the agency.	This program would have limited consequences for the agency. There would be some additional administrative requirements associated with this program.

CHAPTER 7
CONCLUSIONS

Through the collection of school facilities data under the BETA project, the state has, for the first time, the ability to analyze issues related to school facilities. While these data provide a great deal of information about the general condition and level of need for facilities in the state, it is important to remember that it has limitations. If it is the desire of the legislature to have detailed data that will make it possible to calculate facilities costs at a district or campus level, a much more comprehensive assessment of school facilities will be required.

The conduct of an inventory was recommended by all of the previous groups which have examined the issues relating to funding school facilities. With that inventory we are better able to estimate the need for facilities funding. As they have addressed this issue, previous advisory groups to the state have recommended a guaranteed yield approach to facilities funding, with a funding tier separate from the two existing levels of the foundation program. This type of funding approach is outlined in this report and has been offered up to the legislature before. As with the previous occasions, and as with any plan to involve the state in facilities funding, additional revenue sources will be needed to provide funds to school districts.

In determining a state role in funding facilities, the legislature must simultaneously balance several interests. Local schools must be assured a means of providing appropriate housing for students. The state must be certain that its assistance will be used in a responsible manner. Unproductive bureaucracies and processes must be avoided. Costs must fit within revenues, and efficient utilization of resources must be encouraged. This report is an attempt to provide the legislative leadership with some assistance in achieving that balance as they begin to walk the facilities wire.