

Prop. 301 & Education 2000

The Education 2000 proposal (SB1007) makes numerous changes to state laws governing public education. Five provisions are specifically referred to the November 7 ballot as Proposition 301, including an increase in the state sales tax rate. Currently at 5.0 percent, the measure would increase the rate to 5.6 percent.

WHAT GOES TO VOTERS?

In addition to the question of the sales tax rate hike, that same vote on Prop. 301 will also decide the following questions (each of which is discussed in detail below):

- ◆ *An automatic yearly inflation adjustment in K-12 funding;*
- ◆ *Elimination of school district authority to levy for excess utilities in 2009;*
- ◆ *Caps on the qualifying tax rate (QTR) and the county education rate; and*
- ◆ *State income tax credits for low-income households.*

In addition to these provisions, SB1007 contains a conditional enactment requiring voter approval for the entire act to become effective. Many of SB1007's provisions *not* specifically referred to voters are significant and are discussed starting on page 2.

INFLATION ADJUSTMENT

Education 2000 would guarantee automatic inflation growth in the base level or other components of the revenue control limit (RCL) of 2 percent for fiscal year (FY) 2001-2002 through FY 2005-2006. In subsequent years the adjustment is the lesser of 2 percent or the change in the GDP price deflator. Clearly, the intent of this provision is to adjust the base level, but the phrase "or other components" of the RCL is curious. This means that the legislature could choose not to increase the base level, opting instead to adjust any one of the other components, say, for example, the limited English proficiency (LEP) multiplier.

ATRA worked hard in the early 1990s to remove guaranteed inflationary adjustments from state law. Those mandatory inflationary adjustments played a key role in demands for tax increases in the late 1980s.

Also significant is that the new sales tax revenue does not cover the future costs of the mandatory inflation adjustment. According to the Joint Legislative Budget Committee (JLBC), in FY 2001-2002 the inflation adjustment will require an additional \$67 million from the state general fund. By FY 2006 the amount exceeding the sales tax revenue is estimated to reach \$367 million. By 2011 an estimated \$831 million will be needed from taxpayers in addition to Prop. 301's sales tax revenue.

From a taxpayer standpoint, the return to mandatory inflation adjustments is one of the more troubling provisions of SB1007.

EXCESS UTILITIES

SB1007 includes a sunset on the exception from the RCL for excess utilities. Last year, school districts statewide levied \$58 million outside their budget limits for excess utilities. Contingent upon voter approval, districts' ability to levy what amounts to a budget override without voter approval will expire after June 30, 2009.

This provision is a direct result, albeit an imperfect one, of ATRA's legislative advocacy on this issue. However, the nine-year delayed effective date is evidence of the legislature's lack of resolve to deal with the inequities in school finance.

CAPS ON QTR AND COUNTY EDUCATION RATE

Another provision in SB1007 places limits on the two property tax rates set by the legislature. The qualifying tax rate (QTR), which determines the local property tax contribution to which state equalization assistance is added to fund school district budgets, would be capped at its current (tax year 2000) value of \$4.2530 for unified

districts and \$2.1265 for elementary or high school districts. Similarly, the county equalization assistance rate would be limited to the current level, \$0.5123.

ATRA testified in the special session that the benefit of this provision to taxpayers is very limited. The truth in taxation requirements at the state level have been functioning well and taxpayers have seen the second drop in the QTR and county education rate in as many years as the rates have been adjusted to reflect changes in assessed property values. Capping these rates, however, has provided an opportunity for some supporters of SB1007 to characterize this measure as "capping property taxes."

The truth is, this measure will likely have no impact on the school property taxes. Further, the reluctance on the part of the legislature to embrace ATRA's recommendations on expenditures outside the budget limits guarantees growth in school property tax rates.

Capping the QTR and county education rate will not prevent Tucson Unified from levying property taxes with a primary rate of \$7.15 per \$100 of assessed value. Nor will it result in a decrease in Bowie Unified's rate of \$12.14.

STATE INCOME TAX CREDIT FOR LOW-INCOME HOUSEHOLDS

In response to charges that the sales tax is regressive, the final component of the question SB1007 puts to voters is a state income tax credit for low-income households to mitigate the increased sales tax burden. A \$25 credit is allowed for each Arizona resident claimed for a personal or dependent exemption, up to \$100 total. Filers qualifying for the credit would include a married couple or head of household earning \$25,000 or less, or a single person or married person filing separately with a maximum income of \$12,500.



JLBC contends that the amount needed to fund this credit will exceed the \$25 million set aside from the sales tax revenue, dipping into the general fund for about \$16.6 million.

WHAT ELSE DOES THE VOTE ON PROP. 301 DECIDE?

