

CAUSE NO. D-1-GN-11-003130

TEXAS TAXPAYER & STUDENT
FAIRNESS COALITION, *et al.*,

Plaintiffs,

VS.

MICHAEL WILLIAMS, TEXAS
COMMISSIONER OF EDUCATION, *et.al.*,

Defendants

Consolidated Case:

FORT BEND INDEPENDENT SCHOOL
DISTRICT, *et al.*,

Plaintiffs,

VS.

MICHAEL WILLIAMS, TEXAS
COMMISSIONER OF EDUCATION, *et. al.*,

Defendants.

IN THE DISTRICT COURT OF

TRAVIS COUNTY, TEXAS

200TH JUDICIAL DISTRICT

THE ISD PLAINTIFFS' MOTION TO TAKE JUDICIAL NOTICE

The Fort Bend ISD Plaintiffs, the Texas Taxpayer and Student Fairness Coalition Plaintiffs, the Edgewood Plaintiffs, and the Calhoun County ISD Plaintiffs (the "ISD Plaintiffs") hereby request that the Court take judicial notice of the legislative history of (1) the 2006 legislation that created the structure of the current school finance system, (2) the 2011 budget cuts, and (3) the recent 2013 legislation regarding the accountability system and admit them as exhibits to be included in the appellate record.

I.

Standard for Taking Judicial Notice of Legislative History

The Court may use its discretion to take notice of legislative facts. *In re Graves*, 217 S.W.3d 744, 751 n.6 (Tex. App.—Waco 2007, orig. proceeding). Legislative facts are "subject

to judicial notice but are not governed by Rule 201.” *In re Sigmar*, 270 S.W.3d 289, 302 (Tex. App.—Waco 2008, orig. proceeding). Whereas adjudicative facts are those facts that would go to a jury in a jury trial and which are normally proved through the introduction of evidence, legislative facts are those which have relevance to legal reasoning and the lawmaking process and “are not normally the objects of evidentiary proof.” *In re Graves*, 217 S.W.3d at 750 (quotation omitted); Advisory Committee’s Note to Federal Rule 201(a), 1 Tex. Prac., Texas Rules Of Evidence § 201.2 at 59-61 (3d ed. 2002); *cf. First Nat. Bank of Amarillo v. Jarnigan*, 794 S.W.2d 54, 61 (Tex. App.—Amarillo 1990, writ denied) (holding that “adjudicative facts are those facts concerning the immediate parties, who did what, where, when, how, and with what motive or intent.”). In other words, legislative facts “help the tribunal determine the content of the law and of policy and help the tribunal to exercise its judgment or discretion in determining what course of action to take. Legislative facts are ordinarily general and do not concern the immediate parties.” 1 Tex. Prac., Texas Rules of Evidence § 201.2 at 59-61 (3d ed. 2002); *see also Aguirre v. State*, 948 S.W.2d 377, 380 (Tex. App.—Houston [14th Dist.] 1997, pet. ref’d). “[I]ndisputability is not required to justify judicial notice” of legislative facts. *In re Graves*, 217 S.W.3d at 750 (quotation omitted).

“Legislative history includes the enactment history of a statute, that is, actions taken and statements made during legislative consideration.” *Lee v. Mitchell*, 23 S.W.3d 209, 213 (Tex. App.—Dallas 2000, pet. denied). Legislative history falls plainly into the definition of legislative facts because it serves to show the context for the lawmaking process. Accordingly, Texas courts have taken judicial notice of the legislative history of a statute. *See, e.g., Evans v. Am. Publ’g Co.*, 13 S.W.2d 358, 361 (1929) (taking judicial notice of history surrounding enactment of venue statute governing where libel or slander suit against newspaper may be

brought); *Boone v. Pierce*, 218 S.W.2d 347, 348 (Tex. Civ. App.—Waco 1949, writ ref'd) (taking judicial notice of historical context and purpose of Federal Emergency Farm Mortgage Act of 1933).¹

Legislative history is not subject to the requirements of Rule 201 which, on its face, applies only to adjudicative facts. *See* Tex. R. Evid. 201(a); *In re Sigmar*, 270 S.W.3d at 302 (“Matters of legislative fact *or of other non-adjudicative fact* are subject to judicial notice but are not governed by rule of evidence governing judicial notice of adjudicative facts.”); *Jarnigan*, 794 S.W.2d at 61 (“Texas Rule 201, as well as Federal Rule of Evidence 201, upon which it is based, is expressly limited to adjudicative facts.”). Indeed, legislative history may be considered by a Court at any point in the process. *Cf. City of Fort Worth v. Harty*, 862 S.W.2d 776, 778 (Tex. App.—Fort Worth 1993, writ denied) (“We, as an appellate court, have the authority to examine legislative history of a relevant code provision even if it has not been presented to the trial court.”).

II.

The Court Should Take Judicial Notice of, or Otherwise Consider, the Attached Legislative History

A. 2006 Legislative Session

The basic structure of the current school finance system was passed in 2006 through House Bill 1, which compressed property tax rates and established the TRE system, and by House Bill 3, which revised the franchise tax to pay for the property tax reduction. Acts 2006, 79th 3rd C.S., ch. 5, 2006 Gen. Laws 45; Acts 2006, 79th 3rd C.S., ch. 1 2006 Gen Laws 1.

¹ Furthermore, when construing a law or determining legislative intent, the Court may consult the legislative history of a law and consider the legislation’s purpose, the circumstances under which it was enacted, and former statutory provisions on the same or similar subjects. Tex. Gov’t Code § 311.023; *see also*; *Kish v. Van Note*, 692 S.W.2d 463, 467 (Tex. 1985) (noting that the court may look to legislative history to determine the content, scope, and meaning of the law); *Boeing Co. v. Abbott*, 03-10-00411-CV, 2012 WL 753170 (Tex. App.—Austin Mar. 9, 2012, pet. filed). The Court should consider the legislative history of a law when asked to do so by a party. *Ector County v. Hollmann*, 901 S.W.2d 687, 688 (Tex. App.—El Paso 1995, no writ); *City of Fort Worth v. Harty*, 862 S.W.2d 776, 778 (Tex. App.—Fort Worth 1993, writ denied).

Much of the legislative history of House Bill 1 was previously admitted as Exhibits 6393 through 6396. The additional documents for which ISD Plaintiffs now seek judicial notice include statements of legislative intent that were recorded in the House Journal (attached hereto as Exhibits 6520 and 6521), and the official Tax/Fee Equity Note (Exhibit 6522) and the Equalized Education Funding Impact Statement (Exhibit 6523) created by the Legislative Budget Board (“LBB”).²

House Bill 3 from the same legislative session revised the State’s franchise tax in order to broaden its base and (partially) cover the cost of the property tax reduction contained in House Bill 1. The ISD Plaintiffs request the Court to take judicial notice of the bill itself (Exhibit 6524), the bill analysis prepared by the Senate Research Center (Exhibit 6525), the bill analysis prepared by the House Research Organization (Exhibit 6526), the Fiscal Note prepared by the LBB (Exhibit 6527), the Tax/Fee Equity Note prepared by the LBB (Exhibit 6528), and the enrolled bill summary prepared by the Texas Legislative Counsel (Exhibit 6529).

As the Court considers whether the State has met its constitutional obligation to make suitable provision for the support and maintenance of an efficient system of public free schools, it must ask whether the Legislative actions establishing that system were arbitrary—in other words, whether the Legislature’s actions were “taken without reference to guiding rules or principles.” *Neeley v. West Orange-Cove Consol. Indep. Sch. Dist.*, 176 S.W.3d 746, 784 (Tex. 2005). Looking to the legislative history of the bills that established the basic structure of the school finance system will aid the Court in that analysis.

² The Calhoun County Plaintiffs do not join in the request to take judicial notice of Exhibits 6523, but do not oppose the request.

B. 2011 Legislative Session

During the 2011 Session, the Legislature made substantial cuts to public school funding system, and as a result had to modify the statutory formulas established in House Bill 1 from 2006. Senate Finance Committee Chairman and President Pro Tempore of the Senate, Senator Steve Ogden, spoke to the Senate near the beginning of the session. His speech, which discusses the budget situation and the school finance system, provides context for the legislative intent and purpose in passing the related legislation and should be considered by the Court (Exhibit 6530).

C. 2013 Legislative Session

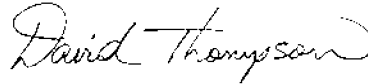
During the 2013 Session, the Legislature passed House Bill 5, which makes changes to graduation requirements and options, state standardized testing requirements, and the state accountability system. Acts 2013, 83rd R.S., ch. 241. The ISD Plaintiffs request the Court to take judicial notice of the bill itself (Exhibit 6531), the bill analysis prepared by the House Research Organization (Exhibit 6532), the Fiscal Note prepared by the LBB (Exhibit 6533), and the attached statements of intent that were recorded in the House Journal (Exhibits 6534 and 6535).

**III.
Prayer**

For the reasons state above, the ISD Plaintiffs respectfully request that the Court take judicial notice of the attached legislative history and admit it as exhibits 6520 through 6535.

Respectfully submitted,

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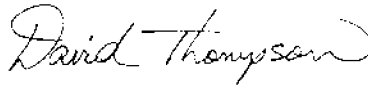
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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing document has been forwarded on this 1st Day of October, 2013 to counsel of record in accordance with Rule 21a of the Texas Rules of Civil Procedure and the Parties' Rule 11 Agreement, as follows:



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HB 5 - POINT OF ORDER

Representative Edwards raised a point of order against further consideration of **HB 5** under Rule 11, Section 2 and Rule 8, Section 3 of the House Rules and Article III, Section 30 of the Texas Constitution on the grounds that the senate amendments are not germane, they change the original purpose of the bill, and the bill contains more than one subject.

The speaker sustained the point of order, speaking as follows:

Representative Edwards raises a point of order against further consideration of **HB 5** on the following grounds: (1) that the senate amendment contains language that is not germane to the bill and therefore violates Rule 11, Section 2 of the House Rules; and (2) that the senate amendment violates Article III Section 30, of the Texas Constitution and Rule 8, Section 3, of the House Rules.

These are the same points of order that the house already sustained on **HB 2** six days ago. All three points of order will be sustained on the same grounds and the same rationale that the points of order were sustained on **HB 2** six days ago (79 H.J. 3 C.S. 235 (2006)).

The points of order are sustained. Accordingly, the chair instructs the chief clerk to return **HB 5** to the senate with a message to that effect.

The ruling precluded further consideration of **HB 5**.

**HB 1 - HOUSE CONCURS IN SENATE AMENDMENTS
TEXT OF SENATE AMENDMENTS**

Representative Chisum called up with senate amendments for consideration at this time,

HB 1, A bill to be entitled An Act relating to public school finance, property tax relief, and related matters; making an appropriation.

HB 1 - STATEMENT OF LEGISLATIVE INTENT

REPRESENTATIVE CASTEEL: Mr. Chisum, will you help me with just a couple things? I'm trying to be supportive. Couple of questions. Always been interested in teacher pay—

REPRESENTATIVE CHISUM: Absolutely.

CASTEEL: And are we being up front when we say we're passing a \$2,000 pay raise when actually \$500 of that is already in the mix for insurance reimbursement. Are we actually doing \$1,500 plus the \$500 or are we doing \$2,000 plus the \$500?

CHISUM: You are correct in the last, it's \$2,000 plus the \$500, which in fact could be used as pay raise or set aside as health insurance and those sort of things.

CASTEEL: So it's \$2,000 plus \$500?

CHISUM: Absolutely.

CASTEEL: And in addition, when the \$500 is back on the table for the paraprofessionals and the other people who work in education?

EXHIBIT
6520

CHISUM: Absolutely, that money is still available.

CASTEEL: Alright, now then, the next question I have is—I've been trying to understand—I thought and I want to believe this that we are actually going to do a true property tax reduction for our folks at home. I mean, we promised that, we've been talking about it the two terms I've been here.

CHISUM: Absolutely.

CASTEEL: Okay, so I'm thinking I want to send home a steak, not a piece of bacon, a steak. So here's my question we're telling Mom and Pop Casteel, "We're going to drive your property tax down, we hope, to a dollar."?

CHISUM: That's correct.

CASTEEL: Alright, and we're going to pass these bills: the governor's plan, the business plan, three, the cigarette tax, maybe or maybe not five, and the liar's affidavit, four. And from those funds, we're going to fund your property tax relief?

CHISUM: That is correct.

CASTEEL: So I'm excited. My left pocket is full. And my family is going to benefit, so I'm happy. But then I look and see in the year 2008, we're somewhere between \$4.2 billion and \$5 billion short and in 2009 it may be \$5.2 billion. In 2010, it may be 10, so now I'm thinking, "Daddy Casteel, you didn't get a steak, you got a piece of bacon. And your left pocket was excitedly full and now it's been jerked out of your right pocket." Now make me feel like my steak is staying with me.

CHISUM: You know, we have a surplus, which was added this morning, and the economy is extremely strong and I know about those fiscal notes.

CASTEEL: I lived through the 80s and I know how the economy can flip, but let's assume the surplus stays the same. We're still short. I think if you look at the numbers if you could, and I understand that the comptroller cannot certify in '08 or '09, you can't do that because it's a guess. But let's play like she could. So if she took the current surplus, and she took what we anticipate from the new business tax, the cigarette tax, the liar's affidavit tax, you're still going to be short. You're still going to be short, unless you're banking on the fact that we're going to win the lottery and in fact the surplus will just be humongous, if it's not—I mean, I'm not going to be here, so I'm not worried. But I'm worried as Mommy and Daddy Casteel because I'll be at home paying, I'll be sending my steak back, I want to make sure that you don't come back and say, "Whoops, made a mistake. We've got to raise you're taxes." Maybe it's a sales tax, maybe it's an income tax, but we have to come back because we've promised you this and we've got to deliver it in these years. Now make me feel better.

CHISUM: Alright, the comptroller actually estimated the price of oil at \$35. Do you know how long it's been since we've had \$35 oil? You've got a reasonable thought about what that is to the State of Texas? There's no evidence that that's going to stop. There's no evidence that the Barnett Shale, which is going to contribute \$3 billion unanticipated to that—it will get even larger.

CASTEEL: I hope you are right, but if ethanol or if some of these price controls or some of these other things that people want to do because they are mad at the oil industry happen, you're still banking on what's coming down.

CHISUM: And I have a lot of confidence in this economic engine in the State of Texas and the fact that we're going to settle for a long time this issue with school finance. And we have reconstructed our business tax, and I think that we're on good ground here, and if I didn't—you know me better than that. I would not stand down here and present this bill.

CASTEEL: Warren, I don't doubt you at all, but what I worry about is the fact that we make promises and then we have to take them back, and I'm telling you it's going to happen based on the figures at this point. So my concern is, when we do this, are we going to be up front with the tax payer? And say it probably will be back in '07 with a tacit sales tax or in '09 will some other kind of tax because this is not going to generate the amount of money that it's going to take—we're going to be \$3, \$4, \$5 billion short each year unless what you and I hope, oil sells for \$200 a barrel, and we get a lot of money. You, me, and the steak.

CHISUM: I agree, Carter, and you know we would not be truthful to the people of Texas if we didn't express that we are concerned about that, but we have some very good economists that worked on this business tax bill. We're bringing a huge number of people back into paying the tax and you know that as well as anybody.

CASTEEL: But you know what? You going to take some people out. I can already tell you that there's law industries—or lawyers in this state—that are in incorporations are going to go into general partnerships. So while you're thinking you're closing some loopholes, you've opened up some more. But I agree. I just want to make sure that we're not getting ourselves in a box, again, by telling the public, "We're going to a dollar, rest assured, you'll never have another problem again." When we're really going to come back with a new tax down the road in order to fund this because we're going to be short.

CHISUM: I don't believe that that's going to happen, Carter. I believe that we will fund this and we will make it work.

CASTEEL: Okay, well I hope you're right, and I don't mean to be a naysayer, but I don't think it's going to happen. Now let me ask you this question, let's assume that—

CHISUM: Carter, we may not because you may not be here to help us and I know you—

CASTEEL: Yeah, well, I'll be at home. I'll be helping you at home. Let me ask you this question, what happens to the needs of—and I'm interested in educators, I'll just use them—what happens to the needs of education two years from now? What happens to the needs in CHIP, or Medicaid, or jails, what happens to them? And I say the reason I ask that is because I don't believe or it doesn't appear to

me, and you can correct me if I'm wrong, that we're not too interested in what educators have to say to us, we're not interested. So how can you assure me that we're going to be able to have the funds to take care of education?

CHISUM: Well, Carter, and maybe we can get Mr. Pitts up here to talk about it, you know if you just take the worst look at this you know the big driver that's driving our budget is healthcare and this doesn't solve that. It doesn't have anything to do with that, but let me tell you we will answer those things, and we will do it in a timely manner, and we will do it because our economy is strong and we're going to do okay. And education will always be in the forefront. And if we have to do something to make sure education stays at the front, I guarantee this house and the senate will make that happen.

CASTEEL: Okay, my question is if you're \$3, \$4, to \$5 billion short a year and you just told me that health is a driving force as well as some other issues, where do those funds come from? Are they coming from the surplus as well?

CHISUM: Well, they're going to come a lot from some of the manners that we've put in through the **HB 2219**. You know we're going to be working on and this rising cost of healthcare is going to rise a lot faster—

CASTEEL: You will agree with me, in the State of Texas we can only spend what we've got. We're not Washington DC.

CHISUM: Absolutely, we can only spend what we've got. And we don't want to do anything differently.

CASTEEL: Are we going to get all this money to do all this stuff without going back to Mom and Pop Casteel and say, "you have to now take money out of that left pocket that we gave you and start funding again through tax increases?" Are you setting yourself up for another tax increase?

CHISUM: Carter, I don't think so. And let me tell you, we're talking about property taxes here and we're not going to go back and redo—we're going to hold that property tax down because we want your mom and pop to stay in their home. We don't want to tax them out of their home.

CASTEEL: But now remember, Mom and Pop Casteel need to go to the store. I've got to buy shoes. So, you may tell me, Carter, your property tax at home is good, but when I go it's my sales tax or some other kind of tax that we've dreamed up here. Then we're going to be back telling the public, "Well, we fixed the property tax, now we've got to go fix this tax." I think we're playing a shell game and it disturbs me. I hope we're not. You're telling me we're not.

CHISUM: No, I'm not telling you we're not. You know exactly that—you are a very intelligent lady and that's the reason we're going to miss you because you point those things out. It is not going to be easy, Carter. It is not going to be easy.

CASTEEL: Well here's all I'm asking. Are we willing, as a body, to tell our people at home we are attempting to help you with property tax, but get ready sister because we'll be back for more?

CHISUM: Absolutely.

CASTEEL: Absolutely. So you're admitting that we'll be back for more?

CHISUM: Carter, it's going to cost more to operate government tomorrow than it does today and we're well aware of that.

(Eiland in the chair)

HB 1 - STATEMENT OF LEGISLATIVE INTENT

REPRESENTATIVE MADDEN: First of all, does Article V in any way take away from the State Board of Education's authority or power to approve and adopt curriculum?

CHISUM: Absolutely not.

MADDEN: If the elected State Board of Education disagrees with the findings of the vertical alignment teams or disagrees with what the commissioners have approved, can the State Board of Education reject their findings and not approve and adopt what the commissioners have approved?

CHISUM: Certainly they can. We're not taking that ability away from what they want to say and they can—so, yes you are right.

MADDEN: I certainly read that in the legislation and in the language there and certainly agree with you. Also, if the State Board of Education disagrees with portions of the commissioner's approved report, can that state board only adopt portions of the report they agree with and not adopt those portions they may disagree with?

CHISUM: I hope you're not asking me about their parliamentary procedure over there where they can divide the question on a report and only adopt parts of that. I would think that would be the case, because you wouldn't want them to adopt something that they didn't agree with, but if you're asking me their parliamentary procedure that they operate their state board then I have to tell you, I'm not aware of that. But it would be my answer to your question, I think yes, they can.

MADDEN: Okay, and it's not our position here to deal with their parliamentary procedures. That is their responsibility, that they have whatever rules of the state board.

CHISUM: That is correct.

REMARKS ORDERED PRINTED

Representative Madden moved to print remarks between Representative Chisum and Representative Madden.

The motion prevailed.

(Speaker in the chair)

REMARKS ORDERED PRINTED

Representative Leibowitz moved to print remarks between Representative Casteel and Representative Chisum.

The motion prevailed.

REMARKS ORDERED PRINTED

Representative Eiland moved to print remarks between Representative Chisum and Representative Eiland.

The motion prevailed.

HB 1 - STATEMENT OF LEGISLATIVE INTENT

REPRESENTATIVE MCREYNOLDS: Warren, strictly for the record, so that we can know intent beyond a question of a doubt and there's no doubt in anybody's mind—let me ask you three questions, please. Is it true that the basic allotment, the guaranteed yield, and the equalized wealth level are all set at the 88th percentile at wealth under this \$1.33?

CHISUM: That is correct in this bill.

MCREYNOLDS: The next applies to the meaningful discretion tier—the next two. Is it true that the first four cents in '07 and '08, and the two cents in '09, in the meaningful discretion tier, there is no recapture and the equalized level is linked to the wealth level of the Austin Independent School District?

CHISUM: That's correct, and that was six pennies in total, not four twice.

MCREYNOLDS: And the last question, Warren, strictly for the record, is it true for the last 11 cents of the meaningful discretion tier that the guaranteed yield is at \$31.95 and the equalized wealth level is a little over \$319,000?

CHISUM: That's exactly right, and that's in this enrichment tier of this bill in that print.

REMARKS ORDERED PRINTED

Representative McReynolds moved to print remarks between Representative Chisum and Representative McReynolds.

The motion prevailed.

The motion to concur in the senate amendments to **HB 1** prevailed by (Record 70): 136 Yeas, 8 Nays, 0 Present, not voting.

Yeas — Mr. Speaker(C); Allen, A.; Alonzo; Anchia; Anderson; Bailey; Berman; Blake; Bohac; Bonnen; Branch; Brown, B.; Brown, F.; Callegari; Campbell; Casteel; Castro; Chavez; Chisum; Cook, B.; Cook, R.; Corte, V.; Crabb; Crownover; Davis, J.; Davis, Y.; Dawson; Delisi; Deshotel; Driver; Dukes; Dunnam; Dutton; Edwards; Eiland; Eissler; Elkins; England; Escobar; Farabee; Flores; Flynn; Frost; Gallego; Gattis; Geren; Giddings; Gonzales; Gonzalez Toureilles; Goodman; Goolsby; Griggs; Grusendorf; Guillen; Haggerty; Hamilton; Hamric; Hardcastle; Harper-Brown; Hartnett; Hegar; Hernandez; Herrero; Hilderbran; Hill; Hochberg; Hodge; Homer; Hope; Hopson; Howard, C.; Howard, D.; Hughes; Hunter; Hupp; Isett, C.N.; Jackson; Jones, D.; Jones, J.; Keel; Keffer, B.; Keffer, J.; King, P.; King, T.; Kolkhorst; Krusee; Kuempel; Laney; Laubenberg; Leibowitz; Luna; Madden; Martinez; Martinez Fischer; McCall; McClendon; McReynolds; Menendez; Merritt; Miller; Morrison; Mowery; Naishtat; Nixon; Orr; Otto; Paxton; Peña; Pickett; Pitts; Puente;

Quintanilla; Raymond; Reyna; Riddle; Ritter; Rose; Seaman; Smith, T.; Smith, W.; Smithee; Solomons; Strama; Straus; Swinford; Talton; Taylor; Thompson; Truitt; Turner; Van Arsdale; Vo; West; Wong; Woolley; Zedler.

Nays — Burnam; Coleman; Farrar; Noriega, R.; Oliveira; Rodriguez; Veasey; Villarreal.

Absent, Excused — Denny; Moreno, P.; Olivo; Phillips; Solis.

Absent — Uresti.

STATEMENT OF VOTE

When Record No. 70 was taken, I was temporarily out of the house chamber. I would have voted yes.

Uresti

REASONS FOR VOTE

I initially voted for **HB 1** in the house because it was a simple bill that achieved the goal of this special session: to reform the school finance system and provide school district property tax relief. The bill that came back from the senate was dramatically different, combining property tax relief with a hodge-podge of education reforms.

While I am glad that teachers, counselors, nurses, and librarians will receive a \$2,000 pay raise, I consider that only a good start toward paying them what they deserve. All education employees, including support personnel, need and deserve a minimum of a \$3,000 salary increase and a restoration of the \$1,000 health care stipend. Our teachers have not received a pay raise from the state since 1999. Even with this \$2,000 pay raise, the average Texas teacher's salary will still lag nearly \$5,000 under the national average. Without better compensation, teachers will continue to leave the profession in droves. According to a study done by Sam Houston State University, 46 percent of Texas teachers are considering leaving the profession with lack of compensation being a major reason.

I am also concerned with other aspects of this bill including:

(1) The Williams amendment added in the senate, which will likely require much of the available revenue in the next biennium and in the future to pay for property tax cuts. This could threaten the legislature's ability to fund education, health care, transportation, public safety, and other pressing state needs in the future.

(2) An incentive pay program that will further emphasize the importance of standardized test taking in schools. Our teachers' priority should be teaching our children, not teaching our children how to take tests.

(3) The continuing erosion of local control with the mandatory school starting date and the low threshold established for allowing the commissioner of education to order the private takeover of public schools.

Despite these concerns, I feel it is important that the legislature meet its duty by fulfilling the property tax relief requirements of the supreme court order. And, although not as much as I wanted, the bill does improve teacher compensation. That is why I voted to concur in senate amendments to **HB 1**.

Leibowitz

I voted against concurrence with senate amendments to **HB 1** because the bill could force future tax increases, especially sales taxes, which disproportionately hurt Texas' poor citizens, or cut governmental services to the same poor, needy Texans. Either way, **HB 1** will have a detrimental impact.

If the spending provisions of the bill are maintained, Texas will have to come up with more than \$5 billion per year in the next biennium. Current revenue projections for the next two years are nowhere near sufficient to cover that cost. Clearly, the next legislature will have to take significant action—either tax increases or large budget cuts—to resolve the shortfall.

Additionally, **HB 1** does much less than it could have to help Texas teachers. While the bill does provide a pay raise, once adjusted for inflation, Texas teachers still earn less than they did in 2000. Consequently, teacher pay in Texas falls further behind the national average. The money in **HB 1** that is dedicated to unproven, and poorly outlined, incentives could have been used to provide another \$1,000 per teacher.

For these reasons, and other, I voted against concurrence of **HB 1**.

Oliveira

Senate Committee Substitute

CSHB 1, relating to public school finance, property tax relief, public school accountability and programs, and related matters; making an appropriation.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

ARTICLE 1. PUBLIC SCHOOL FINANCE AND PROPERTY TAX RELIEF

SECTION 1.01. Section 41.002(a), Education Code, is amended to read as follows:

(a) A school district may not have a wealth per student that exceeds:

(1) the wealth per student that generates the amount of maintenance and operations tax revenue available to a district at the 88th percentile in wealth per student, for the district's maintenance and operations tax effort equal to or less than the rate equal to the sum of the product of the state compression percentage, as determined under Section 42.2516, multiplied by \$1.50;

(2) the wealth per student that generates the amount of maintenance and operations tax revenue available to a school district at the percentile of wealth per student corresponding to the amount of revenue per student per cent of tax effort under Section 42.302(a-1)(2) for which state funds are appropriated for that school year, for the district's maintenance and operations tax effort equal to or less than the rate equal to the sum of the product of the state compression percentage, as determined under Section 42.2516, multiplied by \$1.50, and \$0.04, subject to Section 41.093(b-1); or

LEGISLATIVE BUDGET BOARD

Austin, Texas

TAX/FEE EQUITY NOTE

79TH LEGISLATURE 3rd CALLED SESSION - 2006

May 11, 2006

TO: Honorable Tom Craddick, Speaker of the House, House of Representatives

FROM: John S. O'Brien, Deputy Director, Legislative Budget Board

IN RE: **HB1** by Chisum (Relating to public school finance, property tax relief, public school accountability and programs, and related matters; making an appropriation.), **As Passed 2nd House**

Table 1**House Bill 1, As Passed 2nd House: Summary of Elements**

This analysis is for taxes effective in fiscal 2008.

Revenue Changes

- Reduce school district property maintenance and operations tax rate to \$1.00.
- Allow limited local enrichment in excess of the reduced property tax rate.

Dollar Value of Revenue Changes in Fiscal 2008

- \$5,823.2 million net property tax reduction; \$6,587.7 million decrease from the rate reduction, \$764.6 million increase from local enrichment

Initial Impact in Fiscal 2008

- A net decrease to business of \$3,038.1 million
- A net decrease to households of \$2,785.1 million

Major Industry Initial Impact in Fiscal 2008

- The largest dollar decrease: \$961.6 to the Finance, Insurance & Real Estate industry
- The largest percentage decrease: 11.2 percent to the Agriculture, Forestry & Fishing industry

Final Incidence of Changes Effective in Fiscal 2008

EXHIBIT

6522

- Lowest income level (income range from \$0 to \$14,042):
A decrease of \$133.3 million, or 6.19 percent.
- Middle income level (income range from \$43,403 to \$53,968):
A decrease of \$287.9 million, or 6.58 percent.
- Highest income level (income range from \$146,804 and above):
A decrease of \$1,407.0 million, or 9.17 percent.

Unofficial copy Travis Co. District Clerk Velda L. Price

Initial Tax Impact by Industry:

House Bill 1, As Passed 2nd House, was analyzed using the LBB's multi-tax model to determine the initial impact of the proposed changes relative to current state and local tax law. The results of the analysis are shown in Table 2 below.

Table 2
Comparison of Initial Tax Impact under
Current Law vs. House Bill 1, As Passed 2nd House
Fiscal Year 2008

Comparisons Include Property Tax, Sales and Excise Taxes and Taxes on Business

	Gross State Product: Shares	Current Law Liability	Percent of Total	Proposed Law Liability	Percent of Total	Change in Liability	Percent of Total	Percent Change in Liability
	[%]	[\$ Million]	[%]	[\$ Million]	[%]	[\$ Million]	[%]	[%]
Taxes Paid by Business:								
Agriculture, Forestry & Fishing	0.8	774.6	2.1	687.8	2.0	-86.8	2.9	-11.21
Mining	6.7	4,821.1	12.8	4,564.4	13.1	-256.7	8.4	-5.32
Utilities & Transportation	7.3	4,613.8	12.2	4,226.3	12.2	-387.5	12.8	-8.40
Construction	5.1	1,188.4	3.1	1,158.4	3.3	-30.0	1.0	-2.52
Manufacturing	13.0	5,212.4	13.8	4,710.2	13.6	-502.2	16.5	-9.63
Wholesale & Retail Trade	15.8	3,279.8	8.7	2,999.7	8.6	-280.1	9.2	-8.54
Information	5.1	3,103.9	8.2	2,833.1	8.2	-270.8	8.9	-8.72
Finance, Insurance & Real Estate	19.7	8,695.7	23.0	7,734.1	22.3	-961.6	31.7	-11.06
All Other Services	26.5	6,069.2	16.1	5,806.8	16.7	-262.4	8.6	-4.32
Total Taxes on Business:	100.0	37,758.9	100.0	34,720.8	100.0	-3,038.1	100.0	-8.05
Taxes Paid by Households:								
Residential Owner-Occupied		18,814.1		16,029.0		-2,785.1		-14.80
Personal Consumption		18,872.3		18,872.3		0.0		0.00
Total Taxes on Households:		37,686.4		34,901.3		-2,785.1		-7.39
Total Taxes								
		75,445.3		69,622.1		-5,823.2		-7.72

Tax Incidence by Income Group

Economists commonly distinguish between the initial "impact" of a tax and its "incidence." The initial impact of a tax falls on taxpayers legally liable to pay the tax, while the incidence refers to the ultimate payer of the tax. For example, the initial impact of a business tax falls on the firm incurring the tax liability. Over time, to varying degrees, the tax cost is "shifted" so that the ultimate burden of the tax falls either to consumers in different retail prices, to employees in changed wages, to owners of land and capital in different investment returns, or most likely, to some combination of all three. The degree to which a tax can be shifted, and the amount of time that elapses before a tax can be shifted, depend on the type of tax and the competitiveness of capital, labor, input material and product markets.

The results of this analysis for tax law changes effective with this proposal are shown in Table 3 and Table 4.

Table 3
Tax Incidence by Income Decile
Current Law vs. House Bill 1, As Passed 2nd House
Taxes Effective in Fiscal Year 2008

Comparisons Include Property Tax, Sales and Excise Taxes and Taxes on Business

Decile	Decile Income: Lower Bound	Decile Income: Upper Bound	Current Law Tax	Percent of Total	Proposed Law Tax	Percent of Total	Change in Tax	Percent Change in Tax
	[\$]	[\$]	[\$ Million]	[%]	[\$ Million]	[%]	[\$ Million]	[%]
1	0	14,042	2,153.2	3.6	2,019.9	3.7	-133.3	-6.19
2	14,042	23,872	2,485.7	4.2	2,325.5	4.3	-160.1	-6.44
3	23,872	33,190	3,217.2	5.4	3,014.3	5.5	-202.9	-6.31
4	33,190	43,403	3,552.4	6.0	3,321.7	6.1	-230.7	-6.49
5	43,403	53,968	4,375.1	7.4	4,087.7	7.5	-287.9	-6.58
6	53,968	67,019	5,112.2	8.6	4,772.3	8.7	-339.9	-6.65
7	67,019	82,976	6,151.9	10.4	5,715.5	10.5	-436.4	-7.09
8	82,976	104,865	7,470.7	12.6	6,911.0	12.7	-559.7	-7.49
9	104,865	146,804	9,292.5	15.7	8,525.4	15.6	-767.1	-8.25
10	146,804	and above	15,336.0	25.9	13,929.1	25.5	-1,407.0	-9.17
		Total:	59,147.3	100.0	54,622.3	100.0	-4,525.0	-7.65

Summary of Tax Incidence Findings

House Bill 1, As Passed 2nd House, would ultimately reduce the taxes of all households by \$4,525.0 million for tax law changes effective in 2008. The difference between the initial reduction in revenue of \$5,823.1 million in fiscal 2008 and the ultimate reduction of \$4,525.0 million in tax incidence is primarily due to the exporting of some of the tax changes to non-Texas consumers and businesses, changes in federal tax liability, and the absorption of some of the tax changes by business profits, some of which are received by non-Texas shareholders and business owners.

Table 4
Effective Tax Rate by Income Decile
Current Law vs. House Bill 1, As Passed 2nd House
Taxes Effective in Fiscal Year 2008
Comparisons Include Property Tax, Sales and Excise Taxes and Taxes on Business

Decile	Decile Income: Lower Bound	Decile Income: Upper Bound	Current Law Effective Rate	Proposed Law Effective Rate	Change in Effective Rate	Percent Change in Effective Rate
	[\$]	[\$]	[%]	[%]	[%]	[%]
1	0	14,042	32.76	30.73	-2.03	-6.19
2	14,042	23,872	15.40	14.41	-0.99	-6.44
3	23,872	33,190	13.01	12.19	-0.82	-6.31
4	33,190	43,403	11.14	10.42	-0.72	-6.49
5	43,403	53,968	10.07	9.40	-0.66	-6.58
6	53,968	67,019	9.76	9.11	-0.65	-6.65
7	67,019	82,976	9.49	8.82	-0.67	-7.09
8	82,976	104,865	9.24	8.55	-0.69	-7.49
9	104,865	146,804	8.71	7.99	-0.72	-8.25
10	146,804	and above	6.87	6.24	-0.63	-9.17
		Total:	9.09	8.39	-0.70	-7.65

Summary of Effective Rate Findings

House Bill 1, As Passed 2nd House, would ultimately reduce the effective rate for all households by 7.65 percent for taxes effective in fiscal year 2008. The effective tax rate is the aggregate amount of tax in a given income class divided by the aggregate amount of personal income in that class.

Source Agencies:

LBB Staff: JOB, EB, SD, SM

LEGISLATIVE BUDGET BOARD
Austin, Texas

EQUALIZED EDUCATION FUNDING IMPACT STATEMENT

79TH LEGISLATURE 3rd CALLED SESSION - 2006

May 11, 2006

TO: Honorable Tom Craddick, Speaker of the House, House of Representatives

FROM: John S. O'Brien, Deputy Director, Legislative Budget Board

IN RE: **HB1** by Chisum (Relating to public school finance, property tax relief, public school accountability and programs, and related matters; making an appropriation.), **As Passed 2nd House**

The bill would make formula and/or structural changes to the Foundation School Program. The percent of equalized revenue in the system during each of the first five years following passage is estimated as follows:

Fiscal Year	Percent of Equalized Revenue
2007	97.0
2008	96.0
2009	95.0
2010	95.0
2011	94.0

Source Agencies:

LBB Staff: JOB, UP, JSc

EXHIBIT
6523

AN ACT

relating to certain taxes affecting businesses; making an appropriation; providing penalties.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1. (a) Section 21.02, Tax Code, is amended by amending Subsection (a) and adding Subsection (e) to read as follows:

(a) Except as provided by Subsections ~~[Subsection]~~ (b) and (e) and by Sections 21.021, 21.04, and 21.05, tangible personal property is taxable by a taxing unit if:

(1) it is located in the unit on January 1 for more than a temporary period;

(2) it normally is located in the unit, even though it is outside the unit on January 1, if it is outside the unit only temporarily;

(3) it normally is returned to the unit between uses elsewhere and is not located in any one place for more than a temporary period; or

(4) the owner resides (for property not used for business purposes) or maintains the owner's ~~[his]~~ principal place of business in this state (for property used for business purposes) in the unit and the property is taxable in this state but does not have a taxable situs pursuant to Subdivisions (1) through (3) of this subsection ~~[section]~~.

(e) In this subsection, "portable drilling rig" includes equipment associated with the drilling rig. A portable drilling rig designed for land-based oil or gas drilling or exploration operations is taxable by the taxing unit in which the rig is located on January 1 if the rig was located in the appraisal district that appraises property for the unit for the preceding 365 consecutive days. If the drilling rig was not located in the appraisal district where it is located on January 1 for the preceding 365 days, it is taxable by the taxing unit in which the owner's principal place of business in this state is located on January 1.

(b) Section 21.02, Tax Code, as amended by this section, applies only to the taxable situs of property for an ad valorem tax year that begins on or after January 1, 2007.

(c) This section takes effect January 1, 2007.

SECTION 2. Subchapter A, Chapter 171, Tax Code, is amended to read as follows:

SUBCHAPTER A. DEFINITIONS; TAX IMPOSED

Sec. 171.0001. GENERAL DEFINITIONS. In this chapter:

(1) "Affiliated group" means a group of one or more entities in which a controlling interest is owned by a common owner or owners, either corporate or noncorporate, or by one or more of the member entities.

(2) "Assigned employee" has the meaning assigned by Section 91.001, Labor Code.

(3) "Banking corporation" means each state, national, domestic, or foreign bank, whether organized under the laws of this state, another state, or another country, or under federal law,

1 including a limited banking association organized under Subtitle A,
2 Title 3, Finance Code, and each bank organized under Section 25(a),
3 Federal Reserve Act (12 U.S.C. Sections 611-631) (edge
4 corporations), but does not include a bank holding company as that
5 term is defined by Section 2, Bank Holding Company Act of 1956 (12
6 U.S.C. Section 1841).

7 (4) "Beginning date" means:

8 (A) for a taxable entity chartered or organized
9 in this state, the date on which the taxable entity's charter or
10 organization takes effect; and

11 (B) for any other taxable entity, the date on
12 which the taxable entity begins doing business in this state.

13 (5) "Charter" includes a limited liability company's
14 certificate of organization, a limited partnership's certificate
15 of limited partnership, and the registration of a limited liability
16 partnership.

17 (6) "Client company" has the meaning assigned by
18 Section 91-601, Labor Code.

19 (7) "Combined group" means taxable entities that are
20 part of an affiliated group engaged in a unitary business and that
21 are required to file a group report under Section 171.1014.

22 (8) "Controlling interest" means:

23 (A) for a corporation, either 80 percent or more,
24 owned directly or indirectly, of the total combined voting power of
25 all classes of stock of the corporation, or 80 percent or more,
26 owned directly or indirectly, of the beneficial ownership interest
27 in the voting stock of the corporation; and

1 (B) for a partnership, association, trust, or
2 other entity, 80 percent or more, owned directly or indirectly, of
3 the capital, profits, or beneficial interest in the partnership,
4 association, trust, or other entity.

5 (9) "Internal Revenue Code" means the Internal Revenue
6 Code of 1986 in effect for the federal tax year beginning on January
7 1, 2006, and any regulations adopted under that code applicable to
8 that period.

9 (10) "Lending institution" means an entity that makes
10 loans and is regulated by the Federal Reserve Board, the Office of
11 the Comptroller of the Currency, the Federal Deposit Insurance
12 Corporation, the Texas Department of Banking, the Office of
13 Consumer Credit Commissioner, the Department of Savings and
14 Mortgage Lending, the Credit Union Department, or any comparable
15 regulatory body.

16 (11) "Management company" means a corporation,
17 limited liability company, or other limited liability entity that
18 conducts all or part of the active trade or business of another
19 entity (the "managed entity") in exchange for:

20 (A) a management fee; and

21 (B) reimbursement of specified costs incurred in
22 the conduct of the active trade or business of the managed entity,
23 including "wages and cash compensation" as determined under
24 Sections 171.1013(a) and (b).

25 (12) "Retail trade" means the activities described in
26 Division G of the 1987 Standard Industrial Classification Manual
27 published by the federal Office of Management and Budget.

1 (13) "Savings and loan association" means a savings
2 and loan association or savings bank, whether organized under the
3 laws of this state, another state, or another country, or under
4 federal law.

5 (14) "Shareholder" includes a limited liability
6 company's member and a limited banking association's participant.

7 (15) "Staff leasing services company" has the meaning
8 assigned by Section 91.001, Labor Code.

9 (16) "Total revenue" means the total revenue of a
10 taxable entity as determined under Section 171.1011.

11 (17) "Unitary business" means a single economic
12 enterprise that is made up of separate parts of a single entity or
13 of a commonly controlled group of entities that are sufficiently
14 interdependent, integrated, and interrelated through their
15 activities so as to provide a synergy and mutual benefit that
16 produces a sharing or exchange of value among them and a significant
17 flow of value to the separate parts. In determining whether a
18 unitary business exists, the comptroller shall consider any
19 relevant factor, including whether:

20 (A) the activities of the group members:

21 (i) are in the same general line, such as
22 manufacturing, wholesaling, retailing of tangible personal
23 property, insurance, transportation, or finance; or

24 (ii) are steps in a vertically structured
25 enterprise or process, such as the steps involved in the production
26 of natural resources, including exploration, mining, refining, and
27 marketing; and

1 (B) the members are functionally integrated
2 through the exercise of strong centralized management, such as
3 authority over purchasing, financing, product line, personnel, and
4 marketing.

5 (18) "Wholesale trade" means the activities described
6 in Division F of the 1987 Standard Industrial Classification Manual
7 published by the federal Office of Management and Budget.

8 Sec. 171.0002. DEFINITION OF TAXABLE ENTITY. (a) Except as
9 otherwise provided by this section, "taxable entity" means a
10 partnership, corporation, banking corporation, savings and loan
11 association, limited liability company, business trust,
12 professional association, business association, joint venture,
13 joint stock company, holding company, or other legal entity. The
14 term includes a combined group. A joint venture does not include
15 joint operating or co-ownership arrangements meeting the
16 requirements of Treasury Regulation Section 1.761-2(a)(3) that
17 elect out of federal partnership treatment as provided by Section
18 761(a), Internal Revenue Code.

19 (b) "Taxable entity" does not include:

20 (1) a sole proprietorship;

21 (2) a general partnership the direct ownership of
22 which is entirely composed of natural persons;

23 (3) a passive entity as defined by Section 171.0003;

24 or

25 (4) an entity that is exempt from taxation under
26 Subchapter B.

27 (c) "Taxable entity" does not include an entity that is:

1 (1) a grantor trust as defined by Sections 671 and
2 7701(a)(30)(E), Internal Revenue Code, all of the grantors and
3 beneficiaries of which are natural persons or charitable entities
4 as described in Section 501(c)(3), Internal Revenue Code, excluding
5 a trust taxable as a business entity pursuant to Treasury
6 Regulation Section 301.7701-4(b);

7 (2) an estate of a natural person as defined by Section
8 7701(a)(30)(D), Internal Revenue Code, excluding an estate taxable
9 as a business entity pursuant to Treasury Regulation Section
10 301.7701-4(b);

11 (3) an escrow;

12 (4) a family limited partnership that is a passive
13 entity in which at least 80 percent of the interests are held,
14 directly or indirectly, by members of the same family, including an
15 individual's ancestors, lineal descendants, spouse, and brothers
16 and sisters by the whole or half blood, and the estate of any of
17 these persons, and that is a limited partnership:

18 (A) formed pursuant to the Texas Revised Limited
19 Partnership Act (Article 6132a-1, Vernon's Texas Civil Statutes);

20 (B) formed pursuant to the limited partnership
21 law of any other state; or

22 (C) treated as a partnership for federal income
23 tax purposes;

24 (5) a passive investment partnership that is a passive
25 entity and that is:

26 (A) formed pursuant to the Texas Revised Limited
27 Partnership Act (Article 6132a-1, Vernon's Texas Civil Statutes);

1 (B) formed pursuant to the limited partnership
2 law of any other state; or

3 (C) formed pursuant to the limited partnership
4 laws of any foreign country;

5 (6) a passive investment partnership that is a passive
6 entity and is a general partnership;

7 (7) a trust that is a passive entity:

8 (A) that is taxable as a trust under Section 641,
9 Internal Revenue Code;

10 (B) all of the beneficiaries of which are natural
11 persons or charitable entities as defined in Section 501(c)(3),
12 Internal Revenue Code;

13 (C) that is not a trust taxable as a business
14 entity pursuant to Treasury Regulation Section 301.7701-4(b); and

15 (D) that is organized as a trust and is described
16 in Section 7701(a)(30)(E), Internal Revenue Code;

17 (8) a real estate investment trust (REIT) as defined
18 by Section 856, Internal Revenue Code, and its "qualified REIT
19 subsidiary" entities as defined by Section 856(i)(2), Internal
20 Revenue Code, provided that:

21 (A) a REIT with any amount of its assets in direct
22 holdings of real estate, other than real estate it occupies for
23 business purposes, as opposed to holding interests in limited
24 partnerships or other entities that directly hold the real estate,
25 is a taxable entity; and

26 (B) a limited partnership or other entity that
27 directly holds the real estate as described in Paragraph (A) is not

1 exempt under this subdivision, without regard to whether a REIT
2 holds an interest in it; or

3 (9) a real estate mortgage investment conduit (REMIC),
4 as defined by Section 860D, Internal Revenue Code.

5 (d) An entity that can file as a sole proprietorship for
6 federal tax purposes is not a sole proprietorship for purposes of
7 Subsection (b)(1) and is not exempt under that subsection if the
8 entity is formed in a manner under the statutes of this state or
9 another state that limit the liability of the entity.

10 Sec. 171.0003. DEFINITION OF PASSIVE ENTITY. (a) An entity
11 is a passive entity only if:

12 (1) the entity is a general or limited partnership or a
13 trust, other than a business trust;

14 (2) during the period on which margin is based, the
15 entity's federal gross income consists of at least 90 percent
16 of the following income:

17 (A) dividends, interest, foreign currency
18 exchange gain, periodic and nonperiodic payments with respect to
19 notional principal contracts, option premiums, cash settlement or
20 termination payments with respect to a financial instrument, and
21 income from a limited liability company;

22 (B) distributive shares of partnership income to
23 the extent that those distributive shares of income are greater
24 than zero;

25 (C) gains from the sale of real property,
26 commodities traded on a commodities exchange, and securities; and

27 (D) royalties, bonuses, or delay rental income

1 from mineral properties and income from other nonoperating mineral
2 interests; and

3 (3) the entity does not receive more than 10 percent of
4 its federal gross income from conducting an active trade or
5 business.

