



Commentary on HB 3646 and the State Budget

Our office has received many questions related to the interaction of using state stabilization funds under the federal American Recovery and Reinvestment Act (ARRA), the requirements to provide a salary increase in HB 3646, and some contingency language that is in both bills related to what happens if the US Department of Education denies, in part or in whole, the state's use of stabilization funds.

Texas used \$3.2 billion in federal ARRA stabilization funds to cover shortfalls in the foundation school program and fund HB 3646 (the additional \$1.9 billion that is available to school districts over the next biennium). HB 3646, in turn, contains a requirement that districts use the greater of \$80 per month or \$60 per WADA (after taking out related increases in social security costs and related increases in the cost of payments to TRS based on salaries above the statutory minimum) to fund a salary increase for teachers, full-time certified counselors, full-time school nurses, full-time librarians, and full-time speech pathologists. The bill further states that this increase in salary does not include "any amount the employee would have received for the 2009-10 or 2010-11 school year, as applicable, under the district's salary schedule for the 2008-09 school year, if that schedule had been in effect for the 2009-10 or 2010-11 school year, including any local supplement and any money representing a career ladder supplement the employee would have received in the 2009-10 or 2010-11 school year."

Because of the concern that districts would be required to give a second step increase in 2010-11 based on the above language, the legislature added language stating that the above language is not intended to require an increase in the second year of the biennium.

Do districts have to give a local step increase? If districts have a local salary schedule, then the above language indicates that districts would be required to provide employees to whom the pay increase applies a local step plus the \$800 or \$60 per WADA on top of that amount. A number of districts have indicated that the district does not have a local step salary schedule, but has a hiring schedule instead. In many cases, districts with hiring schedules do not typically provide employees a step increase annually, but rather adopt a new schedule each year. The question here is whether the hiring schedule used in many districts must be considered a step salary schedule for the purposes of determining the required pay increase included in HB 3646. Our understanding is that in prior years, most districts have treated hiring schedules as step schedules when similar language was passed by the Legislature, and this is consistent with interpretations from TASB when similar language was passed in 2006. Given current financial constraints, some districts may well be inclined to challenge the interpretation this year. We do not know of any instances in which this has been litigated, but districts choosing to use this interpretation should be prepared to face a legal challenge from employees believing they were entitled to a local step increase.

How does a district determine how much \$60 per WADA is worth per eligible staff member?

TEA has not yet provided guidance as to how this calculation should be made, but we would suggest a reasonable approach is to take your estimated 2009-10 WADA count multiplied by \$60 as the base. Subtract out any estimated cost increases related to social security or TRS above statutory minimum *that result from the required pay increase*, and divide by the estimated number of staff who are eligible for the pay that you expect to employ in 2009-10 (remember to include individuals funded through federal funds even though they may not be in your budget data). Compare this pay increase to \$80 per month. The greater amount is the level of salary increase that is required for each eligible employee.

What happens if the USDE determines that a mandatory salary increase is not an appropriate use of funds or that Texas' method of distributing funds was inappropriate? There was language in the ARRA as passed at the federal level stating that state spending rules do not apply to federal funds, but that federal rules apply instead. Consider the following from USDE guidance on stabilization funds:

III-D-4. Are the Education Stabilization funds that the Governor awards to LEAs through the State's primary funding formulae considered to be State funds, subject to the requirements that generally apply to funds awarded under those formulae?

No. State funding formulae are used solely as the mechanism to determine the amount of Education Stabilization funds that each LEA will receive. The Education Stabilization funds are Federal funds, and the ARRA, the Federal laws referenced in III-D-1, and other applicable Federal requirements (such as the OMB cost principles) govern their uses.

Given this language, it is possible that the USDE will rule that the state of Texas may not direct districts as to how to spend these federal funds. There is language in HB 3646 that provides for this possibility. The language states that the pay increase portions of HB 3646 are contingent on a determination by the commissioner that payment of wage and salary increases and associated benefits costs are an allowable use of federal funds received under the ARRA. The commissioner may not make such a determination until the state's application for ARRA stabilization funds has been approved by the USDE. The commissioner will not be able to rule on the use of these funds until guidance has been provided from USDE.

Since it may be some time before you know the status of this requirement, the bill contains language allowing districts to adopt employment contracts and agreements that are contingent on the commissioner's ruling (see section 95 of HB 3646).

A second and related question relates to what happens if the USDE rejects, in whole or in part, the state's distribution mechanism for the ARRA stabilization funds. In total, the legislature is using \$3.2 billion in stabilization funds to finance the FSP: \$1.34 billion for back filling the formulas and \$1.9 billion to finance HB 3646. HB 3646 provides for the contingency that the state's application is rejected. In the bill, the commissioner is directed to determine a percentage of each district's FSP entitlement that will flow as federal dollars. He is given the authority to require districts to apply for these funds. If the ARRA stabilization funds are determined to be unavailable, the commissioner is directed to reduce the total amount of funds to which a district or school is entitled under chapters 41 and 42 or other programs, according to the total percentage of each district's funds that will be federal

ARRA stabilization funds. What happens next is unclear. We assume that the state could resubmit an application that would meet federal requirements. Such a resubmission could require a different distribution mechanism (for example, by each district's share of statewide Title I allocations as described in ARRA). ARRA indicates that states can use stabilization funds to fill shortfalls in available state funding for primary funding formulas and that funds should go out based on Title I if no shortfalls exist. Shortfalls would be determined based on state funds directed to public education, not the combination of state and local funds.

Although there is uncertainty as districts approach budgets this year, the most reasonable approach to budgeting as we see it is to use the funding formulas passed in House Bill 3646 as the basis for revenue estimates. Further, although districts will be required to segregate a portion of FSP funds into a new federal ARRA fund at some point, it is not yet known what portion of the FSP will go into this fund nor what the rules will be associated with this fund. For now, we suggest continuing to use the general fund for preparation of budgets with budget amendments as necessary when the time comes.

With respect to salary schedules, there appear to be three options available:

1. Move forward with adopting a salary schedule that provides pay raise as directed in House Bill 3646. Districts that are in the position of wanting to provide the increase, regardless of the outcome of USDE determinations may well decide to adopt a salary schedule that meets the requirements of HB 3646 without waiting for rulings from TEA or USDE.
2. Adopt a salary schedule with a contingency clause that allows you to avoid the increase based on the outcome of the state's application to the USDE and the subsequent commissioner ruling. Districts that are under more severe financial pressure and that need a significant amount of flexible dollars to fill budget shortfalls may wish to adopt a contingent salary schedule and wait for further rulings from USDE and TEA. These districts should continue to budget for the pay increase, but the contingent schedule could leave them in the position of saving resources should the ruling indicate that the mandatory pay increase was inappropriate.
3. Delay the adoption of a salary schedule pending a ruling from TEA and the USDE. Districts could move forward with budget adoption (with the pay increase built into budget assumptions) but delay the adoption of the salary schedule in the hopes that TEA and USDE move quickly to provide specific guidance on the issue.