

MEMORANDUM

TO: Mark Hudson, Staff, Senate and House Interim Committees on Education

FROM: Sharon Shoemaker Walker, Staff Attorney,
Bureau of Legislative Research

DATE: June 4, 2001

Re: The final order issued in the *Lake View School District #25 of Phillips County et al. vs. Mike Huckabee, Governor of the State of Arkansas; et al.* litigation.

OVERVIEW

On May 25, 2001, Chancellor Collins Kilgore of the Chancery Court of Pulaski County Arkansas, Second Division found that the school funding system of the State of Arkansas is inequitable under the Arkansas Constitution. In brief, the court concluded that:

- Substantially equal educational opportunities must be provided to the children of Arkansas;
- Substantially equal education facilities are constitutionally mandated;
- The present funding system will not cure the inequities;
- The burden falls to the State to craft a remedy to allow every school district to have equal facilities;
- Expenditures, not revenues, should be used in calculating the Federal Range Ratio;
- Desegregation monies should not be included in the calculation of the Federal Range Ratio;
- It is not necessary to use the Weighted Average Daily Membership in calculating the Federal Range Ratio;
- Disparities in teacher salaries within the State are unconstitutional;
- Teacher salaries are inadequate as compared to competing markets;
- It is constitutional to use excess debt millages to satisfy the uniform tax rate;
- The method of counting mills to meet the uniform rate of tax used by the State complies with the language of the Arkansas Constitution;
- Preschool programs are necessary to an adequate education;
- The State should first determine what is necessary to provide an adequate education and then craft funding to achieve that aim;
- An adequacy study should be done;
- Evidence was insufficient to support that the State was willful or contemptuous in its failure to correct the constitutional shortcoming in funding for education;
- It is constitutionally mandatory that the State provide an adequate education for its students;
- Resolution of the inequities and inadequacies is left to the General Assembly; and

- Attorney's fees in the amount of \$9,338,035 were awarded to Plaintiffs.

The following is an in-depth summary of the court's order.

I. HISTORY

The case was originally filed in 1992. In 1994, Judge Annabel Imber ruled that the Arkansas funding system was inequitable under the Arkansas Constitution. At that time, the order was stayed for two years for the purpose of giving the State time to enact appropriate corrective legislation. The 1994 order was appealed but dismissed because it was not final. In 1998, the plaintiffs again pursued their case, which was dismissed as moot. That dismissal order was appealed to the Arkansas Supreme Court which ordered a compliance trial and a decision to be made by a chancery court with regard to whether disparities found under the 1994 order were corrected. In September of 2000, the trial took place and Chancellor Kilgore issued the order summarized here.

The plaintiffs had filed another lawsuit known as *Lake View II*, asserting that the State of Arkansas did not provide a constitutionally adequate education system. A non-suit was granted in that case. The court opined that the adequacy issue of *Lake View II* is before the court in this instance. On September 13, 2000 the court ordered that both the equity (funding) and adequacy issues would be heard in the compliance hearing. In keeping with the standard set forth by Judge Imber, the court in this case ruled strict scrutiny to be the standard by which compliance would be measured. The September 13, 2000 order placed the burden of going forward on the State.

II. CONTENTIONS OF THE PARTIES

Defendants' Position

Defendant's maintain that:

(1) Amendment 74 and subsequent legislation cured any inequities in distribution of available funds for public school education in Arkansas.

(2)(A) Use of revenues is more appropriate than use of expenditures in calculating the federal ratio.

(B) The weighted daily average membership is no longer applicable for purposes of calculating the federal range ratio.

(C) Inclusion of the desegregation monies in the federal range ratio calculation was ordered erroneously.

(3)(A) The State has provided an equitable funding formula.

(B) Disparities and shortcomings among individual school districts are accounted for by mismanagement at the local level.

Plaintiff's Position

The Plaintiff's maintain that:

(1) Grave constitutional inequities still exist.

(2) State defendants neglected their constitutional duty to provide sufficient capital improvements for various school districts resulting in deteriorated physical plants and inadequate funding to upgrade facilities.

Alma Intervenors

The Alma Intervenors maintain that Amendment 74 and subsequent legislation cured any inequities in distributing available funds for school education in Arkansas.