6 (a-1) In making the computation under Subsection (a)(3),
7 income described by Subsection (a)(2) may not be treated as income
8 from conducting an active trade or business.

9 (b) The income described by Subsection (a)(2) does not
10 include:

11 (1) rent; or

12 (2) income received by a nonoperator from mineral
13 properties under a joint operating agreement if the nonoperator is
14 a member of an affiliated group and another member of that group is
15 the operator under the same joint operating agreement.

16 Sec. 171.0014. DEFINITION OF CONDUCTING ACTIVE TRADE OR
17 BUSINESS. (a) The definition in this section applies only to
18 Section 171.0003.

19 (b) An entity conducts an active trade or business if:

20 (1) the activities being carried on by the entity
21 include one or more active operations that form a part of the
22 process of earning income or profit; and

23 (2) the entity performs active management and
24 operational functions.

25 (c) Activities performed by the entity include activities
26 performed by persons outside the entity, including independent
27 contractors, to the extent the persons perform services on behalf

1 of the entity and those services constitute all or part of the
2 entity's trade or business.

3 (d) An entity conducts an active trade or business if
4 assets, including royalties, patents, trademarks, and other
5 intangible assets, held by the entity are used in the active trade
6 or business of one or more related entities.

7 (e) For purposes of this section:

8 (1) the ownership of a royalty interest or a
9 nonoperating working interest in mineral rights does not constitute
10 conduct of an active trade or business; and

11 (2) payment of compensation to employees or
12 independent contractors for financial or legal services reasonably
13 necessary for the operation of the entity does not constitute
14 conduct of an active trade or business.

15 Sec. 171.001. TAX IMPOSED. (a) A franchise tax is imposed
16 on[+]

17 ~~[(1)]~~ each taxable entity ~~[corporation]~~ that does
18 business in this state or that is chartered or organized in this
19 state[+, and

20 ~~[(2) each limited liability company that does business~~
21 ~~in this state or that is organized under the laws of this state].~~

22 (b) ~~[In this chapter,~~

23 ~~[(1) "Banking corporation" means each state,~~
24 ~~national, domestic, or foreign bank, whether organized under the~~
25 ~~laws of this state, another state, or another country, or under~~
26 ~~federal law, including a limited banking association organized~~
27 ~~under Subtitle A, Title 3, Finance Code, and each bank organized~~

1 ~~under Section 25(a), Federal Reserve Act (12 U.S.C. Secs. 611-631)~~
2 ~~(edge corporations), but does not include a bank holding company as~~
3 ~~that term is defined by Section 2, Bank Holding Company Act of 1956~~
4 ~~(12 U.S.C. Sec. 1841).~~

5 ~~[(2) "Beginning date" means:~~

6 ~~[(A) for a corporation chartered in this state,~~
7 ~~the date on which the corporation's charter takes effect; and~~

8 ~~[(B) for a foreign corporation, the date on which~~
9 ~~the corporation begins doing business in this state.~~

10 ~~[(3) "Corporation" includes:~~

11 ~~[(A) a limited liability company, as defined~~
12 ~~under the Texas Limited Liability Company Act,~~

13 ~~[(B) a savings and loan association; and~~

14 ~~[(C) a banking corporation.~~

15 ~~[(4) "Charter" includes a limited liability company's~~
16 ~~certificate of organization.~~

17 ~~[(5) "Internal Revenue Code" means the Internal~~
18 ~~Revenue Code of 1986 in effect for the federal tax year beginning on~~
19 ~~or after January 1, 1996, and before January 1, 1997, and any~~
20 ~~regulations adopted under that code applicable to that period.~~

21 ~~[(6) "Officer" and "director" include a limited~~
22 ~~liability company's directors and managers and a limited banking~~
23 ~~association's directors and managers and participants if there are~~
24 ~~no directors or managers.~~

25 ~~[(7) "Savings and loan association" means a savings~~
26 ~~and loan association or savings bank, whether organized under the~~
27 ~~laws of this state, another state, or another country, or under~~

1 ~~federal law.~~

2 ~~[(8) "Shareholder" includes a limited liability~~
3 ~~company's member and a limited banking association's participant.~~

4 ~~[(e)]~~ The tax imposed under this chapter extends to the
5 limits of the United States Constitution and the federal law
6 adopted under the United States Constitution.

7 Sec. 171.0011. ADDITIONAL TAX. (a) Except as provided by
8 Subsection (e), an ~~An~~ additional tax is imposed on a taxable
9 entity ~~corporation~~ that for any reason becomes no longer subject
10 to the ~~earned surplus component of the tax, without regard to~~
11 ~~whether the corporation remains subject to the taxable capital~~
12 ~~component of the~~ tax imposed under this chapter.

13 (b) The additional tax is equal to the appropriate rate
14 under Section 171.001 of the taxable entity's taxable margin ~~[4.5~~
15 ~~percent of the corporation's net taxable earned surplus]~~ computed
16 on the period beginning on the day after the last day for which the
17 tax imposed on taxable margin ~~net taxable earned surplus~~ was
18 computed ~~under Section 171.1532~~ and ending on the date the
19 taxable entity ~~corporation~~ is no longer subject to the ~~earned~~
20 ~~surplus component of the~~ tax imposed under this chapter.

21 (c) The additional tax imposed and any report required by
22 the comptroller are due on the 60th day after the date the taxable
23 entity ~~corporation~~ becomes no longer subject to the ~~earned~~
24 ~~surplus component of the~~ tax imposed under this chapter.

25 (d) Except as otherwise provided by this section, the
26 provisions of this chapter apply to the tax imposed under this
27 section.

(e) An additional tax is not imposed on a taxable entity that becomes no longer subject to the tax imposed under this chapter because the entity qualifies as a passive entity.

Sec. 171.002. RATES; COMPUTATION OF TAX (a) Subject to Section 171.003 and except as provided by Subsection (b), the rate

[The rates] of the franchise tax is one [and

[(1) 0.25] percent per year of privilege period of [net] taxable margin [capital, and

[(2) 4.5 percent of net taxable earned surplus].

(b) The rate of the franchise tax is 0.5 percent per year of privilege period of taxable margin for those taxable entities primarily engaged in retail or wholesale trade. [The amount of franchise tax on each corporation is computed by adding the following:

[(1) the amount calculated by applying the tax rate prescribed by Subsection (a)(1) to the corporation's net taxable capital, and

[(2) the difference between:

[(A) the amount calculated by applying the tax rate prescribed by Subsection (a)(2) to the corporation's net taxable earned surplus, and

[(B) the amount determined under Subdivision (1).]

(c) A taxable entity is primarily engaged in retail or wholesale trade only if:

(1) the total revenue from its activities in retail or wholesale trade is greater than the total revenue from its

1 activities in trades other than the retail and wholesale trades;

2 (2) except as provided by Subsection (c-1), less than
 3 50 percent of the total revenue from activities in retail or
 4 wholesale trade comes from the sale of products it produces or
 5 products produced by an entity that is part of an affiliated group
 6 to which the taxable entity also belongs; and

7 (3) the taxable entity does not provide retail or
 8 wholesale utilities, including telecommunications services and
 9 electricity or gas. [In making a computation under Subsection (b),
 10 an amount computed under Subsection (b)(1) or (b)(2) that is zero or
 11 less is computed as a zero.]

12 (c-1) Subsection (c)(2) does not apply to total revenue from
 13 activities in a retail trade described by Major Group 58 of the
 14 Standard Industrial Classification Manual published by the federal
 15 Office of Management and Budget.

16 (d) A taxable entity [~~corporation~~] is not required to pay
 17 any tax and is not considered to owe any tax for a period if:

18 (1) the amount of tax computed for the taxable entity
 19 [~~corporation~~] is less than \$1,000 [~~\$100~~]; or

20 (2) the amount of the taxable entity's total revenue
 21 [~~corporation's gross receipts~~];

22 [~~(A)~~] from its entire business [~~under Section~~
 23 ~~171.105~~] is less than or equal to \$300,000 or the amount determined
 24 under Section 171.006 [~~\$150,000; and~~

25 [~~(B)~~ from its entire business under Section
 26 ~~171.1051, including the amount excepted under Section 171.1051(a),~~
 27 ~~is less than \$150,000].~~

1 ~~[Sec. 171.005. RATE OF TAX FOR CORPORATION IN PROCESS OF~~
 2 ~~LIQUIDATION. The franchise tax rate on a corporation in the process~~
 3 ~~of liquidation, as defined by Section 171.102 of this code, is the~~
 4 ~~rate established by Section 171.002 of this code.]~~

5 Sec. 171.003. INCREASE IN RATE REQUIRES VOTER APPROVAL.

6 (a) An increase in a rate provided by Section 171.002(a) or (b)
 7 takes effect only if approved by a majority of the registered voters
 8 voting in a statewide referendum held on the question of increasing
 9 the rate. The referendum must specify the increased rate or rates.

10 (b) This section does not apply to a decrease in a rate
 11 provided by Section 171.002(a) or (b). If a rate is decreased, this
 12 section applies to any subsequent increase in that rate.

13 (c) This section does not apply to any change in the tax
 14 imposed by this chapter in relation to:

15 (1) the manner in which the tax is computed, including
 16 the determination of margin and taxable margin and any allowable
 17 deductions or credits;

18 (2) the manner in which the tax is administered or
 19 enforced; or

20 (3) the applicability of the tax to certain entities.

21 Sec. 171.006. ADJUSTMENT OF ELIGIBILITY FOR EXEMPTION AND
 22 COMPENSATION DEDUCTION. (a) In this section, "consumer price
 23 index" means the average over a state fiscal biennium of the
 24 Consumer Price Index for All Urban Consumers (CPI-U), U.S. City
 25 Average, published monthly by the United States Bureau of Labor
 26 Statistics, or its successor in function.

27 (b) Beginning in 2009, on January 1 of each odd-numbered

1 year, the amounts prescribed by Sections 171.002(d)(2) and
2 171.1013(c) are increased or decreased by an amount equal to the
3 amount prescribed by those sections on December 31 of the preceding
4 year multiplied by the percentage increase or decrease during the
5 preceding state fiscal biennium in the consumer price index and
6 rounded to the nearest \$10,000.

7 (c) The amounts determined under Subsection (b) apply to a
8 report originally due on or after the date the determination is
9 made.

10 (d) The comptroller shall make the determination required
11 by this section and may adopt rules related to making that
12 determination.

13 (e) A determination by the comptroller under this section is
14 final and may not be appealed.

15 SECTION 3. Section 171.052, Tax Code, is amended to read as
16 follows:

17 Sec. 171.052. CERTAIN CORPORATIONS. (a) Except as
18 provided by Subsection (c), an [An] insurance organization, title
19 insurance company, or title insurance agent authorized to engage in
20 insurance business in this state now required to pay an annual tax
21 under Chapter 4 or 9, Insurance Code, measured by its gross premium
22 receipts is exempted from the franchise tax. A nonadmitted
23 insurance organization that is required to pay a gross premium
24 receipts tax during a tax year is exempted from the franchise tax
25 for that same tax year.

26 (b) Farm mutuals, local mutual aid associations, and burial
27 associations are not subject to the franchise tax.

(c) An entity is subject to the franchise tax for a tax year in any portion of which the entity is in violation of an order issued by the Texas Department of Insurance under Section 2254.003(b), Insurance Code, that is final after appeal or that is no longer subject to appeal.

SECTION 4. Subchapter B, Chapter 171, Tax Code, is amended by adding Section 171.088 to read as follows:

Sec. 171.088. EXEMPTION--NONCORPORATE ENTITY ELIGIBLE FOR CERTAIN EXEMPTIONS. An entity that is not a corporation but that, because of its activities, would qualify for a specific exemption under this subchapter if it were a corporation, qualifies for the exemption and is exempt from the tax in the same manner and under the same conditions as a corporation.

SECTION 5. Subchapter C, Chapter 171, Tax Code, is amended, including the reenacting and amending of Section 171.109(g), Tax Code, as amended by Chapters 801 and 1198, Acts of the 71st Legislature, Regular Session, 1989, to read as follows:

SUBCHAPTER C. DETERMINATION OF TAXABLE MARGIN [~~CAPITAL AND TAXABLE EARNED SURPLUS~~]; ALLOCATION AND APPORTIONMENT

Sec. 171.101. DETERMINATION OF [~~NET~~] TAXABLE MARGIN [~~CAPITAL~~]. (a) The [~~Except as provided by Subsections (b) and (c), the net~~] taxable margin [~~capital~~] of a taxable entity [~~corporation~~] is computed by:

(1) determining the taxable entity's margin, which is the lesser of:

(A) 70 percent of the taxable entity's total revenue from its entire business, as determined under Section

1 171.1011; or

2 (B) an amount computed by:

3 (i) determining the taxable entity's total
4 revenue from its entire business, under Section 171.1011;

5 (ii) subtracting, at the election of the
6 taxable entity, either:

7 (a) cost of goods sold, as determined
8 under Section 171.1012; or

9 (b) compensation, as determined under
10 Section 171.1013; and

11 (iii) subtracting, in addition to any
12 subtractions made under Subparagraph (ii)(a) or (b), compensation,
13 as determined under Section 171.1013, paid to an individual during
14 the period the individual is serving on active duty as a member of
15 the armed forces of the United States if the individual is a
16 resident of this state at the time the individual is ordered to
17 active duty and the cost of training a replacement for the
18 individual; [adding the corporation's stated capital, as defined by
19 Article 1.02, Texas Business Corporation Act, and the corporation's
20 surplus, to determine the corporation's taxable capital,]

21 (2) apportioning the taxable entity's margin
22 [corporation's taxable capital] to this state as provided by
23 Section 171.106 [171.106(a) or (c), as applicable,] to determine
24 the taxable entity's [corporation's] apportioned margin [taxable
25 capital]; and

26 (3) subtracting from the amount computed under
27 Subdivision (2) any other allowable deductions to determine the

1 taxable entity's ~~[corporation's net]~~ taxable margin ~~[capital]~~.

2 (b) Notwithstanding Subsection (a)(1)(B)(ii), a staff
 3 leasing services company may subtract only compensation as
 4 determined under Section 171.1013.

5 (c) In making a computation under this section, an amount
 6 that is zero or less is computed as a zero. ~~[The net taxable capital~~
 7 ~~of a limited liability company is computed by:~~

8 ~~[(1) adding the company's members' contributions, as~~
 9 ~~provided for under the Texas Limited Liability Company Act, and~~
 10 ~~surplus to determine the company's taxable capital,~~

11 ~~[(2) apportioning the amount determined under~~
 12 ~~Subdivision (1) to this state in the same manner that the taxable~~
 13 ~~capital of a corporation is apportioned to this state under Section~~
 14 ~~171.106(a) or (c), as applicable, to determine the company's~~
 15 ~~apportioned taxable capital, and~~

16 ~~[(3) subtracting from the amount computed under~~
 17 ~~Subdivision (2) any other allowable deductions, to determine the~~
 18 ~~company's net taxable capital.~~

19 ~~[(4) The net taxable capital of a savings and loan~~
 20 ~~association is computed by:~~

21 ~~[(1) determining the association's net worth, and~~

22 ~~[(2) apportioning the amount determined under~~
 23 ~~Subdivision (1) to this state in the same manner that the taxable~~
 24 ~~capital of a corporation is apportioned to this state under Section~~
 25 ~~171.106(a) to determine the association's net taxable capital].~~

26 (d) An election under Subsection (a)(1)(B)(ii) shall be
 27 made by the taxable entity on its annual report and is effective

1 only for that annual report. The election may be changed by filing
2 an amended report.

3 Sec. 171.1011. DETERMINATION OF TOTAL REVENUE FROM ENTIRE
4 BUSINESS. (a) In this section, a reference to an Internal Revenue
5 Service form includes a variant of the form. For example, a
6 reference to Form 1120 includes Forms 1120-A, 1120-S, and other
7 variants of Form 1120. A reference to an Internal Revenue Service
8 form also includes any subsequent form with a different number or
9 designation that substantially provides the same information as the
10 original form.

11 (b) In this section, a reference to an amount entered on a
12 line number on an Internal Revenue Service form includes the
13 corresponding amount entered on a variant of the form, or a
14 subsequent form, with a different line number. The comptroller
15 shall adopt rules as necessary to accomplish the legislative intent
16 prescribed by this subsection and Subsection (a).

17 (c) Except as provided by this section, and subject to
18 Section 171.1014, for the purpose of computing its taxable margin
19 under Section 171.101, the total revenue of a taxable entity is:

20 (1) for a taxable entity treated for federal income
21 tax purposes as a corporation, an amount computed by:

22 (A) adding:

23 (i) the amount entered on line 1c, Internal
24 Revenue Service Form 1120; and

25 (ii) the amounts entered on lines 4 through
26 10, Internal Revenue Service Form 1120; and

27 (B) subtracting:

1 (i) bad debt expensed for federal income
 2 tax purposes that corresponds to items of gross receipts included
 3 in Subsection (c)(1)(A) for the current reporting period or a past
 4 reporting period;

5 (ii) to the extent included in Subsection
 6 (c)(1)(A), foreign royalties and foreign dividends, including
 7 amounts determined under Section 78 or Sections 951-964, Internal
 8 Revenue Code;

9 (iii) to the extent included in Subsection
 10 (c)(1)(A), net distributive income from partnerships and from
 11 trusts and limited liability companies treated as partnerships for
 12 federal income tax purposes and net distributive income from
 13 limited liability companies and corporations treated as S
 14 corporations for federal income tax purposes;

15 (iv) allowable deductions from Internal
 16 Revenue Service Form 1120, Schedule C, to the extent the relating
 17 dividend income is included in total revenue;

18 (v) to the extent included in Subsection
 19 (c)(1)(A), items of income attributable to an entity that is a
 20 disregarded entity for federal income tax purposes; and

21 (vi) to the extent included in Subsection
 22 (c)(1)(A), other amounts authorized by this section;

23 (2) for a taxable entity treated for federal income
 24 tax purposes as a partnership, an amount computed by:

25 (A) adding:

26 (i) the amount entered on line 1c, Internal
 27 Revenue Service Form 1065;

1 (ii) the amounts entered on lines 4 through
2 7, Internal Revenue Service Form 1065; and

3 (iii) the amounts entered on lines 2
4 through 11, Internal Revenue Service Form 1065, Schedule K; and

5 (B) subtracting:

6 (i) bad debt expensed for federal income
7 tax purposes that corresponds to items of gross receipts included
8 in Subsection (c)(2)(A) for the current reporting period or a past
9 reporting period;

10 (ii) to the extent included in Subsection
11 (c)(2)(A), foreign royalties and foreign dividends, including
12 amounts determined under Section 78 or Sections 951-964, Internal
13 Revenue Code;

14 (iii) to the extent included in Subsection
15 (c)(2)(A), net distributive income from partnerships and from
16 trusts and limited liability companies treated as partnerships for
17 federal income tax purposes and net distributive income from
18 limited liability companies and corporations treated as S
19 corporations for federal income tax purposes;

20 (iv) to the extent included in Subsection
21 (c)(2)(A), items of income attributable to an entity that is a
22 disregarded entity for federal income tax purposes; and

23 (v) to the extent included in Subsection
24 (c)(2)(A), other amounts authorized by this section; or

25 (3) for a taxable entity other than a taxable entity
26 treated for federal income tax purposes as a corporation or
27 partnership, an amount determined in a manner substantially

1 equivalent to the amount for Subdivision (1) or (2) determined by
2 rules that the comptroller shall adopt.

3 (d) Subject to Section 171.1014, a corporation that is part
4 of a federal consolidated group shall compute its total revenue
5 under Subsection (c) as if it had filed a separate return for
6 federal income tax purposes.

7 (e) A taxable entity that owns an interest in a passive
8 entity that is not included in a group report under Section 171.1014
9 shall include in the taxable entity's total revenue the taxable
10 entity's share of the net income of the passive entity, but only to
11 the extent the net income of the passive entity was not generated by
12 the margin of any other taxable entity.

13 (f) A taxable entity shall exclude from its total revenue,
14 to the extent included under Subsection (c)(1)(A), (c)(2)(A), or
15 (c)(3), flow-through funds that are mandated by law or fiduciary
16 duty to be distributed to other entities, including taxes collected
17 from a third party by the taxable entity and remitted by the taxable
18 entity to a taxing authority.

19 (g) A taxable entity shall exclude from its total revenue,
20 to the extent included under Subsection (c)(1)(A), (c)(2)(A), or
21 (c)(3), only the following flow-through funds that are mandated by
22 contract to be distributed to other entities:

23 (1) sales commissions to nonemployees, including
24 split-fee real estate commissions;

25 (2) the tax basis as determined under the Internal
26 Revenue Code of securities underwritten; and

27 (3) subcontracting payments handled by the taxable

1 entity to provide services, labor, or materials in connection with
 2 the actual or proposed design, construction, remodeling, or repair
 3 of improvements on real property or the location of the boundaries
 4 of real property.

5 (g-1) A taxable entity that is a lending institution shall
 6 exclude from its total revenue, to the extent included under
 7 Subsection (c)(1)(A), (c)(2)(A), or (c)(3), proceeds from the
 8 principal repayment of loans.

9 (g-2) A taxable entity shall exclude from its total revenue,
 10 to the extent included under Subsection (c)(1)(A), (c)(2)(A), or
 11 (c)(3), the tax basis as determined under the Internal Revenue Code
 12 of securities and loans sold.

13 (g-3) A taxable entity that provides legal services shall
 14 exclude from its total revenue, to the extent included under
 15 Subsection (c)(1)(A), (c)(2)(A), or (c)(3):

16 (1) the following flow-through funds that are mandated
 17 by law, contract, or fiduciary duty to be distributed to the
 18 claimant by the claimant's attorney or to other entities on behalf
 19 of a claimant by the claimant's attorney:

20 (A) damages due the claimant;

21 (B) funds subject to a lien or other contractual
 22 obligation arising out of the representation, other than fees owed
 23 to the attorney;

24 (C) funds subject to a subrogation interest or
 25 other third-party contractual claim; and

26 (D) fees paid an attorney in the matter who is not
 27 a member, partner, shareholder, or employee of the taxable entity;

1 (2) reimbursement of the taxable entity's expenses
2 incurred in prosecuting a claimant's matter that are specific to
3 the matter and that are not general operating expenses; and

4 (3) the actual out-of-pocket expenses of the attorney,
5 not to exceed \$500 per case, of providing pro bono legal services to
6 a person, but only if the attorney maintains records of the pro bono
7 services for auditing purposes in accordance with the manner in
8 which those services are reported to the State Bar of Texas.

9 (h) If the taxable entity belongs to an affiliated group,
10 the taxable entity may not exclude payments described by Subsection
11 (f), (g), (g-1), (g-2), or (g-3) that are made to entities that are
12 members of the affiliated group.

13 (i) Except as provided by Subsection (g), a payment made
14 under an ordinary contract for the provision of services in the
15 regular course of business may not be excluded.

16 (j) Any amount excluded under this section may not be
17 included in the determination of cost of goods sold under Section
18 171.1012 or the determination of compensation under Section
19 171.1013.

20 (k) A taxable entity that is a staff leasing services
21 company shall exclude from its total revenue payments received from
22 a client company for wages, payroll taxes on those wages, employee
23 benefits, and workers' compensation benefits for the assigned
24 employees of the client company.

25 (1) For purposes of Subsection (g)(1):

26 (1) "Sales commission" means:

27 (A) any form of compensation paid to a person for

1 engaging in an act for which a license is required by Chapter 1101,
2 Occupations Code; and

3 (B) compensation paid to a sales representative
4 by a principal in an amount that is based on the amount or level of
5 certain orders for or sales of the principal's product and that the
6 principal is required to report on Internal Revenue Service Form
7 1099-MISC.

8 (2) "Principal" means a person who:

9 (A) manufactures, produces, imports,
10 distributes, or acts as an independent agent for the distribution
11 of a product for sale;

12 (B) uses a sales representative to solicit orders
13 for the product; and

14 (C) compensates the sales representative wholly
15 or partly by sales commission.

16 (m) A taxable entity shall exclude from its total revenue,
17 to the extent included under Subsection (c)(1)(A), (c)(2)(A), or
18 (c)(3), dividends and interest received from federal obligations.

19 (n-1) A taxable entity that is a management company shall
20 exclude from its total revenue reimbursements of specified costs
21 incurred in its conduct of the active trade or business of a managed
22 entity, including "wages and cash compensation" as determined under
23 Sections 171.1013(a) and (b).

24 (n) Except as provided by Subsection (o), a taxable entity
25 that is a health care provider shall exclude from its total revenue,
26 to the extent included under Subsection (c)(1)(A), (c)(2)(A), or
27 (c)(3):

1 (1) the total amount of payments the health care
2 provider received:

3 (A) under the Medicaid program, Medicare
4 program, Indigent Health Care and Treatment Act (Chapter 61, Health
5 and Safety Code), and Children's Health Insurance Program (CHIP);

6 (B) for professional services provided in
7 relation to a workers' compensation claim under Title 5, Labor
8 Code; and

9 (C) for professional services provided to a
10 beneficiary rendered under the TRICARE military health system; and

11 (2) the actual cost to the health care provider for any
12 uncompensated care provided, but only if the provider maintains
13 records of the uncompensated care for auditing purposes and, if the
14 provider later receives payment for all or part of that care, the
15 provider adjusts the amount excluded for the tax year in which the
16 payment is received.

17 (n-1) The comptroller shall adopt rules governing:

18 (1) the computation of the actual cost to a health care
19 provider of any uncompensated care provided under Subsection
20 (n)(2), and

21 (2) the audit requirements related to the computation
22 of those costs.

23 (o) A health care provider that is a health care institution
24 shall exclude from its total revenue, to the extent included under
25 Subsection (c)(1)(A), (c)(2)(A), or (c)(3), 50 percent of the
26 amounts described by Subsection (n).

27 (p) In this section:

1 (1) "Federal obligations" means:

2 (A) stocks and other direct obligations of, and
3 obligations unconditionally guaranteed by, the United States
4 government and United States government agencies; and

5 (B) direct obligations of a United States
6 government-sponsored agency.

7 (2) "Health care institution" means:

8 (A) an ambulatory surgical center;

9 (B) an assisted living facility licensed under
10 Chapter 247, Health and Safety Code;

11 (C) an emergency medical services provider;

12 (D) a home and community support services agency;

13 (E) a hospice;

14 (F) a hospital;

15 (G) a hospital system;

16 (H) an intermediate care facility for the
17 mentally retarded or a home and community-based services waiver
18 program for persons with mental retardation adopted in accordance
19 with Section 1915(c) of the federal Social Security Act (42 U.S.C.
20 Section 1396n);

21 (I) a birthing center;

22 (J) a nursing home;

23 (K) an end stage renal disease facility licensed
24 under Section 251.011, Health and Safety Code; or

25 (L) a pharmacy.

26 (3) "Health care provider" means a taxable entity that
27 participates in the Medicaid program, Medicare program, Children's

Health Insurance Program (CHIP), state workers' compensation program, or TRICARE military health system as a provider of health care services.

(4) "Obligation" means any bond, debenture, security, mortgage-backed security, pass-through certificate, or other evidence of indebtedness of the issuing entity. The term does not include a deposit, a repurchase agreement, a loan, a lease, a participation in a loan or pool of loans, a loan collateralized by an obligation of a United States government agency, or a loan guaranteed by a United States government agency.

(4-a) "Pro bono services" means the direct provision of legal services to the poor, without an expectation of compensation.

(4-b) "Out-of-pocket expenses" means, for purposes of Subsection (g-3)(3), expenses incurred by the attorney in relation to a case, including:

(A) postage expenses;

(B) telephone calls;

(C) faxes; and

(D) paper and other office supplies.

(5) "United States government" means any department or ministry of the federal government, including a federal reserve bank. The term does not include a state or local government, a commercial enterprise owned wholly or partly by the United States government, or a local governmental entity or commercial enterprise whose obligations are guaranteed by the United States government.

(6) "United States government agency" means an

instrumentality of the United States government whose obligations are fully and explicitly guaranteed as to the timely payment of principal and interest by the full faith and credit of the United States government. The term includes the Government National Mortgage Association, the Department of Veterans Affairs, the Federal Housing Administration, the Farmers Home Administration, the Export-Import Bank, the Overseas Private Investment Corporation, the Commodity Credit Corporation, the Small Business Administration, and any successor agency.

(7) "United States government-sponsored agency" means an agency originally established or chartered by the United States government to serve public purposes specified by the United States Congress but whose obligations are not explicitly guaranteed by the full faith and credit of the United States government. The term includes the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, the Farm Credit System, the Federal Home Loan Bank System, the Student Loan Marketing Association, and any successor agency.

(r) A taxable entity shall exclude from its total revenue, to the extent included under Subsection (c)(1)(A), (c)(2)(A), or (c)(3), all revenue received that is directly derived from the operation of a facility that is:

(1) located on property owned or leased by the federal government; and

(2) managed or operated primarily to house members of the armed forces of the United States.

(r) A taxable entity shall exclude, to the extent included

1 under Subsection (c)(1)(A), (c)(2)(A), or (c)(3), total revenue
2 received from oil or gas produced, during the dates certified by the
3 comptroller pursuant to Subsection (s), from:

4 (1) an oil well designated by the Railroad Commission
5 of Texas or similar authority of another state whose production
6 averages less than 10 barrels a day over a 90-day period; and

7 (2) a gas well designated by the Railroad Commission
8 of Texas or similar authority of another state whose production
9 averages less than 250 mcf a day over a 90-day period.

10 (s) The comptroller shall certify dates during which the
11 monthly average closing price of West Texas Intermediate crude oil
12 is below \$40 per barrel and the average closing price of gas is
13 below \$5 per MMBtu, as recorded on the New York Mercantile Exchange
14 (NYMEX).

15 Sec. 171.1012. DETERMINATION OF COST OF GOODS SOLD. (a) In
16 this section:

17 (1) "Goods" means real or tangible personal property
18 sold in the ordinary course of business of a taxable entity.

19 (2) "Production" includes construction, installation,
20 manufacture, development, mining, extraction, improvement,
21 creation, raising, or growth.

22 (3)(A) "Tangible personal property" means:

23 (i) personal property that can be seen,
24 weighed, measured, felt, or touched or that is perceptible to the
25 senses in any other manner;

26 (ii) films, sound recordings, videotapes,
27 books, and other similar property embodying words, ideas, concepts,

images, or sound by the creator of the property for which, as costs are incurred in producing the property, it is intended or is reasonably likely that any tangible medium in which the property is embodied will be mass-distributed by the creator or any one or more third parties in a form that is not substantially altered; and

(iii) a computer program, as defined by Section 151.0031.

(B) "Tangible personal property" does not include:

(i) intangible property; or

(ii) services.

(b) Subject to Section 171.1014, a taxable entity that elects to subtract cost of goods sold for the purpose of computing its taxable margin shall determine the amount of that cost of goods sold as provided by this section.

(c) The cost of goods sold includes all direct costs of acquiring or producing the goods, including:

(1) labor costs;

(2) cost of materials that are an integral part of specific property produced;

(3) cost of materials that are consumed in the ordinary course of performing production activities;

(4) handling costs, including costs attributable to processing, assembling, repackaging, and inbound transportation costs;

(5) storage costs, including the costs of carrying, storing, or warehousing property, subject to Subsection (e);

1 (6) depreciation, depletion, and amortization, to the
2 extent associated with and necessary for the production of goods,
3 including recovery described by Section 197, Internal Revenue Code;

4 (7) the cost of renting or leasing equipment,
5 facilities, or real property directly used for the production of
6 the goods, including pollution control equipment and intangible
7 drilling and dry hole costs;

8 (8) the cost of repairing and maintaining equipment,
9 facilities, or real property directly used for the production of
10 the goods, including pollution control devices;

11 (9) costs attributable to research, experimental,
12 engineering, and design activities directly related to the
13 production of the goods, including all research or experimental
14 expenditures described by Section 174, Internal Revenue Code;

15 (10) geological and geophysical costs incurred to
16 identify and locate property that has the potential to produce
17 minerals;

18 (11) taxes paid in relation to acquiring or producing
19 any material, or taxes paid in relation to services that are a
20 direct cost of production;

21 (12) the cost of producing or acquiring electricity
22 sold; and

23 (13) a contribution to a partnership in which the
24 taxable entity owns an interest that is used to fund activities, the
25 costs of which would otherwise be treated as cost of goods sold of
26 the partnership, but only to the extent that those costs are related
27 to goods distributed to the taxable entity as goods-in-kind in the

1 ordinary course of production activities rather than being sold.

2 (d) In addition to the amounts includable under Subsection
3 (c), the cost of goods sold includes the following costs in relation
4 to the taxable entity's goods:

5 (1) deterioration of the goods;

6 (2) obsolescence of the goods;

7 (3) spoilage and abandonment, including the costs of
8 rework labor, reclamation, and scrap.

9 (4) if the property is held for future production,
10 preproduction direct costs allocable to the property, including
11 costs of purchasing the goods and of storage and handling the goods,
12 as provided by Subsections (c)(4) and (c)(5);

13 (5) postproduction direct costs allocable to the
14 property, including storage and handling costs, as provided by
15 Subsections (c)(4) and (c)(5);

16 (6) the cost of insurance on a plant or a facility,
17 machinery, equipment, or materials directly used in the production
18 of the goods;

19 (7) the cost of insurance on the produced goods;

20 (8) the cost of utilities, including electricity, gas,
21 and water, directly used in the production of the goods;

22 (9) the costs of quality control, including
23 replacement of defective components pursuant to standard warranty
24 policies, inspection directly allocable to the production of the
25 goods, and repairs and maintenance of goods; and

26 (10) licensing or franchise costs, including fees
27 incurred in securing the contractual right to use a trademark,

1 corporate plan, manufacturing procedure, special recipe, or other
2 similar right directly associated with the goods produced.

3 (e) The cost of goods sold does not include the following
4 costs in relation to the taxable entity's goods:

5 (1) the cost of renting or leasing equipment,
6 facilities, or real property that is not used for the production of
7 the goods;

8 (2) selling costs, including employee expenses
9 related to sales;

10 (3) distribution costs, including outbound
11 transportation costs;

12 (4) advertising costs;

13 (5) idle facility expense;

14 (6) rehandling costs;

15 (7) bidding costs, which are the costs incurred in the
16 solicitation of contracts ultimately awarded to the taxable entity;

17 (8) unsuccessful bidding costs, which are the costs
18 incurred in the solicitation of contracts not awarded to the
19 taxable entity;

20 (9) interest, including interest on debt incurred or
21 continued during the production period to finance the production of
22 the goods;

23 (10) income taxes, including local, state, federal,
24 and foreign income taxes, and franchise taxes that are assessed on
25 the taxable entity based on income;

26 (11) strike expenses, including costs associated with
27 hiring employees to replace striking personnel, but not including

1 the wages of the replacement personnel, costs of security, and
2 legal fees associated with settling strikes;

3 (12) officers' compensation;

4 (13) costs of operation of a facility that is:

5 (A) located on property owned or leased by the
6 federal government; and

7 (B) managed or operated primarily to house
8 members of the armed forces of the United States; and

9 (14) any compensation paid to an undocumented worker
10 used for the production of goods. As used in this subdivision:

11 (A) "undocumented worker" means a person who is
12 not lawfully entitled to be present and employed in the United
13 States; and

14 (B) "goods" includes the husbandry of animals,
15 the growing and harvesting of crops, and the severance of timber
16 from realty.

17 (f) A taxable entity may subtract as a cost of goods sold
18 indirect or administrative overhead costs, including all mixed
19 service costs, such as security services, legal services, data
20 processing services, accounting services, personnel operations,
21 and general financial planning and financial management costs, that
22 it can demonstrate are allocable to the acquisition or production
23 of goods, except that the amount subtracted may not exceed four
24 percent of the taxable entity's total indirect or administrative
25 overhead costs, including all mixed service costs. Any costs
26 excluded under Subsection (e) may not be subtracted under this
27 subsection.

1 (g) A taxable entity that is allowed a subtraction by this
2 section for a cost of goods sold and that is subject to Section
3 263A, 460, or 471, Internal Revenue Code, shall capitalize that
4 cost in the same manner and to the same extent that the taxable
5 entity is required or allowed to capitalize the cost under federal
6 law and regulations, except for costs excluded under Subsection
7 (e), or in accordance with Subsections (c), (d), and (f).

8 (h) A taxable entity shall determine its cost of goods sold,
9 except as otherwise provided by this section, in accordance with
10 the methods permitted by federal statutes and regulations. This
11 subsection does not affect the type or category of cost of goods
12 sold that may be subtracted under this section.

13 (i) A taxable entity may make a subtraction under this
14 section in relation to the cost of goods sold only if that entity
15 owns the goods. The determination of whether a taxable entity is an
16 owner is based on all of the facts and circumstances, including the
17 various benefits and burdens of ownership vested with the taxable
18 entity. A taxable entity furnishing labor or materials to a project
19 for the construction, improvement, remodeling, repair, or
20 industrial maintenance (as the term "maintenance" is defined in 34
21 T.A.C. Section 3.357) of real property is considered to be an owner
22 of that labor or materials and may include the costs, as allowed by
23 this section, in the computation of cost of goods sold. Solely for
24 purposes of this section, a taxable entity shall be treated as the
25 owner of goods being manufactured or produced by the entity under a
26 contract with the federal government, including any subcontracts
27 that support a contract with the federal government,

1 notwithstanding that the Federal Acquisition Regulation may
2 require that title or risk of loss with respect to those goods be
3 transferred to the federal government before the manufacture or
4 production of those goods is complete.

5 (j) A taxable entity may not make a subtraction under this
6 section for cost of goods sold to the extent the cost of goods sold
7 was funded by partner contributions and deducted under Subsection
8 (c)(13).

9 (k) Notwithstanding any other provision of this section, if
10 the taxable entity is a lending institution that offers loans to the
11 public and elects to subtract cost of goods sold, the entity may
12 subtract as a cost of goods sold an amount equal to interest
13 expense.

14 (k-1) Notwithstanding any other provision of this section,
15 the following taxable entities may subtract as a cost of goods sold
16 the costs otherwise allowed by this section in relation to tangible
17 personal property that the entity rents or leases in the ordinary
18 course of business of the entity:

19 (1) a motor vehicle rental or leasing company that
20 remits a tax on gross receipts imposed under Section 152.026;

21 (2) a heavy construction equipment rental or leasing
22 company; and

23 (3) a railcar rolling stock rental or leasing company.

24 (l) Notwithstanding any other provision of this section, a
25 payment made by one member of an affiliated group to another member
26 of that affiliated group not included in the combined group may be
27 subtracted as a cost of goods sold only if it is a transaction made

1 at arm's length.

2 (m) In this section, "arm's length" means the standard of
3 conduct under which entities that are not related parties and that
4 have substantially equal bargaining power, each acting in its own
5 interest, would negotiate or carry out a particular transaction.

6 (n) In this section, "related party" means a person,
7 corporation, or other entity, including an entity that is treated
8 as a pass-through or disregarded entity for purposes of federal
9 taxation, whether the person, corporation, or entity is subject to
10 the tax under this chapter or not, in which one person, corporation,
11 or entity, or set of related persons, corporations, or entities,
12 directly or indirectly owns or controls a controlling interest in
13 another entity.

14 Sec. 171.1013. DETERMINATION OF COMPENSATION. (a) Except
15 as otherwise provided by this section, "wages and cash
16 compensation" means the amount entered in the Medicare wages and
17 tips box of Internal Revenue Service Form W-2 or any subsequent form
18 with a different number or designation that substantially provides
19 the same information. The term also includes, to the extent not
20 included above:

21 (1) net distributive income from partnerships and from
22 trusts and limited liability companies treated as partnerships for
23 federal income tax purposes, but only if the person receiving the
24 distribution is a natural person;

25 (2) net distributive income from limited liability
26 companies and corporations treated as S corporations for federal
27 income tax purposes, but only if the person receiving the

1 distribution is a natural person; and

2 (3) stock awards and stock options deducted for
3 federal income tax purposes.

4 (b) Subject to Section 171.1014, a taxable entity that
5 elects to subtract compensation for the purpose of computing its
6 taxable margin under Section 171.101 may subtract an amount equal
7 to:

8 (1) subject to the limitation in Subsection (c), all
9 wages and cash compensation paid by the taxable entity to its
10 officers, directors, owners, partners, and employees; and

11 (2) the cost of all benefits the taxable entity
12 provides to its officers, directors, owners, partners, and
13 employees, including workers' compensation benefits, health care,
14 employer contributions made to employees' health savings accounts,
15 and retirement to the extent deductible for federal income tax
16 purposes.

17 (c) Notwithstanding the actual amount of wages and cash
18 compensation paid by a taxable entity to its officers, directors,
19 owners, partners, and employees, a taxable entity may not include
20 more than \$300,000, or the amount determined under Section 171.006,
21 for any person in the amount of wages and cash compensation it
22 determines under Section 171.101.

23 (c-1) Subject to Section 171.1014, a taxable entity that
24 elects to subtract compensation for the purpose of computing its
25 taxable margin under Section 171.101 may not subtract any wages or
26 cash compensation paid to an undocumented worker. As used in this
27 section "undocumented worker" means a person who is not lawfully

1 entitled to be present and employed in the United States.

2 (d) A taxable entity that is a staff leasing services
3 company:

4 (1) may not include as wages or cash compensation
5 payments described by Section 171.1011(k); and

6 (2) shall determine compensation as provided by this
7 section only for the taxable entity's own employees that are not
8 assigned employees.

9 (e) Subject to the other provisions of this section, in
10 determining compensation, a taxable entity that is a client company
11 that contracts with a staff leasing services company for assigned
12 employees:

13 (1) shall include payments made to the staff leasing
14 services company for wages and benefits for the assigned employees
15 as if the assigned employees were actual employees of the entity;

16 (2) may not include an administrative fee charged by
17 the staff leasing services company for the provision of the
18 assigned employees; and

19 (3) may not include any other amount in relation to the
20 assigned employees, including payroll taxes.

21 (f) A taxable entity that is a management company:

22 (1) may not include as wages or cash compensation any
23 amounts reimbursed by a managed entity; and

24 (2) shall determine compensation as provided by this
25 section for only those wage and compensation payments that are not
26 reimbursed by a managed entity.

27 (g) A taxable entity that is a managed entity shall include

1 reimbursements made to the management company for wages and
2 compensation as if the reimbursed amounts had been paid to
3 employees of the managed entity.

4 (h) Subject to Section 171.1014, a taxable entity that
5 elects to subtract compensation for the purpose of computing its
6 taxable margin under Section 171.101 may not include as wages or
7 cash compensation amounts paid to an employee whose primary
8 employment is directly associated with the operation of a facility
9 that is:

10 (1) located on property owned or leased by the federal
11 government; and

12 (2) managed or operated primarily to house members of
13 the armed forces of the United States.

14 Sec. 171.1014. COMBINED REPORTING; AFFILIATED GROUP
15 ENGAGED IN UNITARY BUSINESS. (a) Taxable entities that are part of
16 an affiliated group engaged in a unitary business shall file a
17 combined group report in lieu of individual reports based on the
18 combined group's business. The combined group may not include a
19 taxable entity that conducts business outside the United States if
20 80 percent or more of the taxable entity's property and payroll, as
21 determined by factoring under Chapter 141, are assigned to
22 locations outside the United States. In applying Chapter 141, if
23 either the property factor or the payroll factor is zero, the
24 denominator is one. The combined group may not include a taxable
25 entity that conducts business outside the United States and has no
26 property or payroll if 80 percent or more of the taxable entity's
27 gross receipts, as determined under Sections 171.103, 171.105, and

1 171.1055, are assigned to locations outside the United States.

2 (b) The combined group is a single taxable entity for
3 purposes of the application of the tax imposed under this chapter.

4 (c) For purposes of Section 171.101, a combined group shall
5 determine its total revenue by:

6 (1) determining the total revenue of each of its
7 members as provided by Section 171.1011 as if the member were an
8 individual taxable entity;

9 (2) adding the total revenues of the members
10 determined under Subdivision (1) together; and

11 (3) subtracting, to the extent included under Section
12 171.1011(c)(1)(A), (c)(2)(A), or (c)(3), items of total revenue
13 received from a member of the combined group.

14 (d) For purposes of Section 171.101, a combined group shall
15 make an election to subtract either cost of goods sold or
16 compensation that applies to all of its members.

17 (e) For purposes of Section 171.101, a combined group that
18 elects to subtract costs of goods sold shall determine that amount
19 by:

20 (1) determining the cost of goods sold for each of its
21 members as provided by Section 171.1012 as if the member were an
22 individual taxable entity;

23 (2) adding the amounts of cost of goods sold
24 determined under Subdivision (1) together; and

25 (3) subtracting from the amount determined under
26 Subdivision (2) any cost of goods sold amounts paid from one member
27 of the combined group to another member of the combined group, but

1 only to the extent the corresponding item of total revenue was
 2 subtracted under Subsection (c)(3).

3 (f) For purposes of Section 171.101, a combined group that
 4 elects to subtract compensation shall determine that amount by:

5 (1) determining the compensation for each of its
 6 members as provided by Section 171.1013 as if each member were an
 7 individual taxable entity;

8 (2) adding the amounts of compensation determined
 9 under Subdivision (1) together; and

10 (3) subtracting from the amount determined under
 11 Subdivision (2) any compensation amounts paid from one member of
 12 the combined group to another member of the combined group, but only
 13 to the extent the corresponding item of total revenue was
 14 subtracted under Subsection (c)(3).

15 (g) A combined group may elect to include in the combined
 16 group an exempt entity that would be included in the group if the
 17 entity were not exempt and to treat the exempt entity as if it were a
 18 taxable entity.

19 Sec 171.1015. REPORTING FOR CERTAIN PARTNERSHIPS IN TIERED
 20 PARTNERSHIP ARRANGEMENT. (a) In this section, "tiered partnership
 21 arrangement" means an ownership structure in which all of the
 22 interests in one partnership, trust, or limited liability company
 23 that is treated for federal income taxes as a partnership or a
 24 limited liability company treated as an S corporation for federal
 25 income tax purposes (an "upper tier partnership") are owned by one
 26 or more other taxable entities (a "lower tier entity"). A tiered
 27 partnership arrangement may have two or more tiers.

1 (b) In addition to the tax it is required to pay under this
2 chapter on its own taxable margin, a taxable entity that is a lower
3 tier entity may pay the tax on the taxable margin of a higher tier
4 partnership if the higher tier partnership submits a report to the
5 comptroller showing the amount of taxable margin that each lower
6 tier entity that owns it should include within the lower tier
7 entity's own taxable margin, according to the profits interest of
8 the lower tier entity. An upper tier partnership is not required to
9 pay tax under this chapter on any taxable margin reported under this
10 section.

11 (c) This section does not apply to that percentage of the
12 taxable margin attributable to a lower tier entity by an upper tier
13 partnership if the lower tier entity is not subject to the tax under
14 this chapter. In this case, the higher tier partnership is liable
15 for the tax on its taxable margin.

16 (d) The comptroller shall adopt rules to administer this
17 section.

