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Nos. 04-1144, 05-0145, and 05-0148

In The Supreme Court of Texas

ALVARADO INDEPENDENT SCHOOL DISTRICT, et al.,
Appellants

v.

SHIRLEY NEELEY, IN HER OFFICIAL CAPACITY AS TEXAS COMMISSIONEROF EDUCATION, THE TEXAS EDUCATION AGENCY, CAROL KEETON STRAYHORN, IN HER OFFICIAL CAPACITY AS TEXAS COMPTROLLER OF PUBLIC ACCOUNTS, AND THE TEXAS STATE BOARD OF EDUCATION,
Appellees

On Direct Appeal from the 250th District Court, Austin, Travis County, Texas

ALVARADO APPELLANTS' REPLY BRIEF

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ALVARADO APPELLANTS' REPLY BRIEF

TO THE HONORABLE SUPREME COURT OF TEXAS:

SUMMARY OF THE ARGUMENT

The State argues that this Court should overrule its prior decisions holding that the efficiency clause of article VII, section 1 is justiciable and that school districts have standing to enforce its provisions. The rule of law and *stare decisis* dictate that this Court overrule its decisions only for compelling reasons. The State has come forward with no arguments that would convince one that this Court's prior decisions are flawed or in error on these issues. Quite the contrary, existing case law fully supports the Court's prior rulings on these questions.

The current system for funding school district maintenance and operations is constitutionally inefficient because of the large disparity between the tax rates for property-poor and property-rich districts to raise the revenue necessary to fund an adequate education for their students. The current maintenance and operations tax rate gap is double what this Court has previously determined was only barely constitutional. The State, however, argues that this Court should either ignore that part of the system which grants large amounts of revenue to wealthy school districts or repudiate its prior analysis in order to uphold the constitutionality of the current system. This Court, however, should do neither.

The State contends that because this Court did not include hold harmless districts (those who are allowed to retain wealth in excess of the cap) in its prior efficiency analysis, they should likewise be excluded now. However, hold

harmless districts were merely a temporary feature of the prior system, but have now been made permanent. As the Legislature has made an explicit determination to provide large amounts of additional revenue to wealthy districts, the judiciary cannot and would not simply ignore this in adjudicating the constitutional efficiency of the system. This Court has considered all inherent, permanent parts of the system in its prior efficiency determinations and there is no reason to deviate from that type of review for this decision.

Finally, the State has come forward with no compelling reasons for overturning the tax rate gap analysis that this Court adopted in its prior efficiency decision. None of the underlying factors with respect to deciding the constitutional question have changed. Rather, what has changed is that the State has made its school finance system considerably less efficient. Simply because the State has moved in a direction of greater inequity in its system, rather than following the constitutional requirement to make the system more efficient, is no reason to abandon this Court's constitutional review.

ARGUMENT

I. Efficiency Presents a Justiciable Question That School Districts Have Standing to Litigate

The State initially argues that this Court should overrule its longstanding precedent that the efficiency clause of article VII, section 1 creates a justiciable claim that school districts have standing to raise. For the reasons set out in pages 9 through 17 of Alvarado Appellee's Brief filed with this Court on May 9, 2005 in appeal number 04-1144, the Court should refuse to overrule its prior holdings on these issues.

II. The Maintenance and Operations Component of the State's School Finance System is not Presumptively Efficient as a Matter of Law

The State contends that so long as its school finance system is constitutionally adequate, then it may ignore the constitutional mandate that the system also be efficient. However, satisfying one constitutional command can never be grounds for writing another one out of the Constitution.

Efficiency, which has been the subject of three *Edgewood* opinions, has different constitutional requirements at different tax rates. At those tax rates up to and necessary for "the achievement of an adequate school system as required by the Constitution," article VII, section 1 requires "'substantially equal access to similar revenues per pupil at similar levels of tax effort.'" *West Orange-Cove Consol. Indep. Sch. Dist. v. Alanis*, 107 S.W.3d 558, 566 (Tex. 2003) (quoting

Edgewood Indep. Sch. Dist. v. Kirby, 777 S.W.2d 391, 395 (Tex. 1989) (*Edgewood I*)). This type of efficiency is commonly referred to as financial efficiency or equity and was the standard by which this Court measured the constitutionality of the school finance system in *Edgewood Indep. Sch. Dist. v. Meno*, 917 S.W.2d 717 (Tex. 1995) (*Edgewood IV*). At tax rates above those necessary to provide a general diffusion of knowledge, the Constitution requires that access to revenue at those tax rates may "'not become so great that it, in effect, destroys the efficiency of the entire system.'" *West Orange-Cove*, 107 S.W.3d at 571 (quoting *Edgewood IV*, 917 S.W.2d at 732).[1] The State argues that if the school finance system provides sufficient revenues for school districts to achieve a general diffusion of knowledge, then the system is per se financially efficient and equity is no longer required. This Court's opinion in *Edgewood IV*, however, does not support the State's contention.