The remaining measures contained in SB1007, although not specifically put to voters in November, are contingent upon voter approval. Among the major programs established in this bill for K-12 public schools are the following:

CLASSROOM SITE FUND

Although last in the line of recipients of the new sales tax, the classroom site fund (CSF) is the centerpiece of the Education 2000 proposal. The CSF becomes a new category of school funding, like the revenue control limit and capital outlay revenue limit, and will comprise part of the general budget limit for each school district.

After new revenue from the sales tax increase is distributed to service debt on revenue bonds and fund other programs in this package, remaining monies, about \$260 million in FY 2002, go into the CSF. Of those monies, 40 percent is allocated to “teacher compensation increases based on performance and employment related expenses” (EREs); 20 percent goes to “teacher base salary increases and employment related expenses.” The remaining 40 percent is to be spent on the following specified maintenance and operation purposes (with input from school principals):

1. Class size reduction;
2. Teacher compensation increases;
3. AIMS intervention programs;
4. Teacher development;
5. Dropout prevention programs; and
6. Teacher liability insurance premiums.

It is interesting to note that SB1007’s calls for compensation based on “performance” are not accompanied by any definition of the term. Moreover, the money can go not only to compensation but also toward “employment related expenses” — e.g., health benefits — even though EREs would not necessarily increase with performance-based salary increases. Given the extreme opposition from the education establishment

to compensation based on performance, ATRA remains doubtful this provision will have any reforming impact.

\$800 MILLION IN BONDS FOR SCHOOL BUILDING DEFICIENCIES

With Prop. 301’s approval, the School Facilities Board (SFB) will be allowed to issue up to \$800 million in “school improvement revenue bonds” to bring school buildings up to the “minimum adequacy guidelines” adopted last year by the SFB. ATRA acknowledged the need for revenue bonds to fund the state’s very costly deficiency correction program and supported this component of the proposal.

Debt service on these bonds will be the first lien on revenue generated by the 0.6 percent sales tax. The provision contains a serious flaw in that the authority to pay the debt service on the bonds, which is intended to run 20 years, is repealed as of June 30, 2005.

Another problem is that the proceeds from these bonds are to be spent on capital projects pursuant to the current deficiency correction law. But this section of law contains a delayed repeal effective July 1, 2003. That means the SFB, assuming the other repeal is corrected, would have approximately two years to issue all \$800 million in bonds and distribute the proceeds to the districts for specified projects. It is doubtful, to say the least, that all districts will be prepared to start work in that time frame.

Moreover, questions remain about the availability of workers and materials to implement \$800 million in construction and renovation work in a two-year period. Simultaneous new construction and building renewal projects under way or scheduled to start prior to July 1, 2003 will add to this problem. For these reasons, ATRA had supported Governor Hull’s early efforts to extend the deadline for deficiency correction by four years.

Revenue bonding for deficiency correction could free up the \$150 million currently appropriated for that purpose.

SAIS

Among the most controversial provisions in SB1007, the Superintendent of Public Instruction’s Student Accountability Information System (SAIS) was opposed by

the education lobby. SAIS will require school districts to submit “student level data” electronically to the Arizona Department of Education (ADE). ADE will notify districts and charter schools of the procedures and data elements by November 15, 2000.

ATRA testified during this year’s regular session in support of SAIS because it provides a means of auditing student counts, arguably the single most important driver of the state budget. Currently, no such verification mechanism exists.

However, ATRA remains concerned about representations made about SAIS as a tool for school reform. Contrary to the claims made by proponents, SAIS will not guarantee that funds follow the student to the school site. SAIS may provide a better understanding of the revenue generated by each student, but it will not create greater efficiencies in the expenditure of funds.

As with many of the programs established in this legislation, the extent of SAIS’s usefulness remains to be seen.

INDEPENDENT PRINCIPALS: LEAP

Another program established in SB1007, and opposed by the education lobby, is the Local Education Accountability Program (LEAP). LEAP would allow school principals to apply to the school district to become “financially and operationally independent.” A school district must select at least one applicant per year until 10 percent of the district’s schools are participating in LEAP.

Under LEAP, principals would receive money directly from the district. Districts would deduct administrative expenses and would remain in control of money generated through special education weights, but monies associated with “teacher salaries, average daily membership and transportation of pupils” would go directly to the principal. Principals would contract with districts to purchase services. Principals would be given a presumably higher degree of control over curricula (“notwithstanding any curriculum adopted by the school district to the contrary”) and over teacher contracts, although the principal remains bound to the district’s salary schedule.