18 ~~[Sec. 171.102. DETERMINATION OF TAXABLE CAPITAL OF~~
19 ~~CORPORATION IN PROCESS OF LIQUIDATION. (a) "Corporation in the~~
20 ~~process of liquidation" means a corporation that:~~

21 ~~[(1) adopts and pursues in good faith a plan to marshal~~
22 ~~the assets of the corporation, to pay or settle with the~~
23 ~~corporation's creditors and debtors, and to apportion the remaining~~
24 ~~assets of the corporation among the corporation's stockholders;~~

25 ~~[(2) adopts the plan by a resolution approved by the~~
26 ~~corporation's board of directors and ratified by a majority of the~~
27 ~~stockholders of record; and~~

1 ~~[(3) conducts the liquidation in the manner provided~~
2 ~~by the law of this state to dissolve a corporation.~~

3 ~~[(b) The taxable capital of a corporation in the process of~~
4 ~~liquidation is the difference between the amount of the~~
5 ~~corporation's stock issued and the amount of the liquidating~~
6 ~~dividends paid on the stock.~~

7 ~~[(c) The president and the secretary of the corporation~~
8 ~~shall file an affidavit with the comptroller containing information~~
9 ~~about the amount of liquidating dividends paid and a statement that~~
10 ~~the corporation is in the process of liquidation. The plan~~
11 ~~described by Subsection (a) of this section for the corporation's~~
12 ~~liquidation shall be attached to and be a part of the affidavit.~~

13 ~~[(d) This section applies only to the computation of a~~
14 ~~corporation's taxable capital under Section 171.101 of this code.]~~

15 Sec. 171.103. DETERMINATION OF GROSS RECEIPTS FROM BUSINESS
16 DONE IN THIS STATE FOR MARGIN ~~[TAXABLE CAPITAL]~~. (a) Subject to
17 Section 171.1035, in ~~[In]~~ apportioning margin ~~[taxable capital]~~,
18 the gross receipts of a taxable entity ~~[corporation]~~ from its
19 business done in this state is the sum of the taxable entity's
20 ~~[corporation's]~~ receipts from:

21 ~~[(1) each sale of tangible personal property if the~~
22 ~~property is delivered or shipped to a buyer in this state regardless~~
23 ~~of the FOB point or another condition of the sale, and each sale of~~
24 ~~tangible personal property shipped from this state to a purchaser~~
25 ~~in another state in which the seller is not subject to taxation;~~

26 ~~[(2) each service performed in this state;~~

27 ~~[(3) each rental of property situated in this state;~~

1 ~~[(4) the use of a patent, copyright, trademark,~~
2 ~~franchise, or license in this state,~~

3 ~~[(5) each sale of real property located in this state,~~
4 ~~including royalties from oil, gas, or other mineral interests; and~~

5 ~~[(6) other business done in this state.~~

6 ~~[Sec. 171.1032. DETERMINATION OF GROSS RECEIPTS FROM~~
7 ~~BUSINESS DONE IN THIS STATE FOR TAXABLE EARNED SURPLUS. (a) Except~~
8 ~~for the gross receipts of a corporation that are subject to the~~
9 ~~provisions of Section 171.1061, in apportioning taxable earned~~
10 ~~surplus, the gross receipts of a corporation from its business done~~
11 ~~in this state is the sum of the corporation's receipts from:]~~

12 (1) each sale of tangible personal property if the
13 property is delivered or shipped to a buyer in this state regardless
14 of the FOB point or another condition of the sale~~[, and each sale of~~
15 ~~tangible personal property shipped from this state to a purchaser~~
16 ~~in another state in which the seller is not subject to any tax on, or~~
17 ~~measured by, net income, without regard to whether the tax is~~
18 ~~imposed];~~

19 (2) each service performed in this state, except that
20 receipts derived from servicing loans secured by real property are
21 in this state if the real property is located in this state;

22 (3) each rental of property situated in this state;

23 (4) the use of a patent, copyright, trademark,
24 franchise, or license in this state;

25 (5) each sale of real property located in this state,
26 including royalties from oil, gas, or other mineral interests; and

27 (6) ~~[each partnership or joint venture to the extent~~

1 ~~provided by Subsection (c), and~~

2 ~~[(7)] other business done in this state.~~

3 (b) A combined group shall include in its gross receipts
4 computed under Subsection (a) the gross receipts of each taxable
5 entity that is a member of the combined group and that has a nexus
6 with this state for the purpose of taxation. ~~[A corporation shall~~
7 ~~deduct from its gross receipts computed under Subsection (a) any~~
8 ~~amount to the extent included under Subsection (a) because of the~~
9 ~~application of Section 78 or Sections 951-964, Internal Revenue~~
10 ~~Code, any amount excludable under Section 171.110(k), and dividends~~
11 ~~received from a subsidiary, associate, or affiliated corporation~~
12 ~~that does not transact a substantial portion of its business or~~
13 ~~regularly maintain a substantial portion of its assets in the~~
14 ~~United States.~~

15 ~~[(c) A corporation shall include in its gross receipts~~
16 ~~computed under Subsection (a) the corporation's share of the gross~~
17 ~~receipts of each partnership and joint venture of which the~~
18 ~~corporation is a part apportioned to this state as though the~~
19 ~~corporation directly earned the receipts, including receipts from~~
20 ~~business done with the corporation.~~

21 ~~[Sec. 171.104. GROSS RECEIPTS FROM BUSINESS DONE IN TEXAS.~~
22 ~~DEDUCTION FOR FOOD AND MEDICINE RECEIPTS. A corporation may deduct~~
23 ~~from its receipts includable under Section 171.103(1) of this code~~
24 ~~the amount of the corporation's receipts from sales of the~~
25 ~~following items, if the items are shipped from outside this state~~
26 ~~and the receipts would be includable under Section 171.103(1) of~~
27 ~~this code in the absence of this section.~~

~~[(1) food that is exempted from the Limited Sales, Excise, and Use Tax Act by Section 151.314(a) of this code, and~~

~~[(2) health care supplies that are exempted from the Limited Sales, Excise, and Use Tax Act by Section 151.313 of this code.]~~

Sec. 171.105. ~~[DETERMINATION OF GROSS RECEIPTS FROM ENTIRE BUSINESS FOR TAXABLE CAPITAL. (a) In apportioning taxable capital, the gross receipts of a corporation from its entire business is the sum of the corporation's receipts from:~~

~~[(1) each sale of the corporation's tangible personal property;~~

~~[(2) each service, rental, or royalty; and~~

~~[(3) other business.~~

~~[(b) If a corporation sells an investment or capital asset, the corporation's gross receipts from its entire business for taxable capital include only the net gain from the sale.~~

~~[Sec. 171.1051.] DETERMINATION OF GROSS RECEIPTS FROM ENTIRE BUSINESS FOR MARGIN [TAXABLE EARNED SURPLUS]. (a) Subject to Section 171.1055 [Except for the gross receipts of a corporation that are subject to the provisions of Section 171.1061], in apportioning margin [taxable earned surplus], the gross receipts of a taxable entity [corporation] from its entire business is the sum of the taxable entity's [corporation's] receipts from:~~

~~(1) each sale of the taxable entity's [corporation's] tangible personal property;~~

~~(2) each service, rental, or royalty; and~~

~~(3) [each partnership and joint venture as provided by~~

1 ~~Subsection (d), and~~

2 ~~[(4)]~~ other business.

3 (b) If a taxable entity ~~[corporation]~~ sells an investment or
4 capital asset, the taxable entity's ~~[corporation's]~~ gross receipts
5 from its entire business for taxable margin ~~[earned surplus]~~
6 includes only the net gain from the sale.

7 (c) A combined group shall include in its gross receipts
8 computed under Subsection (a) the gross receipts of each taxable
9 entity that is a member of the combined group, without regard to
10 whether that entity has a nexus with this state for the purpose of
11 taxation.

12 Sec. 171.1055. EXCLUSION OF CERTAIN RECEIPTS FOR MARGIN
13 APPORTIONMENT. (a) In apportioning margin, receipts excluded from
14 total revenue by a taxable entity under Section 171.1011 may not be
15 included in either the receipts of the taxable entity from its
16 business done in this state as determined under Section 171.103 or
17 the receipts of the taxable entity from its entire business done as
18 determined under Section 171.105.

19 (b) In apportioning margin, receipts derived from
20 transactions between individual members of a combined group that
21 are excluded under Section 171.1014(c)(3) may not be included in
22 the receipts of the taxable entity from its business done in this
23 state as determined under Section 171.103, except that receipts
24 derived from the sale of tangible personal property between
25 individual members of a combined group where one member party to the
26 transaction does not have nexus in this state shall be included in
27 the receipts of the taxable entity from its business done in this

1 state as determined under Section 171.103 to the extent that the
 2 member of the combined group that does not have nexus in this state
 3 resells the tangible personal property without modification to a
 4 purchaser in this state.

5 (c) In apportioning margin, receipts derived from
 6 transactions between individual members of a combined group that
 7 are excluded under Section 171.1014(c)(3) may not be included in
 8 the receipts of the taxable entity from its entire business done as
 9 determined under Section 171.105. ~~A corporation shall deduct from~~
 10 ~~its gross receipts computed under Subsection (a) any amount to the~~
 11 ~~extent included in Subsection (a) because of the application of~~
 12 ~~Section 78 or Sections 951-964, Internal Revenue Code, any amount~~
 13 ~~excludable under Section 171.110(k), and dividends received from a~~
 14 ~~subsidiary, associate, or affiliated corporation that does not~~
 15 ~~transact a substantial portion of its business or regularly~~
 16 ~~maintain a substantial portion of its assets in the United States.~~

17 ~~[(d) A corporation shall include in its gross receipts~~
 18 ~~computed under Subsection (a) the corporation's share of the gross~~
 19 ~~receipts of each partnership and joint venture of which the~~
 20 ~~corporation is a part.]~~

21 Sec. 171.106. APPORTIONMENT OF MARGIN ~~[TAXABLE CAPITAL AND~~
 22 ~~TAXABLE EARNED SURPLUS]~~ TO THIS STATE. (a) ~~[Except as provided by~~
 23 ~~Subsections (c) and (d), a corporation's taxable capital is~~
 24 ~~apportioned to this state to determine the amount of the tax imposed~~
 25 ~~under Section 171.002(b)(1) by multiplying the corporation's~~
 26 ~~taxable capital by a fraction, the numerator of which is the~~
 27 ~~corporation's gross receipts from business done in this state, as~~

1 ~~determined under Section 171.103, and the denominator of which is~~
 2 ~~the corporation's gross receipts from its entire business, as~~
 3 ~~determined under Section 171.105.~~

4 ~~[(b)]~~ Except as provided by this section ~~[Subsections (c)~~
 5 ~~and (d)]~~, a taxable entity's margin ~~[corporation's taxable earned~~
 6 ~~surplus]~~ is apportioned to this state to determine the amount of tax
 7 imposed under Section 171.002 ~~[171.002(b)(2)]~~ by multiplying the
 8 margin ~~[taxable earned surplus]~~ by a fraction, the numerator of
 9 which is the taxable entity's ~~[corporation's]~~ gross receipts from
 10 business done in this state, as determined under Section 171.103
 11 ~~[171.1032]~~, and the denominator of which is the taxable entity's
 12 ~~[corporation's]~~ gross receipts from its entire business, as
 13 determined under Section 171.105 ~~[171.1051]~~.

14 ~~(b)~~ ~~[(c)]~~ A taxable entity's margin ~~[corporation's taxable~~
 15 ~~capital or earned surplus]~~ that is derived, directly or indirectly,
 16 from the sale of management, distribution, or administration
 17 services to or on behalf of a regulated investment company,
 18 including a taxable entity ~~[corporation]~~ that includes trustees or
 19 sponsors of employee benefit plans that have accounts in a
 20 regulated investment company, is apportioned to this state to
 21 determine the amount of the tax imposed under Section 171.002 by
 22 multiplying the taxable entity's ~~[corporation's]~~ total margin
 23 ~~[taxable capital or earned surplus]~~ from the sale of services to or
 24 on behalf of a regulated investment company by a fraction, the
 25 numerator of which is the average of the sum of shares owned at the
 26 beginning of the year and the sum of shares owned at the end of the
 27 year by the investment company shareholders who are commercially

1 domiciled in this state or, if the shareholders are individuals,
2 are residents of this state, and the denominator of which is the
3 average of the sum of shares owned at the beginning of the year and
4 the sum of shares owned at the end of the year by all investment
5 company shareholders. ~~[The corporation shall make a separate~~
6 ~~computation to allocate taxable capital and earned surplus.]~~ In
7 this subsection, "regulated investment company" has the meaning
8 assigned by Section 851(a), Internal Revenue Code.

9 (c) ~~[(d)]~~ A taxable entity's margin ~~[corporation's taxable~~
10 ~~capital or taxable earned surplus]~~ that is derived, directly or
11 indirectly, from the sale of management, administration, or
12 investment services to an employee retirement plan is apportioned
13 to this state to determine the amount of the tax imposed under
14 Section 171.002 by multiplying the taxable entity's ~~[corporation's]~~
15 total margin ~~[taxable capital or earned surplus]~~ from the sale of
16 services to an employee retirement plan company by a fraction, the
17 numerator of which is the average of the sum of beneficiaries
18 domiciled in Texas at the beginning of the year and the sum of
19 beneficiaries domiciled in Texas at the end of the year, and the
20 denominator of which is the average of the sum of all beneficiaries
21 at the beginning of the year and the sum of all beneficiaries at the
22 end of the year. ~~[The corporation shall make a separate computation~~
23 ~~to apportion taxable capital and earned surplus.]~~ In this section,
24 "employee retirement plan" means a plan or other arrangement that
25 is qualified under Section 401(a), Internal Revenue Code, or
26 satisfies the requirements of Section 403, Internal Revenue Code,
27 or a government plan described in Section 414(d), Internal Revenue

1 Code. The term does not include an individual retirement account or
2 individual retirement annuity within the meaning of Section 408,
3 Internal Revenue Code.

4 ~~(d) [(e) On or before January 1, 1998, each entity~~
5 ~~registered with the State Securities Board under The Securities Act~~
6 ~~(Article 581, Vernon's Texas Civil Statutes) that provides~~
7 ~~management, administration, or investment services to an employee~~
8 ~~retirement plan, must file a report with the comptroller containing~~
9 ~~such information as the comptroller deems necessary in order to~~
10 ~~determine the fiscal impact of Subsection (d). The State~~
11 ~~Securities Board and the Securities Commissioner shall cooperate~~
12 ~~with the comptroller in obtaining the information. The Securities~~
13 ~~Commissioner shall impose the penalties provided in The Securities~~
14 ~~Act (Article 581-1 et seq., Vernon's Texas Civil Statutes) against~~
15 ~~any entity that the comptroller certifies is delinquent in the~~
16 ~~filing of the report required by this section.~~

17 ~~[(f) On or before September 1, 1998, the comptroller shall~~
18 ~~issue a report which evaluates the statewide fiscal impact of~~
19 ~~Subsection (d). If the comptroller determines that implementing~~
20 ~~Subsection (d) will not have a negative fiscal impact on this state,~~
21 ~~Subsection (d) shall be effective for reports or returns originally~~
22 ~~due on or after January 1, 1999. If the comptroller determines that~~
23 ~~there will be a negative fiscal impact, that subsection shall not be~~
24 ~~implemented.~~

25 ~~[(g) If this Act and another Act of the 75th Legislature,~~
26 ~~Regular Session, 1997, make the same substantive change from the~~
27 ~~current law but differ in text, this Act prevails regardless of the~~

1 ~~relative dates of enactment.~~

2 ~~[(h)]~~ A banking corporation shall exclude from the
3 numerator of the bank's apportionment factor interest earned on
4 federal funds and interest earned on securities sold under an
5 agreement to repurchase that are held in this state in a
6 correspondent bank that is domiciled in this state. In this
7 subsection, "correspondent" has the meaning assigned by 12 C.F.R.
8 Section 206.2(c).

9 ~~(e)~~ ~~[(i)]~~ Receipts from services that a defense
10 readjustment project performs in a defense economic readjustment
11 zone are not receipts from business done in this state.

12 ~~[Sec. 171.1061. ALLOCATION OF CERTAIN TAXABLE EARNED~~
13 ~~SURPLUS TO THIS STATE. An item of income included in a~~
14 ~~corporation's taxable earned surplus, except that portion derived~~
15 ~~from dividends and interest, that a state, other than this state, or~~
16 ~~a country, other than the United States, cannot tax because the~~
17 ~~activities generating that item of income do not have sufficient~~
18 ~~unitary connection with the corporation's other activities~~
19 ~~conducted within that state or country under the United States~~
20 ~~Constitution, is allocated to this state if the corporation's~~
21 ~~commercial domicile is in this state. Income that can only be~~
22 ~~allocated to the state of commercial domicile because the income~~
23 ~~has insufficient unitary connection with any other state or country~~
24 ~~shall be allocated to this state or another state or country net of~~
25 ~~expenses related to that income. A portion of a corporation's~~
26 ~~taxable earned surplus allocated to this state under this section~~
27 ~~may not be apportioned under Section 171.110(a)(2).]~~

1 Sec. 171.107. DEDUCTION OF COST OF SOLAR ENERGY DEVICE FROM
2 MARGIN ~~[TAXABLE CAPITAL OR TAXABLE EARNED SURPLUS]~~ APPORTIONED TO
3 THIS STATE. (a) In this section, "solar energy device" means a
4 system or series of mechanisms designed primarily to provide
5 heating or cooling or to produce electrical or mechanical power by
6 collecting and transferring solar-generated energy. The term
7 includes a mechanical or chemical device that has the ability to
8 store solar-generated energy for use in heating or cooling or in the
9 production of power.

10 (b) A taxable entity ~~[corporation]~~ may deduct from ~~[its~~
11 ~~apportioned taxable capital the amortized cost of a solar energy~~
12 ~~device or from]~~ its apportioned margin ~~[taxable earned surplus]~~ 10
13 percent of the amortized cost of a solar energy device if:

14 (1) the device is acquired by the taxable entity
15 ~~[corporation]~~ for heating or cooling or for the production of
16 power;

17 (2) the device is used in this state by the taxable
18 entity ~~[corporation]~~; and

19 (3) the cost of the device is amortized in accordance
20 with Subsection (c) ~~[of this section]~~.

21 (c) The amortization of the cost of a solar energy device
22 must:

23 (1) be for a period of at least 60 months;

24 (2) provide for equal monthly amounts or conform to
25 federal depreciation schedules;

26 (3) begin on the month in which the device is placed in
27 service in this state; and

1 (4) cover only a period in which the device is in use
2 in this state.

3 (d) A taxable entity [~~corporation~~] that makes a deduction
4 under this section shall file with the comptroller an amortization
5 schedule showing the period in which a deduction is to be made. On
6 the request of the comptroller, the taxable entity [~~corporation~~]
7 shall file with the comptroller proof of the cost of the solar
8 energy device or proof of the device's operation in this state.

9 ~~[(e) A corporation may elect to make the deduction~~
10 ~~authorized by this section either from apportioned taxable capital~~
11 ~~or apportioned taxable earned surplus for each separate regular~~
12 ~~annual period. An election for an initial period applies to the~~
13 ~~second tax period and to the first regular annual period.]~~

14 Sec. 171.108. DEDUCTION OF COST OF CLEAN COAL PROJECT FROM
15 MARGIN [~~TAXABLE CAPITAL OR TAXABLE EARNED SURPLUS~~] APPORTIONED TO
16 THIS STATE. (a) In this section, "clean coal project" has the
17 meaning assigned by Section 5.001, Water Code.

18 (b) A taxable entity [~~corporation~~] may deduct from its
19 apportioned margin [~~taxable capital the amortized cost of equipment~~
20 ~~or from its apportioned taxable earned surplus~~] 10 percent of the
21 amortized cost of equipment:

- 22 (1) that is used in a clean coal project;
- 23 (2) that is acquired by the taxable entity
24 [~~corporation~~] for use in generation of electricity, production of
25 process steam, or industrial production;
- 26 (3) that the taxable entity [~~corporation~~] uses in this
27 state; and

1 (4) the cost of which is amortized in accordance with
2 Subsection (c).

3 (c) The amortization of the cost of capital used in a clean
4 coal project must:

- 5 (1) be for a period of at least 60 months;
6 (2) provide for equal monthly amounts;
7 (3) begin in the month during which the equipment is
8 placed in service in this state; and
9 (4) cover only a period during which the equipment is
10 used in this state.

11 (d) A taxable entity [~~corporation~~] that makes a deduction
12 under this section shall file with the comptroller an amortization
13 schedule showing the period for which the deduction is to be made.
14 On the request of the comptroller, the taxable entity [~~corporation~~]
15 shall file with the comptroller proof of the cost of the equipment
16 or proof of the equipment's operation in this state.

17 ~~[(e) A corporation may elect to make the deduction~~
18 ~~authorized by this section from apportioned taxable capital or~~
19 ~~apportioned taxable earned surplus, but not from both, for each~~
20 ~~separate regular annual period. An election for an initial period~~
21 ~~applies to the second tax period and to the first regular annual~~
22 ~~period.~~

23 ~~[Sec. 171.109. SURPLUS. (a) In this chapter:~~

24 ~~[(1) "Surplus" means the net assets of a corporation~~
25 ~~minus its stated capital. For a limited liability company,~~
26 ~~"surplus" means the net assets of the company minus its members'~~
27 ~~contributions. Surplus includes unrealized, estimated, or~~

1 ~~contingent losses or obligations or any writedown of assets other~~
2 ~~than those listed in Subsection (i) of this section net of~~
3 ~~appropriate income tax provisions. The definition under this~~
4 ~~subdivision does not apply to earned surplus.~~

5 ~~[(2) "Net assets" means the total assets of a~~
6 ~~corporation minus its total debts.~~

7 ~~[(3) "Debt" means any legally enforceable obligation~~
8 ~~measured in a certain amount of money which must be performed or~~
9 ~~paid within an ascertainable period of time or on demand.~~

10 ~~[(a-1) A legally enforceable obligation that requires the~~
11 ~~return of a like-kind property that was borrowed will be considered~~
12 ~~debt if it is a liability according to generally accepted~~
13 ~~accounting principles and if the return must be made within an~~
14 ~~ascertainable period of time or on demand. The amount that will be~~
15 ~~considered debt is the fair market value measured on the last day on~~
16 ~~which the report is based as required by Section 171.153. For~~
17 ~~purposes of this subsection, "like-kind property" means the same~~
18 ~~quantity, quality, and nature or character as the property~~
19 ~~borrowed.~~

20 ~~[(b) Except as otherwise provided in this section, a~~
21 ~~corporation must compute its surplus, assets, and debts according~~
22 ~~to generally accepted accounting principles. If generally accepted~~
23 ~~accounting principles are unsettled or do not specify an accounting~~
24 ~~practice for a particular purpose related to the computation of~~
25 ~~surplus, assets, or debts, the comptroller by rule may establish~~
26 ~~rules to specify the applicable accounting practice for that~~
27 ~~purpose.~~

1 ~~[(c) A corporation whose taxable capital is less than \$1~~
 2 ~~million may report its surplus according to the method used in the~~
 3 ~~corporation's most recent federal income tax return originally due~~
 4 ~~on or before the date on which the corporation's franchise tax~~
 5 ~~report is originally due. In determining if taxable capital is less~~
 6 ~~than \$1 million, the corporation shall apply the methods the~~
 7 ~~corporation used in computing that federal income tax return unless~~
 8 ~~another method is required under this chapter.~~

9 ~~[(d) A corporation shall report its surplus based solely on~~
 10 ~~its own financial condition. Consolidated reporting of surplus is~~
 11 ~~prohibited.~~

12 ~~[(e) Unless the provisions of Section 171.111 apply due to~~
 13 ~~an election under that section, a corporation may not change the~~
 14 ~~accounting methods used to compute its surplus more often than once~~
 15 ~~every four years without the written consent of the comptroller. A~~
 16 ~~change in accounting methods is not justified solely because it~~
 17 ~~results in a reduction of tax liability.~~

18 ~~[(f) A corporation declaring dividends shall exclude those~~
 19 ~~dividends from its taxable capital, and a corporation receiving~~
 20 ~~dividends shall include those dividends in its gross receipts and~~
 21 ~~taxable capital as of the earlier of:~~

22 ~~[(1) the date the dividends are declared, if the~~
 23 ~~dividends are actually paid within one year after the declaration~~
 24 ~~date; or~~

25 ~~[(2) the date the dividends are actually paid.~~

26 ~~[(g) All oil and gas exploration and production activities~~
 27 ~~conducted by a corporation that reports its surplus according to~~

1 ~~generally accepted accounting principles as required or permitted~~
2 ~~by this chapter must be reported according to the successful~~
3 ~~efforts or the full cost method of accounting.~~

4 ~~[(h) A parent or investor corporation must use the cost~~
5 ~~method of accounting in reporting and calculating the franchise tax~~
6 ~~on its investments in subsidiary corporations or other investees.~~
7 ~~The retained earnings of a subsidiary corporation or other investee~~
8 ~~before acquisition by the parent or investor corporation may not be~~
9 ~~excluded from the cost of the subsidiary corporation or investee to~~
10 ~~the parent or investor corporation and must be included by the~~
11 ~~parent or investor corporation in calculating its surplus.~~

12 ~~[(i) The following accounts may also be excluded from~~
13 ~~surplus, to the extent they are in conformance with generally~~
14 ~~accepted accounting principles or the appropriate federal income~~
15 ~~tax method, whichever is applicable:~~

16 ~~[(1) a reserve or allowance for uncollectable~~
17 ~~accounts; and~~

18 ~~[(2) a contra-asset account for depletion,~~
19 ~~depreciation, or amortization.~~

20 ~~[(j) A corporation may not exclude from surplus:~~

21 ~~[(1) liabilities for compensation and other benefits~~
22 ~~provided to employees, other than wages, that are not debt as of the~~
23 ~~end of the accounting period on which the taxable capital component~~
24 ~~is based, including retirement, medical, insurance,~~
25 ~~postretirement, and other similar benefits; and~~

26 ~~[(2) deferred investment tax credits.~~

27 ~~[(k) Notwithstanding any other provision in this chapter, a~~

~~corporation subject to the tax imposed by this chapter shall use double entry bookkeeping to account for all transactions that affect the computation of that tax.~~

~~[(1) The "first in-first out" and "last in-first out" methods of accounting are acceptable methods for computing surplus.~~

~~[(m) A corporation may not use the push-down method of accounting in computing or reporting its surplus.~~

~~[(n) A corporation must use the equity method of accounting when reporting an investment in a partnership or joint venture.~~

~~[Sec. 171.110. DETERMINATION OF NET TAXABLE EARNED SURPLUS.~~

~~(a) The net taxable earned surplus of a corporation is computed by:~~

~~[(1) determining the corporation's reportable federal taxable income, subtracting from that amount any amount excludable under Subsection (k), any amount included in reportable federal taxable income under Section 78 or Sections 951-964, Internal Revenue Code, and dividends received from a subsidiary, associate, or affiliated corporation that does not transact a substantial portion of its business or regularly maintain a substantial portion of its assets in the United States, and adding to that amount any compensation of officers or directors, or if a bank, any compensation of directors and executive officers, to the extent excluded in determining federal taxable income to determine the corporation's taxable earned surplus,~~

~~[(2) apportioning the corporation's taxable earned surplus to this state as provided by Section 171.106(b) or (c), as applicable, to determine the corporation's apportioned taxable earned surplus,~~

1 ~~[(3) adding the corporation's taxable earned surplus~~
2 ~~allocated to this state as provided by Section 171.1061, and~~

3 ~~[(4) subtracting from that amount any allowable~~
4 ~~deductions and any business loss that is carried forward to the tax~~
5 ~~reporting period and deductible under Subsection (c).~~

6 ~~[(b) Except as provided by Subsection (c), a corporation is~~
7 ~~not required to add the compensation of officers or directors as~~
8 ~~required by Subsection (a)(1) if the corporation is:~~

9 ~~[(1) a corporation that has not more than 35~~
10 ~~shareholders; or~~

11 ~~[(2) an S corporation, as that term is defined by~~
12 ~~Section 1361, Internal Revenue Code.~~

13 ~~[(c) A subsidiary corporation may not claim the exclusion~~
14 ~~under Subsection (b) if it has a parent corporation that does not~~
15 ~~qualify for the exclusion. For purposes of this subsection, a~~
16 ~~corporation qualifies as a parent if it ultimately controls the~~
17 ~~subsidiary, even if the control arises through a series or group of~~
18 ~~other subsidiaries or entities. Control is presumed if a parent~~
19 ~~corporation directly or indirectly owns, controls, or holds a~~
20 ~~majority of the outstanding voting stock of a corporation or~~
21 ~~ownership interests in another entity.~~

22 ~~[(d) A corporation's reportable federal taxable income is~~
23 ~~the corporation's federal taxable income after Schedule C special~~
24 ~~deductions and before net operating loss deductions as computed~~
25 ~~under the Internal Revenue Code, except that an S corporation's~~
26 ~~reportable federal taxable income is the amount of the income~~
27 ~~reportable to the Internal Revenue Service as taxable to the~~

1 ~~corporation's shareholders.~~

2 ~~[(e) For purposes of this section, a business loss is any~~
3 ~~negative amount after apportionment and allocation. The business~~
4 ~~loss shall be carried forward to the year succeeding the loss year~~
5 ~~as a deduction to net taxable earned surplus, then successively to~~
6 ~~the succeeding four taxable years after the loss year or until the~~
7 ~~loss is exhausted, whichever occurs first, but for not more than~~
8 ~~five taxable years after the loss year. Notwithstanding the~~
9 ~~preceding sentence, a business loss from a tax year that ends before~~
10 ~~January 1, 1991, may not be used to reduce net taxable earned~~
11 ~~surplus. A business loss can be carried forward only by the~~
12 ~~corporation that incurred the loss and cannot be transferred to or~~
13 ~~claimed by any other entity, including the survivor of a merger if~~
14 ~~the loss was incurred by the corporation that did not survive the~~
15 ~~merger.~~

16 ~~[(f) A corporation may use either the "first in-first out"~~
17 ~~or "last in-first out" method of accounting to compute its net~~
18 ~~taxable earned surplus, but only to the extent that the corporation~~
19 ~~used that method on its most recent federal income tax report~~
20 ~~originally due on or before the date on which the corporation's~~
21 ~~franchise tax report is originally due.~~

22 ~~[(g) For purposes of this section, an approved Employee~~
23 ~~Stock Ownership Plan controlling a minority interest and voted~~
24 ~~through a single trustee shall be considered one shareholder.~~

25 ~~[(h) A corporation shall report its net taxable earned~~
26 ~~surplus based solely on its own financial condition. Consolidated~~
27 ~~reporting is prohibited.~~

1 ~~[(i) For purposes of this section, any person designated as~~
2 ~~an officer is presumed to be an officer if that person,~~

3 ~~[(1) holds an office created by the board of directors~~
4 ~~or under the corporate charter or bylaws; and~~

5 ~~[(2) has legal authority to bind the corporation with~~
6 ~~third parties by executing contracts or other legal documents.~~

7 ~~[(j) A corporation may rebut the presumption described in~~
8 ~~Subsection (i) that a person is an officer if it conclusively shows,~~
9 ~~through the person's job description or other documentation, that~~
10 ~~the person does not participate or have authority to participate in~~
11 ~~significant policy making aspects of the corporate operations.~~

12 ~~[(k) Dividends and interest received from federal~~
13 ~~obligations are not included in earned surplus or gross receipts~~
14 ~~for earned surplus purposes.~~

15 ~~[(l) In this section:~~

16 ~~[(1) "Federal obligations" means:~~

17 ~~[(A) stocks and other direct obligations of, and~~
18 ~~obligations unconditionally guaranteed by, the United States~~
19 ~~government and United States government agencies; and~~

20 ~~[(B) direct obligations of a United States~~
21 ~~government-sponsored agency.~~

22 ~~[(2) "Obligation" means any bond, debenture,~~
23 ~~security, mortgage-backed security, pass-through certificate, or~~
24 ~~other evidence of indebtedness of the issuing entity. The term does~~
25 ~~not include a deposit, a repurchase agreement, a loan, a lease, a~~
26 ~~participation in a loan or pool of loans, a loan collateralized by~~
27 ~~an obligation of a United States government agency, or a loan~~

1 ~~guaranteed by a United States government agency.~~

2 ~~[(3) "United States government" means any department~~
3 ~~or ministry of the federal government, including, a federal reserve~~
4 ~~bank. The term does not include a state or local government, a~~
5 ~~commercial enterprise owned wholly or partly by the United States~~
6 ~~government, or a local governmental entity or commercial enterprise~~
7 ~~whose obligations are guaranteed by the United States government.~~

8 ~~[(4) "United States government agency" means an~~
9 ~~instrumentality of the United States government whose obligations~~
10 ~~are fully and explicitly guaranteed as to the timely payment of~~
11 ~~principal and interest by the full faith and credit of the United~~
12 ~~States government. The term includes the Government National~~
13 ~~Mortgage Association, the Department of Veterans Affairs, the~~
14 ~~Federal Housing Administration, the Farmers Home Administration,~~
15 ~~the Export-Import Bank, the Overseas Private Investment~~
16 ~~Corporation, the Commodity Credit Corporation, the Small Business~~
17 ~~Administration, and any successor agency.~~

18 ~~[(5) "United States government-sponsored agency"~~
19 ~~means an agency originally established or chartered by the United~~
20 ~~States government to serve public purposes specified by the United~~
21 ~~States Congress but whose obligations are not explicitly guaranteed~~
22 ~~by the full faith and credit of the United States government. The~~
23 ~~term includes the Federal Home Loan Mortgage Corporation, the~~
24 ~~Federal National Mortgage Association, the Farm Credit System, the~~
25 ~~Federal Home Loan Bank System, the Student Loan Marketing~~
26 ~~Association, and any successor agency.]~~

27 Sec. 171.111. TEMPORARY CREDIT ON TAXABLE MARGIN. [NET

1 ~~TAXABLE EARNED SURPLUS.]~~ (a) Not later than March 1, 2007, a
2 taxable entity ~~[1992, a corporation]~~ may notify the comptroller in
3 writing of its intent to preserve its right to take a credit in an
4 amount allowed by this section on the tax due on taxable margin.
5 The taxable entity ~~[not taxable earned surplus. The comptroller~~
6 ~~may not grant an extension. The corporation]~~ may thereafter elect
7 to claim the credit for the current year and future year at or
8 before the original due date of any report due after January 1,
9 2007, ~~[1992,]~~ until the taxable entity ~~[corporation]~~ revokes the
10 election or this section expires, whichever is earlier. A taxable
11 entity ~~[corporation]~~ may claim the credit for not more than 20
12 consecutive privilege periods beginning with the first report due
13 under this chapter after January 1, 2007. ~~[1992.]~~ A taxable entity
14 ~~[corporation]~~ may make only one election under this section and the
15 election may not be conveyed, assigned, or transferred to another
16 entity.

17 (b) The credit allowed under this section for any privilege
18 period is computed by:

19 (1) determining the amount, as of the end of the
20 taxable entity's accounting year ending in 2006, of the difference
21 between (i) the taxable entity's deductible temporary differences
22 and net operating loss carryforwards, net of related valuation
23 allowance amounts, shown on the taxable entity's books and records
24 on the last day of its taxable year ending in 2006, and (ii) the
25 taxable entity's taxable temporary differences as shown on those
26 books and records on that date. The amount of other net deferred
27 tax items may be less than zero. For the purpose of computing the

1 amount of the taxable entity's other net deferred tax items, any
2 credit carryforward allowed under this chapter shall be excluded
3 from the amount of deductible temporary differences to the extent
4 such credit carryforward amount, net of any related valuation
5 allowance amount, is otherwise included in the taxable entity's
6 deductible temporary differences, net of related valuation
7 allowance amounts, shown on the taxable entity's books and records
8 on the last day of the taxable entity's taxable year ending in 2006;

9 ~~[(1) determining the amount, as of the end of the~~
10 ~~corporation's accounting year ending in 1991, that is the~~
11 ~~difference between the basis used for financial accounting purposes~~
12 ~~and the basis used for federal income tax purposes of an asset or a~~
13 ~~liability that at some future date will reverse,]~~

14 (2) apportioning the amount determined under
15 Subdivision (1) to this state in the same manner taxable margin
16 ~~[earned surplus]~~ is apportioned under Section 171.106 ~~[171.106(b)~~
17 ~~or (c), as applicable,]~~ on the first report due on or after January
18 1, 2007; ~~[1992,]~~

19 (3) multiplying the amount determined under
20 Subdivision (2) by 10 ~~[five]~~ percent; and

21 (4) multiplying the amount determined under
22 Subdivision (3) by the tax rate prescribed by Section
23 171.002(a)(2).

24 (c) ~~[In computing the amount under Subsection (b)(1), the~~
25 ~~corporation may not consider differences that result from deferred~~
26 ~~investment tax credits, allowances for funds used during~~
27 ~~construction, or any other timing difference for which a deferred~~

1 ~~tax liability is not required under generally accepted accounting~~
2 ~~principles.~~

3 ~~[(d) After making the election under Subsection (a) the~~
4 ~~corporation must, for purposes of computing its taxable capital~~
5 ~~under this chapter, use the same accounting methods under generally~~
6 ~~accepted accounting principles to account for the assets and~~
7 ~~liabilities that determine the amount of the credit that the~~
8 ~~corporation uses to compute the credit. Notwithstanding Section~~
9 ~~171.109(e), if a corporation changes an accounting method for an~~
10 ~~asset or liability that determines, in whole or in part, the amount~~
11 ~~of the credit during the period the election is in effect, the~~
12 ~~election is automatically revoked.~~

13 ~~[(e)]~~ A taxable entity ~~[corporation]~~ that notifies the
14 comptroller of its intent to preserve its right to take a credit
15 allowed by this section shall submit with its notice of intent a
16 statement of the amount determined under Subsection (b)(1). The
17 comptroller may request that the taxable entity ~~[corporation]~~
18 submit in the annual report for each succeeding privilege period in
19 which the taxable entity ~~[corporation]~~ is eligible to take a credit
20 information relating to the amount determined under Subsection
21 (b)(1). The taxable entity ~~[corporation]~~ shall submit in the form
22 and content the comptroller requires any information relating to
23 the assets and liabilities that determine the amount of the credit,
24 the amount determined under Subsection (b)(1), or any other matter
25 relevant to the computation of the credit for which the taxable
26 entity ~~[corporation]~~ is eligible.

27 (d) A credit that a taxable entity is entitled to under this

1 section does not convey, and may not be assigned or transferred, in
2 relation to a transaction in which the taxable entity is purchased
3 by another entity.

4 ~~(e) [(f) A credit allowed under this section may not be~~
5 ~~carried forward or backward or used to create a business loss~~
6 ~~carryover under Section 171.110.~~

7 ~~[(g) A corporation may not use a credit allowed under this~~
8 ~~section in connection with the computation of the corporation's tax~~
9 ~~on net taxable capital.~~

10 ~~[(h) In addition to the tax imposed by Section 171.002, an~~
11 ~~additional tax is imposed on each corporation during each year the~~
12 ~~corporation takes the credit allowed under this section. The~~
13 ~~additional tax is equal to 0.2 percent of the corporation's net~~
14 ~~taxable capital per year of privilege period.~~

15 ~~[(i)] This section expires September 1, 2026. [2012.~~

16 ~~[Sec. 171.12. GROSS RECEIPTS FOR TAXABLE CAPITAL. (a) For~~
17 ~~purposes of this section, "gross receipts" means all revenues that~~
18 ~~would be recognized annually under a generally accepted accounting~~
19 ~~principles method of accounting, without deduction for the cost of~~
20 ~~property sold, materials used, labor performed, or other costs~~
21 ~~incurred, unless otherwise specifically provided in this chapter.~~

22 ~~[(b) Except as otherwise provided in this section, a~~
23 ~~corporation must compute gross receipts in accordance with~~
24 ~~generally accepted accounting principles. If generally accepted~~
25 ~~accounting principles are unsettled or do not specify an accounting~~
26 ~~practice for a particular purpose related to the computation of~~
27 ~~gross receipts, the comptroller by rule may establish rules to~~

1 ~~specify the applicable accounting practice.~~

2 ~~[(c) A corporation whose taxable capital is less than \$1~~
 3 ~~million may report its gross receipts according to the method used~~
 4 ~~in the corporation's most recent federal income tax return~~
 5 ~~originally due on or before the date on which the corporation's~~
 6 ~~franchise tax report is originally due. In determining if taxable~~
 7 ~~capital is less than \$1 million, the corporation shall apply the~~
 8 ~~methods the corporation used in computing that federal income tax~~
 9 ~~return unless another method is required under this chapter.~~

10 ~~[(d) A corporation shall report its gross receipts based~~
 11 ~~solely on its own financial condition. Consolidated reporting is~~
 12 ~~prohibited.~~

13 ~~[(e) Unless the provisions of Section 171.111 apply due to~~
 14 ~~an election under that section, a corporation may not change its~~
 15 ~~accounting methods used to calculate gross receipts more often than~~
 16 ~~once every four years without the express written consent of the~~
 17 ~~comptroller. A change in accounting methods is not justified~~
 18 ~~solely because it results in a reduction of tax liability.~~

19 ~~[(f) Notwithstanding any other provision in this chapter, a~~
 20 ~~corporation subject to the tax imposed by this chapter shall use~~
 21 ~~double entry bookkeeping to account for all transactions that~~
 22 ~~affect the computation of that tax.~~

23 ~~[(g) Chapter 141 does not apply to this chapter.~~

24 ~~[(h) Except as otherwise provided by this section, a~~
 25 ~~corporation shall use the same accounting methods to apportion its~~
 26 ~~taxable capital as it used to compute its taxable capital.]~~

27 Sec. 171.1121. GROSS RECEIPTS FOR MARGIN [~~TAXABLE EARNED~~]

1 ~~SURPLUS~~]. (a) For purposes of this section, "gross receipts" means
2 all revenues reportable by a taxable entity ~~[corporation]~~ on its
3 federal tax return, without deduction for the cost of property
4 sold, materials used, labor performed, or other costs incurred,
5 unless otherwise specifically provided in this chapter. [~~"Gross~~
6 ~~receipts" does not include revenues that are not included in~~
7 ~~taxable earned surplus. For example, Schedule C special deductions~~
8 ~~and any amounts subtracted from reportable federal taxable income~~
9 ~~under Section 171.110(a)(1) are not included in taxable earned~~
10 ~~surplus and therefore are not considered gross receipts.~~]

11 (b) Except as otherwise provided by this section, a taxable
12 entity ~~[corporation]~~ shall use the same accounting methods to
13 apportion margin ~~[taxable earned surplus]~~ as used in computing
14 reportable federal taxable income.

15 (c) A taxable entity ~~[A corporation shall report its gross~~
16 ~~receipts based solely on its own financial condition. Consolidated~~
17 ~~reporting is prohibited.~~

18 [~~(d) Unless the provisions of Section 171.111 apply due to~~
19 ~~an election under that section, a corporation]~~ may not change its
20 accounting methods used to calculate gross receipts more often than
21 once every four years without the express written consent of the
22 comptroller. A change in accounting methods is not justified
23 solely because it results in a reduction of tax liability.

24 [~~(e) A corporation's share of a partnership's gross receipts~~
25 ~~that is included in the corporation's federal taxable income must~~
26 ~~be used in computing the corporation's gross receipts under this~~
27 ~~section. Unless otherwise provided by this chapter, a corporation~~

1 ~~may not deduct costs incurred from the corporation's share of a~~
2 ~~partnership's gross receipts. The gross receipts must be~~
3 ~~apportioned as though the corporation directly earned them.~~

4 ~~[Sec. 171.113. ALTERNATE METHOD OF DETERMINING TAXABLE~~
5 ~~CAPITAL AND GROSS RECEIPTS FOR CERTAIN CORPORATIONS. (a) This~~
6 ~~section applies only to:~~

7 ~~[(1) a corporation organized as a close corporation~~
8 ~~under Part 12, Texas Business Corporation Act, that has not more~~
9 ~~than 35 shareholders;~~

10 ~~[(2) a foreign corporation organized under the close~~
11 ~~corporation law of another state that has not more than 35~~
12 ~~shareholders; and~~

13 ~~[(3) an S corporation as that term is defined by~~
14 ~~Section 1361, Internal Revenue Code of 1986 (26 U.S.C. Section~~
15 ~~1361).~~

16 ~~[(b) A corporation to which this section applies may elect~~
17 ~~to compute its surplus, assets, debts, and gross receipts according~~
18 ~~to the method the corporation uses to report its federal income tax~~
19 ~~instead of as provided by Sections 171.109(b) and (g) and Section~~
20 ~~171.112(b). This section does not affect the application of the~~
21 ~~other subsections of Sections 171.109 and 171.112 and other~~
22 ~~provisions of this chapter to a corporation making the election.~~

23 ~~[(c) The comptroller may adopt rules as necessary to specify~~
24 ~~the reporting requirements for corporations to which this section~~
25 ~~applies.~~

26 ~~[(d) This section does not apply to a subsidiary corporation~~
27 ~~unless it applies to the parent corporation of the subsidiary.~~

1 ~~[(c) The election under Subsection (b) becomes effective~~
 2 ~~when written notice of the election is received by the comptroller~~
 3 ~~from the corporation. An election under Subsection (b) must be~~
 4 ~~postmarked not later than the due date for the electing~~
 5 ~~corporation's franchise tax report to which the election applies.]~~

6 SECTION 6. Subchapter D, Chapter 171, Tax Code, is amended
 7 to read as follows:

8 SUBCHAPTER D. PAYMENT OF TAX

9 Sec. 171.151. PRIVILEGE PERIOD COVERED BY TAX. The
 10 franchise tax shall be paid for each of the following:

11 (1) an initial period beginning on the taxable
 12 entity's ~~[corporation's]~~ beginning date and ending on the day
 13 before the first anniversary of the beginning date;

14 (2) a second period beginning on the first anniversary
 15 of the beginning date and ending on December 31 following that date;
 16 and

17 (3) after the initial and second periods have expired,
 18 a regular annual period beginning each year on January 1 and ending
 19 the following December 31.

20 Sec. 171.152. DATE ON WHICH PAYMENT IS DUE. (a) Payment of
 21 the tax covering the initial period is due within 90 days after the
 22 date that the initial period ends or, if applicable, within 91 days
 23 after the date of the merger.

24 (b) Payment of the tax covering the second period is due on
 25 the same date as the tax covering the initial period.

26 (c) Payment of the tax covering the regular annual period is
 27 due May 15, of each year after the beginning of the regular annual

1 period. However, if the first anniversary of the taxable entity's
 2 ~~[corporation's]~~ beginning date is after October 3 and before
 3 January 1, the payment of the tax covering the first regular annual
 4 period is due on the same date as the tax covering the initial
 5 period.