Bentonville-Rogers, Little Rock, and Pulaski County Intervenors

The Bentonville-Rogers, Little Rock, and Pulaski County Intervenors:

- (1) Agree with the defendants as to the equity of distribution of the funds.
- (2) Side with the plaintiffs as to the inadequacy of funding of the educational system.

III. FINDINGS OF FACT

Equity

(1) The federal range ratio, the coefficient of variation, and the GINI index of inequality all assist in the mathematic determination of whether variances in the distribution of funds by the State to the school districts are constitutionally acceptable.

(2) The federal range ratio can be satisfied by either the use of revenues provided to the districts by the State or amounts of actual expenditures of the school districts. The use of revenues in this formula shows the State to be in compliance with the 1994 order, whereas use of expenditures shows the State not to be in compliance. The Arkansas Supreme Court has specifically referred to pupil expenditures, and has said that Amendment 74 does not resolve the disparities. Correction of these disparities is at the heart of the 1994 order.

(3) The Constitution provides that the State is solely responsible for the education of its citizens. The State's duties will not end upon disbursement of revenues to school districts. Whether available funds are being efficiently applied to the education of the state's children is to be measured by an accurate accounting of expenditures.

(4) The federal range ratio may be calculated in terms of average daily attendance, average daily membership, or a weighted average daily membership. The 1994 order found that the federal range ratio should be analyzed using the weighted average daily membership.

(5) The 1995 legislation put a new school funding formula in place and eliminated the use of weights. Monies previously distributed by weight are now included in the more generalized equalization funding formula called categorical funding.

(6) In 1994, the court included desegregation money in analyzing the federal range ratio. Defendants argue this money should be excluded from the formula calculation, because it applies to costs unique to the recipients. The inclusion of that money in the calculation is detrimental to the three districts receiving it. Conversely, the plaintiffs maintain that the 1994 order requires desegregation money be used in the calculation, and that a failure to do so would result in a windfall in which all districts should be sharing.

Funding Simplified

(1) Schools are funded through three sources of revenue: federal funds, state monies, and local monies. Because local taxes are levied according to the value of local property, and the value of property varies from district to district, the amount of revenue available to various school districts differs.

(2) Amendment 74 established a uniform rate of ad valorem property taxes to be used solely for maintenance and operation of schools. Amendment 74 also provided for excess debt millages for maintenance and operations. Under the amendment school districts are allowed to obtain the uniform rate of 25 mills using debt service millages rather than millages set aside strictly for maintenance and operations.

(3) State equalization aid is used to equalize wealth among the school districts. The State then calculates base-level revenue, and then supplements the district with the difference between the local resource rate and the base-level revenue figure. Equalization aid is given to districts whose local resource rate is less than base-level revenue. Districts with revenues equal to or in excess of base-level revenue receive no state equalization aid. In fact, these districts may have to roll back millages, spending less on education than the district's patrons are willing to provide.

(4) Additional base funding from the State is used as a guarantee program that all school districts will have minimum state and local revenue. Following the elimination of the weighted average daily membership formula, special cost students were merged into state equalization aid.

(5) Categorical Funding is provided by the State for special student costs. Categorical funding is provided outside the [funding] formula.

(6) Presently three (3) methods are used to provide money for capital expenditures: Growth Facilities Funding, General Facilities Funding, and the Debt Service Funding Supplement. Still, some districts cannot afford to build new buildings, complete necessary repairs, or buy buses.

(7) The funding formulas (Federal Range Ration, Coefficient of Variation, and GINI Index of Inequality) assist in the analysis of disparities in funding for schools, school districts, and students. The formulas do not provide an exclusive way to determine whether or not the State has fulfilled its constitutional duty to provide its children an adequate education. Further, the formulas are also at variance with one another. The results of applying revenues to the funding formula conflict with the results of applying expenditures to the funding formula.

Comparison of Schools and School Districts

(1) The State suggested that mismanagement, not inequitable distributions of funds, are the cause of unconstitutional disparities in education. While there is some evidence of mismanagement at the local level, it is not sufficient to fully support the State's position. Nevertheless, the Arkansas Constitution places the ultimate burden on the State.