In that case, this Court found that at those tax rates necessary to achieve a general diffusion of knowledge[2] there was a 9 cent gap between the property-

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[1] In *Edgewood IV*, the Court held that allowing some districts to tax at rates in excess of $1.50 did not destroy the efficiency of the entire system, but held that if at some point such "supplementation" became necessary to provide a general diffusion of knowledge, then this would violate the efficiency clause. *Edgewood IV*, 917 S.W.2d at 732. Additionally, if such "supplementation" effectively "insulate[d] concentrated areas of property wealth from being taxed to support the public schools" such that the system did not "draw revenue from all property at a substantially similar rate," then that would likewise destroy the efficiency of the entire system. *Edgewood Indep. Sch. Dist. v. Kirby*, 804 S.W.2d 491, 496-97 (Tex. 1991) (*Edgewood II*).

[2] Because neither the definition nor the application of the constitutional requirement for a general diffusion of knowledge were at issue in *Edgewood IV*, the Court presumed that providing an accredited education also provided a general diffusion of knowledge. *West Orange-Cove*, 107 S.W.3d at 581. Based

wealthy and property-poor districts. *Edgewood IV*, 917 S.W.2d at 731. Although the Court held that this disparity did not violate the efficiency clause's requirement for equity, it "stressed that the system was 'minimally acceptable only when viewed through the prism of history.'" In other words, it was better than it had been. But [the court] added: 'Surely Texas can and must do better.'" *West Orange-Cove*, 107 S.W.3d at 572 (quoting *Edgewood IV*, 917 S.W.2d at 726). Indeed, contrary to the State's position in this appeal, the *Edgewood IV* opinion explicitly stated that its "'judgment in [that] case should not be interpreted as a signal that the school finance crisis in Texas has ended.'" *Id.* at 573 (quoting *Edgewood IV*, 917 S.W.2d at 725). Thus, although the Court presumed that the school finance system in *Edgewood IV* was adequate, it still required the system to be equitable up to that level necessary to provide the presumed level of a general diffusion of knowledge.

To support its contrary position, the State cites language from *Edgewood IV* that allowing some school districts to tax at rates in excess of the $1.50 cap does not violate constitutional efficiency because such districts are supplementing an "already efficient system." *Edgewood IV*, 917 S.W.2d at 733. The State reads this language as holding that the system was already efficient because it was

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upon testimony concerning the average cost per student needed to provide an accredited education, the Court established the tax rates necessary for property-poor and property-wealthy school district to provide a general diffusion of knowledge. *Edgewood IV*, 917 S.W.2d at 731 & nn. 10, 12.

presumed to have achieved a general diffusion of knowledge. However, this is simply a misreading of the Court's opinion. The system was considered minimally efficient because, when viewed through the prism of history the "districts now have substantially equal access to the funds necessary for a general diffusion of knowledge." *Id.* at 731. Thus, there is nothing in the *Edgewood IV* opinion to support the proposition that this Court's standard of equity, adopted and used in every *Edgewood* efficiency case, does not apply if the system is otherwise adequate. Indeed, the holding in *Edgewood IV* shows that this argument is wholly without foundation or merit.

III. To Determine the Efficiency of the Maintenance and Operations Part of System the Courts Must Consider All Districts, Including Hold Harmless Districts

In *Edgewood IV*, the Court found that there was a 9 cent disparity in the average tax rate needed for the wealthiest 15% of the districts to achieve a general diffusion of knowledge versus the average tax rate needed for the poorest 15% of districts to achieve a general diffusion of knowledge. *Edgewood IV*, 917 S.W.2d at 731. The Court found this disparity to be minimally acceptable in view of where the finance system had come from, but cautioned that the State must do better. *Id.* at 726. The trial court found that Chapter 41 districts, and thus Tier 2 districts by necessity, could not achieve a general diffusion of knowledge with the amount of funds obtainable at the $1.50 tax rate cap. FOF

291, 4 CR 919. To come up with a calculation similar to that employed in *Edgewood IV*, one must thus look at the maximum amount of revenue a Tier 2 district can obtain under the school finance formulas at a $1.50 tax rate, and then compare that maximum rate to the tax rate needed by the wealthiest 15% of districts to achieve the same amount of revenue.