6 ~~[Sec. 171.153. BUSINESS ON WHICH TAX ON NET TAXABLE CAPITAL~~
 7 ~~IS BASED. (a) The tax covering the initial period is reported on~~
 8 ~~the initial report and is based on the business done by the~~
 9 ~~corporation during the period beginning on the corporation's~~
 10 ~~beginning date and:~~

11 ~~[(1) ending on the last accounting period ending date~~
 12 ~~that is at least six months after the beginning date and at least 60~~
 13 ~~days before the original due date of the initial report; or~~

14 ~~[(2) if there is no such period ending date in~~
 15 ~~Subdivision (1) of this subsection, then ending on the day that is~~
 16 ~~the last day of a calendar month and that is nearest to the end of~~
 17 ~~the corporation's first year of business; or~~

18 ~~[(3) ending on the day after the merger occurs, for the~~
 19 ~~survivor of a merger which occurs after the day on which the tax is~~
 20 ~~based in Subdivision (1) or Subdivision (2), whichever is~~
 21 ~~applicable, of Subsection (a) and before January 1, of the year an~~
 22 ~~initial report is due by the survivor.~~

23 ~~[(b) The tax covering the second period is reported on the~~
 24 ~~initial report and is based on the same business on which the tax~~
 25 ~~covering the initial period is based and is to be prorated based on~~
 26 ~~the length of the second period.~~

27 ~~[(c) The tax covering the regular annual period is based on~~

1 ~~the business done by the corporation during its last accounting~~
2 ~~period that ends in the year before the year in which the tax is due,~~
3 ~~unless a corporation is the survivor of a merger which occurs~~
4 ~~between the end of its last accounting period in the year before the~~
5 ~~report year and January 1 of the report year, in which case the tax~~
6 ~~will be based on the financial condition of the surviving~~
7 ~~corporation for the 12-month period ending on the day after the~~
8 ~~merger. However, if the first anniversary of the corporation's~~
9 ~~beginning date is after October 3 and before January 1, the tax~~
10 ~~covering the first regular annual period is based on the same~~
11 ~~business on which the tax covering the initial period is based and~~
12 ~~is reported on the initial report.~~

13 ~~[Sec. 171.1531. CREDIT FOR SURVIVOR OF MERGER. (a) "Credit~~
14 ~~period" means the period from the date of the merger or the date the~~
15 ~~survivor was required to pay franchise tax, whichever is later,~~
16 ~~through the end of the privilege period for which tax was actually~~
17 ~~paid by the nonsurvivors.~~

18 ~~[(b) The survivor of a merger is entitled to a credit~~
19 ~~against the tax computed on its net taxable capital under Section~~
20 ~~171.062(b)(1) in the amount of the franchise tax computed on net~~
21 ~~taxable capital paid by the nonsurvivors for the credit period,~~
22 ~~provided the tax computed on net taxable capital paid by the~~
23 ~~survivor for the credit period is based on the survivor's financial~~
24 ~~condition after the merger. Only a survivor that is subject to the~~
25 ~~franchise tax is entitled to the merger credit. The merger credit~~
26 ~~shall be allocated among survivors based on net taxable capital~~
27 ~~reported, and as provided by Section 171.153.~~

1 ~~[(c) The credit will be limited to the lesser of the amount~~
2 ~~of tax on net taxable capital paid for the credit period by the~~
3 ~~survivor or by the nonsurvivors.]~~

4 Sec. 171.1532. BUSINESS ON WHICH TAX ON NET TAXABLE MARGIN
5 ~~[EARNED SURPLUS]~~ IS BASED. (a) The tax covering the privilege
6 periods included on the initial report~~[as required by Section~~
7 ~~171.1537]~~ is based on the business done by the taxable entity
8 ~~[corporation]~~ during the period beginning on the taxable entity's
9 ~~[corporation's]~~ beginning date and:

10 (1) ending on the last accounting period ending date
11 that is at least 60 days before the original due date of the initial
12 report; or

13 (2) if there is no such period ending date in
14 Subdivision (1) ~~[of this subsection]~~, then ending on the day that is
15 the last day of a calendar month and that is nearest to the end of
16 the taxable entity's ~~[corporation's]~~ first year of business.

17 (b) The tax covering the regular annual period, other than a
18 regular annual period included on the initial report, is based on
19 the business done by the taxable entity ~~[corporation]~~ during the
20 period beginning with the day after the last date upon which ~~[net]~~
21 taxable margin ~~[earned surplus]~~ on a previous report was based and
22 ending with its last accounting period ending date for federal
23 income tax purposes in the year before the year in which the report
24 is originally due.

25 Sec. 171.154. PAYMENT TO COMPTROLLER. A taxable entity
26 ~~[corporation]~~ on which a tax is imposed by this chapter shall pay
27 the tax to the comptroller.

1 Sec. 171.158. PAYMENT BY FOREIGN TAXABLE ENTITY
2 ~~[CORPORATION]~~ BEFORE WITHDRAWAL FROM STATE. (a) Except as
3 provided by Subsection (b) ~~[of this section]~~, a foreign taxable
4 entity ~~[corporation]~~ holding a registration or certificate of
5 authority to do business in this state may withdraw from doing
6 business in this state by filing a certificate of withdrawal with
7 the secretary of state. The secretary of state shall file the
8 certificate of withdrawal as provided by law.

9 (b) The foreign taxable entity ~~[corporation]~~ may not
10 withdraw from doing business in this state unless it has paid,
11 before filing the certificate of withdrawal, any tax or penalty
12 imposed by this chapter on the taxable entity ~~[corporation]~~.

13 SECTION 7. Subchapter E, Chapter 171, Tax Code, is amended
14 to read as follows:

15 SUBCHAPTER E. REPORTS AND RECORDS

16 Sec. 171.201. INITIAL REPORT. (a) Except as provided by
17 Section 171.202, a taxable entity ~~[corporation]~~ on which the
18 franchise tax is imposed shall file an initial report with the
19 comptroller containing:

20 (1) information showing the financial condition of the
21 taxable entity ~~[corporation]~~ on the day that is the last day of a
22 calendar month and that is nearest to the end of the taxable
23 entity's ~~[corporation's]~~ first year of business;

24 (2) the name and address of:

25 (A) each officer, ~~[and]~~ director, and manager of
26 the taxable entity ~~[corporation]~~;

27 (B) for a limited partnership, each general

1 partner;

2 (C) for a general partnership or limited
3 liability partnership, each managing partner or, if there is not a
4 managing partner, each partner; or

5 (D) for a trust, each trustee;

6 (3) the name and address of the agent of the taxable
7 entity [~~corporation~~] designated under Section 171.354; and

8 (4) other information required by the comptroller.

9 (b) The taxable entity [~~corporation~~] shall file the report
10 on or before the date the payment is due under [~~Subsection (a) of~~]
11 Section 171.152(a) [~~171.152~~].

12 Sec. 171.202. ANNUAL REPORT. (a) Except as provided by
13 Section 171.2022, a taxable entity [~~corporation~~] on which the
14 franchise tax is imposed shall file an annual report with the
15 comptroller containing:

16 (1) financial information of the taxable entity
17 [~~corporation~~] necessary to compute the tax under this chapter;

18 (2) the name and address of each officer and director
19 of the taxable entity [~~corporation~~];

20 (3) the name and address of the agent of the taxable
21 entity [~~corporation~~] designated under Section 171.354; and

22 (4) other information required by the comptroller.

23 (b) The taxable entity [~~corporation~~] shall file the report
24 before May 16 of each year after the beginning of the regular annual
25 period. The report shall be filed on forms supplied by the
26 comptroller.

27 (c) The comptroller shall grant an extension of time to a

1 taxable entity ~~[corporation]~~ that is not required by rule to make
 2 its tax payments by electronic funds transfer for the filing of a
 3 report required by this section to any date on or before the next
 4 November 15, if a taxable entity ~~[corporation]~~;

5 (1) requests the extension, on or before May 15, on a
 6 form provided by the comptroller; and

7 (2) remits with the request:

8 (A) not less than 50 percent of the amount of tax
 9 reported as due on the report filed on or before November 15; or

10 (B) 100 percent of the tax reported as due for the
 11 previous calendar year on the report due in the previous calendar
 12 year and filed on or before May 14.

13 (d) In the case of a taxpayer whose previous return was its
 14 initial report, the optional payment provided under Subsection
 15 (c)(2)(B) or (e)(2)(B) must be equal to ~~[the greater of:~~

16 ~~[(1)]~~ an amount produced by multiplying the ~~[net]~~
 17 taxable margin ~~[capital]~~, as reported on the initial report filed
 18 on or before May 14, by the rate of tax in Section 171.002
 19 ~~[171.002(a)(1)]~~ that is effective January 1 of the year in which the
 20 report is due ~~[, or~~

21 ~~[(2)]~~ an amount produced by multiplying the net taxable
 22 earned surplus, as reported on the initial report filed on or before
 23 May 14, by the rate of tax in Section 171.002(a)(2) that is
 24 effective January 1 of the year in which the report is due].

25 (e) The comptroller shall grant an extension of time for the
 26 filing of a report required by this section by a taxable entity
 27 ~~[corporation]~~ required by rule to make its tax payments by

1 electronic funds transfer to any date on or before the next August
2 15, if the taxable entity [~~corporation~~]:

3 (1) requests the extension, on or before May 15, on a
4 form provided by the comptroller; and

5 (2) remits with the request:

6 (A) not less than 90 percent of the amount of tax
7 reported as due on the report filed on or before August 15; or

8 (B) 100 percent of the tax reported as due for the
9 previous calendar year on the report due in the previous calendar
10 year and filed on or before May 14.

11 (f) The comptroller shall grant an extension of time to a
12 taxable entity [~~corporation~~] required by rule to make its tax
13 payments by electronic funds transfer for the filing of a report due
14 on or before August 15 to any date on or before the next November 15,
15 if the taxable entity [~~corporation~~]:

16 (1) requests the extension, on or before August 15, on
17 a form provided by the comptroller; and

18 (2) remits with the request the difference between the
19 amount remitted under Subsection (e) and 100 percent of the amount
20 of tax reported as due on the report filed on or before November 15.

21 (h) If the sum of the amounts paid under Subsections (e)(2)
22 and (f)(2) is at least 99 percent of the amount reported as due on
23 the report filed on or before November 15, penalties for
24 underpayment with respect to the amount paid under Subsection
25 (f)(2) are waived.

26 (i) If a taxable entity [~~corporation~~] requesting an
27 extension under Subsection (c) or (e) does not file the report due

1 in the previous calendar year on or before May 14 the taxable
2 entity [~~corporation~~] may not receive an extension under Subsection
3 (c) or (e) unless the taxable entity [~~corporation~~] complies with
4 Subsection (c)(2)(A) or (e)(2)(A), as appropriate.

5 Sec. 171.202. EXEMPTION FROM REPORTING REQUIREMENTS. A
6 taxable entity [~~corporation~~] that does not owe any tax under this
7 chapter for any period is not required to file a report under
8 Section 171.201 or [~~7~~] 171.202 [~~or 171.201~~]. The exemption
9 applies only to a period for which no tax is due.

10 Sec. 171.203. PUBLIC INFORMATION REPORT. (a) A
11 corporation on which the franchise tax is imposed, regardless of
12 whether the corporation is required to pay any tax, shall file a
13 report with the comptroller containing:

14 (1) the name of each corporation in which the
15 corporation filing the report owns a 10 percent or greater interest
16 and the percentage owned by the corporation;

17 (2) the name of each corporation that owns a 10 percent
18 or greater interest in the corporation filing the report;

19 (3) the name, title, and mailing address of each
20 person who is an officer or director of the corporation on the date
21 the report is filed and the expiration date of each person's term as
22 an officer or director, if any;

23 (4) the name and address of the agent of the
24 corporation designated under Section 171.354 [~~of this code~~]; and

25 (5) the address of the corporation's principal office
26 and principal place of business.

27 (b) The corporation shall file the report once a year on a

1 form prescribed by the comptroller.

2 (c) The comptroller shall forward the report to the
3 secretary of state.

4 (d) The corporation shall send a copy of the report to each
5 person named in the report under Subsection (a)(3) who is not
6 currently employed by the corporation or a related corporation
7 listed in Subsection (a)(1) or (2). An officer or director of the
8 corporation or another authorized person must sign the report under
9 a certification that:

10 (1) all information contained in the report is true
11 and correct to the best of the person's knowledge; and

12 (2) a copy of the report has been mailed to each person
13 identified in this subsection on the date the return is filed.

14 (e) If a person's name is included in a report under
15 Subsection (a)(3) and the person is not an officer or director of
16 the corporation on the date the report is filed, the person may file
17 with the comptroller a sworn statement disclaiming the person's
18 status as shown on the report. The comptroller shall maintain a
19 record of statements filed under this subsection and shall make
20 that information available on request using the same procedures the
21 comptroller uses for other requests for public information.

22 (f) A public information report that is filed
23 electronically complies with the signature and certification
24 requirements prescribed by Subsection (d).

25 Sec. 171.2035. ADDITIONAL PUBLIC INFORMATION REPORT. (a)
26 A taxable entity that has more than 100,000 employees in this state
27 shall file a report with the comptroller stating the number of the

1 taxable entity's employees in this state that receive assistance
 2 for that employee or the employee's family under the Children's
 3 Health Insurance Program (CHIP) or the Medicaid program.

4 (b) A taxable entity described by Subsection (a) shall file
 5 the report once a year on a form prescribed by the comptroller.

6 Sec. 171.204. INFORMATION REPORT. (a) Except as provided
 7 by Subsection (b), to determine eligibility for the exemption
 8 provided by Section 171.2022, or to determine the amount of the
 9 franchise tax or the correctness of a franchise tax report, the
 10 comptroller may require ~~[an officer of]~~ a taxable entity
 11 ~~[corporation]~~ that may be subject to the tax imposed under this
 12 chapter to file an information report with the comptroller stating
 13 the amount of the taxable entity's margin ~~[corporation's taxable~~
 14 ~~capital and earned surplus]~~, or any other information the
 15 comptroller may request that is necessary to make a determination
 16 under this subsection.

17 (b) The comptroller may require a taxable entity ~~[an officer~~
 18 ~~of a corporation]~~ that does not owe any tax because of the
 19 application of Section 171.002(d)(2) to file an abbreviated
 20 information report with the comptroller stating the amount of the
 21 taxable entity's total revenue ~~[corporation's gross receipts]~~ from
 22 its entire business. The comptroller may not require a taxable
 23 entity ~~[corporation]~~ described by this subsection to file an
 24 information report that requires the taxable entity ~~[corporation]~~
 25 to report or compute its margin ~~[earned surplus or taxable~~
 26 ~~capital]~~.

27 Sec. 171.205. ADDITIONAL INFORMATION REQUIRED BY

1 COMPTROLLER. The comptroller may require a taxable entity
2 ~~[corporation]~~ on which the franchise tax is imposed to furnish to
3 the comptroller information from the taxable entity's
4 ~~[corporation's]~~ books and records that has not been filed
5 previously and that is necessary for the comptroller to determine
6 the amount of the tax.

7 Sec. 171.206. CONFIDENTIAL INFORMATION. Except as provided
8 by Section 171.207 ~~[of this code]~~, the following information is
9 confidential and may not be made open to public inspection:

10 (1) information that is obtained from a record or
11 other instrument that is required by this chapter to be filed with
12 the comptroller; or

13 (2) information, including information about the
14 business affairs, operations, profits, losses, cost of goods sold,
15 compensation, or expenditures of a taxable entity ~~[corporation]~~,
16 obtained by an examination of the books and records, officers,
17 partners, trustees, agents, or employees of a taxable entity
18 ~~[corporation]~~ on which a tax is imposed by this chapter.

19 Sec. 171.207. INFORMATION NOT CONFIDENTIAL. The following
20 information is not confidential and shall be made open to public
21 inspection:

22 (1) information contained in a document filed under
23 this chapter with a county clerk as notice of a tax lien; and

24 (2) information contained in a report required by
25 Section 171.203 or 171.2035 ~~[of this code]~~.

26 Sec. 171.208. PROHIBITION OF DISCLOSURE OF INFORMATION. A
27 person, including a state officer or employee or an owner ~~[a~~

1 ~~shareholder~~ of a taxable entity [~~corporation~~], who has access to a
2 report filed under this chapter may not make known in a manner not
3 permitted by law the amount or source of the taxable entity's
4 [~~corporation's~~] income, profits, losses, expenditures, cost of
5 goods sold, compensation, or other information in the report
6 relating to the financial condition of the taxable entity
7 [~~corporation~~].

8 Sec. 171.209. RIGHT OF OWNER [~~SHAREHOLDER~~] TO EXAMINE OR
9 RECEIVE REPORTS. If an owner [~~a person owning at least one share of~~
10 ~~outstanding stock~~] of a taxable entity [~~corporation~~] on whom the
11 franchise tax is imposed presents evidence of the ownership to the
12 comptroller, the person is entitled to examine or receive a copy of
13 an initial or annual report that is filed under Section 171.201 or
14 171.202 [~~of this code~~] and that relates to the taxable entity
15 [~~corporation~~].

16 Sec. 171.211. PERMITTED USE OF CONFIDENTIAL INFORMATION.

17 (a) To enforce this chapter, the comptroller or attorney general
18 may use information made confidential by this chapter.

19 (1) The comptroller or attorney general may authorize the
20 use of the confidential information in a judicial proceeding in
21 which the state is a party. The comptroller or attorney general may
22 authorize examination of the confidential information by:

- 23 (1) another state officer of this state;
24 (2) a law enforcement official of this state; or
25 (3) a tax official of another state or an official of
26 the federal government if the other state or the federal government
27 has a reciprocal arrangement with this state.

1 Sec. 171.211. EXAMINATION OF ~~[CORPORATE]~~ RECORDS. To
2 determine the franchise tax liability of a taxable entity
3 ~~[corporation]~~, the comptroller may investigate or examine the
4 records of the taxable entity ~~[corporation]~~.

5 Sec. 171.212. REPORT OF CHANGES TO FEDERAL INCOME TAX
6 RETURN. (a) A taxable entity ~~[corporation]~~ must file an amended
7 report under this chapter if:

8 (1) the taxable entity's ~~[corporation's net]~~ taxable
9 margin ~~[earned surplus]~~ is changed as the result of an audit or
10 other adjustment by the Internal Revenue Service or another
11 competent authority; or

12 (2) the taxable entity ~~[corporation]~~ files an amended
13 federal income tax return or other return that changes the taxable
14 entity's ~~[corporation's net]~~ taxable margin ~~[earned surplus]~~.

15 (b) The taxable entity ~~[corporation]~~ shall file the amended
16 report under Subsection (a)(1) not later than the 120th day after
17 the date the revenue agent's report or other adjustment is final.
18 For purposes of this subsection, a revenue agent's report or other
19 adjustment is final on the date on which all administrative appeals
20 with the Internal Revenue Service or other competent authority have
21 been exhausted or waived.

22 (c) The taxable entity ~~[corporation]~~ shall file the amended
23 report under Subsection (a)(2) not later than the 120th day after
24 the date the taxable entity ~~[corporation]~~ files the amended federal
25 income tax return or other return. For purposes of this subsection,
26 a taxable entity ~~[corporation]~~ is considered to have filed an
27 amended federal income tax return if the taxable entity

1 ~~[corporation]~~ is a member of an affiliated group during a period in
2 which an amended consolidated federal income tax report is filed.

3 (d) If a taxable entity ~~[corporation]~~ fails to comply with
4 this section, the taxable entity ~~[corporation]~~ is liable for a
5 penalty of 10 percent of the tax that should have been reported
6 under this section and that had not previously been reported to the
7 comptroller. The penalty prescribed by this subsection is in
8 addition to any other penalty provided by law.

9 SECTION 8. The heading to Subchapter F, Chapter 171, Tax
10 Code, is amended to read as follows:

11 SUBCHAPTER F. FORFEITURE OF CORPORATE AND BUSINESS PRIVILEGES

12 SECTION 9. Subchapter F, Chapter 171, Tax Code, is amended
13 by adding Section 171.2515 to read as follows:

14 Sec. 171.2515. FORFEITURE OF RIGHT OF TAXABLE ENTITY TO
15 TRANSACT BUSINESS IN THIS STATE. (a) The comptroller may, for the
16 same reasons and using the same procedures the comptroller uses in
17 relation to the forfeiture of the corporate privileges of a
18 corporation, forfeit the right of a taxable entity to transact
19 business in this state.

20 (b) The provisions of this subchapter, including Section
21 171.255, that apply to the forfeiture of corporate privileges apply
22 to the forfeiture of a taxable entity's right to transact business
23 in this state.

24 SECTION 10. Section 171.351, Tax Code, is amended to read as
25 follows:

26 Sec. 171.351. VENUE OF SUIT TO ENFORCE CHAPTER. Venue of a
27 civil suit against a taxable entity ~~[corporation]~~ to enforce this

1 chapter is either in a county where the taxable entity's
2 ~~[corporation's]~~ principal office is located according to its
3 charter or certificate of authority or in Travis County.

4 SECTION 11. Section 171.353, Tax Code, is amended to read as
5 follows:

6 Sec. 171.353. APPOINTMENT OF RECEIVER. If a court forfeits
7 a taxable entity's ~~[corporation's]~~ charter or certificate of
8 authority, the court may appoint a receiver for the taxable entity
9 ~~[corporation]~~ and may administer the receivership under the laws
10 relating to receiverships.

11 SECTION 12. Section 171.354, Tax Code, is amended to read as
12 follows:

13 Sec. 171.354. AGENT FOR SERVICE OF PROCESS. Each taxable
14 entity ~~[corporation]~~ on which a tax is imposed by this chapter shall
15 designate a resident of this state as the taxable entity's
16 ~~[corporation's]~~ agent for the service of process.

17 SECTION 13. Sections 171.362(a), (d), and (e), Tax Code,
18 are amended to read as follows:

19 (e) If a taxable entity ~~[corporation]~~ on which a tax is
20 imposed by this chapter fails to pay the tax when it is due and
21 payable or fails to file a report required by this chapter when it
22 is due, the taxable entity ~~[corporation]~~ is liable for a penalty of
23 five percent of the amount of the tax due.

24 (d) If a taxable entity ~~[corporation]~~ electing to remit
25 under ~~[Paragraph (A) of Subdivision (2) of Subsection (c) of]~~
26 Section 171.202(c)(2)(A) ~~[171.202 of this code]~~ remits less than
27 the amount required, the penalties imposed by this section and the

1 interest imposed under Section 111.060 ~~[of this code]~~ are assessed
2 against the difference between the amount required to be remitted
3 under ~~[Paragraph (A) of Subdivision (2) of Subsection (c) of]~~
4 Section 171.202(c)(2)(A) ~~[171.202]~~ and the amount actually
5 remitted on or before May 15.

6 (e) If a taxable entity ~~[corporation]~~ remits the entire
7 amount required by ~~[Subsection (c) of]~~ Section 171.202(c) ~~[171.202~~
8 ~~of this code]~~, no penalties will be imposed against the amount
9 remitted on or before November 15.

10 SECTION 14. Sections ~~171.363~~(a) and (b), Tax Code, are
11 amended to read as follows:

12 (a) A taxable entity ~~[corporation]~~ commits an offense if the
13 taxable entity ~~[corporation]~~ is subject to the provisions of this
14 chapter and the taxable entity ~~[corporation]~~ wilfully:

- 15 (1) fails to file a report;
16 (2) fails to keep books and records as required by this
17 chapter;
18 (3) files a fraudulent report;
19 (4) violates any rule of the comptroller for the
20 administration and enforcement of the provisions of this chapter;
21 or

22 (5) attempts in any other manner to evade or defeat any
23 tax imposed by this chapter or the payment of the tax.

24 (b) A person commits an offense if the person is an
25 accountant or an agent for or an officer or employee of a taxable
26 entity ~~[corporation]~~ and the person knowingly enters or provides
27 false information on any report, return, or other document filed by

1 the taxable entity [~~corporation~~] under this chapter.

2 SECTION 15. Section 171.401, Tax Code, is amended to read as
3 follows:

4 Sec. 171.401. REVENUE DEPOSITED IN GENERAL REVENUE FUND.
5 The revenue from the tax imposed by this chapter [~~on corporations~~]
6 shall be deposited to the credit of the general revenue fund.

7 SECTION 16. (a) Section 313.007, Tax Code, is amended to
8 read as follows:

9 Sec. 313.007. EXPIRATION. Subchapters B, C, and D expire
10 December 31, 2011 [~~2007~~].

11 (b) Section 313.024(a), Tax Code, is amended to read as
12 follows:

13 (a) This subchapter and Subchapters C and D apply only to
14 property owned by an entity [~~a corporation or limited liability~~
15 ~~company~~] to which Chapter 171 [~~Section 171.001~~] applies.

16 (c) Section 313.024(b), Tax Code, is amended to read as
17 follows:

18 (b) To be eligible for a limitation on appraised value under
19 this subchapter, the entity [~~corporation or limited liability~~
20 ~~company~~] must use the property in connection with:

- 21 (1) manufacturing;
- 22 (2) research and development;
- 23 (3) a clean coal project, as defined by Section 5.001,
24 Water Code;
- 25 (4) a gasification project for a coal and biomass
26 mixture; or
- 27 (5) renewable energy electric generation.

1 (d) Section 313.025(b), Tax Code, is amended to read as
2 follows:

3 (b) The governing body of a school district is not required
4 to consider an application for a limitation on appraised value that
5 is filed with the governing body under Subsection (a). If the
6 governing body of the school district does elect to consider an
7 application, the governing body shall request that the Texas
8 Education Agency ~~[engage a third person to]~~ conduct an economic
9 impact evaluation of the application on behalf of the school
10 district, and that agency shall conduct the evaluation as soon as
11 practicable. The governing body shall provide to the Texas
12 Education Agency any information requested by that agency. The
13 Texas Education Agency may develop a methodology to allow
14 comparisons of economic impact for different schedules of addition
15 of qualified investment or qualified property as part of the
16 economic impact evaluation. The economic impact evaluation of the
17 Texas Education Agency is binding on the governing body of the
18 school district and the applicant. The governing body shall
19 provide a copy of the evaluation to the applicant on request. The
20 Texas Education Agency may charge and collect a fee sufficient to
21 cover the costs of providing the economic impact evaluation. The
22 governing body of a school district shall ~~[and]~~ approve or
23 disapprove an application before the 121st day after the date the
24 application is filed, unless the Texas Education Agency's economic
25 impact evaluation has not been received or an extension is agreed to
26 by the governing body and the applicant.

27 (e) Section 313.051, Tax Code, is amended to read as

1 follows:

2 Sec. 313.051. APPLICABILITY. (a) This subchapter applies
3 only to a school district that has territory in:

4 (1) a strategic investment area, as defined by Section
5 171.721; ~~or Tax Code,~~ or

6 (2) ~~in~~ a county:

7 (A) ~~(1)~~ that has a population of less than
8 50,000;

9 (B) ~~(2)~~ that is not partially or wholly located
10 in a metropolitan statistical area; and

11 (C) ~~(3)~~ in which, from 1990 to 2000, according
12 to the federal decennial census, the population:

13 (i) ~~(A)~~ remained the same;

14 (ii) ~~(B)~~ decreased; or

15 (iii) ~~(C)~~ increased, but at a rate of not
16 more than three percent per annum.

17 (a-1) Notwithstanding Subsection (a), if on January 1,
18 2002, this subchapter applied to a school district in whose
19 territory is located a federal nuclear facility, this subchapter
20 continues to apply to the school district regardless of whether the
21 school district ceased or ceases to be described by Subsection (a)
22 after that date.

23 (b) The governing body of a school district to which this
24 subchapter applies may enter into an agreement in the same manner as
25 a school district to which Subchapter B applies may do so under
26 Subchapter B, subject to Sections 313.052-313.054. Except as
27 otherwise provided by this subchapter, the provisions of Subchapter

1 B apply to a school district to which this subchapter applies. For
2 purposes of this subchapter, a property owner is required to create
3 only at least 10 new jobs on the owner's qualified property. At
4 least 80 percent of all the new jobs created must be qualifying jobs
5 as defined by Section 313.021(3), except that, for a school
6 district described by Subsection (a)(2), each qualifying job must
7 pay at least 110 percent of the average weekly wage for
8 manufacturing jobs in the region designated for the regional
9 planning commission, council of governments, or similar regional
10 planning agency created under Chapter 391, Local Government Code,
11 in which the district is located.

12 (f) Section 313.051(b), Tax Code, as amended by this
13 section, applies only to a limitation on the appraised value for
14 school district maintenance and operations ad valorem tax purposes
15 for which the owner files an application on or after the effective
16 date of this Act. A limitation on the appraised value for school
17 district maintenance and operations ad valorem tax purposes for
18 which the owner files an application before the effective date of
19 this Act is governed by the law as it existed immediately before the
20 effective date of this Act, and that law is continued in effect for
21 that purpose.

22 SECTION 17. (a) The repeal of Section 171.111, Tax Code,
23 by this Act does not affect a credit that accrued under that section
24 before the effective date of this Act.

25 (b) A corporation that has any unused credits accrued before
26 the effective date of this Act under Section 171.111, Tax Code, may
27 claim those unused credits on or with the tax report for the period

1 in which the credits were accrued, and the former law under which
2 the corporation accrued the credits is continued in effect for
3 purposes of determining the amount of the credits the corporation
4 may claim and the manner in which the corporation may claim the
5 credits.

6 SECTION 18. (a) The following provisions of Chapter 171,
7 Tax Code, are repealed:

- 8 (1) Subchapter L;
- 9 (2) Subchapter M;
- 10 (3) Subchapter N;
- 11 (4) Subchapter O;
- 12 (5) Subchapter P;
- 13 (6) Subchapter Q;
- 14 (7) Subchapter R;
- 15 (8) Subchapter S;
- 16 (9) Subchapter T;
- 17 (10) Subchapter U as added by Chapter 209, Acts of the
18 78th Legislature, Regular Session, 2003; and
- 19 (11) Subchapter U as added by Chapter 1274, Acts of the
20 78th Legislature, Regular Session, 2003.

21 (b) This section does not affect a credit authorized by a
22 provision listed in Subsection (a) of this section that accrued
23 under Chapter 171, Tax Code, before the effective date of this Act
24 or a credit that continues to accrue under Section 19 of this Act.

25 (c) A corporation that has any unused credits accrued before
26 the effective date of this Act under a provision other than
27 Subchapter O, P, or Q, Chapter 171, Tax Code, may claim those unused

1 credits on or with the tax report for the period in which the
2 credits were accrued, and the former law under which the
3 corporation accrued the credits is continued in effect for purposes
4 of determining the amount of the credits the corporation may claim
5 and the manner in which the corporation may claim the credits.

6 (d) A corporation that has any unused credits accrued before
7 the effective date of this Act under Subchapter O, Chapter 171, Tax
8 Code, may claim those unused credits on or with the tax report for
9 the period in which the credit was accrued. However, if the
10 corporation was allowed to carry forward unused credits under that
11 subchapter, the corporation may continue to apply those credits on
12 or with each consecutive report until the earlier of the date the
13 credit would have expired under the terms of Subchapter O, Chapter
14 171, Tax Code, had it continued in existence, or December 31, 2027,
15 and the former law under which the corporation accrued the credits
16 is continued in effect for purposes of determining the amount of the
17 credits the corporation may claim and the manner in which the
18 corporation may claim the credits.

19 (e) A corporation that has any unused credits accrued before
20 the effective date of this Act under Subchapter P, Chapter 171, Tax
21 Code, may claim those unused credits on or with the tax report for
22 the period in which the credit was accrued. However, if the
23 corporation was allowed to carry forward unused credits under that
24 subchapter, the corporation may continue to apply those credits on
25 or with each consecutive report until the earlier of the date the
26 credit would have expired under the terms of Subchapter P, Chapter
27 171, Tax Code, had it continued in existence, or December 31, 2012,

1 and the former law under which the corporation accrued the credits
2 is continued in effect for purposes of determining the amount of the
3 credits the corporation may claim and the manner in which the
4 corporation may claim the credits.

5 (f) A corporation that has any unused credits accrued before
6 the effective date of this Act under Subchapter Q, Chapter 171, Tax
7 Code, may claim those unused credits on or with the tax report for
8 the period in which the credit was accrued. However, if the
9 corporation was allowed to carry forward unused credits under that
10 subchapter, the corporation may continue to apply those credits on
11 or with each consecutive report until the earlier of the date the
12 credit would have expired under the terms of Subchapter Q, Chapter
13 171, Tax Code, had it continued in existence, or December 31, 2012,
14 and the former law under which the corporation accrued the credits
15 is continued in effect for purposes of determining the amount of the
16 credits the corporation may claim and the manner in which the
17 corporation may claim the credits.

18 (g) The comptroller shall adopt rules to administer this
19 section.

20 SECTION 19. A written agreement between the Texas
21 Department of Economic Development or its successor and a taxpayer
22 effective before June 1, 2006, that allows for credits against the
23 tax imposed under Chapter 171, Tax Code, continues in effect and the
24 credits allowed under the agreement continue to accrue and may be
25 claimed in the manner provided by the agreement against the tax
26 imposed under Chapter 171, Tax Code, as amended by this Act, for the
27 duration of the agreement. The former law under which the agreement

1 was made and under which the taxpayer received the entitlement to
2 the credits is continued in effect for purposes of determining the
3 amount of the credits the taxpayer may claim and the manner in which
4 the taxpayer may claim the credits.

5 SECTION 20. The comptroller shall adopt rules to implement
6 the legislative intent in Sections 171.1012(e)(14) and
7 171.1013(c-1), Tax Code.

8 SECTION 21. The franchise tax imposed by Chapter 171, Tax
9 Code, as amended by this Act, is not an income tax and Pub. L. No.
10 86-272 does not apply to the tax.

11 SECTION 22. (a) Subject to other provisions of this
12 section, this Act applies to reports originally due on or after the
13 effective date of this Act.

14 (b) For an entity becoming subject to the franchise tax
15 under this Act:

16 (1) margin or gross receipts occurring before June 1,
17 2006, may not be considered for purposes of determining taxable
18 margin or for apportionment purposes;

19 (2) an entity subject to the franchise tax on January
20 1, 2008, that was not previously subject to the tax and for which
21 January 1, 2008, is not the beginning date, shall file an annual
22 report due May 15, 2008, based on the period:

23 (A) if the entity has an accounting period that
24 ends on or after January 1, 2007, and before June 1, 2007:

25 (i) beginning on the later of:

26 (a) June 1, 2006; or

27 (b) the date the entity was organized

1 in this state or, if a foreign entity, the date it began doing
2 business in this state; and

3 (ii) ending on the date that accounting
4 period ends in 2007;

5 (B) if the entity has an accounting period that
6 ends on or after June 1, 2007, and before December 31, 2007:

7 (i) beginning on the date that accounting
8 period begins; and

9 (ii) ending on the date that accounting
10 period ends in 2007; and

11 (C) if the entity has an accounting period that
12 ends on December 31, 2007, or if the entity does not have an
13 accounting period that ends in 2007:

14 (i) beginning on the later of:

15 (a) January 1, 2007; or

16 (b) the date the entity was organized
17 in the state or, if a foreign entity, the date it began doing
18 business in this state; and

19 (ii) ending on December 31, 2007; and

20 (3) an entity subject to the franchise tax as it
21 existed before the effective date of this Act at any time after
22 December 31, 2006, and before January 1, 2008, but not subject to
23 the franchise tax on January 1, 2008, shall file a final report for
24 the privilege of doing business at any time after June 30, 2007, and
25 before January 1, 2008, based on the period:

26 (A) beginning on the later of:

27 (i) January 1, 2007; or

1 (ii) the date the entity was organized in
2 this state or, if a foreign entity, the date it began doing business
3 in this state; and

4 (B) ending on the date the entity became no
5 longer subject to the franchise tax.

6 (c) For purposes of this Act, an existing partnership is
7 considered as continuing if it is not terminated.

8 (d) A partnership is considered terminated only if no part
9 of any business, financial operation, or venture of the partnership
10 continues to be carried on by any of its partners in a partnership.

11 (e) For a merger or consolidation of two or more
12 partnerships, the resulting partnership is, for purposes of this
13 Act, considered the continuation of any merging or consolidating
14 partnership whose members own an interest of more than 50 percent in
15 the capital and profits of the resulting partnership.

16 (f) For a division of a partnership into two or more
17 partnerships, the resulting partnerships, other than any resulting
18 partnership the members of which had an interest of 50 percent or
19 less in the capital and profits of the prior partnership, are, for
20 purposes of this Act, considered a continuation of the prior
21 partnership.

22 SECTION 23. (a) The comptroller shall require the entities
23 specified by this section to file an information report in the
24 manner provided by this section. The information report is
25 confidential and exempt from disclosure under Chapter 552,
26 Government Code.

27 (b) The information report required under this section must

1 contain the same information that an entity required to file the
2 report would have submitted in its report due to the comptroller in
3 2006 under Chapter 171, Tax Code, if the changes made by this Act to
4 Chapter 171, Tax Code, had been in effect January 1, 2006. The
5 information report shall also contain the total of maintenance and
6 operations school property taxes paid by the entity to school
7 districts in Texas in the 2005, 2006, and 2007 tax years. The
8 comptroller shall provide the forms and instructions to the
9 entities required to file a report under this section.

10 (c) The comptroller shall take action to revoke the charter,
11 as that term is defined by Section 171.0001, Tax Code, as added by
12 this Act, of an entity that does not file an information return in
13 the manner and under the time limits provided by this section.

14 (d) The comptroller shall identify and require the
15 following entities to file an information report under this
16 section:

17 (1) the 1,000 entities that paid or are required to pay
18 the most franchise tax for the annual reporting period ending
19 December 31, 2005, under Chapter 171, Tax Code, as that chapter
20 existed on the effective date of this section;

21 (2) the 1,000 entities doing business in this state
22 that had the greatest amount of gross receipts in 2005, as
23 determined under Sections 171.105 and 171.1051, Tax Code, as those
24 sections existed on the effective date of this section;

25 (3) the 1,000 entities doing business in this state
26 with the greatest number of employees in this state, according to
27 records maintained by the Texas Workforce Commission, in 2005; and

1 (4) the 1,000 entities doing business in this state
2 with the greatest school maintenance-and-operations property tax
3 levy in this state, according to records maintained or collected
4 for this purpose by the Property Tax Division of the Office of the
5 Comptroller, in 2005;

6 (e) An entity may be listed in one or more of the categories
7 under Subsection (d) of this section. An entity that is listed more
8 than once is required by this section to file only one information
9 return.

10 (f) The comptroller:

11 (1) shall identify the entities described by
12 Subsection (d) of this section;

13 (2) shall prepare all forms and instructions required
14 for those entities to file their information reports as required by
15 this section;

16 (3) shall provide those forms and instructions to
17 those entities on or after November 15, 2006, but before December 2,
18 2006;

19 (4) shall require the entities to submit their
20 information reports on or before February 15, 2007, and February
21 15, 2008;

22 (5) may not grant any extensions for filing the
23 information reports; and

24 (6) shall report to the governor, the lieutenant
25 governor, and the members of the legislature, on or before April 1,
26 2007, and April 1, 2008, the results of the information reports,
27 stating the amount of revenue generated by the tax under Chapter

1 171, Tax Code, in each year, the amount that would have been
2 generated from the entities submitting information reports under
3 this section if the changes made by this Act to Chapter 171, Tax
4 Code, had been in effect January 1, 2006, and the school maintenance
5 and operations property taxes paid by the entities in the 2005,
6 2006, and 2007 tax years.

7 (g) The report required under Subsection (f)(6) of this
8 section may not be formatted in a manner or include any information
9 that discloses or effectively discloses the specific identity of a
10 reporting entity.

11 (h) This section takes effect as provided by Section 27 of
12 this Act.

13 SECTION 24. (a) The supreme court has exclusive and
14 original jurisdiction over a challenge to the constitutionality of
15 this Act or any part of this Act and may issue injunctive or
16 declaratory relief in connection with the challenge.

17 (b) The supreme court shall rule on a challenge filed under
18 this section on or before the 120th day after the date the challenge
19 is filed.

20 (c) This section takes effect as provided by Section 27 of
21 this Act.

22 SECTION 25. (a) The amount of \$2 million is appropriated
23 out of the general revenue fund to the comptroller of public
24 accounts for the state fiscal biennium ending August 31, 2007, for
25 the implementation of this Act and for audit and enforcement
26 activities.

27 (b) This section takes effect as provided by Section 27 of

1 this Act.

2 SECTION 26. Except as otherwise provided by Section 27 of
3 this Act, this Act takes effect January 1, 2005, and applies to
4 reports originally due on or after that date.

5 SECTION 27. A section of this Act that provides that it
6 takes effect as provided by this section takes effect June 1, 2006,
7 if this Act receives a vote of two-thirds of all the members elected
8 to each house, as provided by Section 39, Article III, Texas
9 Constitution. If this Act does not receive the vote necessary for
10 effect on that date, that section takes effect September 1, 2006.

H.B. No. 3

President of the Senate

Speaker of the House

I certify that H.B. No. 3 was passed by the House on April 24, 2006, by the following vote: Yeas 88, Nays 68, 0 present, not voting; passed subject to the provisions of Article III, Section 49a, of the Constitution of the State of Texas.

Chief Clerk of the House

I certify that H.B. No. 3 was passed by the Senate on May 2, 2006, by the following vote: Yeas 16, Nays 14; passed subject to the provisions of Article III, Section 49a, of the Constitution of the State of Texas.

Secretary of the Senate

H.B. No. 3

I certify that the amounts appropriated in the herein H.B. No. 3, 3rd Called Session of the 79th Legislature, are within amounts estimated to be available in the affected fund.

Certified _____

Comptroller of Public Accounts

APPROVED: _____

Date

Governor

BILL ANALYSIS

Senate Research Center

H.B. 3
By: Keffer, Jim et al. (Ogden)
Finance
4/27/2006
Engrossed

AUTHOR'S/SPONSOR'S STATEMENT OF INTENT

The Texas Supreme Court held in *Neeley v. West Orange-Cove Consolidated Independent School District*, that the state school finance system relies on revenues derived from a tax that, in effect, is a state property tax prohibited by the Texas Constitution. The court required the legislature to correct the constitutional violation by June 1, 2006. Since many Texas businesses that receive liability protection from the State do not pay the franchise tax, H.B. 3 raises state revenue by amending Chapter 171, Tax Code, to close the loopholes in the current franchise tax by extending coverage to certain active businesses. At the same time, it broadens the tax base and lowers the rate.

RULEMAKING AUTHORITY

Rulemaking authority is expressly granted to the comptroller of public accounts in SECTION 2 (Section 171.006), SECTION 5 (Sections 171.1011 and 171.1015), SECTION 18, and SECTION 20 of this bill.

SECTION BY SECTION ANALYSIS

SECTION 1. (a) Amends Section 21.02, Tax Code, by amending Subsection (a) and adding Subsection (e), as follows:

(a) Makes conforming and nonsubstantive changes.

(e) Defines "portable drilling rig." Sets forth the circumstances under which a portable drilling rig is taxable, and the taxing unit responsible for collecting said tax.

(b) Makes application of Section 21.02, Tax Code, as amended by this section, prospective to January 1, 2007.

(c) Effective date, this section: January 1, 2007.

SECTION 2. Amends Subchapter A, Chapter 171, Tax Code, as follows:

New heading: SUBCHAPTER A. DEFINITIONS; TAX IMPOSED.

Sec. 171.0001. GENERAL DEFINITIONS. Defines "affiliated group," "assigned employee," "banking corporation," "beginning date," "charter," "client company," "combined group," "controlling interest," "Internal Revenue Code," "lending institution," "management company," "retail trade," "savings and loan association," "shareholder," "staff leasing services company," "total revenue," "unitary business," and "wholesale trade."

Sec. 171.0002. DEFINITION OF TAXABLE ENTITY. (a) Defines "taxable entity."

(b) and (c) Define what a "taxable entity" does not include.

(d) Provides that an entity that can file as a sole proprietorship for federal tax purposes is not a sole proprietorship for purposes of Subsection (b)(1) and is not

exempt under that subsection if the entity is formed in a manner under the statutes of this state or another state that limit the liability of the entity.

Sec. 171.0003. DEFINITION OF PASSIVE ENTITY. Sets forth the instances under which an entity is a passive entity.

Sec. 171.0004. DEFINITION OF CONDUCTING ACTIVE TRADE OR BUSINESS.

(a) Provides that the definition in this section applies only to Section 171.0003.

(b) Sets forth the circumstances under which an entity conducts an active trade or business.

(c) Provides that the activities performed by the entity include certain actions by others.

(d) Provides that an entity conducts active trade or business if assets, including royalties, patents, trademarks, and other intangible assets, held by the entity are used in the active trade or business of one or more related entities.

(e) Sets forth certain instances that do not constitute the conduct of an active trade or business for the purposes of this section.

Sec. 171.001. TAX IMPOSED. Provides that a franchise tax is imposed on each taxable entity, rather than corporation, that does business in this state or is chartered or organized in this state. Deletes existing text relating to taxing limited liability companies. Deletes existing definitions for this chapter.

Sec. 171.0011. ADDITIONAL TAX. (a) Provides that an additional tax is imposed on a taxable entity that for any reason becomes no longer subject to the tax imposed under this chapter, except as provided by Subsection (c). Deletes existing text relating to the earned surplus component of the tax. Makes conforming changes.

(b) Sets forth the manner in which the additional tax is computed. Makes conforming changes.

(c) Makes conforming changes.

(d) Makes no changes to this subsection.

(e) Provides that an additional tax is not imposed on a taxable entity that becomes no longer subject to the tax imposed under this chapter because the entity qualifies as a passive entity.

Sec. 171.002. RATES; COMPUTATION OF TAX. (a) Provides that the rate of the franchise tax is one percent per year of privilege period of taxable margin, subject to Section 171.003 and except as provided by Subsection (b). Deletes existing text relating to the rates of the franchise tax.

(b) Provides that the rate of the franchise tax is 0.5 percent per year of privilege of taxable margin for those taxable entities primarily engaged in retail or wholesale trade. Deletes existing text relating to the computation of the franchise tax on corporations.

(c) Sets forth the conditions under which a taxable entity is primarily engaged in retail or wholesale trade. Deletes existing text relating to computations made under Subsection (b).

(c-1) Provides that Subsection (c)(2) does not apply to total revenue from activities in a retail trade described by Major Group 58 of the Standard Industrial Classification Manual published by the federal Office of Management and Budget.

- (d) Sets forth the conditions under which a taxable entity is not required to pay any tax and is not considered to owe any tax for a period.

Deletes text of existing Section 171.005 (Rate of Tax for Corporation in Process of Liquidation).

Sec. 171.003. INCREASE IN RATE REQUIRES VOTER APPROVAL. (a) Provides that an increase in a rate provided by Section 171.002(a) or (b) takes effect only if approved by majority vote in a statewide referendum held on the question of increasing the rate. Requires the referendum to specify the increased rate or rates.

- (b) Provides that this section does not apply to a decrease in a rate provided by Section 171.002(a) or (b), but does apply to a subsequent rate increase if the rate is decreased.

- (c) Sets forth certain conditions under which this section does not apply to any change in the tax imposed by this chapter.

Sec. 171.006. ADJUSTMENT OF ELIGIBILITY FOR EXEMPTION AND COMPENSATION DEDUCTION. (a) Defines "consumer price index."

- (b) Sets forth the manner in which the amounts prescribed by Section 171.002(d)(2) and 171.1013(c) are increased or decreased in relation to the consumer price index. Provides that said increase or decrease occurs on January 1 of each odd-numbered year, beginning in 2009.

- (c) Provides that the amounts determined under Subsection (b) apply to a report originally due on or after the date the determination is made.

- (d) Requires the comptroller of public accounts (comptroller) to make the determination required by this section and authorizes the comptroller to adopt rules related to making that determination.

- (e) Provides that a determination made by the comptroller under this section is final and is prohibited from being appealed.

SECTION 3. Amends Section 171.052, Tax Code, to provide that an entity is subject to the franchise tax for a tax year in any portion of which the entity is in violation of an order issued by the Texas Department of Insurance under Section 2254.003(b), Insurance Code, that is final after appeal or that is no longer subject to appeal. Makes conforming changes.

SECTION 4. Amends Subchapter B, Chapter 171, Tax Code, by adding Section 171.088, as follows:

Sec. 171.088. EXEMPTION--NONCORPORATE ENTITY ELIGIBLE FOR CERTAIN EXEMPTIONS. Sets forth certain guidelines under which an entity that is not a corporation, but would qualify for a specific exemption under this chapter because of its activities, may qualify for the tax.

SECTION 5. Amends Subchapter C, Chapter 171, Tax Code, including the reenacting and amending of Section 171.109(g), Tax Code, as amended by Chapters 801 and 1198, Acts of the 71st Legislature, Regular Session, 1989, as follows:

New heading: SUBCHAPTER C. DETERMINATION OF TAXABLE MARGIN;
ALLOCATION AND APPORTIONMENT

Sec. 171.101. New heading: DETERMINATION OF TAXABLE MARGIN. (a) Sets forth the manner in which the taxable margin of a taxable entity is computed. Deletes existing text relating to the computation of the taxable capital of a corporation.

- (b) Authorizes a staff leasing services company to subtract only compensation as determined under Section 171.1013, notwithstanding Subsection (a)(1)(B)(ii).
- (c) Provides that in making a computation under this section, an amount that is zero or less is computed as a zero. Deletes existing text relating to the net taxable capital of a limited liability company and a savings and loan association.
- (d) Requires an election under Subsection (a)(1)(B)(ii) to be made by the taxable entity on its annual report and provides that the election is effective only for that annual report. Authorizes the election to be changed by filing an amended report.