(2) Wealthy school districts are able to provide more educational resources than poor districts, and therefore students in Arkansas do not have an equal opportunity to learn. The court cites Lake View as an example of the limitations of a poor school district. The court also goes on to discuss the limitations of the Holly Grove School District, Barton Elementary in Phillips County and Lee County

Schools. To contrast, the court discusses the lower rate of poverty and numerous curriculum opportunities offered by the Fort Smith School District.

Capital Needs

(1) School buildings throughout the State need repair and updating, if not replacement. Some districts need additional buildings. Physical plant problems include poor or nonexistent heating and air conditioning systems, broken and missing windows, missing floor tiles, leaking roofs, asbestos problems, missing ceiling tiles, and walls in need of repair. These problems are particularly acute in Eastern Arkansas.

(2) The Debt Service Funding Supplement is intended to assist schools which have incurred debt intended to be paid through revenues from increased millages. Poor school districts have not been able to borrow because the voters would not approve the debt millages or because the property value of the district is so low that insufficient capital could be raised and may not qualify for the debt service funding supplement or the district would find the supplement insufficient to meet their capital requirements. Poor districts cannot incur the debt available to a richer district.

(3) The Revolving Loan Fund does not provide much help to some districts because the fund aid must be repaid out of next year's State aid with the result that any aid received from the fund will be withheld from its next year's State aid. Districts utilizing the fund may go into deeper debt. Money spent on refinancing debt and debt service is diverted from educating children.

(4) Using assessed value per student to determine the wealth of a district does not create a correlation between a district being above average in wealth and being above average in expenditures per student.

Adequacy

(1) The components of large-scale education resist standardization. Because of technological advances and ongoing efforts to improve our schools, the process of change is a permanent state making the search for fiscal solutions difficult.

(2) Students are staying in school longer thereby placing heavier burdens on available resources.

(3) Law demands more of the schools while the percentage of the State budget available for schools has decreased.

(4) Cultural and demographic changes, new technologies, and new standards for student achievement and accountability of teachers and administrators accelerate the demands and complications of public education.

Financial Adequacy

The State must provide adequate funding to allow a program to be developed that will produce the expected outcomes.

(1) The State bears the responsibility to ensure adequate funding for all students. It may not permit a local district to underfund its portion of that obligation.

(2) The Arkansas school funding formula is based on available revenue and is not related to achieving an adequate education.

(3) The court indicated that Act 917 of 1995 required that a committee be formed to produce a report to the Department of Education or Education Committees in the Senate and House on the question of adequacy.

(4) The purpose of the Arkansas Educational Excellence Trust Fund has been defeated. The fund was intended to be supplemental to State funding, not in place of it. However, the percentage of the State budget being devoted to education and subject to revenue stabilization has gone down since the creation of the Educational Excellence Trust Fund. The combination of the trust fund and the money allocated from the State roughly equal the percentage of state funding being spent prior to the creation of the trust fund.

(5) The Director of the Department of Education is responsible for recommending the funding formula allocation, the biennial operating budget, and the Department of Education budget to the Governor and the State Board for approval. The Governor's Office requested the Director to maintain the 1999 budget within a limited percentage increase over the previous biennium.

(6) An agency budget and appropriation are not the same thing. An appropriation is simply the authority to spend the money if it is available. An agency's budget is based on the available funding. It is possible to have appropriation authority to spend far in excess of the actual funding available. The Department of Education has the authority to loan school districts funds, primarily for buses and small construction projects.

(7) The only categorical funds going out for special education are to those districts that have high cost students as defined above. Money for special education is otherwise included in the equalization aid under the new formula.

(8) The poverty index funds in Arkansas assist only children in kindergarten and first grade. Children falling under the poverty index generally come from homes unable to provide opportunities such as internet access, ample reading and writing supplies, and parents who emphasize the importance of education and reading at an early age. A concentration of poverty index students placed in one classroom over taxes the teacher and puts a strain on available resources. These students typically require extraordinary resources to help them achieve proficiency.

Educational Adequacy

Adequacy is more than the question of how much money is spent on education. Whether a state's funding system is adequate is only part of the adequacy equation. The statistics entered into evidence in this case demonstrate that an Arkansas education is not adequate. Adequacy is determined by statistical performance.

ACTAAP

The Arkansas Comprehensive Testing and Accountability Program (ACTAAP) is the blueprint for education in Arkansas. There are four purposes of ACTAAP: improve student learning and classroom instruction; establish accountability; provide evaluation; and assist policymakers in decisions regarding how to accomplish the other three goals.