Presumably anticipating that districts will discourage principals from applying, SB1007 provides that “a school district

governing board shall not take any personnel action against a principal applying to participate” in LEAP. Principals would also be protected against personnel action “that is directly or indirectly contingent on the amount of services that the school will contract to purchase from the school district.” Personnel action is defined as:

1. a disciplinary or corrective action;
2. a transfer or reassignment;
3. a suspension, demotion or dismissal;
4. an unfavorable performance evaluation;
5. a reduction in pay, benefits or awards; and
6. other significant changes in duties or responsibilities that are inconsistent with the principal’s salary or employment classification.

The LEAP program appears to give participating principals the financial autonomy denied to school districts during the last two regular legislative sessions (with strong opposition from ATRA) to invest their own money and spend interest earned rather than return it to taxpayers.

In certain respects, it would appear that LEAP schools would operate financially in a manner similar to charter schools. One difference, however, is found in the lack of accountability for LEAP schools. If a charter school is not in compliance with its charter and other rules governing charter schools, its sponsor can shut the school down. It is more than a little ironic that a school district, which has the ability to close its schools for any number of reasons, may not be able to close a LEAP school because the principal is protected from reassignment.

Conceptually, the sweeping reforms anticipated by the LEAP program are consistent with research indicating that strong principals are a critical element in school success. Nevertheless, there are many questions left unanswered in statutory provisions establishing LEAP and, if Prop. 301 passes in November, significant legislative work will be required.

A LONGER SCHOOL YEAR

Voter acceptance of SB1007 would extend the required hours of school programs for each grade level and increase the school year over a five-year period by one day per year, from the current 175 days to 180 days.

A provision that will merit close scrutiny is the requirement in sweeping catchall

language that the Superintendent of Public Instruction cause the adjustment of “all relevant school funding formulas” to reflect the 180-day school year.

“UNDERPERFORMING” AND “FAILING” SCHOOLS

SB1007 requires ADE to compile an “annual achievement profile” for each public school consisting of AIMS scores and passage rates, adequate yearly progress data, and dropout rates. The data would in turn be used to identify “underperforming schools” which failed to meet specified thresholds in any of the three areas. District governing boards must notify residents of the schools attendance area and develop an improvement plan.

If the problem persists for a second year, the school will be designated a “failing” school and will be assigned an “instructional trouble solutions team.” The governing board will also be required to include a statement in subsequent governing board election pamphlets that a certain number of schools were designated as “failing.” Students from “failing” schools will be authorized to take advantage of a tutoring program at state expense. A “failing schools tutoring fund” is established with revenue generated by the sales tax increase.

SWAT AUDITS

Inspired by the *Education Week* statistic indicating that Arizona spends only 57 cents out of every dollar in the classroom, the legislation creates a “school-wide audit team” (SWAT) in the office of the Auditor General to conduct performance audits and monitor school districts to determine the percentage of every dollar spent in the classroom by a school district. A random SWAT audit shall be conducted for each school district at least once every five years. The Auditor General’s office estimates the costs of these provisions — which are not covered by the sales tax increase — at \$7 million.

UNIVERSITIES

Success at the ballot for SB1007 will also result in significant new revenue for Arizona’s universities. A “technology and research initiative fund” is established, managed by the Arizona Board of Regents (ABOR). Up to 20 percent of the fund can

be used for “capital projects relating to new economy initiatives.” Awards from this fund must be related to one of the following: a specific academic or research field; designed to expand access to baccalaureate or post-baccalaureate education or time-bound and place-bound students; or to implement the recommendations of the Arizona Partnership for the New Economy or the Governor’s Task Force on Higher Education. The monies may be used “to develop new and existing programs that will prepare students to contribute in high technology industries” located in Arizona. ABOR must give preference to funding requests developed in conjunction with private industry, private entities or federal agencies.

Arizona State University also receives a \$2.5 million appropriation for lease-purchase of buildings.

COMMUNITY COLLEGES

Each of the state’s 10 community college districts will establish a separate “workforce development account” into which monies from the 0.6 percent tax will be spent on “workforce development and job training purposes.” SB1007 identifies these as:

1. partnerships with business and educational institutions;
2. additional faculty for improved and expanded classroom instruction and course offerings;
3. technology, equipment and technology infrastructure for advanced teaching and learning in classrooms and laboratories;
4. student services such as assessment, advisement and counseling for new and expanded job opportunities; and
5. the purchase, lease or lease-purchase of real property for new construction, remodeling or repair of buildings or facilities on real property.

In other words, community college districts can spend this money virtually any way they want to.

JLBC projects that community colleges will receive over \$11 million in the first year. The first million dollars for each of the first 13 years will go to districts that have been previously designated for capital matching monies. In most instances this revenue will go to districts for capital construction completed and paid for by taxpayers long ago.

ATRA has argued in the past that capital matching dollars should go toward offsetting property taxes. SB1007 contains no such provision.