Sec. 171.1011. DETERMINATION OF TOTAL REVENUE FROM ENTIRE BUSINESS. (a) Provides that in this section, a reference to an Internal Revenue Service (IRS) form includes a variant of the form, and provides examples.

- (b) Provides that in this section, a reference to an amount entered on a line number on an IRS form includes the corresponding amount entered on a variant of the form, or a subsequent form, with a different line number. Requires the comptroller to adopt rules as necessary to accomplish the legislative intent prescribed by this subsection and Subsection (a).
- (c) Sets forth the manner in which the total revenue of a taxable entity is determined.
- (d) Requires a corporation that is part of a federal consolidated group, subject to Section 171.1014, to compute its total revenue under Subsection (c) as if it had filed a separate return for federal income tax purposes.
- (e) Requires a taxable entity that owns an interest in a passive entity that is not included in a group report under Section 171.1014 to include certain amounts in the taxable entity's total revenue.
- (f) Requires a taxable entity to exclude certain flow-through funds from its total revenue, to the extent included under Subsection (c)(1)(A), (c)(2)(A), or (c)(3).
- (g) Requires a taxable entity to exclude certain flow-through funds from its total revenue, to the extent included under Subsection (c)(1)(A), (c)(2)(A), or (c)(3).
- (g-1) Requires a taxable entity that is a lending institution to exclude from its total revenue, to the extent included under above referenced subsections, proceeds from the principal repayment of loans.
- (g-2) Requires a taxable entity to exclude from its total revenue, to the extent included under above referenced subsections, the tax basis as determined under the Internal Revenue Code of securities and loans sold.
- (g-3) Requires a taxable entity that provides legal services to exclude certain amounts from its total revenue, to the extent included under above referenced subsections.
- (h) Prohibits the taxable entity, if it belongs to an affiliated group, from excluding certain payments that are made to entities that are members of the affiliated group.
- (i) Prohibits a payment made under an ordinary contract for the provision of services in the regular course of business from being excluded, except as provided by Subsection (g).
- (j) Prohibits any amount excluded under this section from being included in the determination of cost of goods sold under Section 171.1012 or the determination of compensation under Section 171.1013.

(k) Requires a taxable entity that is a staff leasing services company to exclude certain payments from its total revenue.

(l) Defines "sales commission" and "principal" for the purposes of Subsection (g)(1).

(m) Requires a taxable entity to exclude from its total revenue dividends and interest received from federal obligations, to the extent included under Subsection (c)(1)(A), (c)(2)(A), or (c)(3).

(m-1) Requires a taxable entity that is a management company to exclude certain reimbursements of specified costs from its total revenue.

(n) Requires a taxable entity that is a health care provider to exclude certain amounts from its total revenue, except as provided by Subsection (c).

(n-1) Requires the comptroller to adopt rules governing the computation of the actual cost to a health care provider of certain uncompensated care, and the audit requirements related to these computations.

(o) Requires a health care provider that is a health care institution to exclude from its total revenue 50 percent of the amounts described by Subsection (n), to the extent included under Subsection (c)(1)(A), (c)(2)(A), or (c)(3).

(p) Defines, for this section, "federal obligations," "health care institution," "health care provider," "obligation," "pro bono services," "out-of-pocket expenses," "United States government," "United States government agency," and "United State-sponsored agency."

(q) Requires a taxable entity to exclude certain amounts from its total revenue, to the extent included under Subsection (c)(1)(A), (c)(2)(A), or (c)(3).

(r) Requires a taxable entity to exclude certain amounts from its total revenue, to the extent included under Subsection (c)(1)(A), (c)(2)(A), or (c)(3).

(s) Requires the comptroller to certify dates during which the monthly average closing price of West Texas Intermediate crude oil is below \$40 per barrel, and the average closing price of gas is below \$5 per MMBtu, as recorded on the New York Mercantile Exchange.

Sec. 171.1012. DETERMINATION OF COST OF GOODS SOLD. (a) Defines "goods," "production," and "tangible personal property."

(b) Requires a taxable entity that elects to subtract cost of goods sold for the purpose of computing its taxable margin, subject to Section 171.1014, to determine the amount of that cost of goods sold as provided by this section.

(c) Sets forth those items included in determining the cost of goods sold.

(d) Sets forth additional items included in determining the cost of goods sold in relation to the taxable entity's goods.

(e) Sets forth certain items that are not included in determining the cost of goods sold in relation to the taxable entity's goods.

(f) Authorizes a taxable entity to subtract certain costs as a cost of goods sold. Prohibits any costs excluded under Subsection (e) from being subtracted under this subsection.

(g) Requires a taxable entity that is allowed a subtraction by this section for a cost of goods sold and that is subject to specific sections of the Internal Revenue Code to capitalize that cost in a specific manner.

(h) Requires a taxable entity to determine its cost of goods sold, except as otherwise provided by this section, in accordance with methods permitted by federal statutes and regulations. Provides that this subsection does not affect the type or category of cost of goods sold that may be subtracted under this section.

(i) Authorizes a taxable entity to make a subtraction under this section in relation to the cost of goods sold only if that entity owns the goods. Sets forth the manner in which taxable entities are determined to be the owner of real property, labor or materials, or goods being manufactured or produced.

(j) Prohibits a taxable entity from making a subtraction under this section for cost of goods sold to the extent the costs was funded by partner contributions and deducted under Subsection (c)(13).

(k) Authorizes a taxable entity, if the entity is a lending institution that offers loans to the public and elects to subtract the cost of goods sold, to subtract as a cost an amount equal to interest expense, notwithstanding any other provision of this section.

(k-1) Authorizes specified taxable entities to subtract as a cost of goods sold the costs otherwise allowed by this section in relation to tangible personal property that the entity rents or leases in the ordinary course of business, notwithstanding any other provision of this section.

(l) Authorizes a payment made by one member of an affiliated group to another member of the group not included in the combined group to be subtracted as a cost of goods sold only if it is a transaction made at arm's length, notwithstanding any other provision of this section.

(m) Defines "arm's length."

(n) Defines "related party."

Sec. 171.1013. DETERMINATION OF COMPENSATION. (a) Defines "wages and cash compensation."

(b) Authorizes a taxable entity that elects to subtract compensation for the purpose of computing its taxable margin under Section 171.101 to subtract certain amounts, subject to Section 171.1014.

(c) Prohibits a taxable entity from including more than \$300,000, or the amount determined under Section 171.006, for any person in the amount of wages and cash compensation it determines under Section 171.101, notwithstanding the actual amount of wages and cash compensation paid by the taxable entity to its officers, directors, owners, partners, and employees.

(c-1) Prohibits a taxable entity from subtracting any wages or cash compensation paid to an undocumented worker, subject to Section 171.1014. Defines "undocumented worker."

(d) Sets forth certain requirements and prohibitions of a staff leasing services company in determining its wages or cash compensation payments.

(e) Sets forth the manner in which a taxable entity that is a client company that contracts with a staff leasing services company determines compensation.

- (f) Sets forth certain requirements and prohibition of a management company in determining its wages or cash compensation payments.
- (g) Requires a managed entity to include reimbursements made to the management company for wages and compensation as if the reimbursed amounts had been paid to employees of the managed entity.
- (h) Prohibits a taxable entity that subtracts compensation in computing its taxable margin from including amounts paid to an employee whose primary employment is directly associated with the operation of certain facilities as wages or cash compensation, subject to Section 171.1014.

Sec. 171.1014. COMBINED REPORTING; AFFILIATED GROUP ENGAGED IN UNITARY BUSINESS. (a) Requires taxable entities that are part of an affiliated group engaged in a unitary business to file a combined group report in lieu of individual reports based on the combined group's business. Prohibits the combined group from including a taxable entity that conducts business outside the United States if 80 percent or more of the entity's property and payroll are assigned to locations outside of the United States. Sets forth guidelines to determine how an entity's property and payroll are assigned.

- (b) Provides that the combined group is a single taxable entity for purposes of the application of the tax imposed under this chapter.
- (c) Sets forth guidelines to determine a combined group's total revenue, for purposes of Section 171.101.
- (d) Requires a combined group to make an election to subtract either costs of goods sold or compensation that applies to all of its members, for purposes of Section 171.101.
- (e) Sets forth requirements in determining the amount of cost of goods sold for a combined group that subtracts said cost, for purposes of Section 171.101.
- (f) Sets forth requirements in determining the amount of compensation for a combined group that subtracts said amount, for purposes of Section 171.101.
- (g) Authorizes a combined group to elect to include in the combined group an exempt entity that would be included in the group if the entity were not exempt, and to treat the exempt entity as if it were a taxable entity.

Sec. 171.1015. REPORTING FOR CERTAIN PARTNERSHIPS IN TIERED PARTNERSHIP ARRANGEMENT. (a) Defines "tiered partnership arrangement."

- (b) Authorizes a taxable entity that is a lower tier entity, in addition to the tax it is required to pay under this chapter on its own taxable margin, to pay the tax on the taxable margin of a higher tier partnership if the higher tier partnership submits a report to the comptroller showing the amount of taxable margin that each lower tier entity that owns it should include within the lower tier entity's own taxable margin, according to the profits interest of the lower tier entity. Provides that an upper tier partnership is not required to pay tax under this chapter on any taxable margin reported under this section.
- (c) Provides that this section does not apply to that percentage of the taxable margin attributable to a lower tier entity by an upper tier entity partnership if the lower tier entity is not subject to the tax under this chapter. Provides that in this case, the higher tier partnership is liable for the tax on its taxable margin.
- (d) Requires the comptroller to adopt rules to administer this section.

Deletes text of existing Section 171.102 (Determination of Taxable Capital of Corporation in Process of Liquidation).

Sec. 171.103. New heading: DETERMINATION OF GROSS RECEIPTS FROM BUSINESS DONE IN THIS STATE FOR MARGIN. (a) Sets forth the manner in which the gross receipts of a taxable entity from its business done in this state is determined for the purpose of apportioning margin. Deletes existing text relating to determining the gross receipts of a corporation. Makes conforming changes. Deletes portions of existing text of Section 171.1032 relating to determining the gross receipts of a corporation in apportioning taxable capital.

Sec. 171.105. New heading: DETERMINATION OF GROSS RECEIPTS FROM ENTIRE BUSINESS FOR MARGIN. (a) Deletes existing text of Section 171.105, and redesignates text of existing Section 171.1051. Sets forth the manner in which the gross receipts of a taxable entity from its entire business are determined for the purpose of apportioning margin. Deletes existing text relating to determining the gross receipts of a corporation. Makes conforming changes.

(b) Makes conforming changes.

(c) Requires a combined group to include in its gross receipts computed under Subsection (a) the gross receipts of each taxable entity that is a member of the combined group, without regard to whether that entity has a nexus with this state for the purposes of taxation.

Sec. 171.1055. EXCLUSION OF CERTAIN RECEIPTS FOR MARGIN APPORTIONMENT. (a) Prohibits receipts excluded from total revenue by a taxable entity under Section 171.1011, in apportioning margin, from being included in either the receipts of the taxable entity from its business done in this state as determined under Section 171.103 or the receipts of the taxable entity from its entire business done as determined under Section 171.105.

(b) Prohibits receipts derived from transactions between individual members of a combined group that are excluded under Section 171.1014(c)(3), in apportioning margin, from being included in the receipts of the taxable entity from its business done in this state as determined under Section 171.103, except that receipts derived from the sale of a combined group where one member party to the transaction does not have nexus in this state is required to be included in the receipts of the taxable entity from its business done in this state as determined under Section 171.103 to the extent that the member of the combined group that does not have nexus in this state resells the tangible personal property without modification to a purchase in this state.

(c) Prohibits receipts derived from transactions between individual members of a combined group that are excluded under Section 171.1014(c)(3), in apportioning margin, from being included in the receipts of the taxable entity from its entire business done as determined under Section 171.105.

Deletes text of existing Sections 171.1051(c) and (d).

Sec. 171.106. New heading: APPORTIONMENT OF MARGIN TO THIS STATE. Deletes existing text relating to the apportionment of a corporation's taxable capital. Deletes existing text relating to certain entities registered with the State Securities Board filing a report with the comptroller and a requirement of the comptroller to issue a report evaluating the statewide fiscal impact of certain provisions of this section, as it previously existed. Makes conforming changes.

Deletes text of existing Section 171.1061. (Allocation of Certain Taxable Earned Surplus to this State).

Sec. 171.107. New heading: DEDUCTION OF COST OF SOLAR ENERGY DEVICE FROM MARGIN APPORTIONED TO THIS STATE. (b) Authorizes a taxable entity, rather than a corporation, to deduct from its apportioned margin, rather than taxable

earned surplus, 10 percent of the amortized cost of a solar energy device if meets certain criteria. Deletes existing text relating to a corporation's deduction of a solar energy device.

(c) Requires the amortization of the cost of a solar energy device to provide for equal monthly amounts or conform to federal depreciation schedules.

(d) Makes conforming changes. Deletes existing Subsection (e) relating to a corporation deductions.

Sec. 171.108. New heading: DEDUCTION OF COST OF CLEAN COAL PROJECT FROM MARGIN APPORTIONED TO MARGIN APPORTIONED TO THIS STATE. Makes conforming changes. Deletes existing Subsections (e) relating to a corporations deductions. Deletes existing Sections 171.109 and 171.110 relating to a surplus and a determination of net taxable earned surplus.

Sec. 171.111. New heading: TEMPORARY CREDIT ON TAXABLE MARGIN. (a) Authorizes a taxable entity, not later than March 1, 2007, rather than not later than March 1, 1992, to notify the comptroller in writing of its intent to preserve its right to take a credit in an amount allowed by this section on the tax due on taxable margin. Makes conforming changes.

(b) Provides that the credit allowed under this section for any privilege period is computer in certain manner. Deletes existing text relating to the method of computing the credit.

(c) Redesignates Subsections (c) - (e) as Subsection (c). Deletes existing text relating to a corporation computing a certain amount and the manner it computes the amount. Deletes existing text relating to requirements after a certain election. Makes conforming changes.

(d) Provides that a credit that a taxable entity is to is entitled to under this section does not convey, and is prohibited from being assigned or transferred, in relation to a transaction in which the taxable entity is purchased by another entity.

(e) Redesignates Subsections (f) - (i) as Subsection (e). Provides that this section expires September 1, 2026, rather than September 1, 2012. Deletes Section 171.112 relating to gross receipts for taxable capital.

Sec. 171.1121. New heading: GROSS RECEIPTS FOR MARGIN. Makes conforming changes. Deletes existing Section 171.113 relating to an alternative method of determining taxable capital and gross receipts for certain corporations.

SECTION 6. Amends Subchapter D, Chapter 171, Tax Code, as follows:

Sec. 171.152. Makes a conforming change.

Deletes existing Sections 171.153 and 171.1531 relating to business on which tax on net taxable capital is based and credit for survivor of merger.

Sec. 171.1532. New heading: BUSINESS ON WHICH TAX ON NET TAXABLE MARGIN IS BASED. Makes conforming changes.

Sec. 171.154. Makes a conforming change.

Sec. 171.158. New heading: PAYMENT BY FOREIGN TAXABLE ENTITY BEFORE WITHDRAWAL FROM STATE. (a) Authorizes a foreign taxable entity holding a registration or certificate of authority to do business in this state, except as provided by Subsection (b), to withdraw from business in this state by filing a certificate of withdrawal with the secretary of state. Makes conforming changes and a nonsubstantive change.

(b) Makes conforming changes.

SECTION 7. Amends Subchapter E, Chapter 171, Tax Code, as follows:

Sec. 171.201. (a) Requires a taxable entity on which the franchise tax is imposed, except as provided by Section 171.202 (Exemption From Reporting Requirements), to file an initial report with comptroller containing certain information. Makes conforming changes.

(b) Makes conforming and nonsubstantive changes.

Sec. 171.202. (a) - (c) Makes conforming changes.

(d) Requires the optional payment under Subsection (c)(2)(B) or (c)(2)(B), in the case of a taxpayer whose previous return was its initial report, to be a certain amount.

(e), (f), and (i) Makes conforming changes.

Sec. 171.2022. Makes conforming changes.

Sec. 171.203. Makes a nonsubstantive change.

Sec. 171.2035. ADDITIONAL PUBLIC INFORMATION REPORT. (a) Requires a taxable entity that has more than 100,000 employees in this state to file a report with the comptroller stating the number of the taxable entity's employees in this state that receive assistance for that employee or the employee's family under the Children's Health Insurance Program (CHIP) or the Medicaid program.

(b) Requires a taxable entity described by Subsection (a) to file the report once a year on a form prescribed by the comptroller.

Sec. 171.204. INFORMATION REPORT. (a) Authorizes the comptroller, except as provided by Subsection (b), to determine eligibility for the exemption provided by Section 171.2022, or to determine the amount of the franchise tax or the correctness of a franchise tax report, to require a taxable entity, rather than an officer of a taxable entity, that may be subject to the tax imposed under this chapter to file an information report with the comptroller stating the amount of the taxable entity's margin, or any other information the comptroller may request that is necessary to make a determination under this subsection. Makes conforming changes.

(b) Makes conforming changes.

Sec. 171.205. Makes conforming changes.

Sec. 171.206. Provides that certain information is confidential and is prohibited from being made open to public inspection. Makes a nonsubstantive change.

Sec. 171.207. Makes a conforming and a nonsubstantive change.

Sec. 171.208. Prohibits a person, including certain state employees or an owner a taxable entity, who has access to a report filed under this chapter from making known in a manner not permitted by law the amount or source of the taxable entity's income, profits, losses, expenditures, cost of goods sold, compensation, or other information in the report relating to the financial condition of the taxable entity. Makes conforming changes.

Sec. 171.209. New heading: RIGHT OF OWNER TO EXAMINE OR RECEIVE REPORTS. Makes conforming changes and a nonsubstantive change.

Sec. 171.211. New heading: EXAMINATION OF RECORDS. Makes conforming changes.

Sec. 171.212. Requires a taxable entity to file an amended report under this chapter if the taxable entity files an amended federal income tax return that changes the taxable entity's taxable margin, rather than earned surplus. Makes conforming changes.

SECTION 8. Amends the heading to Subchapter F, Chapter 171, Tax Code, to read as follows:

SUBCHAPTER F. FORFEITURE OF CORPORATE AND BUSINESS PRIVILEGES

SECTION 9. Amends Subchapter F, Chapter 171, Tax Code, by adding Section 171.2515, as follows:

Sec. 171.2515. FORFEITURE OF RIGHT OF TAXABLE ENTITY TO TRANSACT BUSINESS IN THIS STATE. (a) Authorizes the comptroller to, for the same reasons and using the same procedures the comptroller uses in relation to the forfeiture of the corporate privileges of a corporation, forfeit the right of a taxable entity to transact business in this state.

(b) Provides that the provisions of this subchapter, including Section 171.255 (Liability of Director and Officers), that apply to the forfeiture of corporate privileges apply to the forfeiture of a taxable entity's right to transact business in this state.

SECTION 10. Amends Section 171.351, Tax Code, to make conforming changes.

SECTION 11. Amends Section 171.353, Tax Code, to make conforming changes.

SECTION 12. Amends Section 171.354, Tax Code, to make conforming changes.

SECTION 13. Amends Sections 171.362(a), (d), and (e), Tax Code, to make conforming and nonsubstantive changes.

SECTION 14. Amends Sections 171.363(a) and (b), Tax Code, to make conforming changes.

SECTION 15. Amends Section 171.401, Tax Code, to make a conforming change.

SECTION 16. (a) Amends Section 313.007, Tax Code, as follows:

Sec. 313.007. Provides that Subchapters B, C, and D expire December 31, 2011, rather than December 31, 2007.

(b) Amends Section 313.024(a), Tax Code, to provide that this subchapter and Subchapters C and D apply only to property owned by an entity to which Chapter 171 (Franchise Tax), rather than Section 171.001 (Tax Imposed), applies.

(c) Amends Section 313.024(b), Tax Code, to make a conforming change.

(d) Amends Section 313.025(b), Tax Code, to provide that the governing body of a school district is not required to consider an application for a limitation on appraised value that is filed with the governing body under Subsection (a). Requires the governing body, if the governing body of the school district does elect to consider an application, to request that TEA conduct an economic impact evaluation of the application on behalf of the school district, rather than engage a third person to conduct an economic impact evaluation of the application on behalf of the school district, and provides that TEA is required to conduct the evaluation as soon as practicable. Requires the governing body to provide to TEA any information requested by TEA. Authorizes TEA to develop a methodology to allow comparisons of economic impact for different schedules of addition of qualified investment or qualified property as part of the economic impact evaluation. Provides that the economic impact evaluation of TEA is binding on the

governing body of the school district and the applicant. Requires the governing body to provide a copy of the evaluation to the applicant on request. Authorizes TEA to charge and collect a fee sufficient to cover the costs of providing the economic impact evaluation. Requires the governing body of a school district to approve or disapprove an application before the 121st day after the date the application is filed, unless TEA's economic impact evaluation has not been received or an extension is agreed to by the governing body and the applicant. Makes a nonsubstantive change.

(e) Amends Section 313.051, Tax Code, as follows:

Sec. 313.051. (a) Provides that this chapter applies only to a school district that has territory in certain areas or counties.

(a-1) Provides that notwithstanding Subsection (a), if on January 1, 2002, this subchapter applied to a school district in whose territory is located a federal nuclear facility, this subchapter continues to apply to the school district regardless of whether the school district ceased or ceases to be described by Subsection (a) after that date.

(b) Requires at least 80 percent of all the new jobs created to be certain qualifying jobs, except that, for a school district described by Subsection (a)(2), each qualifying job is required to pay at least 110 percent of the average weekly wage for manufacturing jobs in the region designated for the regional planning commission, council of governments, or similar regional planning agency created under Chapter 391 (Regional Planning Commissions), Local Government Code, in which the district is located.

(f) Provides that Section 313.051(b), Tax Code, as amended by this section, applies only to a limitation on the appraised value for school district maintenance and operations ad valorem tax purposes for which the owner files an application on or after the effective date of this Act. Provides that a limitation on the appraised value for school district maintenance and operations ad valorem tax purposes for which the owner files an application before the effective date of this Act is governed by the law as it existed immediately before the effective date of this Act, and that law is continued in effect for that purpose.

SECTION 17. (a) Provides that the repeal of Section 171.111 (Temporary Credit on Net Taxable Earned Surplus), Tax Code, by this Act does not affect a credit that accrued under that section before the effective date of this Act.

(b) Authorizes a corporation that has any unused credits accrued before the effective date of this Act under Section 171.111, Tax Code, to claim those unused credits on or with the tax report for the period in which the credits were accrued, and provides that the former law under which the corporation accrued the credits is continued in effect for purposes of determining the amount of the credits the corporation may claim and the manner in which the corporation may claim the credits.

SECTION 18. (a) Repealer: Subchapter L (Tax Credit Wages Paid To Texas Department of Criminal Justice Work Program Participants or Former Participants); Subchapter M (Tax credit for Wages Paid to Certain Children Committed to Texas Youth Commission); Subchapter N (Tax credit for Establishing Day-Care Center or Purchasing Child Services); Subchapter O (Tax credit for Certain Research and Development Activities); Subchapter P (Tax credits for certain Job Creation Activities); Subchapter Q (Tax Credits for Certain Capital Investments); Subchapter R (Tax Credit for Contributions to Before and After School Programs); Subchapter S (Credits Limitation); Subchapter T (Tax Credit for Wages Paid to Persons With Certain Disabilities); Subchapter U (Tax Credit for Title Insurance Holding Companies) as added by Chapter 209, Acts of the 78th Legislature, Regular Session, 2003; and Subchapter U (Tax Credit for Title Insurance Holding Companies) as added by Chapter 1274, Acts of the 78th Legislature, Regular Session, 2003.

(b) Provides that this section does not affect a credit authorized by a provision listed in Subsection (a) of this section that accrued under Chapter 171, Tax Code, before the effective date of this Act or a credit that continues to accrue under Section 19 of this Act.

(c) Authorizes a corporation that has any unused credits accrued before the effective date of this Act under a provision other than Subchapter O, P, or Q, Chapter 171, Tax Code, to claim those unused credits on or with the tax report for the period in which the credits were accrued, and provides that the former law under which the corporation accrued the credits is continued in effect for purposes of determining the amount of the credits the corporation may claim and the manner in which the corporation may claim the credits.

(d) Authorizes a corporation that has any unused credits accrued before the effective date of this Act under Subchapter O, Chapter 171, Tax Code, to claim those unused credits on or with the tax report for the period in which the credit was accrued. Authorizes the corporation, if the corporation was allowed to carry forward unused credits under that subchapter, to continue to apply those credits on or with each consecutive report until the earlier of the date the credit would have expired under the terms of Subchapter O, Chapter 171, Tax Code, had it continued in existence, or December 31, 2027, and provides that the former law under which the corporation accrued the credits is continued in effect for purposes of determining the amount of the credits the corporation may claim and the manner in which the corporation may claim the credits.

(e) Authorizes a corporation that has any unused credits accrued before the effective date of this Act under Subchapter P, Chapter 171, Tax Code, to claim those unused credits on or with the tax report for the period in which the credit was accrued. Authorizes the corporation, if the corporation was allowed to carry forward unused credits under that subchapter, to continue to apply those credits on or with each consecutive report until the earlier of the date the credit would have expired under the terms of Subchapter P, Chapter 171, Tax Code, had it continued in existence, or December 31, 2012, and provides that the former law under which the corporation accrued the credits is continued in effect for purposes of determining the amount of the credits the corporation may claim and the manner in which the corporation may claim the credits.

(f) Authorizes a corporation that has any unused credits accrued before the effective date of this Act under Subchapter Q, Chapter 171, Tax Code, to claim those unused credits on or with the tax report for the period in which the credit was accrued. Authorizes the corporation, if the corporation was allowed to carry forward unused credits under that subchapter, to continue to apply those credits on or with each consecutive report until the earlier of the date the credit would have expired under the terms of Subchapter Q, Chapter 171, Tax Code, had it continued in existence, or December 31, 2012, and provides that the former law under which the corporation accrued the credits is continued in effect for purposes of determining the amount of the credits the corporation may claim and the manner in which the corporation may claim the credits.

(g) Requires the comptroller to adopt rules to administer this section.

SECTION 19. Provides that a written agreement between the Texas Department of Economic Development or its successor and a taxpayer effective before June 1, 2006, that allows for credits against the tax imposed under Chapter 171, Tax Code, continues in effect and the credits allowed under the agreement continue to accrue and may be claimed in the manner provided by the agreement against the tax imposed under Chapter 171, Tax Code, as amended by this Act, for the duration of the agreement. Provides that the former law under which the agreement was made and under which the taxpayer received the entitlement to the credits is continued in effect for purposes of determining the amount of the credits the taxpayer may claim and the manner in which the taxpayer may claim the credits.

SECTION 20. Requires the comptroller to adopt rules to implement the legislative intent in Sections 171.1012(e)(14) and 171.1013(c-1), Tax Code.

SECTION 21. Provides that the franchise tax imposed by Chapter 171, Tax Code, as amended by this Act, is not an income tax and Pub. L. No. 86-272 does not apply to the tax.

SECTION 22. (a) Provides that subject to other provisions of this section, this Act applies to reports originally due on or after the effective date of this Act.

(b) Sets forth the requirements for an entity becoming subject to the franchise tax under this Act.

(c) Provides that for purposes of this Act, an existing partnership is considered as continuing if it is not terminated.

(d) Provides that a partnership is considered terminated only if no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership.

(e) Provides that for a merger or consolidation of two or more partnerships, the resulting partnership is, for purposes of this Act, considered the continuation of any merging or consolidating partnership whose members own an interest of more than 50 percent in the capital and profits of the resulting partnership.

(f) Provides that for a division of a partnership into two or more partnerships, the resulting partnerships, other than any resulting partnership the members of which had an interest of 50 percent or less in the capital and profits of the prior partnership, are, for purposes of this Act, considered a continuation of the prior partnership.

SECTION 23. (a) Requires the comptroller to require the entities specified by this section to file an information report in the manner provided by this section. Provides that the information report is confidential and exempt from disclosure under Chapter 552 (Public Information), Government Code.

(b) Requires the information report required under this section to contain the same information that an entity required to file the report would have submitted in its report due to the comptroller in 2006 under Chapter 171, Tax Code, if the changes made by this Act to Chapter 171, Tax Code had been in effect January 1, 2006. Requires the information report to also contain the total of maintenance and operations school property taxes paid by the entity to school districts in Texas in the 2005, 2006, and 2007 tax years. Requires the comptroller to provide the forms and instructions to the entities required to file a report under this section.

(c) Requires the comptroller to take action to revoke the charter, as that term is defined by Section 171.0001, Tax Code, as added by this Act, of an entity that does not file an information return in the manner and under the time limits provided by this section.

(d) Requires the comptroller to identify and require certain entities to file an information report under this section.

(e) Authorizes an entity to be listed in one or more of the categories under Subsection (d) of this section. Provides that an entity that is listed more than once is required by this section to file only one information return.

(f) Sets forth certain duties required of the comptroller.

(g) Prohibits the report required under Subsection (f)(6) of this section from being formatted in a manner or including any information that discloses or effectively discloses the specific identity of a reporting entity.

(h) Provides that this section takes effect as provided by Section 27 of this Act.

SECTION 24. (a) Provides that the supreme court has exclusive and original jurisdiction over a challenge to the constitutionality of this Act or any part of this Act and may issue injunctive or declaratory relief in connection with the challenge.

(b) Requires the supreme court to rule on a challenge filed under this section on or before the 120th day after the date the challenge is filed.

(c) Provides that this section takes effect as provided by Section 27 of this Act.

SECTION 25. (a) Provides that the amount of \$2 million is appropriated out of the general revenue fund to the comptroller for the state fiscal biennium ending August 31, 2007, for the implementation of this Act and for audit and enforcement activities.

(b) Provides that this section takes effect as provided by Section 27 of this Act.

SECTION 26. Effective date: January 1, 2008, except as otherwise provided by Section 27. Makes application of this Act prospective for reports originally due on or after the effective date.

SECTION 27. Effective date of sections noted as taking effect as provided by this section: June 1, 2006, or September 1, 2006.

Unofficial copy Travis Co. District Clerk Velda L. Price

SUBJECT: Restructuring the Texas franchise tax

COMMITTEE: Ways and Means — committee substitute recommended

VOTE: 7 ayes — J. Keffer, Villarreal, Grusendorf, Luna, Ritter, Smithee, Woolley

1 nay — Paxton

1 absent — Edwards

WITNESSES: For — Bill Allaway, Texas Taxpayers and Research Association; John Hawkins, Texas Hospital Association; Paul Kennedy, Texas Dental Association; Scott Norman, Texas Association of Builders; Karen Reagan, Texas Federation of Drug Stores; Steve Stagner, Texas Council of Engineering Companies; Heather Vasek, Texas Association for Home Care, Inc.; Kristie Zamrazil, Texas Pharmacy Association

Against — Hayes Fuller, Texas Association of Defense Counsel

On — Karey Barton, James LeBas, Texas Tax Reform Commission; Chuck Courtney, Texas Retailers Association; John W. Fainter, Jr., Association of Electric Companies of Texas, Inc.; Jay Harvey, Texas Trial Lawyers Association; Steve Kuntz, Glen Rosenbaum, Law Firm Legislative Coalition; David C. Palmer, International Council of Shopping Centers

BACKGROUND: Under Tax Code, ch. 171, the state levies the corporate franchise tax, Texas' primary business tax, in exchange for granting the privilege (franchise) of doing business in Texas. The tax applies only to for-profit corporations and, since 1991, to limited liability companies (LLCs) chartered or organized in Texas, as well as to foreign corporations and LLCs based or doing business in the state. As such, franchise taxpayers include professional corporations, banks, savings and loan associations, state-limited banking associations, and professional LLCs, but not limited partnerships, sole proprietorships, or non-corporate associations.

Insurance and open-end investment companies (e.g., mutual funds) and most non-profit corporations are excepted, as are corporations with gross

receipts less than \$150,000 and firms owing \$100 or less in tax. Major exemptions and exclusions include interest earned on federal securities, business loss carryover, and officer/director compensation paid by companies with 35 or fewer shareholders.

A dual calculation method determines the amount of tax liability. Taxpayers pay the greater of a 0.25 percent tax on taxable capital (assets' net worth) or a 4.5 percent tax on earned surplus (modified net income). The income component generates the most revenue and is paid by about 75 percent of franchise taxpayers.

In fiscal 2004-05, the franchise tax made up about 7.5 percent of state tax revenue, generating more than \$4 billion. For fiscal 2006-07 the tax is projected to increase by 17.2 percent to \$4.7 billion, including \$2.3 billion in fiscal 2006 and \$2.4 billion in fiscal 2007. Franchise tax payments are due on May 15 of each year, and all revenue goes into the general revenue fund.

In recent years, some large Texas-based firms have reorganized as partnerships under state law. As such, they no longer must pay the franchise tax. Examples include Dell Computer and SBC Communications (now AT&T). Firms accomplish this by forming wholly owned out-of-state subsidiaries, usually in tax-friendly states such as Delaware – hence, the resulting entity has been nicknamed “the Delaware sub.” Typically, the subsidiaries enter into limited partnerships wherein the general corporate partner owns 0.1 percent of the operating assets in Texas and the limited partners own 99.9 percent. Under the comptroller’s administrative rules, foreign corporations acting as limited partners are not considered to be doing business in Texas for tax purposes and thus are not subject to the franchise tax. The franchise tax liability of the general partner corporation typically is zero because its 0.1 percent interest fails to generate total receipts greater than the \$150,000 income threshold.

A second accounting method used by some large firms is termed the “Geoffrey” loophole, named after the Toys R Us Inc. giraffe mascot. Under this method, corporations establish a subsidiary in another state that charges the Texas operations for the use of certain intangible assets, such as corporate trademarks. This method diverts money out of the Texas operations, and the franchise tax is applied only to what remains.

Insurance Code, ch. 4 imposes insurance premium taxes on the amount of gross premiums written by insurance companies, with the rates varying depending on the type of insurance. In fiscal 2004-05 the state collected \$2.4 billion in insurance premium taxes.

DIGEST:

CSHB 3 would establish a new mechanism for calculating the franchise tax and revise the base of the entities subject to the tax. The revised tax would take effect January 1, 2008.

Overview of the revised franchise tax. Under CSHB 3, the base of taxable entities subject to the revised franchise tax would include businesses in Texas that enjoy state liability protection. The bill would exclude sole proprietorships, general partnerships that were owned directly by individual persons, certain unincorporated passive entities that only receive a limited amount of income from active business, and entities such as non-profit organizations that currently are exempt from the franchise tax. Businesses with no more than \$300,000, indexed for inflation, in total revenue would be exempt from the tax, as would businesses that owed less than \$100 under the tax.

The revised tax would be computed by determining a taxable entity's total revenue. From this amount the entity could choose to deduct either its cost of goods sold or total compensation, up to \$300,000 per employee, indexed to inflation. If the entity's margin after making its deduction was greater than 70 percent of its total revenue, the business would be taxed on only 70 percent of its total revenue. The business then would apportion to Texas the amount of revenue from business done in this state and would subtract any other allowable deductions to determine the entity's taxable margin.

Once the business's taxable margin had been determined, a rate of 1 percent would be applied to that margin for all taxable entities that were not engaged in retail or wholesale trade. For a taxable entity that was engaged primarily in retail or wholesale trade, a rate of 0.5 percent would be applied to the entity's taxable margin.

Taxable entities. CSHB 3 would define "taxable entity" as a partnership, corporation, banking corporation, savings and loan corporation, limited liability company, business trust, professional association, joint venture, joint stock company, holding company, or other legal entity. The definition of taxable entity would not include:

- a sole proprietorship;
- a non-corporate general partnership (i.e., a partnership directly owned by one or more individuals); or
- a passive entity.

The definition of taxable entity also would exclude an entity currently exempt from the existing franchise tax. This would include insurance companies required to pay insurance premium taxes, non-profit corporations, cooperatives, and credit unions. In addition, the definition of taxable entity would exclude an entity that was not a corporation but that would qualify for exemption under current law if it were a corporation, such as a nonprofit organization.

A taxable entity would not be subject to the new tax if it owed less than \$100 under the tax or if the entity's total revenue was less than or equal to \$300,000. On January 1 of each odd-numbered year beginning in 2009, this \$300,000 threshold would be recalculated based on the percent change in the consumer price index during the preceding fiscal biennium, and the resulting amount would be rounded to the nearest \$10,000.

Exemption for passive entities. Passive entities would be exempt from the new franchise tax. The bill would define "passive entity" as an entity that was a general or limited partnership or trust, other than a business trust, at least 90 percent of whose income came from investments, excluding rent or income received from mineral properties that were under a joint operating agreement in which a member of the group was the operator under that agreement. No more than 10 percent of the passive entity's federal gross income could come from active business. A royalty interest or non-operating working interest in a mineral right would not be considered "active business." Compensation payment to individuals for financial and legal services that were necessary for the entity's operation also would not constitute active business.

The bill would establish a test to determine whether an entity was conducting active business. Under the test, a business would be considered to have conducted active business if the entity's activities included operations that earned income and if the entity performed active management and operational functions. Activities performed for the entity by an individual such as an independent contractor would be considered activities performed by the entity if the individual performed services that constituted some part of the entity's business. If an entity used its assets in

the business of a related entity, then that activity would be considered active business.

Definition of total revenue. A taxable entity's tax liability under CSHB 3 would be determined by computing the entity's "taxable margin." An entity's "total revenue" would be the base from which the entity's taxable margin was calculated. Upon determining an entity's total revenue, the entity would deduct either cost of goods sold or compensation to determine its taxable margin.

For a corporation, partnership, or other taxable entity, total revenue would be the sum of gross receipts and other income such as dividends, interest, rents, royalties, and capital gain income. From this amount, the entity would subtract items such as bad debt, foreign royalties and dividends, deductions allowed by the Internal Revenue Service, and distributive income from partnerships, limited liability corporations, and "S" corporations, and certain other amounts.

If a taxable entity had an interest in a passive entity, that taxable entity would include its share of income from the passive entity, but only to the extent that the passive entity's net income was not generated by a separate taxable entity.

Total revenue exclusions. The bill would enumerate several expenses and "flow-through funds," or funds passed through a taxable entity to another entity, that would be excluded from the total revenue of a taxable entity. This would include specific exclusions relevant to legal services entities and staff leasing entities. A taxable entity belonging to an affiliated group could not exclude such payments if they were made to another member of that group.

An amount excluded from total revenue could not be deducted as cost of goods sold or compensation in a taxable entity's determination of its taxable margin. Dividends from federal obligations and bonds would be excluded from total revenue.

Health care deduction. Health care providers could exclude some payments from total revenue for the purposes of calculating their business tax obligation. Providers could exempt the total amount of payments from Medicaid, Medicare, the Children's Health Insurance Program (CHIP), workers' compensation, and the TRICARE military health system. In

addition, the cost of uncompensated services, at rates set by the comptroller, could be excluded from total revenue as long as audit requirements were met. Health care institutions, including hospitals, assisted living facilities, and others, could exempt 50 percent of those amounts.

Determination of taxable margin. A taxable entity's margin would be determined by deducting either cost of goods sold or compensation from the entity's total revenue. Once a year, an entity would make an election on its annual report to subtract either cost of goods sold or compensation. If the difference after deduction was less than 70 percent of the entity's total revenue, that amount would be the entity's margin. If the difference was greater or equal to 70 percent of the entity's total revenue, the entity's margin would be 70 percent of its total revenue.

Upon determining its margin, an entity would determine its "apportioned margin" by apportioning to Texas the proportion of business performed in this state, according to the bill's apportionment rules. From this amount, the entity would subtract any other allowable deductions. The result would be the entity's "taxable margin."

An entity could change its election of which deduction it chose by filing an amended annual report.

Cost of goods sold. If an entity chose the cost of goods sold deduction in determining its taxable margin, the bill would authorize deductions of all direct costs associated with the acquisition or production of goods. These would include costs for such direct expenses as labor, materials, handling costs, storage costs, equipment leasing, depreciation associated with production of the goods, research, design, equipment maintenance, geological exploration costs, taxes stemming from the cost of production, and electricity costs.

The bill also would allow for deduction of a contribution to a partnership partially owned by a taxable entity for activities that otherwise would be eligible for deduction as cost of goods sold. This provision would apply only if those costs were related to goods obtained, rather than sold, by the taxable entity. Various other costs also would be deductible, including deterioration and obsolescence of goods, certain preproduction costs, insurance costs related to the goods, utility costs used in production of the goods, quality control costs, and licensing costs. The bill would specify

several costs that could not be included in cost of goods sold, including officer compensation.

Indirect and administrative overhead costs could be subtracted if the costs were allocated to the production of the goods. Such deductions could not exceed 4 percent of the entity's total indirect and administrative overhead costs. A lending institution could deduct interest expenses as cost of goods sold.

Compensation deduction. If an entity chose the compensation deduction in determining its taxable margin, the bill would authorize the deduction of wages and cash compensation and benefits for each employee of an entity.

Wages and cash compensation would include the amount entered in the Medicare wages and tips box on an employees' W-2 tax form, as well as net distributive income accruing to a natural person from partnerships, trusts, limited liability corporations, and "S" corporations. Stock awards and options also would qualify for deduction as wages and cash compensation. An entity could deduct no more than \$300,000 in wages and cash compensation per employee. On January 1 of each odd-numbered year beginning in 2009, the \$300,000 cap on the wages and cash compensation deduction would be adjusted based on the percent change in the consumer price index during the preceding fiscal biennium, and the resulting amount would be rounded to the nearest \$10,000.

In addition to the wages and cash compensation deduction, an entity could deduct all benefits provided to its employees, including workers' compensation, health care, and retirement benefits. The benefits deduction would not be subject to the \$300,000 cap.

Calculation of tax. Under the bill, the revised franchise tax would be computed by applying one of two rates to a taxable entity's taxable margin, depending on the type of business activity in which the taxable entity primarily was engaged. If a taxable entity primarily was engaged in retail or wholesale trade, a rate of 0.5 percent would be applied to the entity's taxable margin. If the entity was not engaged primarily in retail or wholesale trade, a rate of 1 percent would be applied to the entity's taxable margin.

An entity primarily would be engaged in retail or wholesale trade if:

- the total revenue from its retail and wholesale trade activities was greater than its total revenue from other activities;
- less than 50 percent of its total revenue in retail or wholesale trade came from the sale of products it produced (excluding eating and drinking establishments); and
- the entity did not provide utilities, including telecommunications, electricity, or gas.

Combined reporting. Under CSHB 3, a group of two or more taxable entities would have to report as a single entity if the entities were part of an affiliated group as defined by a common ownership test and were engaged in a unitary business. The combined group would determine its total revenue and elect to deduct either cost of goods sold or compensation to establish the group's taxable margin.

Apportionment. A taxable entity's proportion of business performed in Texas would be apportioned to the state to determine the entity's tax liability. The taxable entity's margin would be apportioned to Texas by multiplying the entity's margin by the quotient of:

- the taxable entity's gross receipts from business done in Texas; divided by
- the taxable entity's gross receipts from its entire business.

A combined group would include in its gross receipts from business done in Texas the gross receipts of each taxable entity that was a member of the combined group that had nexus in Texas. In determining a combined group's total gross receipts, the combined group would include the gross receipts of each entity that was a member of the group, whether or not the member had nexus in Texas.

In apportioning margin, exclusions taken by an entity when determining the entity's total revenue could not be included in the entity's receipts in Texas or receipts from the entity's entire business. Receipts from the sale of property between one member of a combined group with nexus in Texas and another member of the combined group with nexus outside Texas would be included in the receipts of business done in Texas of the taxable entity, provided that the member that did not have nexus in Texas resold the property to a purchaser in Texas.

Penalties. The comptroller would be authorized to forfeit the right of a taxable entity to transact business in the state in the same manner that the comptroller can forfeit a corporation's corporate privileges under current law.

Transition provisions, reporting, and other provisions. A taxable entity that owed the franchise tax under the bill would have to file an initial informational report with the comptroller and an annual report containing information necessary to compute the tax on the taxable entity.

The comptroller would require an information report from each of the 1,000 entities that paid the most franchise tax in calendar year 2005 under the existing franchise tax, the 1,000 entities that had the greatest gross receipts in 2005, and the 1,000 entities with the most employees in the state in 2005. This information would be used by the comptroller to report to the governor, the lieutenant governor, and the Legislature the amount of revenue that would have been generated from the entities if the new franchise tax had been in effect on January 1, 2006. This report would be delivered by April 1, 2007.

The bill would establish provisions for the transition of existing franchise taxpayers to the new franchise tax established under the bill. Franchise tax credits existing under current law would be repealed. Certain outstanding credits eligible to be carried forward under current law could be applied to an entity's tax burden under the bill, including those under a written agreement between a taxpayer and the Department of Economic Development.

A lawsuit contending that the new franchise tax established under CSHB 3 was unconstitutional would be heard in Travis County district court. The bill specifies that the franchise tax as amended by CSHB 3 is not an income tax and federal law (Pub. L. No. 86-272) concerning state taxation of income from interstate commerce does not apply.

Revenue from the tax imposed under the bill would go into the state's general revenue fund. The bill would appropriate \$2 million in general revenue to the comptroller for fiscal 2006-07 for audit and enforcement activities.

The tax imposed under the bill would take effect January 1, 2008, and would apply to reports due on or after that date.

The bill would take effect June 1, 2006, if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2006.

**SUPPORTERS
SAY:**

CSHB 3 would replace the current franchise tax, which has become a voluntary and divisive corporate income tax, with a fairer, more broadly based business levy.

The current franchise tax no longer tracks growth in the state's economy, mainly because the burgeoning service sector uses business structures not subject to the tax. Avoidance has become commonplace, especially among large corporations that have restructured themselves as out-of-state partnerships to take advantage of the so-called "Delaware sub." Closing that loophole is made problematic by legitimate out-of-state partnerships doing business in Texas that never have paid the tax. Even if that problem were corrected, the franchise tax has other loopholes.

Rather than try to plug this leaky fiscal dike, the state should scrap the franchise tax for a reformed franchise tax based on an entity's margin — a measure of revenue that allows for the deduction of certain business costs. This would raise about \$3.4 billion in state revenue in fiscal 2008, and more than \$4 billion annually by fiscal 2011, according to the Legislative Budget Board (LBB). A broad-based, low-rate tax based on margins would track economic growth and help the state deal with inflation, providing a stable and predictable stream of revenue.

The reformed franchise tax or margins tax would balance the state's revenue needs with the cost of doing business while providing new state revenue that could be used to reduce school property taxes, which are burdensome for Texas families and economically inefficient for Texas businesses. Even though Texas would collect more revenue from businesses under the new tax, businesses would benefit from a significant reduction in property taxes. HB 2 by Pitts, also on today's calendar, would dedicate to school property tax reduction any increased revenue over current rates generated by a new broad-based business tax enacted during the third called session.

By taxing all entities that enjoy the benefit of liability protection from the state, CSHB 3 would return the franchise tax to its original intent. Since liability protection was extended to partnerships in the 1980s, many businesses have been able to reorganize to avoid the corporate franchise

tax. Although they contribute nothing to franchise tax revenues, these businesses benefit from the state's educational system and from other state services. CSHB 3 would correct this disparity by covering service-sector businesses more effectively and would track growth within the Texas economy much more accurately than does the current franchise tax. Texas has a growing population with expanding needs, and CSHB 3 presents a golden opportunity to establish a stable revenue source to pay for state services.

A business's margin as defined under CSHB 3 would be a more appropriate base for the franchise tax than the current base, which requires a firm to pay taxes on the greater of either earned surplus or taxable capital. The bill would provide businesses with a choice of deducting either cost of goods sold or compensation, a feature that would enable businesses with very different structures, expenses, and profit margins to thrive under the tax. While a manufacturing firm that produces goods for sale likely would choose to deduct the costs associated with producing those goods, a service-based business would be able to deduct its primary expense, which is employee wages. The compensation deduction would be a particularly desirable aspect of the reformed franchise tax because a business could reduce its tax liability by offering higher salaries, hiring more employees, and expanding health care benefits.