The State's own expert witness testified that it took the average Chapter 41 district, as opposed to the wealthiest 15%, only $1.33 to achieve the same amount of maintenance and operations revenue available to a Tier 2 district at $1.50. State Ex. 16429 at 55; 28 RR 51-52. Although this 17 cent disparity is not exactly equal to the calculation used in *Edgewood IV*, it is not a difference that the State can complain about because using only the wealthiest 15% of districts would produce an even larger tax rate disparity. However, the State does complain about the tax rate gap it introduced into evidence because the State included hold harmless districts in its calculation of the gap. The State offers a variety of reasons for criticizing its own evidence, none of which have any merit.

The State first argues that this Court should determine the efficiency of the maintenance and operations portion of school finance system by ignoring hold harmless districts in its analysis. Based upon an examination of only part of the school finance system, the State puts forth various numbers in an attempt to show that the 17 cent gap its expert testified to is not the right number, but rather

that the system's financial efficiency has either improved or become only slightly worse. However, because the State's numbers are not based on the actual school finance system, they have no validity with respect to the efficiency of the system currently in place.

As the State correctly points out, this Court did not consider hold-harmless districts in its *Edgewood IV* efficiency review because the law under consideration required their elimination within a three-year period. Had the Court considered these districts in its opinion, it almost assuredly would have found the system unconstitutionally inefficient since it found the system barely constitutional even after full implementation. The State now argues, however, that because hold harmless districts were excluded from the Court's consideration in *Edgewood IV* it would be comparing apples and oranges to include them now.

Specifically, the State argues that to include hold harmless districts in the efficiency analysis now would be comparing a total gap to the supposedly partial gap considered in *Edgewood IV*. Contrary to the State's assertion, the Court looked at the total gap in *Edgewood IV* and should do so as well in this case. In *Edgewood IV*, the Court initially determined the efficiency of the system by focusing on that "inherent, permanent part of the system established by Senate Bill 7." *Edgewood IV*, 917 S.W.2d at 731. By necessity, this excluded the hold harmless districts because they were only a temporary feature of that system.

The Court later in its opinion expressly reviewed the three year phase out of the hold harmless provision and determined that it was not so unfavorable to property-poor districts so as to render the entire system unconstitutionally inefficient. *Id.* at 734.

Under the Court's *Edgewood IV* analysis, it did consider the permanent total gap between property-wealthy and property-poor districts. Because hold harmless districts are now an "inherent, permanent part of the system," they must be considered when determining the efficiency of any part of the system. Leaving these districts out of the constitutional evaluation of efficiency would not only turn a blind eye to the reality of the current system, but would also require the Court to discard the analysis it expressly used in *Edgewood IV*.

The State also argues that hold harmless districts should be excluded from an efficiency analysis because to include them allegedly would be to consider the ability of those districts to generate and spend local taxes in excess of the amounts necessary to provide a general diffusion of knowledge. This particular argument makes no sense in that by definition the State's 17 cent tax rate gap calculation is for the maximum amount of funds that can be obtained by Tier 2 districts, which the district court held was insufficient to achieve a general diffusion of knowledge. Thus, the tax rates required by any Chapter 41 district, whether hold harmless or not, to achieve this level of funding could not be in

excess of the amount necessary to achieve a general diffusion of knowledge. Because hold harmless districts are simply part of the reality of the current school finance system, the State correctly included them when it introduced evidence of the actual maintenance and operations tax rate gap between property-rich and property-poor districts.

IV. The State Has Offered No Compelling Reasons for This Court to Repudiate its Prior Tests for Analyzing the Constitutionality of the School Finance System

The State also argues that the Court should abandon the tax rate gap analysis it used in *Edgewood IV* and use the disparity in revenue yielded under the Foundation School Program ("FSP") because the FSP excludes revenue retained by hold harmless districts. It is true that the FSP excludes revenue retained by hold harmless districts, but that is because it excludes all revenue retained by every Chapter 41 district. The FSP, by definition, only includes those districts that are eligible for Tier 2 funds under Chapter 42 of the Education Code. *See* TEX. EDUC. CODE ANN. §§ 42.002(b); .251(a). Indeed, the only relationship between any Chapter 41 district and the FSP is that either its detached property or its recaptured revenue provides additional sources for funding the FSP. *Id.* §§ 41.004(d); .094(b). Thus all Chapter 41 districts, whether hold harmless or not, are outside of the FSP, *id.* §§ 41.002; .003, and the State's attempt to somehow create a revenue gap "within the FSP" is unavailing since

only Tier 2 districts are a part of the FSP. The "within the FSP" revenue gap number alluded to by the State is a meaningless number that has absolutely no connection to this Court's prior tax rate gap calculation used to determine the efficiency of the system. The State's number has no correlation to the amount of maintenance and operations revenue needed for a general diffusion of knowledge, reveals nothing about the relevant tax rate disparities and should be disregarded by this Court.