The Schools

A number of schools and school districts are not able to meet the standards necessary for adequacy.

State Efforts

(1) The appropriate way for a state to exercise its responsibilities is not through detailed spending control but close observation of student performance. The Standard Assurance Unit of the Department of Education is available for that role. It has three responsibilities: accreditation of schools, standards review, and assistance to schools in academic distress.

(2) If a school district is found to be not in compliance with one or more of the standards of accreditation, the district can suffer various consequences, ranging from citation, to probation, to a loss of accreditation. If a school loses accreditation after two consecutive years of probation, then it would be subject to a number of penalties including annexation, consolidation and other remedies.

(3) Act 917 of 1995 requires the Department of Education to establish rules and regulations to determine which schools could be identified in academic distress in phases one, two, or three.

(4) An individual academic improvement plan is required for all students who fail to perform at the proficiency level as measured by the Benchmark exams.

(5) ACTAAP has a unique feature known as a school performance report, or school report card, while measures individual schools and is reported publicly. Report cards issued by districts and by schools are part of the overall policy adopted to ensure a general, suitable, and efficient system of education. The report card will include the SAT-9 Norm Reference test scores, the Benchmark exams, a promotion rate, a school safety indicator, a percentage of teachers that are fully certified, a percentage with master's degrees, and one year's district data on the millage rate and average teacher salaries.

(6) The gap between proficiency and deficiency has increased each year as students who are not proficient in the fourth grade have progressed through the system. The State has a remarkably serious problem with student performance. At these levels, students will not be able to compete successfully with their peers.

Remediation

(1) The most recent statistics available indicate that the remediation rate for high school students entering college was 58% in either English or mathematics. This remediation rate reflects strictly seniors that graduated from high school. Further, it measures only those students who go on to colleges. It is a logical conclusion that those who graduate but do not go on to college will have an even greater deficiency in either math or English.

(2) Entering students or students already in school may also be in need of remediation in order to perform at grade level. The remediation rate of children in school directly relates to the children not being prepared upon entering the first grade.

(3) Students who need remediation are less likely to graduate from high school, go to college, become part of a skilled work force and are more likely to become engaged in criminal activity, enter the criminal justice system, and go to jail and prison where the State's annual cost to maintain the individual far exceeds

the cost to remediate the student and make him an economic and cultural asset to the State.

(4) Teachers are given no extra time to plan or extra pay for students who are behind when they reach their classrooms. The State does not provide any additional money or aides in order to help remediate those who need it.

(5) One-on-one instruction is an accepted means of remediating students.

(6) A student who is not proficient in one of the ACTAAP testing areas must be remediated. However, there is no additional help from the State to assist an individual child in need of remediation.

(7) The Department of Education offers additional teacher training to school districts as the districts' part of the Smart Start and Smart Step initiatives. However, there is no money provided to the districts to send the teachers to that training.

(8) The change in mandatory attendance laws which occurred in 1987 has had a significant impact on the schools. The fact that students are not allowed to drop out, resulted in an increased expense because more remediation is required for the students who at one time would have left the system. Each school district is required to have an alternative school for secondary students who just cannot adapt to the traditional high school.

Teacher Salaries

(1) Arkansas' entry level teachers' salaries are dead last among all of its eight bordering states. This underscores the State's labor market disadvantage in the competition for teaching talent. The State's average beginning salary is 82% of the national average. There is also competition between school districts for talent.

(2) The stricter licensing requirements and the increased expectation of teachers have not been accompanied by a concomitant increase in pay. There are as many as 12,000 certified teachers in Arkansas at present who are not teaching because of low pay.

(3) The differences that exist are so great that they work to destabilize the education system by driving qualified teachers away from districts where they are most needed. Schools and school districts with more disadvantaged students need more qualified teachers per student. However, the schools with the higher number of disadvantaged students are typically the schools which have the lower teacher salaries. The State Board of Education is in the process now of trying to advance a comprehensive strategy to attract, motivate and retain high caliber teachers to the teaching profession. That strategy demands increases in salaries. The working conditions in the schools such as lack of supplies and inadequate facilities also make recruiting and retaining teachers very difficult. Teachers' salaries are the most critical need Arkansas must to address. ACTAAP, Smart Start, and Smart Step all depend primarily on the classroom teacher to function. The challenges of finding ways of retaining quality teachers and attracting new teachers is going to take additional funding. The single most important factor necessary to ensure that the State's system of education meets the *Rose* factors is the availability of well educated, well motivated, and well compensated teachers.