By imposing a lower tax rate of 0.5 percent on retailers and wholesalers, CSHB 3 would take into account the smaller profit margins under which these firms typically operate. While a retailer or wholesaler may collect a large amount of total revenue relative to other entities, only a small percentage of that amount may actually be profit. Since the tax under the bill would use total revenue as part of its base, it would be appropriate to tax firms with historically smaller margins at a lower rate, and doing so would bring the tax liability of those firms into line with other sectors.

The bill would use a widely accepted definition of total revenue based on federal corporate and partnership income tax definitions while excluding foreign income and revenue that already had been taxed elsewhere. These provisions are necessary to avoid the double taxation of some types of receipts. The bill's combined reporting provisions would ensure that entities were not double-taxed on joint assets and also would prevent entities from reorganizing into untaxed structures similar to those that exist under the current franchise tax.

The only tax that would allow a firm to escape taxation when it took a loss would be a tax on profit. Due to the constitutional prohibition against taxation of income, a business tax on the profits of partnerships would be unconstitutional without approval by the voters in a statewide referendum. Thus, the state must choose between taxing partnerships or profit, because it cannot do both. The choice of deducting cost of goods sold or compensation provided to a taxable entity would establish the entity's taxable margin, a concept that is entirely dissimilar to gross receipts.

CSHB 3 would establish the most fair and equitable business tax under the limitations provided by the Texas Constitution. By excluding sole proprietorships, the bill would avoid conflict with the constitutional prohibition against an income tax. The attorney general has indicated that this plan would not constitute an income tax and likely would be upheld in court.

The bill would provide a reasonable 70 percent limit on the amount of a business's total revenue that would be subject to taxation. This limit would be fair to a business whose cost of goods sold or compensation deduction did not provide a meaningful limitation on the business's taxable margin. In addition, a generous small business exemption in the bill would allow a business with less than \$300,000 in total revenue to remain exempt from taxation. This exemption would be twice the exemption under the current franchise tax and would be indexed to inflation.

The bill would retain Texas' favorable rules for apportionment of revenue. Under these provisions, Texas isolates and taxes in a straightforward manner business activity done only within the state, an approach favored by many firms that operate in multiple states.

The bill would eliminate the unfair "throwback rule," under which sales of items shipped from a corporation doing business in Texas to a state in which the corporation is not subject to taxation are "thrown back" to Texas and taxed under the franchise tax. Corporations can avoid taxation by locating in a state without a throwback rule and delivering their goods to Texas, escaping taxation in both Texas and the origination state. Repealing the throwback rule would allow Texas to provide an incentive for corporations to locate in the state.

The credit for providers of health care services under the state and federally funded programs would serve an important policy goal of

encouraging provider participation in these programs. While for-profit health care providers should be required to pay the new tax, the state also should recognize that compensation rates for government-funded programs are very low. Medicaid and Medicare, for example, pay providers between 40 percent and 60 percent of the reimbursement paid by commercial plans. Thus, the bill would ensure that providers who take these partially funded cases would not be taxed excessively. The offset of uncompensated care costs also would encourage health care providers and institutions to continue to serve as a vital part of the Texas safety net, which is very important considering that 25 percent of the state's population is uninsured.

**OPPONENTS
SAY:**

CSHB 3 would launch an unprecedented and untested business tax scheme in Texas that is unlike any other in the nation, with unknown economic and legal consequences for the state. By bringing in thousands of firms that currently have no tax liability, the bill could cause a substantial disruption in the state's economy, potentially undermining the impressive growth in revenue that the sales tax and existing franchise tax have yielded in the last year. Lawsuits challenging the tax would be inevitable, and the resulting legal process could throw the state's revenue system into question. With all of the uncertainties facing the Texas economy and school finance system, now simply is not the time to adopt a radically revised business tax.

With more than \$3 billion in surplus revenue available, it is precisely the wrong time to embark on a risky and massive expansion of the business tax. All taxes have economic consequences, and all business taxes ultimately are passed on to consumers in the form of higher prices and lower wages. According to the LBB, CSHB 3 would represent an increase of close to 50 percent in fiscal 2008-09 over revenues that would have been collected under the existing franchise tax. While some businesses would profit from a reduction in property tax liability, many businesses undoubtedly would be worse off under the proposed system. Rather than expanding business taxes to pay for a reduction in school property taxes, the Legislature should expend the balance of the state surplus on property tax reduction and reduce spending on state services to eliminate over-taxation in the future.

By using total revenue as the base in calculating the tax, the revised franchise tax under CSHB 3 essentially would be a modified gross receipts tax — an unfair tax that does not take into account a taxpayer's ability to

pay. Even if a business lost money, that entity's taxable margin would be based on the total revenue of the business. Although a business could deduct either cost of goods sold or compensation, there would be no guarantee that the taxable liability of the entity reasonably was related to an entity's income. It is possible that an entity that lost money in a given year still could be forced to pay tax to the state.

Even if the Legislature significantly reduced school property taxes, CSHB 3 likely would represent a substantial increase in the tax liability of private industry in Texas and would mark a shift in the tax burden from individuals to businesses. The Comptroller's Office has estimated that the revised franchise tax on average would translate to a levy of 7 percent of business net income. This rate would be substantially higher than the 4.5 percent rate on earned surplus under the existing franchise tax, and the tax would allow for too few deductions. Every industry is unique, and many forms of business have specific costs and assets that might not work under the broad outlines contained in this bill.

Offering an exclusion for all government-funded health care programs would fail to recognize that rates for the same service may vary widely among programs and that some providers may be compensated at near market rates. For example, TRICARE may pay more for a service than Medicaid. A better way to encourage participation in government-funded programs would be to adequately reimburse for services in programs under the state's control, such as Medicaid, CHIP, and workers' compensation.

**OTHER
OPPONENTS
SAY:**

A broad-based business tax should apply to all businesses, regardless of the manner in which they choose to organize. Many sole proprietorships and partnerships that generate a great deal of business would remain untaxed under CSHB 3. Leaving some organizations untaxed would create an incentive for businesses to reorganize into untaxed entities. In addition, the state would be forgoing a substantial amount of revenue by excluding passive entities from taxation. These entities should be taxed as well, although perhaps at a lower rate.

Certain service-sector business such as law firms have almost no cost of goods sold as defined under the bill and would be left with no choice other than the compensation deduction. Because compensation would be capped at \$300,000, the taxable margin of many of these firms would be higher than the average margin on which other businesses were taxed. For

service-sector professions that fall into this category, additional deductions should be authorized, such as a higher cap on the compensation deduction or an allowance for such expenses as rent, utilities, or employer Social Security contributions.

Not all retailers operate under small profit margins, and it would be inappropriate to group them all together and allow them to be taxed at half the rate of other businesses. The bill should provide some test or further refinement of the definition of retailers and wholesalers who would be eligible to apply the 0.5 percent tax rate to the taxable margin. For the sake of equity, the bill should make an allowance for firms whose revenue structures more closely resemble those of firms taxed at the rate of 1 percent.

Under Article VIII, Sec. 24(a) of the Texas Constitution, no law enacted by the Legislature could impose a tax on a person's net income, including a person's share of partnership and unincorporated association income, unless a majority of Texas voters approved such a tax in a statewide referendum. CSHB 3 likely would run afoul of this prohibition, given that revenue from unincorporated partnerships would be taxed under the bill. Because a tax would be levied on the margins of unincorporated partnerships from which the income of individuals was derived, a court could find the revised franchise tax under CSHB 3 to be in violation of the personal income tax prohibition.

If health care providers are to be granted a tax credit for the cost of uncompensated care under CSHB 3, it only would be fair to offer a similar credit to attorneys who provide pro bono legal services. Just as the health care credit would encourage participation in state and federal health care programs, a credit for attorneys would create an incentive for lawyers to provide vital free and reduced cost legal services to low-income Texans.

NOTES:

According to the Legislative Budget Board, CSHB 3 would cost the state \$2 million in general revenue-related funds in fiscal 2007 due to an appropriation to the comptroller for the performance of audit and enforcement activities. In fiscal 2008-09 the bill would result in a net increase of \$6.95 billion in general revenue-related funds.

HB 3 as introduced would not have allowed deductions for health care providers of payments from state and federal health care programs and costs of uncompensated care. The committee substitute also made limited

changes to sections dealing with passive entities, cost of goods sold, wages and cash compensation, and apportionment.

On April 21, the House adopted a Calendars Committee rule requiring all amendments to HB 3 be filed by 5 p.m. Saturday and their fiscal impact be determined by the LBB with assistance from the Comptroller's Office.

Unofficial copy Travis Co. District Clerk Velda L. Price

LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 79TH LEGISLATURE 3rd CALLED SESSION - 2006

April 27, 2006

TO: Honorable Steve Ogden, Chair, Senate Committee on Finance

FROM: John S. O'Brien, Deputy Director, Legislative Budget Board

IN RE: HB3 by Keffer, Jim (Relating to certain taxes affecting businesses; making an appropriation; providing penalties.), **As Engrossed**

Estimated Two-year Net Impact to General Revenue Related Funds for HB3, As Engrossed: a negative impact of (\$2,000,000) through the biennium ending August 31, 2007.
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Appropriations:

Fiscal Year	Appropriation out of GENERAL REVENUE FUND 1
2006	\$0
2007	\$2,000,000

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2007	(\$2,000,000)
2008	\$3,382,899,421
2009	\$3,450,189,314
2010	\$3,717,381,314
2011	\$3,964,526,877

All Funds, Five-Year Impact:

Fiscal Year	Probable Revenue Gain/ (Loss) from GENERAL REVENUE FUND 1	Probable Savings/(Cost) from GENERAL REVENUE FUND 1	Change in Number of State Employees from FY 2006
2007	\$0	(\$2,000,000)	22.3
2008	\$3,386,651,000	(\$3,751,579)	55.8
2009	\$3,453,870,000	(\$3,680,686)	55.8
2010	\$3,721,062,000	(\$3,680,686)	55.8
2011	\$3,967,725,000	(\$3,198,123)	55.8

Fiscal Analysis

The bill would amend Chapter 171 of the Tax Code to modify the franchise tax rate and base. The bill would also amend Chapter 21.02 and Chapter 313 of the Tax Code. In addition, the bill would make an appropriation.

EXHIBIT 6527

The bill would extend tax responsibility to certain types of partnerships and other business entities that are not currently subject to the tax. However, sole proprietorships and general partnerships directly owned by natural persons only would remain exempt from the tax. In addition, the term "taxable entity" would exclude businesses meeting the bill's definition of a passive entity or those currently exempt under Subchapter B of Chapter 171. An entity currently subject to the franchise tax that would become exempt under this bill because it is a passive entity would not owe the additional tax imposed by Section 171.0011. A taxable entity with total gross receipts of less than \$300,000, or an annual tax liability of less than \$1,000, would owe no tax.

The bill would replace the current franchise tax base of taxable capital and taxable earned surplus with a new base, called "taxable margin." To arrive at its taxable margin, a firm would first have to calculate its "total margin" as the minimum of three values: 1) 70 percent of total revenue, 2) total revenue minus cost of goods sold, and 3) total revenue minus total compensation and benefits. "Taxable margin" would be total margin apportioned to Texas using a gross receipts ratio similar to the current franchise tax plus any margin allocated to this state.

The tax rate on taxable margin would be 1.0 percent for taxable entities not primarily engaged in wholesale or retail trade, as defined in the bill. For taxable entities primarily engaged in wholesale or retail trade, the tax rate would be 0.5 percent. Voter approval would be required for a rate increase subsequent to enactment.

Taxable entities that qualified as "health care providers," other than "health care institutions" under this bill would be allowed to deduct from total revenue all payments received from certain health insurance programs, plus their actual costs of uncompensated care. Those taxable entities that qualified as "health care institutions" under the bill would be allowed to deduct 50 percent of their payments from qualifying health insurance program payments and uncompensated care costs. The health insurance program payments that could be deducted would include those from Medicare, Medicaid, the Indigent Health program, the Children's Health Insurance Program, workers' compensation, and the TRICARE military system.

The bill contains a section, titled "Determination of Cost of Goods Sold", with definitions of certain terms, including "goods," "production," and "tangible personal property." This section would identify certain costs that would be included in the cost of goods sold, and other costs that would not be included in cost of goods sold.

The bill contains a section, titled "Determination of Compensation," defining "wages and cash compensation" to include net distributive income from certain types of entities distributed to natural persons and stock awards expensed for federal income tax purposes and stock options exercised during the tax year. A taxable entity electing to deduct compensation would be allowed to deduct wages and cash compensation and the cost of all benefits provided to employees, officers, and owners, to the extent deductible for federal income tax purposes. The amount of compensation that could be deducted for any person could not exceed \$300,000.

The bill would instruct the Comptroller to use the consumer price index to adjust the \$300,000 limits for compensation deductions and gross receipts taxability at the beginning of each odd-numbered year, beginning in 2002.

The bill would alter the manner in which certain members of an affiliated group must report franchise tax. Under current law, all taxable entities report on a stand-alone basis, with no combining of revenue or expenses with other taxable entities. Under this bill, a group of two or more taxpayers would have to report as a single taxable entity if two conditions applied: 1) the entities were in an affiliated group defined by a common ownership test, and 2) the entities were engaged in a unitary business, as defined in the bill. The bill specifies the methods such a taxable entity would employ to calculate total revenue, cost of goods sold, and total compensation. The bill would allow a combined group to include an exempt entity in the group report if the entity would have been in the combined group were it not exempt.

The apportionment of taxable margin for a combined group would include in the factor for gross receipts in Texas the gross receipts of each entity that was a member of the group and that had nexus

with Texas. The factor for gross receipts everywhere would include the gross receipts of all members of the combined group without regard for whether the entity had nexus with Texas. In addition, transactions among members of the combined group eliminated in the calculation of total revenue, cost of goods sold, and compensation would be eliminated from the numerator and denominator of the apportionment ratio. An exception to the exclusion of receipts from transactions among members of the combined group would occur if the transaction involved tangible personal property and one party to the transaction had nexus with Texas, but the other party did not have nexus.

The bill would transition existing franchise taxpayers to the new base and tax rates beginning with the franchise tax report due in May 2008. A taxpayer's liability would be based on the taxpayer's taxable margin during the accounting year that ended in calendar 2007.

Taxpayers becoming subject to the franchise tax because of this bill would have to file an initial information report. Such an entity doing business in Texas before January 1, 2008, would have to file an annual report on May 15, 2008, based on a period specified in the bill.

Taxpayers subject to the franchise tax in its current form at any time after December 31, 2006, but not subject to the franchise tax on January 1, 2008, would have to file a final report based on a period specified in the bill.

The franchise tax credits existing under current law would be repealed. Franchise tax credits that had been earned but not used by the effective date of the bill could be used to reduce franchise tax liability after the effective date if the credits earned had carry-forward provisions in existing law and the carry-forward period were still open for the taxpayer who earned the credits.

The bill would create a temporary credit on taxable margin. The credit would be based on a taxable entity's net operating loss carryforward calculated at the end of the entity's accounting year in 2006. Ten percent of the apportioned net operating loss could be used by the taxable entity to offset taxable margin. The credit could not be conveyed, assigned, or transferred in relation to a transaction in which the taxable entity is purchased by another entity. The credit provision would expire September 1, 2026.

The bill would require a taxable entity that has more than 100,000 employees in Texas to file an additional public information report stating the number of the entity's employees in this state that receive assistance for the employee or the employee's family under the Children's Health Insurance Program or the Medicaid Program.

The bill would direct the Comptroller to require specified entities to file an information report by February 15, 2007, with no possibility of extension. The information report would contain the information the entity would have provided on its 2006 report if the provisions of this bill had been in effect for the period covered by the 2006 report. The information report would also have to contain the total amount of school maintenance and operations school property taxes paid by the entity to school districts in Texas in the 2005, 2006, and 2007 tax years. The entities that would have to file the information report would include: the 1,000 entities with the largest franchise tax liability for the reporting period ending December 31, 2005; the 1,000 entities doing business in this state with the largest amount of total gross receipts; the 1,000 entities doing business in this state with the greatest number of employees; and the 1,000 entities doing business in this state with greatest school maintenance-and-operations tax levy in this state for 2005.

The bill would provide exclusive and original jurisdiction to the Supreme Court for a challenge to the constitutionality of the bill's provisions.

The bill would appropriate \$2 million to the Comptroller's Office for the biennium ending August 31, 2007, for implementation of this bill and for audit and enforcement purposes.

The bill would amend Chapter 21.02 of the Tax Code to specify the taxable situs of a portable drilling rig.

The bill would amend Chapter 313 of the Tax Code to direct the Texas Education Agency to conduct an economic impact evaluation of an application for limitation of value if requested by a school

district that had received such an application, allow certain school districts to retain rural designations, and specify use of regional weekly wage data for certain school districts in the evaluation of an application.

The bill would take effect January 1, 2008; and its provisions would apply to reports due on or after that date. The sections of the bill relating to information reports, the venue of a law suit, and the appropriation of funds to the Comptroller would take effect June 1, 2006, if the bill received two-thirds votes of all members in each house. Otherwise, those sections would take effect September 1, 2006.

Methodology

The estimate was based on data from the Internal Revenue Service's Statistics of Income publications, the U.S. Census Bureau, and information in the Comptroller's franchise tax data files.

The administrative cost estimate for fiscal 2007 reflects the funds that would be necessary for initial implementation of this bill and for audit and enforcement purposes. The estimates for the subsequent years reflect the funds that would be necessary to handle the additional workload due to the expansion of the tax base.

It is anticipated that the overall fiscal impact on the Secretary of State (SOS) will be minimal. Although a reduction in the number of Public Information Report transactions processed annually will result in some savings to the SOS each year the bill is in effect, these savings will be offset by the additional costs incurred by the anticipated increase in the number of involuntary termination/revocation transactions that will be required of the SOS each year the bill is in effect.

The bill would create additional workload demands on the Office of Attorney General's (OAG) Taxation division because it changes the franchise tax base and imposes the new tax on most business entities. The current franchise tax is imposed only on corporations and limited liability companies.

The future case load resulting from the passage of this legislation is unknown and difficult to predict. The OAG anticipates any additional legal work in 2006 resulting from the passage of this bill could be reasonably absorbed with current resources. However, the OAG may request additional resources for 2007-2010 through the regular budget process as workload trends mature as a result of the passage of this bill.

This analysis assumes the bill will be effective 90 days after passage.

Technology

There would be a technology cost to the Comptroller's Office of \$786,554 in fiscal 2007 for programming changes and computer costs. In fiscal 2008, \$709,773; fiscal 2009-10, \$707,273; and fiscal 2011, \$224,726 would be necessary for computer costs.

Local Government Impact

No fiscal implication to units of local government is anticipated.

Source Agencies: 304 Comptroller of Public Accounts

LBB Staff: JOB, SD, SM

LEGISLATIVE BUDGET BOARD
Austin, Texas

TAX/FEE EQUITY NOTE

79TH LEGISLATURE 3rd CALLED SESSION - 2006

April 27, 2006

TO: Honorable Steve Ogden, Chair, Senate Committee on Finance

FROM: John S. O'Brien, Deputy Director, Legislative Budget Board

IN RE: **HB3** by Keffer, Jim (Relating to certain taxes affecting businesses; making an appropriation; providing penalties.), **As Engrossed**

Table 1
House Bill 3, As Engrossed: Summary of Elements

This analysis is for taxes effective in fiscal 2008.

Revenue Changes

- Replace the franchise tax with a margins tax.

Dollar Value of Revenue Changes in Fiscal 2008

- \$3,386.7 million business tax increase
- \$3,386.7 million net tax increase

Initial Impact in Fiscal 2008

- A net increase to business of \$3,386.7 million
- A net increase to households of \$0.0 million

Major Industry Initial Impact in Fiscal 2008

- The largest dollar decrease: \$22.1 to the Mining industry
- The largest percentage decrease: 0.5 percent to the Mining industry
- The largest dollar increase: \$1,133.6 to the All Other Services industry
- The largest percentage increase: 18.7 percent to the All Other Services industry

Final Incidence of Changes Effective in Fiscal 2008

EXHIBIT
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- Lowest income level (income range from \$0 to \$14,042):
An increase of \$67.8 million, or 3.15 percent.
- Middle income level (income range from \$43,403 to \$53,968):
An increase of \$168.6 million, or 3.85 percent.
- Highest income level (income range from \$146,804 and above):
An increase of \$651.9 million, or 4.25 percent.

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Initial Tax Impact by Industry:

House Bill 3, As Engrossed, was analyzed using the LBB's multi-tax model to determine the initial impact of the proposed changes relative to current state and local tax law. The results of the analysis are shown in Table 2 below.

Table 2
Comparison of Initial Tax Impact under
Current Law vs. House Bill 3, As Engrossed
Fiscal Year 2008

Comparisons Include Property Tax, Sales and Excise Taxes and Taxes on Business

	Gross State Product: Shares	Current Law Liability	Percent of Total	Proposed Law Liability	Percent of Total	Change in Liability	Percent of Total	Percent Change in Liability
	[%]	[\$ Million]	[%]	[\$ Million]	[%]	[\$ Million]	[%]	[%]
Taxes Paid by Business:								
Agriculture, Forestry & Fishing	0.8	774.6	2.1	872.9	2.1	98.3	2.9	12.69
Mining	6.7	4,821.1	12.8	4,799.0	11.7	-22.1	-0.7	-0.46
Utilities & Transportation	7.3	4,613.8	12.2	4,878.8	11.9	265.0	7.8	5.74
Construction	5.1	1,188.4	3.1	1,379.7	3.4	191.3	5.6	16.10
Manufacturing	13.0	5,212.4	13.8	6,128.6	14.9	916.2	27.1	17.58
Wholesale & Retail Trade	15.8	3,279.8	8.7	3,416.1	8.3	136.3	4.0	4.16
Information	5.1	3,103.9	8.2	3,611.9	8.8	508.0	15.0	16.37
Finance, Insurance & Real Estate	19.7	8,695.7	23.0	8,855.8	21.5	160.1	4.7	1.84
All Other Services	26.5	6,069.2	16.1	7,202.8	17.5	1,133.6	33.5	18.68
Total Taxes on Business:	100.0	37,958.9	100.0	41,145.6	100.0	3,386.7	100.0	8.97
Taxes Paid by Households:								
Residential Owner-Occupied		18,814.1		18,814.1		0.0		0.00
Personal Consumption		18,872.3		18,872.3		0.0		0.00
Total Taxes on Households:		37,686.4		37,686.4		0.0		0.00
Total Taxes								
		75,445.3		78,832.0		3,386.7		4.49

Tax Incidence by Income Group

Economists commonly distinguish between the initial "impact" of a tax and its "incidence." The initial impact of a tax falls on taxpayers legally liable to pay the tax, while the incidence refers to the ultimate payer of the tax. For example, the initial impact of a business tax falls on the firm incurring the tax liability. Over time, to varying degrees, the tax cost is "shifted" so that the ultimate burden of the tax falls either to consumers in different retail prices, to employees in changed wages, to owners of land and capital in different investment returns, or most likely, to some combination of all three. The degree to which a tax can be shifted, and the amount of time that elapses before a tax can be shifted, depend on the type of tax and the competitiveness of capital, labor, input material and product markets.

The results of this analysis for tax law changes effective with this proposal are shown in Table 3 and Table 4.

Table 3
Tax Incidence by Income Decile
Current Law vs. House Bill 3, As Engrossed
Taxes Effective in Fiscal Year 2008

Comparisons Include Property Tax, Sales and Excise Taxes and Taxes on Business

Decile	Decile Income: Lower Bound	Decile Income: Upper Bound	Current Law Tax	Percent of Total	Proposed Law Tax	Percent of Total	Change in Tax	Percent Change in Tax
	[\$]	[\$]	[\$ Million]	[%]	[\$ Million]	[%]	[\$ Million]	[%]
1	0	14,042	2,153.2	3.6	2,221.1	3.6	67.8	3.15
2	14,042	23,872	2,485.7	4.2	2,580.0	4.2	94.3	3.79
3	23,872	33,190	3,217.2	5.4	3,337.7	5.4	120.5	3.75
4	33,190	43,403	3,552.4	6.0	3,682.7	6.0	130.3	3.67
5	43,403	53,968	4,375.1	7.4	4,544.2	7.4	168.6	3.85
6	53,968	67,019	5,112.2	8.6	5,301.5	8.6	189.3	3.70
7	67,019	82,976	6,151.9	10.4	6,392.7	10.4	240.8	3.91
8	82,976	104,865	7,470.7	12.6	7,759.6	12.6	288.9	3.87
9	104,865	146,804	9,292.5	15.7	9,650.5	15.7	358.0	3.85
10	146,804	and above	15,336.0	25.9	15,987.9	26.0	651.9	4.25
		Total:	59,147.3	100.0	61,457.8	100.0	2,310.4	3.91

Summary of Tax Incidence Findings

House Bill 3, As Engrossed, would ultimately increase the taxes of all households by \$2,310.4 million for tax law changes effective in 2008. The difference between the initial increase in revenue of \$3,386.7 million in fiscal 2008 and the ultimate increase of \$2,310.4 million in tax incidence is primarily due to the exporting of some of the tax changes to non-Texas consumers and businesses, changes in federal tax liability, and the absorption of some of the tax changes by business profits, some of which are received by non-Texas shareholders and business owners.

Table 4
Effective Tax Rate by Income Decile
Current Law vs. House Bill 3, As Engrossed
Taxes Effective in Fiscal Year 2008

Comparisons Include Property Tax, Sales and Excise Taxes and Taxes on Business

Decile	Decile Income: Lower Bound	Decile Income: Upper Bound	Current Law Effective Rate	Proposed Law Effective Rate	Change in Effective Rate	Percent Change in Effective Rate
	[\$]	[\$]	[%]	[%]	[%]	[%]
1	0	14,042	32.76	33.79	1.03	3.15
2	14,042	23,872	15.40	15.99	0.58	3.79
3	23,872	33,190	13.01	13.50	0.49	3.75
4	33,190	43,403	11.14	11.55	0.41	3.67
5	43,403	53,968	10.07	10.45	0.39	3.85
6	53,968	67,019	9.76	10.12	0.36	3.70
7	67,019	82,976	9.49	9.86	0.37	3.91
8	82,976	104,865	9.24	9.60	0.36	3.87
9	104,865	146,804	8.71	9.04	0.34	3.85
10	146,804	and above	6.87	7.16	0.29	4.25
		Total:	9.09	9.44	0.36	3.91

Summary of Effective Rate Findings

House Bill 3, As Engrossed, would ultimately increase the effective rate for all households by 3.91 percent for taxes effective in fiscal year 2008. The effective tax rate is the aggregate amount of tax in a given income class divided by the aggregate amount of personal income in that class.

Source Agencies:

LBB Staff: JOB, SD, SM

Legislative Session: 79(3)**EXHIBIT****6529****House Bill 3 (3rd C.S.)****Effective:** See below**House Author:** Keffer, Jim et al.**Senate Sponsor:** Ogden et al.

House Bill 3 amends provisions of the Tax Code to broaden the base of businesses that are subject to the state franchise tax and to restructure the tax. Under the restructuring, taxable entities include partnerships, corporations, banking corporations, savings and loan associations, limited liability companies, business trusts, professional associations, business associations, certain joint ventures, joint stock companies, holding companies, and other legal entities, including combined groups. Entities not subject to the franchise tax include, among others, sole proprietorships, general partnerships directly owned by individual persons, certain grantor trusts, escrows, real estate investment trusts, real estate mortgage investment conduits, and certain passive entities that receive only a limited amount of income from the conduct of an active business. In addition, an entity that is not a corporation but that, because of its activities, would be exempted under the franchise tax as it existed before the restructuring is also exempt under the restructured tax, including insurance companies required to pay insurance premium taxes, nonprofit corporations, cooperatives, and credit unions, among others. However, House Bill 3 does subject certain insurance companies to the franchise tax for the tax year any portion of which the entity is in violation of final orders issued by the Texas Department of Insurance in relation to excessive or discriminatory rate practices.

Before changes to Chapter 171, Tax Code, enacted in House Bill 3, the franchise tax was based on a corporation's net taxable capital (taxed at a rate of 0.25 percent) or an entity's net earned surplus (taxed at a rate of 4.5 percent). Under House Bill 3, the franchise tax is paid on an entity's "taxable margin," which is computed using as a base an entity's "total revenue." Total revenue is generally the business's gross receipts and other income minus items such as bad debt, foreign royalties and dividends, federal income tax deductions, and distributive income from certain entities. In addition, House Bill 3 lists a number of expenses and "flow-through funds" (funds that pass through the taxable entity to another entity) that are excluded from the computation of total revenue. Such expenses and flow-through funds include, but are not limited to, taxes collected from a third party to be remitted to a taxing authority; principal repayment of loans collected by lending institutions; certain amounts relating to legal services, including damages due to a legal claimant, reimbursement for expenses incurred specific to the prosecution of a claimant's matter, and up to \$500 of actual out-of-pocket expenses per pro bono case; certain amounts relating to staff leasing services, including payments received from a client company for wages, payroll taxes, and employee and workers' compensation benefits for the assigned employees of the client company; and certain health care provider costs and compensation, including payments received under the Medicaid program, Medicare program, Indigent Health Care and Treatment Act, Children's Health Insurance Program (CHIP), TRICARE military health system, and certain workers' compensation claims, as well as the actual cost of any uncompensated care. If the health care provider is a health care institution, the exclusion for provider payments and uncompensated care is limited to 50 percent of payments received or of the value of the care given.

Under the restructured franchise tax, for an entity to arrive at its taxable margin, the entity calculates its total "margin" as the lesser of three values: (1) 70 percent of total revenue; (2) total revenue minus costs of goods sold; and (3) total revenue minus total compensation and benefits. The bill also includes certain deductions for costs and compensation associated with persons called to active military duty. The entity makes an annual choice to deduct from its total revenue either its costs of goods sold or its total compensation. The bill specifies criteria used to determine the entity's costs of goods sold (basically all direct costs of acquiring or producing goods) and its total compensation (basically wages, cash compensation, and workers' compensation, health care, and retirement benefits), with total compensation limited to \$300,000 (indexed for inflation) per employee. On determining its total margin, an entity then determines its "apportioned margin" by allocating to Texas the proportion of business performed in the state. From that amount, the entity subtracts any other allowable deductions to determine the entity's "taxable margin," i.e., the amount on which the entity is taxed. In addition, the bill sets out specific reporting requirements in determining taxable margin for affiliated groups engaged in unitary business and for certain tiered partnership arrangements.

House Bill 3 includes a two-tiered tax rate. A taxable entity engaged primarily in retail or wholesale trade pays, on its taxable margin, the franchise tax at a rate of 0.5 percent. All other taxable entities pay at a rate of 1.0 percent. The bill sets out criteria for determining whether a business is engaged primarily in retail or wholesale

trade. Any increase in the rates must be approved by a majority of the registered voters voting in a statewide referendum. No election is required for a decrease in the rates.

House Bill 3 exempts from the franchise tax those businesses that have no more than \$300,000 (indexed for inflation) in total revenue or that owe less than \$1,000 in franchise taxes.

For a taxable entity with more than 100,000 employees in Texas, the bill requires the entity to file an annual report with the comptroller stating the number of its Texas employees or the employees' family members that receive CHIP or Medicaid benefits.

For enforcement purposes, the comptroller is authorized to forfeit the right of a taxable entity to transact business in the state in the same manner the comptroller is authorized to forfeit a corporation's corporate privileges in the state.

House Bill 3 amends the procedure under the Texas Economic Development Act by which a school district may consider an application for a limitation on appraised value to require the Texas Education Agency to conduct an economic impact evaluation on the proposed limitation rather than allowing the district itself to hire a third party to perform the evaluation. The evaluation is binding on the district and the applicant.

House Bill 3 requires the comptroller to identify and obtain an information report from each of the 1,000 entities that paid or were required to pay the most franchise tax in calendar year 2005, the 1,000 entities that had the greatest amount of gross receipts in 2005, the 1,000 entities with the most employees in the state in 2005, and the 1,000 entities with the greatest school maintenance and operations (M&O) property tax levy in 2005. From the information, the comptroller must report to state leadership by April 1, 2007, and April 1, 2008, the amount of franchise tax revenue that would have been generated from the entities if the restructured franchise tax had been in effect on January 1, 2006, and the M&O property taxes paid by the entities in the 2005, 2006, and 2007 tax years. The provisions described by this paragraph take effect September 1, 2006.

House Bill 3 stipulates that the restructured franchise tax is not an income tax and that the federal law concerning state taxation of income from interstate commerce does not apply.

In addition, the bill stipulates that the Supreme Court of Texas has exclusive and original jurisdiction over a challenge to the constitutionality of the bill or any provision of the bill and may issue injunctive or declaratory relief in connection with the challenge. The court is required to rule on such a challenge on or before the 120th day after the challenge is filed. The provisions described by this paragraph take effect September 1, 2006.

Except as otherwise noted, House Bill 3 takes effect January 1, 2008.

Spanish by the end of the session. With that, Mr. President, I gladly second the nomination of my very dear friend, Senator Steve Ogden, for the position of President Pro Tempore of our Texas Senate. Thank you.

The President declared that the Honorable Steve Ogden had been duly elected President Pro Tempore of the 82nd Legislature by acclamation.

The President appointed the following Committee to Escort Senator Ogden and his family to the President's Rostrum: Senators Duncan, Chair; Williams, Lucio, Hinojosa, and Shapiro.

Senator Ogden and his party were then escorted to the President's Rostrum by the committee.

OATH OF OFFICE ADMINISTERED

The President administered the Constitutional Oath of Office to Senator Ogden as follows:

I, _____, do solemnly swear, that I will faithfully execute the duties of the office of President Pro Tempore of the Senate of the State of Texas, and will to the best of my ability preserve, protect, and defend the Constitution and laws of the United States and of this state, so help me God.

ADDRESS BY PRESIDENT PRO TEMPORE

President Pro Tempore Ogden addressed the Senate as follows:

Thank you, my fellow Senators. Back on November 2, I think it was, the election day here in Texas, I woke my wife up and said, come on, Bev, get out of bed. You get to go vote for me one more time. Her response is not repeatable. But I think she did. You know, Tommy was talking about how long I've been married. Lucky man. I've been married for 37 years. Why? Well, you marry a woman because you love that woman. But there's always been something very special about my wife. She gave me confidence. It may surprise you that when I was younger, I was kind of an absent-minded, pencil-neck, awkward, geeky, jock type. Might surprise you. She didn't see it that way. And I still remember as a young man thinking how lucky and fortunate I was to have a woman of such beauty and talent to think I was something special. She gave me confidence. Because she believed in me, I believed in myself. And I've drug her all over this country. The day we got married eleven in the morning in Annapolis, Maryland, at ten o'clock at night I was in San Francisco with her. Her comment on our wedding night that she was kind of tired was true. But from the time we were first married, to nine and a half months later when she presented me with our first son, to the time I said, you know, it's time to go to sea, take care of the family, to the time I said we're going back to Texas, to the time I volunteered her to be a CPS caseworker, she's always been there at my side. She has been the wind beneath my wings. And I would like to thank her for 37 years. Ken Herman wrote a beautiful piece in the *Austin American-Statesman* on January 6th, concerning a recent tragic and sorrowful event, the death of

EXHIBIT
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Corporal Tevan Nguyen in Afghanistan. Much of what he wrote about, I observed myself. Corporal Tevan Nguyen was from Hutto, Texas. He was killed in Afghanistan on December the 28th while on patrol with his Marine unit. Since that time, our country has lost 10 more soldiers and Marines. Well, last Thursday I was in Brownwood, Texas, to pay my respects to Tevan Nguyen and his family and his memory. Now, Tevan Nguyen's last name is not spelled W-I-N. It's spelled N-G-U-Y-E-N. Tevan Nguyen's father, who lives and worked in Hutto, Texas, escaped from Vietnam and came here to this country and to this state for the freedom and the opportunity that it offers. Why was Tevan being born in Brownwood? Because his mother, Amy Salazar Nguyen was from Brownwood. And Tam Nguyen, his father, and Amy Nguyen, his mother, and Monique Stearns, the mother of his four-month-old son, and his four-month-old son, were all there in a small Catholic church in Brownwood, Texas, across the street from Howard Payne University. In this church, many people were there. His high school coaches were there, his friends, the people he played football with in Hutto. The service was in English. The choir sang in Spanish. The patriot guard, the Patriot Riders stood at attention outside the church. And when we left the church and joined the funeral procession, which was going to a country cemetery in Brown County, Texas, about 15 miles outside of Brownwood, the streets were lined with thousands of Texans. And they were all standing at attention and saluting Tevan Nguyen and waving their flags. And as I was standing at this cemetery, this beautiful, peaceful place in Central Texas, and I watched the Marines stand at attention as they lowered Tevan Nguyen's body in the ground, and I watched his father, and I watched his mother stay there until their son was properly buried, I thought, this is a snapshot of Texas in 2011. And all of us were there, all of us who were there, all several thousand of us who were there were all united, we were all united in our sorrow at the tragic loss of an American hero. But we were also united in our love for this country and our love for this state. And we were united in our determination to stay free. Tevan Nguyen and thousands like him have given their lives for our freedom and our right to govern ourselves. We owe it to him and we owe it to all who have sacrificed so much for us, to give them our best efforts on their behalf. So, let's roll up our sleeves and let's get to work. One of the things that I think has made our state better and stronger than other states, and to a certain extent the federal government, is that in our Constitution we are required to balance our budget. And we also, in our Constitution, generally have to ask the people for permission before we borrow their money. The federal government has neither of these requirements and it needs to change. The federal budget deficit is over \$14 trillion. Trillions are numbers that are so big it's hard to imagine. We usually associate them with space travel, and the reason that we don't use trillions in space is because it's too big. We use light years. A light year, by the way, is 5.6 trillion miles. The federal budget deficit is bigger than the entire economy of the United States. The annual deficit is bigger than the entire gross state product of the State of Texas. If you could

spend a million dollars every day since Christ was born, you would still have another 700 years to go before you spent your first trillion. After the last election, Congress of the United States along with the President got together and had a great, allegedly, bipartisan victory over taxes and over spending. The only problem with it is, it added \$850 billion to this \$14 trillion deficit. Article V of the United States Constitution gives us here in Texas an opportunity to change that. And one of the things that we need to debate and discuss and pass in this body, as soon as possible, is a resolution calling on the Congress, under Article V of the United States Constitution, to call a constitutional convention for the purposes of balancing the federal budget. Texas has done this before. Texas did this back in 1976 and '79. It was ignored. It was forgotten. We dare not let it happen again. A lot of the talk on my nominating speech is about our budget. I'd like to share with you a couple of numbers that haven't been widely discussed because there's a blizzard of numbers and a blizzard of opinions and blizzards of this and that. The Comptroller said that the total state revenue in the next biennium is 177.8 billion. That's everything, general revenue, federal funds, other funds, whole thing, 177.8 billion. Two years ago, her revenue estimate was 167.7 billion, 10 billion less than now. And my point is this, that a lot can happen in the next 140 days, and our job in this Texas Senate is to manage the problem and not let the problem manage us. And I know, with \$177.8 billion, and \$9.2 billion in the Rainy Day Fund, we can get the job done. It will not be easy, it will not be painless, but we can do it. One of the areas that we have got to address is Medicaid. How we deal with Medicaid will determine how the rest of the budget goes. In the current biennium we appropriated \$44 billion of all funds to Medicaid. And as a result of the federal stimulus that was enacted two years ago, the federal government reimbursed Texas out of that \$44 billion. Seventy percent was paid for with federal tax receipts and 30 percent was paid for with our tax receipts. We believe that there will no longer be such a stimulus. We believe that the federal government cannot do it and be fiscally responsible. And so, we're anticipating a federal match that's more like 58-32, 58-42. The difference between a 60-40 match and a 70-30 match, just to round off the numbers, is four and a half billion dollars, 10 percent of 44 billion. And that four and a half billion dollars that's not coming from the federal government has got to be replaced with something. Some of it has to be reform. Medicaid cries out for reform. Every hospital in this state and every procedure in every hospital in this state has a different formula for reimbursement. Makes no sense. It has been estimated by our Lieutenant Governor and others that if we converted Medicaid to a managed care program, we could save \$4 billion. The governor, 30, over 30 governors, of the State of Texas had petitioned the federal government for relief. A system that can, that only sends you 60 percent of the money but ties you up with 100 percent of the regulations will not work. And so, our first job, Senators, is to figure out how to save Medicaid. We have got to reform it and we have got to work together to fill, as a minimum, the four and a half billion dollar hole that exists because we

are not going to receive any more federal stimulus money. If you look at our budget with respect to education and health and human services, Article II and Article III, 81 percent of all the general revenue that we appropriate is appropriated in Article III and Article II. It is impossible to balance this budget without making cuts in Article II and Article III. In Article III, which is the entire education budget, we appropriate approximately \$50 billion. If you look at the Foundation School Program, we appropriate about 35 billion of that 50 billion. The Foundation School Program has serious structural problems. And in order to balance this budget we're going to have to fix public school finance. And the biggest problem with public school finance is a term called target revenue. If you go back and you remember what we did in 2006 and 2007, we basically held all of our school districts harmless. And what we said in 2006 was, look, school districts, we know that by cutting school property taxes, some of you guys are not going to get as much money as you used to, so we promise that you'll always get the same amount of money forever. School districts get to pick between how much money they got in 2005, or how much money they got in 2006, and we promised to keep giving them the same amount of money no matter what, per student. So, the money keeps going up because population's going up. We have to fix target revenue in order to balance this budget. Target revenue is a form of hold harmless. I asked the LBB how much hold harmless is costing us and the Foundation School Program, and the answer is five and a half billion dollars. So, there's where your hole is. Four and a half billion in Medicaid and five and a half billion in the Foundation School Program. We have got to fix that; we can. And the last thing I want to talk to you about with respect to the budget is the state's business tax, what's called the gross margins receipts tax. We enacted that, again, back in 2006 as part of the largest property tax cut in the history of this state. And we did. We cut school property taxes by \$14 billion. And we were going to pay for that in part with a new business tax called gross receipts, the margins tax. Problem is that the margin tax has underperformed what we have predicted ever since we enacted it. In fact, it's underperformed by a huge amount. On average, year after year after year, starting on 2006, the margins tax has underperformed what we predicted when we enacted all these property tax cuts by approximately \$2 billion a year. Part of the deficit that the Comptroller was talking about in the current biennium of 4.3 billion, 1.2 billion of that is as a result of the margins tax underperforming what we predicted. And here's the reality, none of us were elected to go out and raise taxes on anybody. But the margin tax is different because if we don't fix the margins tax, at least change the trajectory of the margins tax, then school property taxes will go up for sure. And so, when we're balancing this budget in the areas of public education, we have got to work on that issue of target revenue and fix it, and we have got to work with our colleagues in the House to fix the margins tax if we want to keep property taxes as low as they currently are. Last thing I'd like to share with you is my concerns about Border security. It's a big issue in the campaign. The Governor's already

brought up an aspect of that. I decided during the campaign that I didn't really know what I was talking about. So, I got on the plane, and I went to Del Rio, and I went to Laredo, and I'm going to go to El Paso, and I went to McAllen, and I spent a good week along the Border, and I came back more alarmed than before I left. I believe that this issue is a national security issue. I believe that Mexico could fail as a country because of the war that's going on in northern Mexico which is spilling across the river into Texas. Mexico is our largest trading partner. The United States runs the biggest trade surplus with Mexico than any other country in the world, the biggest trade surplus. If the Mexican economy collapses because of this drug war, the Texas economy will suffer. And the human cost is going to be bigger than that. And it is, and the refugees, and the people that are basically seeking political asylum in this country because Mexico is no longer governable, could overwhelm us. And so, we've got to petition the federal government for help. Because I believe if it was not so easy to import drugs in the United States across the Rio Grande River there probably wouldn't even be anything to fight for in northern Mexico, and the war could be won. So, we've got to do our part. And one of the things that we should do is put Border inspection stations for all vehicles going from the United States into Mexico. I think we have 27 ports of entry. Obviously, there's a lot of people checking you when you're going north, but there's not a 24-hour presence checking you going south. And what's going on in our drug war is that drugs are coming in the United States and stolen cars are leaving and stolen guns are leaving and millions of dollars of cash is leaving. I was in Laredo and I asked Senator Zaffirini, got any trouble with car theft down here? She laughed. The room, I said, how many people had your car stolen? Two-thirds of the people in Laredo, Texas, in that room, raised their hand and said my car's been stolen down here. Where are they going? They're going to Mexico. But we, as Members of this Legislature, need to think and work to secure our Border. It is a national security issue, it is a state security issue, and none of us can afford to have Mexico fail as a country because Mexico loses this war along the Border. Enough preaching. Thank you for this honor. I will do my very best to fulfill the duties that I have just sworn to undertake. And I ask every one of my fellow Senators to check your political considerations and your political ambition at the door, and let's work, and let's do our very best for the 25 million people that call Texas home. Thank you.

VIDEO RELEASE POLICY WAIVED

On motion of Senator Eltife and by unanimous consent, the Senate policy that governs the release of recordings of the Senate proceedings was waived in order to grant the request of Senator Ogden for a DVD of today's session.

SENATE CONCURRENT RESOLUTION 3

The President laid before the Senate the following resolution:

BE IT RESOLVED by the 82nd Legislature, That a joint committee, composed of six members of the senate appointed by the lieutenant governor and six members of the house of representatives appointed by the speaker of the house, arrange for the canvass of the votes cast for governor and lieutenant governor at the general election held on November 2, 2010, and that a joint session of the senate and house be held in the hall of the house of representatives at 10:00 a.m., on Thursday, January 13, 2011, for the purpose of counting the votes, receiving the report, and hearing the declaration of the results of the canvass; and, be it further

RESOLVED, That the senate and house of representatives sit in joint session at 11:00 a.m. on Tuesday, January 18, 2011, for the inauguration of the governor-elect and lieutenant governor-elect of Texas as determined by the canvass of the votes; and, be it further

RESOLVED, That a joint committee, composed of five members of the senate appointed by the lieutenant governor and five members of the house of representatives appointed by the speaker of the house, make arrangements for the joint session and oath-taking ceremony on January 18, 2011; and, be it further

RESOLVED, That the Department of Public Safety of the State of Texas be, and is hereby, instructed to close all vehicle entrances to the Capitol grounds on Tuesday, January 18, 2011, except for those vehicles approved by the inaugural committee as necessary for use in connection with the ceremony and the program following.

OGDEN

SCR 3 was read.

On motion of Senator Ogden, the resolution was considered immediately and was adopted by a viva voce vote.

All Members are deemed to have voted "Yea" on the adoption of the resolution.

BENEDICTION

His Eminence, Daniel Cardinal DiNardo, Archdiocese of Galveston-Houston, offered the benediction as follows:

Almighty and compassionate Lord, You have revealed Your glory to all nations and have care for all. We humbly thank You for this land, our state, a land rich in resources but above all rich in its many people. May we be a people mindful of Your love, justice, and kindness. Save us from violence, discord, and confusion, from pride and arrogance, and from every evil way. God of wisdom and justice, through Your authority is rightly administered, laws are enacted, and judgment is decreed. Let the light of Your divine wisdom direct the deliberations of this Legislature and shine forth in all its proceedings and laws framed for our rule and governance. May this Senate seek to preserve the common good and continue to bring us the blessings of liberty and equality. Assist with Your spirit of counsel and fortitude the Lieutenant Governor, the State Senators, that their administration be conducted in right judgment and be eminently useful to the citizens of this

AN ACT

relating to public school accountability, including assessment,
and curriculum requirements; providing a criminal penalty.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1. (a) Section 7.010(c), Education Code, is amended
to read as follows:

(c) The electronic student records system must permit an
authorized state or district official or an authorized
representative of an institution of higher education to
electronically transfer to and from an educational institution in
which the student is enrolled and retrieve student transcripts,
including information concerning a student's:

- (1) course or grade completion;
- (2) teachers of record;
- (3) assessment instrument results;
- (4) receipt of special education services, including
placement in a special education program and the individualized
education program developed; and
- (5) personal graduation plan as described by Section
28.0212 or 28.02121, as applicable.