A serious flaw in SB1007 is a provision that exempts these new “workforce development” revenues from the colleges’ constitutional expenditure limits. Earlier versions of Education 2000 appropriately contained a constitutional amendment requiring voter approval to exclude this money from the expenditure limits.

In what ATRA views as an unconstitutional approach, SB1007 simply amends the Constitution by reference. To wit: “Monies received under this section shall not be considered to be local revenues for the purposes of Article IX, Section 21, Constitution of Arizona.”

DISTRIBUTION OF NEW TAX REVENUE

Monies generated by the 0.6 percent sales tax will be distributed as follows:

1. The amount necessary to pay debt service on outstanding state school improvement revenue bonds;
2. Twelve percent of the remaining monies to universities for the technology and research initiative;
3. Three percent of remaining monies to the community colleges’ workforce development accounts;
4. An amount to colleges run by a “qualifying Indian tribe” (currently Diné College) that would have gone to the college had it been under the jurisdiction of the State Board;
5. Amounts to fund increases in state aid resulting from added school days:
 - a. \$15.3 million in FY 2001-02
 - b. \$31.5 million in FY 2002-03
 - c. \$48.7 million in FY 2003-04
 - d. \$67.0 million in FY 2004-05
 - e. \$86.3 million in FY 2005-06 and thereafter;
6. \$7.8 million to ADE for school safety programs and \$200,000 for character education matching grants;
7. Up to \$7.0 million to ADE to fund failing schools accountability measures and SAIS;
8. \$1.5 million to the failing schools tutoring fund;
9. \$25.0 million to reimburse the general fund for the income tax credit for low-income households; and
10. Remaining monies to the classroom site fund.

MISCELLANEOUS

A new reporting requirement — Currently, the auditor general must prescribe a uniform system of financial records (USFR) that requires certain revenues to be accounted for. SB1007 adds a requirement that the USFR include an apportionment (i.e., breakdown) of revenues in excess of the RCL, for example, desegregation revenue. It remains to be seen how the auditor general’s office will implement this requirement.

What is of primary interest to those who monitor this are *expenditures*, not *revenues*. Plans for revenues are presented in school district budgets but are subject to change. On the other hand, expenditure reports require districts to report how they actually spent the money.

Burden of proof on pupil — Places the burden of proof on the pupil to overturn the decision of a teacher to promote, retain, pass or fail the pupil.

Personal liability insurance — Requires each school district to provide teachers with personal liability insurance.

Tax credits — Increases the \$500 tax credit for contributions to a school tuition organization to \$675. Increases the \$200 tax credit for school extracurricular fees to \$250. JLBC estimates the fiscal impact of these provisions at \$3.75 million for FY 2002. This impact is not covered by the 0.6 percent sales tax.

Trigger amended — \$20 million triggered revenue for FY 2000-01 (set in the biennial budget from 1999’s 1st Special Session) is amended, directing the entire amount to teacher salaries.

CONCLUSION

ATRA had supported the Education 2000 proposal on the condition that increased funding be accompanied by desperately needed school finance reforms. ATRA argued that greater funding at the state level provided an opportunity to remedy severe spending and taxation inequities between districts that are allowed under our current school finance system. SB1007 falls well short of that goal.

From the outset, much of the debate supporting the tax increase was based on Arizona’s low ranking in maintenance and operation (M&O) expenditures per pupil. ATRA dedicated significant time and effort attempting to educate policy makers and the media on the meaning of the rankings (that they exclude capital expenditures, for example) and the danger of basing major policy decisions on an isolated statistic.

Voters need to recognize that the added revenue in Prop. 301 will likely yield less than \$350 per pupil, resulting in a shift in Arizona’s ranking (assuming other states remain constant) from 47th to 46th (NEA, FY 1999). Such a change will not likely relieve Arizonans of any self-imposed guilt associated with the ranking.

Education 2000, as it emerged in SB1007 and Proposition 301, does provide for additional school days and the identification of failing schools — clearly laudable moves in the right direction; however, this legislation is also a missed opportunity to repair a broken school finance system that treats both schools and taxpayers unequally and unfairly.

DISTRIBUTION OF REVENUE FROM 0.6% SALES TAX

		FY 2002*
1st lien	Debt service on school improvement revenue bonds	\$70,000,000
After debt service	Universities (12%)	\$44,160,000
	Community Colleges (3%)	\$11,040,000
	Dine College	\$370,000
Next after higher ed	Additional school days (\$15.3 million, first year only)	\$15,305,900
	School safety programs	\$7,800,000
	Character education matching grants	\$200,000
	SAIS and failing schools program (up to \$7 million)	\$2,500,000
	Failing schools tutoring fund	\$1,500,000
	Low income tax credit	\$25,000,000
Last	Left over from sales tax for classroom site fund	\$260,124,100

*JLBC figures