IV. STATEMENT OF LAW

(1) The Arkansas Constitution requires that the State provide a “general, suitable and efficient system of free public schools equally available to all.” While Arkansas has not defined the terms “general, suitable, and efficient”, courts in other states have defined these terms.

(2) The Arkansas Constitution mandates the General Assembly provide for the support of the common schools and empowers school districts to levy an annual tax for the maintenance of schools.

(3) The General Assembly responded with Amendment 74, which allows for variances in funding to local school districts to raise additional funds to enhance the educational system within the school districts.

(4) It remains the responsibility of the State of Arkansas to provide for the support of public schools and to ensure that those schools provide an adequate, or general, suitable and efficient educational system.

(5) The 1994 order states that the Arkansas school funding system violates the Arkansas Constitution by failing to provide a “general, suitable and efficient system of free public schools.” Meeting the bare minimum requirements of educational offerings is not what the Arkansas Constitution demands and is not an equal education opportunity.

(6) Amendment 74 mandates that the uniform rate of tax shall not be an additional levy for maintenance and operation of the schools, but shall replace a portion of the existing rate of tax levied by each school district available for maintenance and operation of schools in the school district.

(7) In its statement, the court went on to define "base local revenue per student," "local revenue per student," and to provide the law regarding the Arkansas Comprehensive Testing, Assessment, and Accountability Program Act (ACTAAP) as it relates to the purpose of ACTAAP and the meaning of "remediation" in the context of this case.

V. CONCLUSIONS OF LAW

A. Equity

(1) The stark contrast in what curriculum various districts offer is a clear example of students being deprived of their rights of equal protection provided by the Arkansas Constitution. Under the Arkansas Constitution school districts throughout the State must provide substantially equal educational opportunities for their children. Denying these opportunities based solely on a school district’s location in a poorer part of the State is not a compelling reason for the State to abandon its constitutional obligations.

(2) Buildings properly equipped and suitable for instruction are critical and must be provided. The State cannot shift its responsibility to local school districts. The State has the burden of ensuring every school district has substantially equal facilities.

(3) School districts that are most endowed with resources have inherent advantages, whereas, schools on the bottom of the economic ladder struggle to achieve equality. The present funding system will not cure these inequities.

(4) The equal protection and opportunity guaranteed by the Arkansas Constitution have not been realized. School districts do not have an equal opportunity to build, renovate or maintain the necessary physical plant. To provide an equal opportunity, the State should form an adequate remedy allowing every school district to be on equal footing in regard to facilities, equipment, supplies, etc. Under the Arkansas Constitution school districts throughout the State must provide substantially equal buildings, properly equipped, and suitable for instruction of students.

(5) Expenditures, not revenues, should be used in calculating the Federal Range Ratio for the following reasons: (1) The Supreme Court used the term "expenditures" in expressing concern that "disparities in per pupil expenditures" be corrected; (2) An accurate accounting of expenditures is the best measure of whether available funds are being efficiently applied to education; and (3) The 1994 order specifies that expenditures and not revenues be used in the calculation.

(6) Desegregation money provided to the school districts in Pulaski County should not be included in calculating the Federal Range Ratio because these funds compensate the Pulaski County School Districts for expenses unique to them.

(7) The Plaintiffs were unable to overcome the presumption of constitutionality in the State's use of categorical funding. Therefore, it is not necessary to use Weighted Average Daily Membership in calculating the Federal Range Ratio.

(8) The teachers' salary disparity within the State is unconstitutional. The disparity is the result of local school district discretion and bears no rational relation to the State's interest in providing a general, suitable and efficient education for our children. Moreover, the salary disparities act to destabilize local districts that cannot or will not pay competitive salaries and are unable to hire and retain quality teachers.

(9) Amendment 74 and Article 2, §§ 2, 3 and 18 have not been violated by allowing school districts to use excess debt millages to satisfy the uniform tax rate of 25 mills. The requirement that millages dedicated to the retirement of debt be equal to 150% of the indebtedness virtually always results in excess debt millages. This is represented in the bond indenture, and, therefore, the voters must be presumed to know that the excess millages are to be available for maintenance and operations.