(b) This section applies beginning with the 2014-2015
school year.

SECTION 2. (a) Section 7.062(e), Education Code, is amended
to read as follows:

1 (e) The rules must:

2 (1) limit the amount of assistance provided through a
3 grant to not more than:

4 (A) for a construction project, \$200 per square
5 foot of the science laboratory to be constructed; or

6 (B) for a renovation project, \$100 per square
7 foot of the science laboratory to be renovated;

8 (2) require a school district to demonstrate, as a
9 condition of eligibility for a grant, that the existing district
10 science laboratories are insufficient in number to comply with the
11 curriculum requirements imposed for the distinguished level of
12 achievement under the foundation [~~recommended and advanced~~] high
13 school program [~~programs~~] under Section 28.025 [~~28.025(b-1)(1)~~];
14 and

15 (3) provide for ranking school districts that apply
16 for grants on the basis of wealth per student and giving priority in
17 the award of grants to districts with low wealth per student.

18 (b) This section applies beginning with the 2014-2015
19 school year.

20 SECTION 3. Subchapter C, Chapter 7, Education Code, is
21 amended by adding Section 7.064 to read as follows:

22 Sec. 7.064. CAREER AND TECHNOLOGY CONSORTIUM. (a) The
23 commissioner shall investigate available options for the state to
24 join a consortium of states for the purpose of developing sequences
25 of academically rigorous career and technology courses in career
26 areas that are high-demand, high-wage career areas in this state.

27 (b) The curricula for the courses must include the

1 appropriate essential knowledge and skills adopted under
2 Subchapter A, Chapter 28.

3 (c) If the commissioner determines that joining a
4 consortium of states for this purpose would be beneficial for the
5 educational and career success of students in the state, the
6 commissioner may join the consortium on behalf of the state.

7 SECTION 4. (a) Section 12.111(b), Education Code, is
8 amended to read as follows:

9 (b) A charter holder of an open-enrollment charter school
10 shall consider including in the school's charter a requirement that
11 the school develop and administer personal graduation plans under
12 Sections [Section] 28.0212 and 28.02121.

13 (b) This section applies beginning with the 2014-2015
14 school year.

15 SECTION 5. (a) Section 25.083, Education Code, is amended
16 to read as follows:

17 Sec. 25.083. SCHOOL DAY INTERRUPTIONS. (a) The board of
18 trustees of each school district shall adopt and strictly enforce a
19 policy limiting interruptions of classes during the school day for
20 nonacademic activities such as announcements and sales promotions.
21 At a minimum, the policy must limit announcements other than
22 emergency announcements to once during the school day.

23 (b) The board of trustees of each school district shall
24 adopt and strictly enforce a policy limiting the removal of
25 students from class for remedial tutoring or test preparation. A
26 district may not remove a student from a regularly scheduled class
27 for remedial tutoring or test preparation if, as a result of the

1 removal, the student would miss more than 10 percent of the school
2 days on which the class is offered, unless the student's parent or
3 another person standing in parental relation to the student
4 provides to the district written consent for removal from class for
5 such purpose.

6 (b) This section applies beginning with the 2013-2014
7 school year.

8 SECTION 6. (a) The heading to Section 25.092, Education
9 Code, is amended to read as follows:

10 Sec. 25.092. MINIMUM ATTENDANCE FOR CLASS CREDIT OR FINAL
11 GRADE.

12 (b) This section applies beginning with the 2013-2014
13 school year.

14 SECTION 7. (a) Sections 25.092(a), (a-1), (b), and (d),
15 Education Code, are amended to read as follows:

16 (a) Except as provided by this section, a student in any
17 grade level from kindergarten through grade 12 may not be given
18 credit or a final grade for a class unless the student is in
19 attendance for at least 90 percent of the days the class is offered.

20 (a-1) A student who is in attendance for at least 75 percent
21 but less than 90 percent of the days a class is offered may be given
22 credit or a final grade for the class if the student completes a
23 plan approved by the school's principal that provides for the
24 student to meet the instructional requirements of the class. A
25 student under the jurisdiction of a court in a criminal or juvenile
26 justice proceeding may not receive credit or a final grade under
27 this subsection without the consent of the judge presiding over the

1 student's case.

2 (b) The board of trustees of each school district shall
3 appoint one or more attendance committees to hear petitions for
4 class credit or a final grade by students who are in attendance
5 fewer than the number of days required under Subsection (a) and have
6 not earned class credit or a final grade under Subsection (a-1).
7 Classroom teachers shall comprise a majority of the membership of
8 the committee. A committee may give class credit or a final grade
9 to a student because of extenuating circumstances. Each board of
10 trustees shall establish guidelines to determine what constitutes
11 extenuating circumstances and shall adopt policies establishing
12 alternative ways for students to make up work or regain credit or a
13 final grade lost because of absences. The alternative ways must
14 include at least one option that does not require a student to pay a
15 fee authorized under Section 11.158(a)(15). A certified public
16 school employee may not be assigned additional instructional duties
17 as a result of this section outside of the regular workday unless
18 the employee is compensated for the duties at a reasonable rate of
19 pay.

20 (d) If a student is denied credit or a final grade for a
21 class by an attendance committee, the student may appeal the
22 decision to the board of trustees. The decision of the board may be
23 appealed by trial de novo to the district court of the county in
24 which the school district's central administrative office is
25 located.

26 (b) This section applies beginning with the 2013-2014
27 school year.

1 SECTION 8. (a) Section 28.002, Education Code, is amended
2 by amending Subsection (c) and adding Subsections (g-1), (g-2), and
3 (o) to read as follows:

4 (c) The State Board of Education, with the direct
5 participation of educators, parents, business and industry
6 representatives, and employers shall by rule identify the essential
7 knowledge and skills of each subject of the required curriculum
8 that all students should be able to demonstrate and that will be
9 used in evaluating instructional materials under Chapter 31 and
10 addressed on the assessment instruments required under Subchapter
11 B, Chapter 39. As a condition of accreditation, the board shall
12 require each district to provide instruction in the essential
13 knowledge and skills at appropriate grade levels and to make
14 available to each high school student in the district an Algebra II
15 course.

16 (g-1) A district may also offer a course or other activity,
17 including an apprenticeship or training hours needed to obtain an
18 industry-recognized credential or certificate, that is approved by
19 the board of trustees for credit without obtaining State Board of
20 Education approval if:

21 (1) the district develops a program under which the
22 district partners with a public or private institution of higher
23 education and local business, labor, and community leaders to
24 develop and provide the courses; and

25 (2) the course or other activity allows students to
26 enter:

27 (A) a career or technology training program in

1 the district's region of the state;

2 (B) an institution of higher education without
3 remediation;

4 (C) an apprenticeship training program; or

5 (D) an internship required as part of
6 accreditation toward an industry-recognized credential or
7 certificate for course credit.

8 (g-2) Each school district shall annually report to the
9 agency the names of the courses, programs, institutions of higher
10 education, and internships in which the district's students have
11 enrolled under Subsection (g-1). The agency shall make available
12 information provided under this subsection to other districts.

13 (o) In approving career and technology courses, the State
14 Board of Education must determine that at least 50 percent of the
15 approved courses are cost-effective for a school district to
16 implement.

17 (b) This section applies beginning with the 2014-2015
18 school year.

19 SECTION 9. Subchapter A, Chapter 28, Education Code, is
20 amended by adding Section 28.00222 to read as follows:

21 Sec. 28.00222. INCREASE IN ADVANCED TECHNOLOGY AND
22 CAREER-RELATED COURSES. (a) Not later than September 1, 2014, the
23 State Board of Education shall ensure that at least six advanced
24 career and technology education or technology applications
25 courses, including courses in personal financial literacy
26 consistent with Section 28.0021 and in statistics, are approved to
27 satisfy a fourth credit in mathematics.

1 (b) Not later than January 1, 2015, the commissioner shall
 2 review and report to the governor, the lieutenant governor, the
 3 speaker of the house of representatives, and the presiding officer
 4 of each standing committee of the legislature with primary
 5 responsibility over public primary and secondary education
 6 regarding the progress of increasing the number of courses approved
 7 for the career and technology education or technology applications
 8 curriculum. The commissioner shall include in the report a
 9 detailed description of any new courses, including instructional
 10 materials and required equipment, if any.

11 (c) This section expires September 1, 2015.

12 SECTION 10. (a) Section 28.014, Education Code, is amended
 13 to read as follows:

14 Sec. 28.014. COLLEGE PREPARATORY COURSES. (a) Each school
 15 district shall partner with at least one institution of higher
 16 education to develop and provide ~~[The commissioner of education and~~
 17 ~~the commissioner of higher education shall develop and recommend to~~
 18 ~~the State Board of Education for adoption under Section 28.002 the~~
 19 ~~essential knowledge and skills of]~~ courses in college preparatory
 20 mathematics~~[, science, social studies,]~~ and English language
 21 arts. The courses must be designed:

22 (1) for students at the 12th grade level whose
 23 performance on:

24 (A) [who do not meet college readiness standards
 25 ~~on]~~ an end-of-course assessment instrument required under Section
 26 39.023(c) does not meet college readiness standards; or

27 (B) coursework, a college entrance examination,

1 or an assessment instrument designated under Section 51.3062(c)
2 indicates that the student is not ready to perform entry-level
3 college coursework; and

4 (2) to prepare students for success in entry-level
5 college courses.

6 (b) A course developed under this section must be provided:

7 (1) on the campus of the high school offering the
8 course; or

9 (2) through distance learning or as an online course
10 provided through an institution of higher education with which the
11 school district partners as provided by Subsection (a).

12 (c) Appropriate faculty of each high school offering
13 courses under this section and appropriate faculty of each
14 institution of higher education with which the school district
15 partners shall meet regularly as necessary to ensure that each
16 course is aligned with college readiness expectations. The
17 commissioner of education, in coordination with the commissioner of
18 higher education, may adopt rules to administer this subsection.

19 (d) Each school district shall provide a notice to each
20 district student to whom Subsection (a) applies and the student's
21 parent or guardian regarding the benefits of enrolling in a course
22 under this section.

23 (e) A student who successfully completes an English
24 language arts [a] course developed under this section may use the
25 credit earned in the course toward satisfying the advanced English
26 language arts [applicable mathematics or science] curriculum
27 requirement for the foundation [recommended or advanced] high

1 school program under Section 28.025(b-1)(1) ~~[28.025]~~. A student
2 who successfully completes a mathematics course developed under
3 this section may use the credit earned in the course toward
4 satisfying an advanced mathematics curriculum requirement under
5 Section 28.025 after completion of the mathematics curriculum
6 requirements for the foundation high school program under Section
7 28.025(b-1)(2).

8 (f) A course provided under this section may be offered for
9 dual credit at the discretion of the institution of higher
10 education with which a school district partners under this section.

11 (g) Each school district, in consultation with each
12 institution of higher education with which the district partners,
13 shall develop or purchase ~~[(c) The agency, in consultation with~~
14 ~~the Texas Higher Education Coordinating Board, shall adopt an~~
15 ~~end-of-course assessment instrument for each course developed~~
16 ~~under this section to ensure the rigor of the course. A school~~
17 ~~district shall, in accordance with State Board of Education rules,~~
18 ~~administer the end-of-course assessment instrument to a student~~
19 ~~enrolled in a course developed under this section. Each school~~
20 ~~district shall adopt a policy that requires a student's performance~~
21 ~~on the end-of-course assessment instrument to account for 15~~
22 ~~percent of the student's final grade for the course. A student's~~
23 ~~performance on an end-of-course assessment instrument administered~~
24 ~~under this subsection may be used, on a scale of 0-40, in~~
25 ~~calculating whether the student satisfies the graduation~~
26 ~~requirements established under Section 39.025.~~

27 ~~[(d) The agency, in coordination with the Texas Higher~~

1 ~~Education Coordinating Board, shall adopt a series of questions to~~
2 ~~be included in an end-of-course assessment instrument administered~~
3 ~~under Subsection (c) to be used for purposes of Section~~
4 ~~51.3062. The questions must be developed in a manner consistent~~
5 ~~with any college readiness standards adopted under Sections 39.233~~
6 ~~and 51.3062.~~

7 ~~[(e) The State Board of Education shall adopt]~~
8 instructional materials for a course developed under this section
9 consistent ~~[in accordance]~~ with Chapter 31. The instructional
10 materials must include technology resources that enhance the
11 effectiveness of the course and draw on established best practices.

12 ~~(h) [(f)]~~ To the extent applicable, a district ~~[the~~
13 ~~commissioner]~~ shall draw from curricula and instructional
14 materials developed under Section ~~[Sections]~~ 28.008 ~~[and 61.0763]~~
15 in developing a course and related instructional materials under
16 this section. ~~A [Not later than September 1, 2010, the State Board~~
17 ~~of Education shall adopt essential knowledge and skills for each~~
18 ~~course developed under this section. The State Board of Education~~
19 ~~shall make each] course developed under this section and the~~
20 related instructional materials shall be made available to students
21 ~~[school districts] not later than the 2014-2015 school year. [As~~
22 ~~required by Subsection (c), a school district shall adopt a policy~~
23 ~~requiring a student's performance on an end-of-course assessment~~
24 ~~instrument administered under that subsection to account for 15~~
25 ~~percent of the student's grade for a course developed under this~~
26 ~~section not later than the 2014-2015 school year.] This subsection~~
27 expires September 1, 2015.

1 (b) This section applies beginning with the 2013-2014
2 school year.

3 SECTION 11. Section 28.0211, Education Code, is amended by
4 amending Subsection (m) and adding Subsection (m-1) to read as
5 follows:

6 (m) The commissioner shall certify, not later than July 1 of
7 each school year or as soon as practicable thereafter, whether
8 sufficient funds have been appropriated statewide for the purposes
9 of this section and Section 28.0217. A determination by the
10 commissioner is final and may not be appealed. For purposes of
11 certification, the commissioner shall consider:

12 (1) the average cost per student per assessment
13 instrument administration;

14 (2) the number of students that require accelerated
15 instruction because the student failed to perform satisfactorily on
16 an assessment instrument;

17 (3) whether sufficient funds have been appropriated to
18 provide support to students in grades three through 12 identified
19 as being at risk of dropping out of school, as defined in Section
20 29.081(d); and

21 (4) whether sufficient funds have been appropriated to
22 provide instructional materials that are aligned with the
23 assessment instruments under Sections 39.023(a) and (c).

24 (m-1) For purposes of certification under Subsection (m),
25 the commissioner may not consider Foundation School Program funds
26 except for compensatory education funds under Section
27 42.152. This section may be implemented only if the commissioner

1 certifies that sufficient funds have been appropriated during a
2 school year for administering the accelerated instruction programs
3 specified under this section and Section 28.0217, including teacher
4 training for that purpose.

5 SECTION 12. (a) The heading to Section 28.0212, Education
6 Code, is amended to read as follows:

7 Sec. 28.0212. JUNIOR HIGH OR MIDDLE SCHOOL PERSONAL
8 GRADUATION PLAN.

9 (b) This section applies beginning with the 2014-2015
10 school year.

11 SECTION 13. (a) Sections 28.0212(a) and (b), Education
12 Code, are amended to read as follows:

13 (a) A principal of a junior high or middle school shall
14 designate a school ~~[guidance]~~ counselor, teacher, or other
15 appropriate individual to develop and administer a personal
16 graduation plan for each student enrolled in the ~~[a]~~ junior high
17 or ~~[r]~~ middle ~~[r]~~ or high school who:

18 (1) does not perform satisfactorily on an assessment
19 instrument administered under Subchapter B, Chapter 39; or

20 (2) is not likely to receive a high school diploma
21 before the fifth school year following the student's enrollment in
22 grade level nine, as determined by the district.

23 (b) A personal graduation plan under this section must:

24 (1) identify educational goals for the student;

25 (2) include diagnostic information, appropriate
26 monitoring and intervention, and other evaluation strategies;

27 (3) include an intensive instruction program

1 described by Section 28.0213;

2 (4) address participation of the student's parent or
3 guardian, including consideration of the parent's or guardian's
4 educational expectations for the student; and

5 (5) provide innovative methods to promote the
6 student's advancement, including flexible scheduling, alternative
7 learning environments, on-line instruction, and other
8 interventions that are proven to accelerate the learning process
9 and have been scientifically validated to improve learning and
10 cognitive ability.

11 (b) This section applies beginning with the 2014-2015
12 school year.

13 SECTION 14. (a) Subchapter B, Chapter 28, Education Code,
14 is amended by adding Section 28.02121 to read as follows:

15 Sec. 28.02121. HIGH SCHOOL PERSONAL GRADUATION PLAN. (a)
16 The agency, in consultation with the Texas Workforce Commission and
17 the Texas Higher Education Coordinating Board, shall prepare and
18 make available to each school district in English and Spanish
19 information that explains the advantages of the distinguished level
20 of achievement described by Section 28.025(b-15) and each
21 endorsement described by Section 28.025(c-1). The information must
22 contain an explanation:

23 (1) concerning the benefits of choosing a high school
24 personal graduation plan that includes the distinguished level of
25 achievement under the foundation high school program and includes
26 one or more endorsements to enable the student to achieve a class
27 rank in the top 10 percent for students at the campus; and

1 (2) that encourages parents, to the greatest extent
 2 practicable, to have the student choose a high school personal
 3 graduation plan described by Subdivision (1).

4 (b) A school district shall publish the information
 5 provided to the district under Subsection (a) on the Internet
 6 website of the district and ensure that the information is
 7 available to students in grades nine and above and the parents or
 8 legal guardians of those students in the language in which the
 9 parents or legal guardians are most proficient. A district is
 10 required to provide information under this subsection in the
 11 language in which the parents or legal guardians are most
 12 proficient only if at least 20 students in a grade level primarily
 13 speak that language.

14 (c) A principal of a high school shall designate a school
 15 counselor or school administrator to review personal graduation
 16 plan options with each student entering grade nine together with
 17 that student's parent or guardian. The personal graduation plan
 18 options reviewed must include the distinguished level of
 19 achievement described by Section 28.025(b-15) and the endorsements
 20 described by Section 28.025(c-1). Before the conclusion of the
 21 school year, the student and the student's parent or guardian must
 22 confirm and sign a personal graduation plan for the student.

23 (d) A personal graduation plan under Subsection (c) must
 24 identify a course of study that:

25 (1) promotes:

26 (A) college and workforce readiness; and

27 (B) career placement and advancement; and

1 (2) facilitates the student's transition from
2 secondary to postsecondary education.

3 (e) A school district may not prevent a student and the
4 student's parent or guardian from confirming a personal graduation
5 plan that includes pursuit of a distinguished level of achievement
6 or an endorsement.

7 (f) A student may amend the student's personal graduation
8 plan after the initial confirmation of the plan under this section.
9 If a student amends the student's personal graduation plan, the
10 school shall send written notice to the student's parents regarding
11 the change.

12 (b) This section applies beginning with the 2014-2015
13 school year.

14 SECTION 15. Subchapter B, Chapter 28, Education Code, is
15 amended by adding Section 28.0217 to read as follows:

16 Sec. 28.0217. ACCELERATED INSTRUCTION FOR HIGH SCHOOL
17 STUDENTS. Each time a student fails to perform satisfactorily on an
18 assessment instrument administered under Section 39.023(c), the
19 school district in which the student attends school shall provide
20 to the student accelerated instruction in the applicable subject
21 area, using funds appropriated for accelerated instruction under
22 Section 28.0211. Accelerated instruction may require
23 participation of the student before or after normal school hours
24 and may include participation at times of the year outside normal
25 school operations.

26 SECTION 16. (a) Section 28.025, Education Code, is amended
27 by amending Subsections (a), (b), (b-1), (b-2), (b-3), (b-4),

1 (b-5), (b-7), (b-9), (b-10), (b-11), and (e) and adding Subsections
2 (b-12), (b-13), (b-14), (b-15), (b-16), (b-17), (b-18), (b-19),
3 (c-1), (c-2), (c-3), (c-4), (c-5), (e-1), (e-2), (e-3), (h), (h-1),
4 and (h-2) to read as follows:

5 (a) The State Board of Education by rule shall determine
6 curriculum requirements for the foundation ~~[minimum, recommended,~~
7 ~~and advanced]~~ high school program ~~[programs]~~ that are consistent
8 with the required curriculum under Section 28.002. ~~The [Subject to~~
9 ~~Subsection (b-1), the]~~ State Board of Education shall designate the
10 specific courses in the foundation curriculum under Section
11 28.002(a)(1) required under ~~[for a student participating in]~~ the
12 foundation ~~[minimum, recommended, or advanced]~~ high school
13 program. Except as provided by this section ~~[Subsection (b-1)]~~,
14 the State Board of Education may not designate a specific course or
15 a specific number of credits in the enrichment curriculum as
16 requirements for the ~~[recommended]~~ program.

17 (b) A school district shall ensure that each student, on
18 entering ninth grade, indicates in writing an endorsement under
19 Subsection (c-1) that the student intends to earn. A district shall
20 permit a student to choose, at any time, to earn an endorsement
21 other than the endorsement the student previously indicated. A
22 student may graduate under the foundation high school program
23 without earning an endorsement if, after the student's sophomore
24 year:

25 (1) the student and the student's parent or person
26 standing in parental relation to the student are advised by a school
27 counselor of the specific benefits of graduating from high school

1 with one or more endorsements; and

2 (2) the student's parent or person standing in
 3 parental relation to the student files with a school counselor
 4 written permission, on a form adopted by the agency, allowing the
 5 student to graduate under the foundation high school program
 6 without earning an endorsement ~~[enrolls in the courses necessary to~~
 7 ~~complete the curriculum requirements identified by the State Board~~
 8 ~~of Education under Subsection (a) for the recommended or advanced~~
 9 ~~high school program unless the student, the student's parent or~~
 10 ~~other person standing in parental relation to the student, and a~~
 11 ~~school counselor or school administrator agree in writing signed by~~
 12 ~~each party that the student should be permitted to take courses~~
 13 ~~under the minimum high school program and the student:~~

14 ~~[(1) is at least 16 years of age;~~

15 ~~[(2) has completed two credits required for graduation~~
 16 ~~in each subject of the foundation curriculum under Section~~
 17 ~~28.002(a)(1); or~~

18 ~~[(3) has failed to be promoted to the tenth grade one~~
 19 ~~or more times as determined by the school district].~~

20 (b-1) The State Board of Education by rule shall require
 21 that:

22 ~~[(1) except as provided by Subsection (b-2),]~~ the
 23 curriculum requirements for the foundation ~~[recommended and~~
 24 ~~advanced]~~ high school program ~~[programs]~~ under Subsection (a)
 25 include a requirement that students successfully complete:

26 (1) [(A)] four credits in English language arts ~~[each~~
 27 ~~subject of the foundation curriculum]~~ under Section

1 28.002(a)(1)(A), including one credit in English I, one credit in
2 English II, one credit in English III, and one credit in an advanced
3 English course authorized under Subsection (b-2);

4 (2) three credits in mathematics under Section
5 28.002(a)(1)(B), including one credit in Algebra I, one credit in
6 geometry, and one credit in any advanced mathematics course
7 authorized under Subsection (b-2);

8 (3) three credits in science under Section
9 28.002(a)(1)(C), including one credit in biology, one credit in any
10 advanced science course authorized under Subsection (b-2), and one
11 credit in integrated physics and chemistry or in an additional
12 advanced science course authorized under Subsection (b-2);

13 (4) three credits in social studies under Section
14 28.002(a)(1)(D) [28.002(a)(1)], including one credit in United
15 States history, at least one-half credit in government and at least
16 one-half credit in economics, and one credit in world geography or
17 world history [to meet the social studies requirement];

18 (5) except as provided under Subsections (b-12),
19 (b-13), and (b-14) [(B) for the recommended high school program],
20 two credits in the same language in a language other than English
21 under Section 28.002(a)(2)(A) [and, for the advanced high school
22 program, three credits in the same language in a language other than
23 English under Section 28.002(a)(2)(A)]; [and]

24 (6) five [(C) for the recommended high school
25 program, six] elective credits [and, for the advanced high school
26 program, five elective credits];

27 (7) [(2) one or more credits offered in the required

1 ~~curriculum for the recommended and advanced high school programs~~
2 ~~include a research writing component, and~~

3 ~~[(3) the curriculum requirements for the minimum,~~
4 ~~recommended, and advanced high school programs under Subsection (a)~~
5 ~~include a requirement that students successfully complete.~~

6 ~~[(A)]~~ one credit in fine arts under Section
7 28.002(a)(2)(D); and

8 (8) ~~[(B)]~~ except as provided by Subsection (b-11), one
9 credit in physical education under Section 28.002(a)(2)(C).

10 (b-2) In adopting rules under Subsection (b-1), the State
11 Board of Education shall provide for ~~[allow]~~ a student to comply
12 with the curriculum requirements for an advanced English course
13 under Subsection (b-1)(1) taken after successful completion of
14 English I, English II, and English III, for an advanced [a]
15 mathematics course under Subsection (b-1)(2) [(b-1)(1)] taken
16 after the successful completion of Algebra I and geometry, and for
17 any advanced [either after the successful completion of or
18 ~~concurrently with Algebra II or a]~~ science course under Subsection
19 (b-1)(3) [(b-1)(1) taken after the successful completion of biology
20 and chemistry and either after the successful completion of or
21 ~~concurrently with physics]~~ by successfully completing a course in
22 the appropriate content area that has been approved as an advanced
23 course by board rule or that is offered as an advanced course for
24 credit without board approval as provided by Section 28.002(g-1)
25 ~~[career and technical course designated by the State Board of~~
26 ~~Education as containing substantively similar and rigorous~~
27 ~~academic content. A student may use the option provided by this~~

1 ~~subsection for not more than two courses]~~.

2 (b-3) In adopting rules for purposes of Subsection (b-2) ~~[to~~
3 ~~provide students with the option described by Subsection~~
4 ~~(b-1)(1)(A)]~~, the State Board of Education must approve a variety
5 of advanced English, mathematics, and science courses that may be
6 taken ~~[after the completion of Algebra II and physics]~~ to comply
7 with the foundation high school ~~[recommended]~~ program
8 requirements, provided that each approved course prepares students
9 to enter the workforce successfully or postsecondary education
10 without remediation.

11 (b-4) A school district may offer the curriculum described
12 in Subsections (b-1)(1) through (4) ~~[Subsection (b-1)(1)(A)]~~ in an
13 applied manner. Courses delivered in an applied manner must cover
14 the essential knowledge and skills, and the student shall be
15 administered the applicable end-of-course assessment instrument as
16 provided by Sections 39.023(c) and 39.025.

17 (b-5) A school district may offer a mathematics or science
18 course to be taken by a student after completion of Algebra II and
19 physics ~~[to comply with the recommended program requirements in~~
20 ~~Subsection (b-1)(1)(A)]~~. A course approved under this subsection
21 must be endorsed by an institution of higher education as a course
22 for which the institution would award course credit or as a
23 prerequisite for a course for which the institution would award
24 course credit.

25 (b-7) The State Board of Education, in coordination with the
26 Texas Higher Education Coordinating Board, shall adopt rules to
27 ensure that a student may comply with the curriculum requirements

1 under the foundation [~~minimum, recommended, or advanced~~] high
 2 school program or for an endorsement under Subsection (c-1) [~~for~~
 3 ~~each subject of the foundation curriculum, under Section~~
 4 ~~28.002(a)(1) and for languages other than English under Section~~
 5 ~~28.002(a)(2)(A)] by successfully completing appropriate courses in
 6 the core curriculum of an institution of higher education under
 7 Section 61.822. Notwithstanding Subsection (b-15) or (c) of this
 8 section, Section 39.025, or any other provision of this code and
 9 notwithstanding any school district policy, a student who has
 10 completed the core curriculum of an institution of higher education
 11 under Section 61.822, as certified by the institution in accordance
 12 with commissioner rule, is considered to have earned a
 13 distinguished level of achievement under the foundation high school
 14 program and is entitled to receive a high school diploma from the
 15 appropriate high school as that high school is determined in
 16 accordance with commissioner rule. A student who is considered to
 17 have earned a distinguished level of achievement under the
 18 foundation high school program under this subsection may apply for
 19 admission to an institution of higher education for the first
 20 semester or other academic term after the semester or other
 21 academic term in which the student completes the core curriculum.~~

22 (b-9) A school district, with the approval of the
 23 commissioner, may allow [~~The agency shall establish a pilot program~~
 24 ~~allowing~~] a student [~~attending school in a county with a population~~
 25 ~~of more than one million and in which more than 75 percent of the~~
 26 ~~population resides in a single municipality] to satisfy the fine
 27 arts credit required under Subsection (b-1)(7) [~~(b-1)(3)(A)]~~ by~~

1 participating in a community-based fine arts program not provided
2 by the school district in which the student is enrolled. The fine
3 arts program must provide instruction in the essential knowledge
4 and skills identified for fine arts by the State Board of Education
5 under Section 28.002(c). The fine arts program may be provided on or
6 off a school campus and outside the regular school day. [~~Not later~~
7 ~~than December 1, 2010, the agency shall provide to the legislature a~~
8 ~~report regarding the pilot program, including the feasibility of~~
9 ~~expanding the pilot program statewide.~~]

10 (b-10) A school district, with the approval of the
11 commissioner, may allow a student to comply with the curriculum
12 requirements for the physical education credit required under
13 Subsection (b-1)(8) [~~(b-1)(3)(B)~~] by participating in a private or
14 commercially sponsored physical activity program provided on or off
15 a school campus and outside the regular school day.

16 (b-11) In adopting rules under Subsection (b-1), the State
17 Board of Education shall allow a student who is unable to
18 participate in physical activity due to disability or illness to
19 substitute one credit in English language arts, mathematics,
20 science, or social studies, one credit in a course that is offered
21 for credit as provided by Section 28.002(g-1), or one academic
22 elective credit for the physical education credit required under
23 Subsection (b-1)(8) [~~(b-1)(3)(B)~~]. A credit allowed to be
24 substituted under this subsection may not also be used by the
25 student to satisfy a graduation requirement other than completion
26 of the physical education credit. The rules must provide that the
27 determination regarding a student's ability to participate in

1 physical activity will be made by:

2 (1) if the student receives special education services
3 under Subchapter A, Chapter 29, the student's admission, review,
4 and dismissal committee;

5 (2) if the student does not receive special education
6 services under Subchapter A, Chapter 29, but is covered by Section
7 504, Rehabilitation Act of 1973 (29 U.S.C. Section 794), the
8 committee established for the student under that Act; or

9 (3) if each of the committees described by
10 Subdivisions (1) and (2) is inapplicable, a committee established
11 by the school district of persons with appropriate knowledge
12 regarding the student.

13 (b-12) In adopting rules under Subsection (b-1), the State
14 Board of Education shall adopt criteria to allow a student to comply
15 with the curriculum requirements for the two credits in a language
16 other than English required under Subsection (b-1)(5) by
17 substituting two credits in computer programming languages.

18 (b-13) In adopting rules under Subsection (b-1), the State
19 Board of Education shall allow a student to substitute credit in
20 another appropriate course for the second credit in the same
21 language in a language other than English otherwise required by
22 Subsection (b-1)(5) if the student, in completing the first credit
23 required under Subsection (b-1)(5), demonstrates that the student
24 is unlikely to be able to complete the second credit. The board
25 rules must establish:

26 (1) the standards and, as applicable, the appropriate
27 school personnel for making a determination under this subsection;

1 and

2 (2) appropriate substitute courses for purposes of
3 this subsection.

4 (b-14) In adopting rules under Subsection (b-1), the State
5 Board of Education shall allow a student who, due to disability, is
6 unable to complete two courses in the same language in a language
7 other than English, as provided under Subsection (b-1)(5), to
8 substitute for those credits two credits in English language arts,
9 mathematics, science, or social studies or two credits in career
10 and technology education, technology applications, or other
11 academic electives. A credit allowed to be substituted under this
12 subsection may not also be used by the student to satisfy a
13 graduation credit requirement other than credit for completion of a
14 language other than English. The rules must provide that the
15 determination regarding a student's ability to participate in
16 language-other-than-English courses will be made by:

17 (1) if the student receives special education services
18 under Subchapter A, Chapter 29, the student's admission, review,
19 and dismissal committee; or

20 (2) if the student does not receive special education
21 services under Subchapter A, Chapter 29, but is covered by Section
22 504, Rehabilitation Act of 1973 (29 U.S.C. Section 794), the
23 committee established for the student under that Act.

24 (b-15) A student may earn a distinguished level of
25 achievement under the foundation high school program by
26 successfully completing:

27 (1) four credits in mathematics, which must include

1 Algebra II and the courses described by Subsection (b-1)(2);

2 (2) four credits in science, which must include the
3 courses described by Subsection (b-1)(3);

4 (3) the remaining curriculum requirements under
5 Subsection (b-1); and

6 (4) the curriculum requirements for at least one
7 endorsement under Subsection (c-1).

8 (b-16) A student may satisfy an elective credit required
9 under Subsection (b-1)(6) with a credit earned to satisfy the
10 additional curriculum requirements for the distinguished level of
11 achievement under the foundation high school program or an
12 endorsement under Subsection (c-1). This subsection may apply to
13 more than one elective credit.

14 (b-17) The State Board of Education shall adopt rules to
15 ensure that a student may comply with the curriculum requirements
16 under Subsection (b-1)(6) by successfully completing an advanced
17 career and technical course, including a course that may lead to an
18 industry-recognized credential or certificate or an associate
19 degree.

20 (b-18) In adopting rules under Subsection (b-1), the State
21 Board of Education shall allow a student to comply with the
22 curriculum requirements under Subsection (b-1) by successfully
23 completing a dual credit course.

24 (b-19) In adopting rules under Subsection (b-1), the State
25 Board of Education shall adopt criteria to allow a student to comply
26 with curriculum requirements for the world geography or world
27 history credit under Subsection (b-1)(4) by successfully

1 completing a combined world history and world geography course
2 developed by the State Board of Education.

3 (c-1) A student may earn an endorsement on the student's
4 diploma and transcript by successfully completing curriculum
5 requirements for that endorsement adopted by the State Board of
6 Education by rule. The State Board of Education by rule shall
7 provide students with multiple options for earning each
8 endorsement, including, to the greatest extent possible, coherent
9 sequences of courses. The State Board of Education by rule must
10 permit a student to enroll in courses under more than one
11 endorsement curriculum before the student's junior year. An
12 endorsement under this subsection may be earned in any of the
13 following categories:

14 (1) science, technology, engineering, and mathematics
15 (STEM), which includes courses directly related to science,
16 including environmental science, technology, including computer
17 science, engineering, and advanced mathematics;

18 (2) business and industry, which includes courses
19 directly related to database management, information technology,
20 communications, accounting, finance, marketing, graphic design,
21 architecture, construction, welding, logistics, automotive
22 technology, agricultural science, and heating, ventilation, and
23 air conditioning;

24 (3) public services, which includes courses directly
25 related to health sciences and occupations, education and training,
26 law enforcement, and culinary arts and hospitality;

27 (4) arts and humanities, which includes courses

1 directly related to political science, world languages, cultural
2 studies, English literature, history, and fine arts; and

3 (5) multidisciplinary studies, which allows a student
4 to:

5 (A) select courses from the curriculum of each
6 endorsement area described by Subdivisions (1) through (4); and

7 (B) earn credits in a variety of advanced courses
8 from multiple content areas sufficient to complete the
9 distinguished level of achievement under the foundation high school
10 program.

11 (c-2) In adopting rules under Subsection (c-1), the State
12 Board of Education shall:

13 (1) require a student in order to earn any endorsement
14 to successfully complete:

15 (A) four credits in mathematics, which must
16 include:

17 (i) the courses described by Subsection
18 (b-1)(2); and

19 (ii) an additional advanced mathematics
20 course authorized under Subsection (b-2) or an advanced career and
21 technology course designated by the State Board of Education;

22 (B) four credits in science, which must include:

23 (i) the courses described by Subsection
24 (b-1)(3); and

25 (ii) an additional advanced science course
26 authorized under Subsection (b-2) or an advanced career and
27 technology course designated by the State Board of Education; and

1 (C) two elective credits in addition to the
2 elective credits required under Subsection (b-1)(6); and

3 (2) develop additional curriculum requirements for
4 each endorsement with the direct participation of educators and
5 business, labor, and industry representatives, and shall require
6 each school district to report to the agency the categories of
7 endorsements under Subsection (c-1) for which the district offers
8 all courses for curriculum requirements, as determined by board
9 rule.

10 (c-3) In adopting rules under Subsection (c-1), the State
11 Board of Education shall adopt criteria to allow a student
12 participating in the arts and humanities endorsement under
13 Subsection (c-1)(4), with the written permission of the student's
14 parent or a person standing in parental relation to the student, to
15 comply with the curriculum requirements for science required under
16 Subsection (c-2)(1)(B)(ii) by substituting for an advanced course
17 requirement a course related to that endorsement.

18 (c-4) Each school district must make available to high
19 school students courses that allow a student to complete the
20 curriculum requirements for at least one endorsement under
21 Subsection (c-1). A school district that offers only one
22 endorsement curriculum must offer the multidisciplinary studies
23 endorsement curriculum.

24 (c-5) A student may earn a performance acknowledgment on the
25 student's diploma and transcript by satisfying the requirements for
26 that acknowledgment adopted by the State Board of Education by
27 rule. An acknowledgment under this subsection may be earned:

1 (1) for outstanding performance:
2 (A) in a dual credit course;
3 (B) in bilingualism and biliteracy;
4 (C) on a college advanced placement test or
5 international baccalaureate examination; or
6 (D) on the PSAT, the ACT-Plan, the SAT, or the
7 ACT; or

8 (2) for earning a nationally or internationally
9 recognized business or industry certification or license.

10 (e) Each school district shall report the academic
11 achievement record of students who have completed the foundation [~~a~~
12 ~~minimum, recommended, or advanced~~] high school program on
13 transcript forms adopted by the State Board of Education. The
14 transcript forms adopted by the board must be designed to clearly
15 [~~differentiate between each of the high school programs and~~]
16 identify whether a student received a diploma or a certificate of
17 coursework completion.

18 (e-1) A school district shall clearly indicate a
19 distinguished level of achievement under the foundation high school
20 program as described by Subsection (b-15), an endorsement described
21 by Subsection (c-1), and a performance acknowledgment described by
22 Subsection (c-5) on the diploma and transcript of a student who
23 satisfies the applicable requirements. The State Board of
24 Education shall adopt rules as necessary to administer this
25 subsection.

26 (e-2) At the end of each school year, each school district
27 shall report through the Public Education Information Management

1 System (PEIMS) the number of district students who during that
2 school year, were:

- 3 (1) enrolled in the foundation high school program;
4 (2) pursuing the distinguished level of achievement
5 under the foundation high school program as provided by Subsection
6 (b-15); and
7 (3) enrolled in a program to earn an endorsement
8 described by Subsection (c-1).

9 (e-3) Information reported under Subsection (e-2) must be
10 disaggregated by all student groups served by the district,
11 including categories of race, ethnicity, socioeconomic status,
12 sex, and populations served by special programs, including students
13 in special education programs under Subchapter A, Chapter 29.

14 (h) The commissioner by rule shall adopt a transition plan
15 to implement and administer the amendments made by H.B. No. 5, 83rd
16 Legislature, Regular Session, 2013, replacing the minimum,
17 recommended, and advanced high school programs with the foundation
18 high school program beginning with the 2014-2015 school year.
19 Under the transition plan, a student who entered the ninth grade
20 before the 2014-2015 school year must be permitted to complete the
21 curriculum requirements required for high school graduation under:

22 (1) the foundation high school program, if the student
23 chooses during the 2014-2015 school year to take courses under this
24 program;

25 (2) the minimum high school program, as that program
26 existed before the adoption of H.B. No. 5, 83rd Legislature,
27 Regular Session, 2013, if the student was participating in that

1 program before the 2014-2015 school year;

2 (3) the recommended high school program, as that
3 program existed before the adoption of H.B. No. 5, 83rd
4 Legislature, Regular Session, 2013, if the student was
5 participating in that program before the 2014-2015 school year; or

6 (4) the advanced high school program, as that program
7 existed before the adoption of H.B. No. 5, 83rd Legislature,
8 Regular Session, 2013, if the student was participating in that
9 program before the 2014-2015 school year.

10 (h-1) This subsection and Subsection (h) expire September
11 1, 2018.

12 (h-2) This subsection applies only to a student
13 participating in the minimum, recommended, or advanced high school
14 program who is completing the fourth year of high school during the
15 2013-2014 school year. The commissioner by rule shall permit a
16 student who does not satisfy the curriculum requirements of the
17 high school program in which the student is participating to
18 graduate if the student satisfies the curriculum requirements
19 established for the foundation high school program under this
20 section as amended by H.B. No. 5, 83rd Legislature, Regular
21 Session, 2013, and any other requirement required for graduation.
22 This subsection expires September 1, 2015.

23 (b) Except as provided by Subsection (c) of this section,
24 this section applies beginning with the 2014-2015 school year.

25 (c) Section 28.025(h-2), Education Code, as added by this
26 section, applies during the 2013-2014 school year.

27 SECTION 17. (a) Section 28.0253(e), Education Code, is

1 amended to read as follows:

2 (e) A student who receives a high school diploma through the
3 pilot program is considered to have earned a distinguished level of
4 achievement under ~~[completed]~~ the foundation ~~[recommended]~~ high
5 school program adopted under Section 28.025 ~~[28.025(a)]~~. The
6 student is not guaranteed admission to any institution of higher
7 education or to any academic program at an institution of higher
8 education solely on the basis of having received the diploma
9 through the program. The student may apply for admission to an
10 institution of higher education for the first semester or other
11 academic term after the semester or other academic term in which the
12 student earns a diploma through the pilot program.

13 (b) This section applies beginning with the 2014-2015
14 school year.

15 SECTION 18. (a) Section 28.026, Education Code, is amended
16 to read as follows:

17 Sec. 28.026. NOTICE OF REQUIREMENTS FOR AUTOMATIC COLLEGE
18 ADMISSION AND FINANCIAL AID. (a) The board of trustees of a school
19 district and the governing body of each open-enrollment charter
20 school that provides a high school shall require each high school in
21 the district or provided by the charter school, as applicable, to
22 post appropriate signs in each counselor's office, in each
23 principal's office, and in each administrative building indicating
24 the substance of Section 51.803 regarding automatic college
25 admission and stating the curriculum requirements for financial aid
26 authorized under Title 3. To assist in the dissemination of that
27 ~~[this]~~ information, the ~~[school]~~ district or charter school shall:

1 (1) require that each high school counselor and class
2 advisor be provided a detailed explanation of the substance of
3 Section 51.803 and the curriculum requirements for financial aid
4 authorized under Title 3;

5 (2) provide each district or school student, at the
6 time the student first registers for one or more classes required
7 for high school graduation, with a written notification, including
8 a detailed explanation in plain language, of the substance of
9 Section 51.803, the curriculum requirements for financial aid
10 authorized under Title 3, and the benefits of completing the
11 requirements for that automatic admission and financial aid;

12 (3) require that each high school counselor and senior
13 class advisor explain to eligible students the substance of Section
14 51.803; and

15 (4) not later than the 14th day after the last day of
16 classes for the fall semester or an equivalent date in the case of a
17 school operated on a year-round system under Section 25.084,
18 provide each ~~[eligible]~~ senior student eligible under Section
19 51.803 and each student enrolled in the junior year of high school
20 who has a grade point average in the top 10 percent of the student's
21 high school class, and the student's parent or guardian, with a
22 written notification of the student's eligibility with a detailed
23 explanation in plain language of the substance of Section 51.803.

24 (b) The commissioner shall adopt forms, including specific
25 language, to use in providing notice under Subsections (a)(2) and
26 (4). In providing notice under Subsection (a)(2) or (4), a school
27 district or open-enrollment charter school shall use the

1 appropriate form adopted by the commissioner. The notice to a
 2 student and the student's parent or guardian under Subsections
 3 (a)(2) and (4) [~~Subsection (a)(4)~~] must be on a single form that
 4 contains [~~may contain one or more~~] signature lines to indicate
 5 receipt of notice by the student and [~~or~~] the student's parent or
 6 guardian. The notice under Subsection (a)(2) must be signed by the
 7 student's counselor in addition to being signed by the student and
 8 the student's parent or guardian.

9 (b) This section applies beginning with the 2014-2015
 10 school year.

11 SECTION 19. (a) Sections 28.027(a) and (b), Education
 12 Code, are amended to read as follows:

13 (a) In this section, "applied STEM course" means an applied
 14 science, technology, engineering, or mathematics course offered as
 15 part of a school district's career and technology education or
 16 technology applications curriculum.

17 (b) The State Board of Education shall establish a process
 18 under which an applied STEM course may be reviewed and approved for
 19 purposes of satisfying the mathematics and science curriculum
 20 requirements for the foundation [~~recommended~~] high school program
 21 [~~imposed~~] under Section 28.025 [~~28.025(b-1)(1)(A)~~] through
 22 substitution of the applied STEM course for a specific mathematics
 23 or science course otherwise required under the foundation
 24 [~~recommended~~] high school program [~~and completed during the~~
 25 ~~student's fourth year of mathematics or science course work~~]. [~~The~~
 26 ~~State Board of Education may only approve a course to substitute for~~
 27 ~~a mathematics course taken after successful completion of Algebra I~~

1 ~~and geometry and after successful completion of or concurrently~~
 2 ~~with Algebra II.~~] The State Board of Education may only approve a
 3 course to substitute for a science course taken after successful
 4 completion of biology ~~[and chemistry and after successful~~
 5 ~~completion of or concurrently with physics].~~

6 (b) This section applies beginning with the 2014-2015
 7 school year.

8 SECTION 20. Section 29.081, Education Code, is amended by
 9 adding Subsections (b-1), (b-2), and (b-3) and amending Subsection
 10 (d) to read as follows:

11 (b-1) Each school district shall offer before the next
 12 scheduled administration of the assessment instrument, without
 13 cost to the student, additional accelerated instruction to each
 14 student in any subject in which the student failed to perform
 15 satisfactorily on an end-of-course assessment instrument required
 16 for graduation.

17 (b-2) A district that is required to provide accelerated
 18 instruction under Subsection (b-1) shall separately budget
 19 sufficient funds, including funds under Section 42.152, for that
 20 purpose. A district may not budget funds received under Section
 21 42.152 for any other purpose until the district adopts a budget to
 22 support additional accelerated instruction under Subsection (b-1).

23 (b-3) A district shall evaluate the effectiveness of
 24 accelerated instruction programs under Subsection (b-1) and
 25 annually hold a public hearing to consider the results.