The State additionally argues that the 17 cent tax rate gap should not be used "because the amount of funding necessary for a general diffusion of knowledge is not calculable." State Appellee's Brief, at 28. This is a curious position, however, given the State's claim that it knows that the amount of funding needed is less than what school districts have because "they can tax substantially below the cap and still provide a general diffusion of knowledge." *Id.* at 29. This argument is internally inconsistent and would require this Court to overrule its opinions in *Edgewood IV* and *West Orange-Cove*. On the one hand, the State argues that it is impossible to approximate the amount of maintenance and operations funds a district would require to provide its students with an adequate education. On the other hand, it argues that this incalculable number is less than $4,273.00, the maximum amount of maintenance and operations funds available to a Tier 2 district. The State may not have it both ways. If they want to

argue that the level of funding needed for an adequate education is less than a certain amount, then they must acknowledge that it is subject to being calculated. In this case, although the trial court's findings do not specify the amount of funding necessary to provide a general diffusion of knowledge, the trial court did find that the amount required exceeded the amount of revenue available to Chapter 41 districts, which was all that was necessary to find that the system was constitutionally inadequate.

Moreover, to accept the State's argument would require overruling the tests this Court has adopted for determining the State's compliance with the efficiency clause of article VII, section 1 and the state property prohibition in article VIII, section 1-e. In *Edgewood IV*, this Court predicated its efficiency analysis on the amount of funds necessary to provide a general diffusion of knowledge. *Edgewood IV*, 917 S.W.2d at 731-32 & nn. 10, 12. Thus, this Court requires at least an approximation or range of funding needed for an adequate education in order to determine the system's efficiency. Additionally, in *West Orange-Cove* this Court held that a school district can prove a violation of article VIII, section 1-e by demonstrating that it must tax at the maximum allowable rate simply to provide a general diffusion of knowledge. *West Orange-Cove*, 107 S.W.3d at 582. In order to establish this type of claim, this Court recognized that districts must prove that the cost of providing an adequate education exceeds the

amount of funding available. Consequently, this Court's prior opinions base their constitutional evaluation of the State's system on establishing the cost of providing an adequate education in relation to the amount of available funding. If the cost of providing such an education is not calculable, then this Court must repudiate its prior decisions. However, the evidence introduced at trial and the facts found by the trial court show that the cost of an adequate education can be judicially assessed and thus this argument by the State is without merit.

V. The Dramatic Decrease in Efficiency of the Maintenance and Operations Part of the Current System Renders it Unconstitutional

The State concedes that the 17 cent tax rate gap has increased the system's inefficiency. However, it argues that when viewed in the context of the total system it is not so much worse as to render the system unconstitutionally inefficient. This argument fails because it disregards this Court's clear holding that the prior system was constitutional only because the State had made sufficient progress in improving equity and because the numbers used by the State actually disregard the inefficiencies of the entire system.

Using a rather imaginative calculation, the State contends that the current 17 cent maintenance and operations tax rate gap, as a percentage of the total equalized system, is only 50% more inequitable than the 9 cent tax rate gap approved in *Edgewood IV*. The State achieves this remarkable feat by comparing the 17 cent gap to a $1.79 equalized system consisting of $1.50 for maintenance

and operations and $.29 for facilities based upon the maximum amount available under the Existing Debt Allotment ("EDA"). This analysis suffers from certain fatal flaws. First, the State is mixing the efficiency of the maintenance and operations component of the system with the efficiency of the facilities component. The Alvarado Appellants' appeal pertains only to maintenance and operations and thus including the facilities component in its calculation renders the State's analysis inapplicable to the issues in this appeal. Second, as pointed out in the Alvarado Appellees' Brief, a school district that passes a new bond issue for facilities is not eligible for EDA and thus, aside from the minimal amount of IFA, there is no equalized system for new facilities. *See* Alvarado Appellees' Brief, at 35-42. Thus, the calculation made by the State is inapposite to the issue of the inefficiency of the maintenance and operations component of the current system.

However, even if the actual maintenance and operations tax rate gap were only 50% greater, as opposed to the actual 100% increase, that would still not save the system from being unconstitutionally inefficient. In upholding the 9 cent tax rate gap in *Edgewood IV*, this Court could not have made it any clearer that the system was constitutional only because of the strides the State had made towards greater efficiency. This Court's essential guidance to the State was "so far so good, but you must do better." When the State disregards its

constitutional responsibilities as outlined by this Court by expressly building dramatically larger inefficiencies into a system that was only minimally efficient at best, it cannot now argue that its much less efficient system passes constitutional muster.

CONCLUSION

Based upon the foregoing, the Alvarado Appellants respectfully request this Court to reverse the trial court's judgment and render judgment that the current school finance system violates the efficiency clause of Article VII, section 1 in the manner that it funds the maintenance and operations of Texas school districts.

Respectfully submitted,

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