(10) Plaintiffs complain that this use of excess debt service mills does not satisfy Amendment 74 and that the amendment requires each school district to levy twenty-five mills, independent of any other mills, exclusively for maintenance and operations. Amendment 74(b)(2) states in part, "Except as provided in this subsection the uniform rate of tax shall not be an additional levy for maintenance and operation of the schools but shall replace a portion of the existing rate of tax levied by each school district available for maintenance and operation of schools." The Plaintiffs argue for a result that could easily have been obtained by more specific language in the amendment. However, no such language is present, and therefore, the method of counting mills to meet the uniform rate of tax used by the State complies with the language of the Arkansas Constitution.

B. Adequacy

(1) Teachers' salaries in this State are wholly inadequate under the *Rose* standards to attract and maintain qualified teachers to provide our students with the education that the Arkansas Constitution requires and as articulated in detail in *Rose* and the 1994 order. The requirements of ACTAAP cannot be met without high quality personnel, but there is no money available to hire them. No deficiency in our education system is in more urgent need of attention than teachers' salaries.

(2) To provide our children with an adequate education as required by the Arkansas Constitution and ACTAAP, the State must provide pre-school programs allowing Arkansas' children to compete academically with their peers. The urgency of this need equals that of the deficiency in teacher salaries.

(3) Only an adequate education system available to all will be equitable. The State funds its educational system by first determining how much money is available and then deciding how to divide it. The State does not first determine what is required to provide an adequate education and then craft funding to meet the need. The court concluded an adequacy study to be necessary, but did not specify who is to conduct the study or when. It appears this is a matter for the General Assembly to address.

C. Contempt

The Court declined Plaintiffs' request that the State Defendants be held in contempt of court for failure to comply with the terms of the 1994 order. The State attempted through legislation to ensure a more equitable funding of the schools. These efforts fail to correct all of the constitutional shortcomings but there is insufficient evidence to indicating that the failure was willful or contemptuous.

VI. REMEDY

(1) The court recognized the exceptional intractability and complexity of the problem at hand. There is a shortage of resources. Nonetheless, the court finds that an adequate education for children is necessary. It is required by Arkansas Constitution.

(2) The problem needs immediate attention. The courts should only be resorted to when all else has failed. The court left the issues to the legislature for the time being.

VII. ATTORNEYS' FEES

(1) The Supreme Court, in its March 2, 2000, Order in *Lake View*, held that this court erred in denying attorneys' fees to the Plaintiffs. The defense of sovereign immunity is barred by the principle of waiver. The fee request was based on the benefit derived by the State and all members of the Class from new legislation passed since the 1994 order. In this case, the attorneys agreed that a common fund of \$130,000,000 for school districts was created through new legislation resulting from the Plaintiffs' lawyers' efforts.

(2) Once the court determines that a common fund or benefit has been created, the next step is to determine reasonable attorneys' fees. Taking into consideration the circumstances of the case, the expert testimony regarding attorneys' fees in this case, the affidavits filed by the Plaintiffs' lawyers, the responsive brief filed by the State Defendants, the contingency nature of the case, and the factors as set forth by the Fifth Circuit and the Arkansas Supreme Court, and for the Plaintiffs' efforts in creating a substantial benefit for the State as well as the common fund of \$130,000,000, the court ordered that the Plaintiffs' lawyers be awarded \$8,500,000 for the liability phase of this lawsuit. (This amount is approximately 6.5% of the \$130,000,000 common fund which is quite low compared to other percentage fee cases.)

(3) The Plaintiffs' lawyers submitted affidavits stating the hours worked on this case between June 19, 2000 and November 1, 2000. Combined, the attorneys worked 2,086.90 hours during that time. However, no hourly rate was stated. The court allowed an hourly rate of \$150.00 for work between February, 1998 and November 1, 2000. The court awarded \$838,035 for the time period beginning February, 1998 through November 1, 2000.

(4) Plaintiffs' lawyers were awarded total attorneys' fees in the amount of \$9,338,035 with, however, no additional award for costs or fees for the Plaintiffs' Solicitor.