26 (d) For purposes of this section, "student at risk of
 27 dropping out of school" includes each student who is under 26 [21]

1 years of age and who:

2 (1) was not advanced from one grade level to the next
3 for one or more school years;

4 (2) if the student is in grade 7, 8, 9, 10, 11, or 12,
5 did not maintain an average equivalent to 70 on a scale of 100 in two
6 or more subjects in the foundation curriculum during a semester in
7 the preceding or current school year or is not maintaining such an
8 average in two or more subjects in the foundation curriculum in the
9 current semester;

10 (3) did not perform satisfactorily on an assessment
11 instrument administered to the student under Subchapter B, Chapter
12 39, and who has not in the previous or current school year
13 subsequently performed on that instrument or another appropriate
14 instrument at a level equal to at least 110 percent of the level of
15 satisfactory performance on that instrument;

16 (4) if the student is in prekindergarten,
17 kindergarten, or grade 1, 2, or 3, did not perform satisfactorily on
18 a readiness test or assessment instrument administered during the
19 current school year;

20 (5) is pregnant or is a parent;

21 (6) has been placed in an alternative education
22 program in accordance with Section 37.006 during the preceding or
23 current school year;

24 (7) has been expelled in accordance with Section
25 37.007 during the preceding or current school year;

26 (8) is currently on parole, probation, deferred
27 prosecution, or other conditional release;

1 (9) was previously reported through the Public
2 Education Information Management System (PEIMS) to have dropped out
3 of school;

4 (10) is a student of limited English proficiency, as
5 defined by Section 29.052;

6 (11) is in the custody or care of the Department of
7 Protective and Regulatory Services or has, during the current
8 school year, been referred to the department by a school official,
9 officer of the juvenile court, or law enforcement official;

10 (12) is homeless as defined by 42 U.S.C. Section
11 11302, and its subsequent amendments; or

12 (13) resided in the preceding school year or resides
13 in the current school year in a residential placement facility in
14 the district, including a detention facility, substance abuse
15 treatment facility, emergency shelter, psychiatric hospital,
16 halfway house, or foster group home.

17 SECTION 21. (a) Section 29.096(e), Education Code, is
18 amended to read as follows:

19 (1) The commissioner shall establish minimum standards for
20 a local collaborative agreement, including a requirement that the
21 agreement must be signed by an authorized school district or
22 open-enrollment charter school officer and an authorized
23 representative of each of the other participating entities that is
24 a partner in the collaboration. The program must:

25 (1) limit participation in the program to students
26 authorized to participate by a parent or other person standing in
27 parental relationship;

1 (2) have as a primary goal graduation from high school
2 ~~[under at least the recommended high school program];~~

3 (3) provide for local businesses or other employers to
4 offer paid employment or internship opportunities and advanced
5 career and vocational training;

6 (4) include an outreach component and a lead
7 educational staff member to identify and involve eligible students
8 and public and private entities in participating in the program;

9 (5) serve a population of students of which at least 50
10 percent are identified as students at risk of dropping out of
11 school, as described by Section 29.081(d);

12 (6) allocate not more than 15 percent of grant funds
13 and matching funds, as determined by the commissioner, to
14 administrative expenses;

15 (7) include matching funds from any of the
16 participating entities; and

17 (8) include any other requirements as determined by
18 the council.

19 (i) This section applies beginning with the 2014-2015
20 school year.

21 SECTION 22. Section 29.182(b), Education Code, is amended
22 to read as follows:

23 (b) The state plan must include procedures designed to
24 ensure that:

25 (1) all secondary and postsecondary students have the
26 opportunity to participate in career and technology education
27 programs;

1 (2) the state complies with requirements for
2 supplemental federal career and technology education funding;
3 ~~[and]~~

4 (3) career and technology education is established as
5 a part of the total education system of this state and constitutes
6 an option for student learning that provides a rigorous course of
7 study consistent with the required curriculum under Section 28.002
8 and under which a student may receive specific education in a career
9 and technology program that:

10 (A) incorporates competencies leading to
11 academic and technical skill attainment;

12 (B) leads to:

13 (i) an industry-recognized license,
14 credential, or certificate; or

15 (ii) at the postsecondary level, an
16 associate or baccalaureate degree;

17 (C) includes opportunities for students to earn
18 college credit for coursework; and

19 (D) includes, as an integral part of the program,
20 participation by students and teachers in activities of career and
21 technical student organizations supported by the agency and the
22 State Board of Education; and

23 (4) a school district provides, to the greatest extent
24 possible, to a student participating in a career and technology
25 education program opportunities to enroll in dual credit courses
26 designed to lead to a degree, license, or certification as part of
27 the program.

1 SECTION 23. (a) Sections 29.190(a) and (c), Education
2 Code, are amended to read as follows:

3 (a) A student is entitled to a subsidy under this section
4 if:

5 (1) the student:

6 (A) successfully completes the career and
7 technology program of a school district in which the student
8 receives training and instruction for employment [~~in a current or~~
9 ~~emerging high-demand, high-wage, high-skill occupation, as~~
10 ~~determined under Subsection (c)~~]; or

11 (B) is enrolled in a special education program
12 under Subchapter A; and

13 (2) the student passes a certification examination to
14 qualify for a license or certificate [~~for the occupation; and~~

15 ~~[(3) the student submits to the district a written~~
16 ~~application in the form, time, and manner required by the district~~
17 ~~for the district to subsidize the cost of an examination described~~
18 ~~by Subdivision (2)].~~

19 (c) On approval by the commissioner, the agency shall pay
20 each school district an amount equal to the cost paid by the
21 district [~~or student~~] for the certification examination. To obtain
22 reimbursement for a subsidy paid under this section, a district
23 must:

24 (1) pay the fee for the examination [~~or pay the student~~
25 ~~the amount of the fee paid by the student for the examination~~]; and

26 (2) submit to the commissioner a written application
27 on a form prescribed by the commissioner stating the amount of the

1 fee paid under Subdivision (1) for the certification examination.

2 (b) This section applies beginning with the 2013-2014
3 school year.

4 SECTION 24. (a) Section 29.402(b), Education Code, is
5 amended to read as follows:

6 (b) A person who is under 26 years of age is eligible to
7 enroll in a dropout recovery program under this subchapter if the
8 person:

9 (1) must complete not more than three course credits
10 to complete the curriculum requirements for the foundation
11 ~~[minimum, recommended, or advanced]~~ high school program~~[, as~~
12 ~~appropriate,]~~ for high school graduation; or

13 (2) has failed to perform satisfactorily on an
14 end-of-course assessment instrument administered under Section
15 39.023(c) or an assessment instrument administered under Section
16 39.023(c) as that section existed before amendment by Chapter 1312
17 (S.B. 1031), Acts of the 80th Legislature, Regular Session, 2007.

18 (b) This section applies beginning with the 2014-2015
19 school year.

20 SECTION 25. (a) Section 29.904(d), Education Code, is
21 amended to read as follows:

22 (d) A plan developed under this section:

23 (1) must establish clear, achievable goals for
24 increasing the percentage of the school district's graduating
25 seniors, particularly the graduating seniors attending a high
26 school described by Subsection (a), who enroll in an institution of
27 higher education for the academic year following graduation;

1 (2) must establish an accurate method of measuring
2 progress toward the goals established under Subdivision (1) that
3 may include the percentage of district high school students and the
4 percentage of students attending a district high school described
5 by Subsection (a) who:

6 (A) are enrolled in a course for which a student
7 may earn college credit, such as an advanced placement or
8 international baccalaureate course or a course offered through
9 concurrent enrollment in high school and at an institution of
10 higher education;

11 (B) are enrolled in courses that meet the
12 curriculum requirements for the distinguished level of achievement
13 under the foundation [~~recommended or advanced~~] high school program
14 as determined under Section 28.025;

15 (C) have submitted a free application for federal
16 student aid (FAFSA);

17 (D) are exempt under Section 51.3062(p) or (q)
18 from administration of an assessment instrument under Section
19 51.3062 or have performed successfully on an assessment instrument
20 under Section 51.3062;

21 (E) graduate from high school;

22 (F) graduate from an institution of higher
23 education; and

24 (G) have taken college entrance examinations and
25 the average score of those students on the examinations;

26 (3) must cover a period of at least five years; and

27 (4) may be directed at district students at any level

1 of primary or secondary education.

2 (b) This section applies beginning with the 2014-2015
3 school year.

4 SECTION 26. (a) Section 31.0211(c), Education Code, is
5 amended to read as follows:

6 (c) Subject to Subsection (d), funds allotted under this
7 section may be used to:

8 (1) purchase:

9 (A) materials on the list adopted by the
10 commissioner, as provided by Section 31.0231;

11 (B) instructional materials, regardless of
12 whether the instructional materials are on the list adopted under
13 Section 31.024;

14 (C) consumable instructional materials,
15 including workbooks;

16 (D) instructional materials for use in bilingual
17 education classes, as provided by Section 31.029;

18 (E) instructional materials for use in college
19 preparatory courses under Section 28.014, as provided by Section
20 31.031,

21 (F) supplemental instructional materials, as
22 provided by Section 31.035;

23 (G) ~~[(F)]~~ state-developed open-source
24 instructional materials, as provided by Subchapter B-1;

25 (H) ~~[(G)]~~ instructional materials and
26 technological equipment under any continuing contracts of the
27 district in effect on September 1, 2011; and

1 (1) ~~[(H)]~~ technological equipment necessary to
2 support the use of materials included on the list adopted by the
3 commissioner under Section 31.0231 or any instructional materials
4 purchased with an allotment under this section; and

5 (2) pay:

6 (A) for training educational personnel directly
7 involved in student learning in the appropriate use of
8 instructional materials and for providing for access to
9 technological equipment for instructional use; and

10 (B) the salary and other expenses of an employee
11 who provides technical support for the use of technological
12 equipment directly involved in student learning.

13 (b) This section applies beginning with the 2014-2015
14 school year.

15 SECTION 27. Subchapter B, Chapter 31, Education Code, is
16 amended by adding Section 31.0215 to read as follows:

17 Sec. 31.0215. INSTRUCTIONAL MATERIAL ALLOTMENT PURCHASES.

18 (a) The commissioner shall, as early as practicable during each
19 fiscal year, notify each school district and open-enrollment
20 charter school of the estimated amount to which the district or
21 charter school will be entitled under Section 31.0211 during the
22 next fiscal year.

23 (b) The commissioner may allow a school district or
24 open-enrollment charter school to place an order for instructional
25 materials before the beginning of a fiscal year and to receive
26 instructional materials before payment. The commissioner shall
27 limit the cost of an order placed under this section to 80 percent

1 of the estimated amount to which a school district or
 2 open-enrollment charter school is estimated to be entitled as
 3 provided by Subsection (a) and shall first credit any balance in a
 4 district or charter school instructional materials account to pay
 5 for an order placed under this section.

6 (c) The commissioner shall make payments for orders placed
 7 under this section as funds become available to the instructional
 8 materials fund and shall prioritize payment of orders placed under
 9 this section over reimbursement of purchases made directly by a
 10 school district or open-enrollment charter school.

11 (d) The commissioner shall ensure that publishers of
 12 instructional materials are informed of any potential delay in
 13 payment and that payment is subject to the availability of
 14 appropriated funds. A publisher may decline to accept an order
 15 placed under this section.

16 (e) Chapter 2251, Government Code, does not apply to
 17 purchases of instructional materials under this section.

18 (f) The commissioner may adopt rules to implement this
 19 section.

20 SECTION 28. (a) Subchapter B, Chapter 31, Education Code,
 21 is amended by adding Section 31.031 to read as follows:

22 Sec. 31.031. COLLEGE PREPARATORY INSTRUCTIONAL MATERIALS.

23 (a) A school district may purchase with the district's
 24 instructional materials allotment or otherwise acquire
 25 instructional materials for use in college preparatory courses
 26 under Section 28.014.

27 (b) The commissioner shall adopt rules regarding the

1 purchase of instructional materials under this section.

2 (b) This section applies beginning with the 2014-2015
3 school year.

4 SECTION 29. (a) The heading to Section 33.007, Education
5 Code, is amended to read as follows:

6 Sec. 33.007. COUNSELING REGARDING POSTSECONDARY [~~HIGHER~~]
7 EDUCATION.

8 (b) This section takes effect beginning with the 2014-2015
9 school year.

10 SECTION 30. (a) Sections 33.007(a) and (b), Education
11 Code, are amended to read as follows:

12 (a) Each school counselor at an elementary, middle, or
13 junior high school, including an open-enrollment charter school
14 offering those grades, shall advise students and their parents or
15 guardians regarding the importance of postsecondary [~~higher~~]
16 education, coursework designed to prepare students for
17 postsecondary [~~higher~~] education, and financial aid availability
18 and requirements.

19 (b) During the first school year a student is enrolled in a
20 high school or at the high school level in an open-enrollment
21 charter school, and again during each [~~a student's senior~~] year of a
22 student's enrollment in high school or at the high school level, a
23 school counselor shall provide information about postsecondary
24 [~~higher~~] education to the student and the student's parent or
25 guardian. The information must include information regarding:

26 (1) the importance of postsecondary [~~higher~~]
27 education;

1 (2) the advantages of earning an endorsement and a
2 performance acknowledgment and completing the distinguished level
3 of achievement under the foundation [~~recommended or advanced~~] high
4 school program [~~adopted~~] under Section 28.025 [~~28.025(a)~~];

5 (3) the disadvantages of taking courses to prepare for
6 a high school equivalency examination relative to the benefits of
7 taking courses leading to a high school diploma;

8 (4) financial aid eligibility;

9 (5) instruction on how to apply for federal financial
10 aid;

11 (6) the center for financial aid information
12 established under Section 61.0776;

13 (7) the automatic admission of certain students to
14 general academic teaching institutions as provided by Section
15 51.803;

16 (8) the eligibility and academic performance
17 requirements for the TEXAS Grant as provided by Subchapter M,
18 Chapter 56; and

19 (9) the availability of programs in the district under
20 which a student may earn college credit, including advanced
21 placement programs, dual credit programs, joint high school and
22 college credit programs, and international baccalaureate programs.

23 (b) This section applies beginning with the 2014-2015
24 school year.

25 SECTION 31. (a) Section 39.023, Education Code, is amended
26 by amending Subsections (a-2), (b), (c), (c-3), (e), and (h) and
27 adding Subsections (b-1), (e-1), (e-2), and (e-3) to read as

1 follows:

2 (a-2) Except as required by federal law, a [A] student is
3 not required to be assessed in a subject otherwise assessed at the
4 student's grade level under Subsection (a) if the student:

5 (1) is enrolled in a course in the subject intended for
6 students above the student's grade level and will be administered
7 an assessment instrument adopted or developed under Subsection (a)
8 that aligns with the curriculum for the course in which the student
9 is enrolled; or

10 (2) is enrolled in a course in the subject for which
11 the student will receive high school academic credit and will be
12 administered an end-of-course assessment instrument adopted under
13 Subsection (c) for the course.

14 (b) The agency shall develop or adopt appropriate
15 criterion-referenced alternative assessment instruments to be
16 administered to each student in a special education program under
17 Subchapter A, Chapter 29, for whom an assessment instrument adopted
18 under Subsection (a), even with allowable accommodations, would not
19 provide an appropriate measure of student achievement, as
20 determined by the student's admission, review, and dismissal
21 committee, including assessment instruments approved by the
22 commissioner that measure growth. The assessment instruments
23 developed or adopted under this subsection, including the
24 assessment instruments approved by the commissioner, must, to the
25 extent allowed under federal law, provide a district with options
26 for the assessment of students under this subsection.

27 (b-1) The agency, in conjunction with appropriate

1 interested persons, shall redevelop assessment instruments adopted
2 or developed under Subsection (b) for administration to
3 significantly cognitively disabled students in a manner consistent
4 with federal law. An assessment instrument under this subsection
5 may not require a teacher to prepare tasks or materials for a
6 student who will be administered such an assessment instrument.
7 Assessment instruments adopted or developed under this subsection
8 shall be administered not later than the 2014-2015 school year.

9 (c) The agency shall also adopt end-of-course assessment
10 instruments for secondary-level courses in Algebra I, ~~[Algebra II,~~
11 ~~geometry,]~~ biology, ~~[chemistry, physics,]~~ English I, English II,
12 ~~[English III, world geography, world history,]~~ and United States
13 history. The Algebra I ~~], Algebra II, and geometry]~~ end-of-course
14 assessment instrument [instruments] must be administered with the
15 aid of technology. The English I and English II end-of-course
16 assessment instruments must each assess essential knowledge and
17 skills in both reading and writing in the same assessment
18 instrument and must provide a single score. A school district shall
19 comply with State Board of Education rules regarding administration
20 of the assessment instruments listed in this subsection ~~[and shall~~
21 ~~adopt a policy that requires a student's performance on an~~
22 ~~end-of-course assessment instrument for a course listed in this~~
23 ~~subsection in which the student is enrolled to account for 15~~
24 ~~percent of the student's final grade for the course. If a student~~
25 ~~retakes an end-of-course assessment instrument for a course listed~~
26 ~~in this subsection, as provided by Section 39.025, a school~~
27 ~~district is not required to use the student's performance on the~~

1 ~~subsequent administration or administrations of the assessment~~
2 ~~instrument to determine the student's final grade for the course].~~

3 If a student is in a special education program under Subchapter A,
4 Chapter 29, the student's admission, review, and dismissal
5 committee shall determine whether any allowable modification is
6 necessary in administering to the student an assessment instrument
7 required under this subsection. The State Board of Education shall
8 administer the assessment instruments. The State Board of
9 Education shall adopt a schedule for the administration of
10 end-of-course assessment instruments that complies with the
11 requirements of Subsection (c-3).

12 (c-3) In adopting a schedule for the administration of
13 assessment instruments under this section, the State Board of
14 Education shall require:

15 (1) assessment instruments administered under
16 Subsection (a) to be administered on a schedule so that the first
17 assessment instrument is administered at least two weeks later than
18 the date on which the first assessment instrument was administered
19 under Subsection (a) during the 2006-2007 school year; and

20 (2) the spring administration of end-of-course
21 assessment instruments under Subsection (c) to occur in each school
22 district not earlier than the first full week in May, except that
23 the spring administration of the end-of-course assessment
24 instruments in English I and [7] English II [~~and English III~~] must
25 be permitted to occur at an earlier date.

26 (e) Under rules adopted by the State Board of Education,
27 every third year, the agency shall release the questions and answer

1 keys to each assessment instrument administered under Subsection
2 (a), (b), (c), (d), or (l), excluding any assessment instrument
3 administered to a student for the purpose of retaking the
4 assessment instrument, after the last time the instrument is
5 administered for that school year. To ensure a valid bank of
6 questions for use each year, the agency is not required to release a
7 question that is being field-tested and was not used to compute the
8 student's score on the instrument. The agency shall also release,
9 under board rule, each question that is no longer being
10 field-tested and that was not used to compute a student's score.
11 During the 2014-2015 and 2015-2016 school years, the agency shall
12 release the questions and answer keys to assessment instruments as
13 described by this subsection each year.

14 (e-1) Under rules adopted by the commissioner, for the
15 2012-2013 school year, the agency each year shall release the
16 questions and answer keys to each assessment instrument
17 administered under Subsection (a), (c), (d), or (l), excluding any
18 assessment instrument administered to a student for the purpose of
19 retaking the assessment instrument, after the last time the
20 instrument is administered for that school year. This subsection
21 expires December 31, 2013.

22 (e-2) Under rules adopted by the commissioner, for the
23 2013-2014 school year, the agency each year shall release the
24 questions and answer keys to each assessment instrument
25 administered under Subsection (b), (c), or (l), excluding any
26 assessment instrument administered to a student for the purpose of
27 retaking the assessment instrument and any assessment instrument

1 covering a subject or course for which the questions and answer keys
2 for the 2012-2013 assessment instrument covering that subject or
3 course were released, after the last time the instrument is
4 administered for the 2013-2014 school year. This subsection expires
5 December 31, 2014.

6 (e-3) Under rules adopted by the commissioner, for the
7 2013-2014 school year, the agency each year shall release the
8 questions and answer keys to each assessment instrument
9 administered under Subsection (a), (b), (c), (d), or (l) during the
10 2013-2014 school year after the last time any assessment instrument
11 is administered for the 2013-2014 school year. This subsection
12 expires December 31, 2014.

13 (h) The agency shall notify school districts and campuses of
14 the results of assessment instruments administered under this
15 section ~~[at the earliest possible date determined by the State~~
16 ~~Board of Education, but]~~ not later than the 21st day after the date
17 the assessment instrument is administered ~~[beginning of the~~
18 ~~subsequent school year]~~. The school district shall disclose to
19 each district teacher the results of assessment instruments
20 administered to students taught by the teacher in the subject for
21 the school year in which the assessment instrument is administered.

22 (b) This section applies beginning with the 2013-2014
23 school year.

24 SECTION 32. (a) Section 39.0232, Education Code, is
25 amended to read as follows:

26 Sec. 39.0232. USE OF END-OF-COURSE ASSESSMENT INSTRUMENT AS
27 PLACEMENT INSTRUMENT; CERTAIN USES PROHIBITED. (a) To the extent

1 practicable, the agency shall ensure that any high school
2 end-of-course assessment instrument developed by the agency is
3 developed in such a manner that the assessment instrument may be
4 used to determine the appropriate placement of a student in a course
5 of the same subject matter at an institution of higher education.

6 (b) A student's performance on an end-of-course assessment
7 instrument may not be used:

8 (1) in determining the student's class ranking for any
9 purpose, including entitlement to automatic college admission
10 under Section 51.803 or 51.804, or

11 (2) as a sole criterion in the determination of
12 whether to admit the student to a general academic teaching
13 institution in this state.

14 (c) Subsection (b)(2) does not prohibit a general academic
15 teaching institution from implementing an admission policy that
16 takes into consideration a student's performance on an
17 end-of-course assessment instrument in addition to other criteria.

18 (d) In this section, "general academic teaching
19 institution" has the meaning assigned by Section 61.003.

20 (b) This section applies beginning with the 2013-2014
21 school year.

22 SECTION 33. (a) Section 39.0233(a), Education Code, is
23 amended to read as follows:

24 (a) The agency, in coordination with the Texas Higher
25 Education Coordinating Board, shall adopt a series of questions to
26 be included in an end-of-course assessment instrument administered
27 under Section 39.023(c) to be used for purposes of Section 51.3062.

1 The questions adopted under this subsection must be developed in a
2 manner consistent with any college readiness standards adopted
3 under Sections 39.233 [~~39.113~~] and 51.3062.

4 (b) This section applies beginning with the 2013-2014
5 school year.

6 SECTION 34. (a) Subchapter B, Chapter 39, Education Code,
7 is amended by adding Section 39.0238 to read as follows:

8 Sec. 39.0238. ADOPTION AND ADMINISTRATION OF POSTSECONDARY
9 READINESS ASSESSMENT INSTRUMENTS. (a) In addition to other
10 assessment instruments adopted and developed under this
11 subchapter, the agency shall adopt or develop appropriate
12 postsecondary readiness assessment instruments for Algebra II and
13 English III that a school district may administer at the district's
14 option.

15 (b) To the extent practicable, the agency shall ensure that
16 each postsecondary readiness assessment instrument:

17 (1) assesses essential knowledge and skills and
18 growth;

19 (2) is developed in a manner that measures a student's
20 performance under the college readiness standards established
21 under Section 28.008; and

22 (3) is validated by national postsecondary education
23 experts for college readiness content and performance standards.

24 (c) In adopting a schedule for the administration of
25 postsecondary readiness assessment instruments under this section,
26 the State Board of Education shall require the annual
27 administration of the postsecondary readiness assessment

1 instruments to occur not earlier than the second full week in May.

2 (d) The agency shall adopt a policy requiring each school
3 district that elects to administer postsecondary readiness
4 assessment instruments under Subsection (a) to annually:

5 (1) administer the applicable postsecondary readiness
6 assessment instrument to each student enrolled in a course for
7 which a postsecondary readiness assessment instrument is adopted or
8 developed under Subsection (a), including applied Algebra II; and

9 (2) report the results of the postsecondary readiness
10 assessment instruments to the agency.

11 (e) The agency shall annually deliver a report to the
12 governor, the lieutenant governor, the speaker of the house of
13 representatives, and the presiding officers of the standing
14 committees of the legislature with jurisdiction over public
15 education. The report must include a summary of student performance
16 on the preceding year's postsecondary readiness assessment
17 instruments.

18 (f) The results of a postsecondary readiness assessment
19 instrument administered under this section may not be used by:

20 (1) the agency for accountability purposes for a
21 school campus or school district;

22 (2) a school district:

23 (A) for the purpose of teacher evaluations; or

24 (B) in determining a student's final course grade
25 or determining a student's class rank for the purpose of high school
26 graduation; or

27 (3) an institution of higher education:

1 (A) for admission purposes; or

2 (B) to determine eligibility for a TEXAS grant.

3 (g) A school district may not administer an additional
 4 benchmark assessment instrument solely for the purpose of preparing
 5 for a postsecondary readiness assessment instrument administered
 6 under this section. In this subsection, "benchmark assessment
 7 instrument" means a district-required assessment instrument
 8 designed to prepare students for a postsecondary readiness
 9 assessment instrument administered under this section.

10 (h) The agency shall acknowledge a school district that
 11 elects to administer the postsecondary readiness assessment
 12 instruments as provided by Subsection (a).

13 (b) This section applies beginning with the 2015-2016
 14 school year.

15 SECTION 35. (a) Section 39.025, Education Code, is amended
 16 by amending Subsections (a), (a-1), (b), and (b-2) and adding
 17 Subsection (a-4) to read as follows:

18 (a) The commissioner shall adopt rules requiring a student
 19 participating in the recommended or advanced high school program to
 20 be administered each end-of-course assessment instrument listed in
 21 Section 39.023(c) and requiring a student participating in the
 22 minimum high school program to be administered an end-of-course
 23 assessment instrument listed in Section 39.023(c) only for a course
 24 in which the student is enrolled and for which an end-of-course
 25 assessment instrument is administered. A student is required to
 26 achieve~~[, in each subject in the foundation curriculum under~~
 27 ~~Section 28.002(a)(1), a cumulative score that is at least equal to~~

1 ~~the product of the number of end-of-course assessment instruments~~
2 ~~administered to the student in that subject and]~~ a scale score that
3 indicates satisfactory performance, as determined by the
4 commissioner under Section 39.0241(a), on each end-of-course
5 assessment instrument listed under Section 39.023(c) that is
6 administered to the student as provided by this subsection. For
7 each scale score required under this subsection that is not based on
8 a 100-point scale scoring system, the commissioner shall provide
9 for conversion, in accordance with commissioner rule, of the scale
10 score to an equivalent score based on a 100-point scale scoring
11 system. ~~[A student must achieve a minimum score as determined by~~
12 ~~the commissioner to be within a reasonable range of the scale score~~
13 ~~under Section 39.0241(a) on an end-of-course assessment instrument~~
14 ~~for the score to count towards the student's cumulative score. For~~
15 ~~purposes of this subsection, a student's cumulative score is~~
16 ~~determined using the student's highest score on each end-of-course~~
17 ~~assessment instrument administered to the student.]~~ A student may
18 not receive a high school diploma until the student has performed
19 satisfactorily on ~~[the]~~ end-of-course assessment instruments in
20 the manner provided under this subsection. This subsection does
21 not require a student to demonstrate readiness to enroll in an
22 institution of higher education.

23 (a-1) A student enrolled in a college preparatory course
24 under Section 28.014 who satisfies the Texas Success Initiative
25 (TSI) college readiness benchmarks prescribed by the Texas Higher
26 Education Coordinating Board under Section 51.3062(f) on an
27 assessment instrument designated by the Texas Higher Education

1 Coordinating Board under Section 51.3062(c) administered at the end
2 of the college preparatory course satisfies the requirements
3 concerning an end-of-course assessment in an equivalent course as
4 prescribed by Subsection (a). The commissioner ~~[by rule]~~ shall
5 determine a method by which a student's satisfactory performance on
6 an advanced placement test, an international baccalaureate
7 examination, an SAT Subject Test, the SAT, the ACT, or any
8 nationally recognized norm-referenced ~~[another]~~ assessment
9 instrument used by institutions of higher education to award course
10 credit based on satisfactory performance on the ~~[determined by the~~
11 ~~commissioner to be at least as rigorous as an end-of-course]~~
12 assessment instrument shall ~~[adopted under Section 39.023(c) may]~~
13 be used to satisfy ~~[as a factor in determining whether the student~~
14 ~~satisfies]~~ the requirements concerning an end-of-course assessment
15 instrument in an equivalent course as prescribed by ~~[of]~~ Subsection
16 (a) ~~[, including the cumulative score requirement of that~~
17 ~~subsection]~~. The commissioner shall ~~[by rule may]~~ determine a
18 method by which a student's satisfactory performance on the PSAT ~~[a~~
19 ~~Preliminary Scholastic Assessment Test (PSAT) assessment]~~ or the
20 ACT-Plan shall ~~[a preliminary American College Test (ACT)~~
21 ~~assessment may]~~ be used to satisfy ~~[as a factor in determining~~
22 ~~whether the student satisfies]~~ the requirements concerning an
23 end-of-course assessment instrument in an equivalent course as
24 prescribed by ~~[of]~~ Subsection (a). A student who fails to perform
25 satisfactorily on a test or other assessment instrument authorized
26 under this subsection, other than the PSAT or the ACT-Plan, may
27 retake that test or other assessment instrument for purposes of

1 this subsection or may take the appropriate end-of-course
2 assessment instrument. A student who fails to perform
3 satisfactorily on the PSAT or the ACT-Plan must take the
4 appropriate end-of-course assessment instrument. The commissioner
5 shall adopt rules as necessary for the administration of this
6 subsection.

7 (a-4) The admission, review, and dismissal committee of a
8 student in a special education program under Subchapter A, Chapter
9 29, shall determine whether, to receive a high school diploma, the
10 student is required to achieve satisfactory performance on
11 end-of-course assessment instruments.

12 (b) Each time an end-of-course assessment instrument
13 adopted under Section 39.023(c) is administered, a student who
14 failed to achieve a [minimum] score requirement under Subsection
15 (a) may [shall] retake the assessment instrument. [A student who
16 fails to perform satisfactorily on an Algebra II or English III
17 end-of-course assessment instrument under the college readiness
18 performance standard, as provided under Section 39.024(b), may
19 retake the assessment instrument. Any other student may retake an
20 end-of-course assessment instrument for any reason.] A student is
21 not required to retake a course as a condition of retaking an
22 end-of-course assessment instrument.

23 (b-2) If a school district determines that a student, on
24 completion of grade 11, is unlikely to achieve the [cumulative]
25 score requirement under Subsection (a) [requirements] for one or
26 more end-of-course assessment instruments administered to the
27 student as provided [subjects prescribed] by Subsection (a) for

1 receiving a high school diploma, the district shall require the
 2 student to enroll in a corresponding content-area college
 3 preparatory course for which an end-of-course assessment
 4 instrument has been adopted, if available. A student who enrolls in
 5 a college preparatory course described by this subsection shall be
 6 administered an end-of-course assessment instrument for the
 7 course, with the end-of-course assessment instrument scored on a
 8 scale as determined by the commissioner ~~[not to exceed 20 percent of~~
 9 ~~the cumulative score requirements required to graduate as~~
 10 ~~determined under Subsection (a)].~~ A student may use the student's
 11 score on the end-of-course assessment instrument for the college
 12 preparatory course towards satisfying the ~~[cumulative]~~ score
 13 requirement ~~[requirements]~~ prescribed by Subsection (a).

14 (b) This section applies beginning with the 2013-2014
 15 school year.

16 SECTION 39. (a) Effective September 1, 2014, Section
 17 39.025(a), Education Code, is amended to read as follows:

18 (a) The commissioner shall adopt rules requiring a student
 19 ~~[participating]~~ in the foundation ~~[recommended or advanced]~~ high
 20 school program under Section 28.025 to be administered each
 21 end-of-course assessment instrument listed in Section 39.023(c)
 22 ~~[and requiring a student participating in the minimum high school~~
 23 ~~program to be administered an end-of-course assessment instrument~~
 24 ~~listed in Section 39.023(c) only for a course in which the student~~
 25 ~~is enrolled and for which an end-of-course assessment instrument is~~
 26 ~~administered]~~. A student is required to achieve~~[, in each subject~~
 27 ~~in the foundation curriculum under Section 28.002(a)(1), a~~

~~1 cumulative score that is at least equal to the product of the number~~
~~2 of end-of-course assessment instruments administered to the~~
~~3 student in that subject and] a scale score that indicates~~
 4 satisfactory performance, as determined by the commissioner under
 5 Section 39.0241(a), on each end-of-course assessment instrument
 6 listed under Section 39.023(c). For each scale score required
 7 under this subsection that is not based on a 100-point scale scoring
 8 system, the commissioner shall provide for conversion, in
 9 accordance with commissioner rule, of the scale score to an
 10 equivalent score based on a 100-point scale scoring system. [A
~~11 student must achieve a minimum score as determined by the~~
~~12 commissioner to be within a reasonable range of the scale score~~
~~13 under Section 39.0241(a) on an end-of-course assessment instrument~~
~~14 for the score to count towards the student's cumulative score. For~~
~~15 purposes of this subsection, a student's cumulative score is~~
~~16 determined using the student's highest score on each end-of-course~~
~~17 assessment instrument administered to the student.] A student may~~
 18 not receive a high school diploma until the student has performed
 19 satisfactorily on [the] end-of-course assessment instruments in
 20 the manner provided under this subsection. This subsection does
 21 not require a student to demonstrate readiness to enroll in an
 22 institution of higher education.

23 (b) This section applies beginning with the 2014-2015
 24 school year.

25 SECTION 37. (a) Subchapter B, Chapter 39, Education Code,
 26 is amended by adding Section 39.0263 to read as follows:

27 Sec. 39.0263. ADMINISTRATION OF DISTRICT-REQUIRED

1 BENCHMARK ASSESSMENT INSTRUMENTS TO PREPARE STUDENTS FOR
2 STATE-ADMINISTERED ASSESSMENT INSTRUMENTS. (a) In this section,
3 "benchmark assessment instrument" means a district-required
4 assessment instrument designed to prepare students for a
5 corresponding state-administered assessment instrument.

6 (b) Except as provided by Subsection (c), a school district
7 may not administer to any student more than two benchmark
8 assessment instruments to prepare the student for a corresponding
9 state-administered assessment instrument.

10 (c) The prohibition prescribed by this section does not
11 apply to the administration of a college preparation assessment
12 instrument, including the PSAT, the ACT-Plan, the SAT, or the ACT,
13 an advanced placement test, an international baccalaureate
14 examination, or an independent classroom examination designed or
15 adopted and administered by a classroom teacher.

16 (d) A parent of or person standing in parental relation to a
17 student who has special needs, as determined in accordance with
18 commissioner rule, may request administration to the student of
19 additional benchmark assessment instruments.

20 (b) This section applies beginning with the 2013-2014
21 school year.

22 SECTION 38. (a) Section 39.027, Education Code, is amended
23 by adding Subsection (a-2) to read as follows:

24 (a-2) Unless a student is enrolled in a school in the United
25 States for a period of at least 60 consecutive days during a year,
26 the student may not be considered to be enrolled in a school in the
27 United States for that year for the purpose of determining a number

1 of years under Subsection (a)(1), (2), or (3).

2 (b) This section applies beginning with the 2013-2014
3 school year.

4 SECTION 39. Section 39.0301, Education Code, is amended by
5 adding Subsection (a-1) to read as follows:

6 (a-1) In establishing procedures under Subsection (a)(1)
7 for the administration of assessment instruments, the commissioner
8 shall ensure that the procedures are designed to minimize
9 disruptions to school operations and the classroom environment. In
10 implementing the procedures established under Subsection (a)(1)
11 for the administration of assessment instruments, a school district
12 shall minimize disruptions to school operations and the classroom
13 environment.

14 SECTION 40. Subchapter B, Chapter 39, Education Code, is
15 amended by adding Section 39.038 to read as follows:

16 Sec. 39.038. RESTRICTION ON APPOINTMENTS TO ADVISORY
17 COMMITTEES. The commissioner may not appoint a person to a
18 committee or panel that advises the commissioner or agency
19 regarding state accountability systems under this title or the
20 content or administration of an assessment instrument if the person
21 is retained or employed by an assessment instrument vendor.

22 SECTION 41. (a) Subchapter B, Chapter 39, Education Code,
23 is amended by adding Section 39.039 to read as follows:

24 Sec. 39.039. PROHIBITION ON POLITICAL CONTRIBUTION OR
25 ACTIVITY BY CERTAIN CONTRACTORS. (a) A person who is an agent of an
26 entity that has been contracted to develop or implement assessment
27 instruments required under Section 39.023 commits an offense if the

1 person makes or authorizes a political contribution to or takes
2 part in, directly or indirectly, the campaign of any person seeking
3 election to or serving on the State Board of Education.

4 (b) A person who is an agent of an entity that has been
5 contracted to develop or implement assessment instruments required
6 under Section 39.023 commits an offense if the person serves as a
7 member of a formal or informal advisory committee established by
8 the commissioner, agency staff, or the State Board of Education to
9 advise the commissioner, agency staff, or the State Board of
10 Education regarding policies or implementation of the requirements
11 of this subchapter.

12 (c) An offense under this section is a Class B misdemeanor.

13 (b) This section applies September 1, 2013.

14 SECTION 42. (a) Section 39.053, Education Code, is amended
15 by amending Subsections (c) and (g-1) and adding Subsections (c-1)
16 and (c-2) to read as follows:

17 (c) Indicators of student achievement adopted under this
18 section must include:

19 (1) the results of assessment instruments required
20 under Sections 39.023(a), (c), and (1), including the results of
21 assessment instruments required for graduation retaken by a
22 student, aggregated across grade levels by subject area, including:

23 (A) for the performance standard determined by
24 the commissioner under Section 39.0241(a):

25 (i) the percentage of students who
26 performed satisfactorily on the assessment instruments, aggregated
27 across grade levels by subject area; and

1 (ii) for students who did not perform
2 satisfactorily, the percentage of students who met the standard for
3 annual improvement, as determined by the agency under Section
4 39.034, on the assessment instruments, aggregated across grade
5 levels by subject area; and

6 (B) for the college readiness performance
7 standard as determined under Section 39.0241:

8 (i) the percentage of students who
9 performed satisfactorily on the assessment instruments, aggregated
10 across grade levels by subject area; and

11 (ii) for students who did not perform
12 satisfactorily, the percentage of students who met the standard for
13 annual improvement, as determined by the agency under Section
14 39.034, on the assessment instruments, aggregated across grade
15 levels by subject area;

16 (2) dropout rates, including dropout rates and
17 district completion rates for grade levels 9 through 12, computed
18 in accordance with standards and definitions adopted by the
19 National Center for Education Statistics of the United States
20 Department of Education; ~~and~~

21 (3) high school graduation rates, computed in
22 accordance with standards and definitions adopted in compliance
23 with the No Child Left Behind Act of 2001 (20 U.S.C. Section 6301 et
24 seq.);

25 (4) the percentage of students who successfully
26 completed the curriculum requirements for the distinguished level
27 of achievement under the foundation high school program;

1 (5) the percentage of students who successfully
 2 completed the curriculum requirements for an endorsement under
 3 Section 28.025(c-1); and

4 (6) at least three additional indicators of student
 5 achievement to evaluate district and campus performance, which must
 6 include either:

7 (A) the percentage of students who satisfy the
 8 Texas Success Initiative (TSI) college readiness benchmarks
 9 prescribed by the Texas Higher Education Coordinating Board under
 10 Section 51.3062(f) on an assessment instrument in reading,
 11 writing, or mathematics designated by the Texas Higher Education
 12 Coordinating Board under Section 51.3062(c); or

13 (B) the number of students who earn:
 14 (i) at least 12 hours of postsecondary
 15 credit required for the foundation high school program under
 16 Section 28.025 or to earn an endorsement under Section 28.025(c-1);
 17 (ii) at least 30 hours of postsecondary
 18 credit required for the foundation high school program under
 19 Section 28.025 or to earn an endorsement under Section 28.025(c-1);
 20 (iii) an associate's degree; or
 21 (iv) an industry certification.

22 (c-1) An indicator adopted under Subsection (c) that would
 23 measure improvements in student achievement cannot negatively
 24 affect the commissioner's review of a school district or campus if
 25 that district or campus is already achieving at the highest level
 26 for that indicator.

27 (c-2) The commissioner by rule shall determine a method by

1 which a student's performance may be included in determining the
2 performance rating of a school district or campus under Section
3 39.054 if, before the student graduates, the student:

4 (1) satisfies the Texas Success Initiative (TSI)
5 college readiness benchmarks prescribed by the Texas Higher
6 Education Coordinating Board under Section 51.3062(f) on an
7 assessment instrument designated by the Texas Higher Education
8 Coordinating Board under Section 51.3062(c); or

9 (2) performs satisfactorily on an assessment
10 instrument under Section 39.023(c), notwithstanding Subsection
11 (d).

12 (g-1) In computing dropout and completion rates under
13 Subsection (c)(2), the commissioner shall exclude:

14 (1) students who are ordered by a court to attend a
15 high school equivalency certificate program but who have not yet
16 earned a high school equivalency certificate;

17 (2) students who were previously reported to the state
18 as dropouts, including a student who is reported as a dropout,
19 reenrolls, and drops out again, regardless of the number of times of
20 reenrollment and dropping out;

21 (3) students in attendance who are not in membership
22 for purposes of average daily attendance;

23 (4) students whose initial enrollment in a school in
24 the United States in grades 7 through 12 was as unschooled refugees
25 or asylees as defined by Section 39.027(a-1);

26 (5) students who are in the district exclusively as a
27 function of having been detained at a county detention facility but

1 are otherwise not students of the district in which the facility is
2 located; and

3 (6) students who are incarcerated in state jails and
4 federal penitentiaries as adults and as persons certified to stand
5 trial as adults.

6 (b) This section applies beginning with the 2013-2014
7 school year.

8 SECTION 43. (a) Section 39.053(f), Education Code, is
9 amended to read as follows:

10 (f) Annually, the commissioner shall define the state
11 standard for the current school year for each student achievement
12 indicator described by Subsection (c) and shall project the state
13 standards for each indicator for the following two school years.
14 The commissioner shall periodically raise the state standards for
15 the student achievement indicator described by Subsection
16 (c)(1)(B)(i) for accreditation as necessary to reach the goals of
17 achieving, by not later than the 2019-2020 school year:

18 (1) student performance in this state, disaggregated
19 by race, ethnicity, and socioeconomic status, that ranks nationally
20 in the top 10 states in terms of college readiness; and

21 (2) student performance, ~~[including the percentage of~~
22 ~~students graduating under the recommended or advanced high school~~
23 ~~program]~~ with no significant achievement gaps by race, ethnicity,
24 and socioeconomic status.

25 (b) This section applies beginning with the 2014-2015
26 school year.

27 SECTION 44. (a) Section 39.054(a), Education Code, is

1 amended to read as follows:

2 (a) The commissioner shall adopt rules to evaluate school
3 district and campus performance and~~[, not later than August 8 of~~
4 ~~each year,]~~ assign each district ~~[and campus]~~ a performance rating
5 of A, B, C, D, or F. In adopting rules under this subsection, the
6 commissioner shall determine the criteria for each designated
7 letter performance rating. A district performance rating of A, B,
8 or C [that] reflects acceptable performance and a district
9 performance rating of D or F reflects [ex] unacceptable
10 performance. The commissioner shall also assign each campus a
11 performance rating of exemplary, recognized, acceptable, or
12 unacceptable. A campus performance rating of exemplary,
13 recognized, or acceptable reflects acceptable performance, and a
14 campus performance rating of unacceptable reflects unacceptable
15 performance. A district may not receive a performance rating of A
16 if the district includes any campus with a performance rating of
17 unacceptable. Not later than August 8 of each year, the performance
18 rating of each district and campus shall be made publicly available
19 as provided by rules adopted under this subsection. If a district
20 or campus received a performance rating that reflected [ex]
21 unacceptable performance for the preceding school year, the
22 commissioner shall notify the district of a subsequent such
23 designation on or before June 15.

24 (b) This section applies beginning with the 2016-2017
25 school year.

26 SECTION 45. (a) Section 39.054(b), Education Code, is
27 amended to read as follows:

1 (b) In evaluating performance, the commissioner shall
2 evaluate against state standards and consider the performance of
3 each campus in a school district and each open-enrollment charter
4 school on the basis of the campus's or school's performance on the
5 student achievement indicators adopted under Section 39.053, other
6 than, to the greatest extent possible, the student achievement
7 indicator adopted under Section 39.053(c)(1) [39.053(c)].

8 (b) This section applies beginning with the 2013-2014
9 school year.

10 SECTION 46. (a) Subchapter C, Chapter 39, Education Code,
11 is amended by adding Section 39.0545 to read as follows:

12 Sec. 39.0545. SCHOOL DISTRICT EVALUATION OF PERFORMANCE IN
13 COMMUNITY AND STUDENT ENGAGEMENT; COMPLIANCE. (a) Each school
14 district shall evaluate the district's performance and the
15 performance of each campus in the district in community and student
16 engagement and in compliance as provided by this section and assign
17 the district and each campus a performance rating of exemplary,
18 recognized, acceptable, or unacceptable for both overall
19 performance and each individual evaluation factor listed under
20 Subsection (b). Not later than August 8 of each year, the district
21 shall report each performance rating to the agency and make the
22 performance ratings publicly available as provided by commissioner
23 rule.

24 (b) For purposes of assigning the performance ratings under
25 Subsection (a), a school district must evaluate:

26 (1) the following programs or specific categories of
27 performance at each campus:

- 1 (A) fine arts;
2 (B) wellness and physical education;
3 (C) community and parental involvement, such as:
4 (i) opportunities for parents to assist
5 students in preparing for assessments under Section 39.023;
6 (ii) tutoring programs that support
7 students taking assessments under Section 39.023; and
8 (iii) opportunities for students to
9 participate in community service projects;
10 (D) the 21st Century Workforce Development
11 program;
12 (E) the second language acquisition program;
13 (F) the digital learning environment;
14 (G) dropout prevention strategies; and
15 (H) educational programs for gifted and talented
16 students; and
17 (2) the record of the district and each campus
18 regarding compliance with statutory reporting and policy
19 requirements.
20 (c) A school district shall use criteria developed by a
21 local committee to evaluate:
22 (1) the performance of the district's campus programs
23 and categories of performance under Subsection (b)(1); and
24 (2) the record of the district and each campus
25 regarding compliance under Subsection (b)(2).
26 (b) This section applies beginning with the 2013-2014
27 school year.

1 SECTION 47. Section 39.056, Education Code, is amended by
2 adding Subsection (f) to read as follows:

3 (f) A district which takes action with regard to the
4 recommendations provided by the investigators as prescribed by
5 Subsection (e) shall make a reasonable effort to seek assistance
6 from a third party in developing an action plan to improve district
7 performance using improvement techniques that are goal oriented and
8 research based.

9 SECTION 48. (a) Section 39.057(a), Education Code, is
10 amended to read as follows:

11 (a) The commissioner shall authorize special accreditation
12 investigations to be conducted:

13 (1) when excessive numbers of absences of students
14 eligible to be tested on state assessment instruments are
15 determined;

16 (2) when excessive numbers of allowable exemptions
17 from the required state assessment instruments are determined;

18 (3) in response to complaints submitted to the agency
19 with respect to alleged violations of civil rights or other
20 requirements imposed on the state by federal law or court order;

21 (4) in response to established compliance reviews of
22 the district's financial accounting practices and state and federal
23 program requirements;

24 (5) when extraordinary numbers of student placements
25 in disciplinary alternative education programs, other than
26 placements under Sections 37.006 and 37.007, are determined;

27 (6) in response to an allegation involving a conflict

1 between members of the board of trustees or between the board and
 2 the district administration if it appears that the conflict
 3 involves a violation of a role or duty of the board members or the
 4 administration clearly defined by this code;

5 (7) when excessive numbers of students in special
 6 education programs under Subchapter A, Chapter 29, are assessed
 7 through assessment instruments developed or adopted under Section
 8 39.023(b);

9 (8) in response to an allegation regarding or an
 10 analysis using a statistical method result indicating a possible
 11 violation of an assessment instrument security procedure
 12 established under Section 39.0301, including for the purpose of
 13 investigating or auditing a school district under that section;

14 (9) when a significant pattern of decreased academic
 15 performance has developed as a result of the promotion in the
 16 preceding two school years of students who did not perform
 17 satisfactorily as determined by the commissioner under Section
 18 39.0241(a) on assessment instruments administered under Section
 19 39.023(e), (c), or (1);

20 (10) ~~[when excessive numbers of students graduate~~
 21 ~~under the minimum high school program,~~

22 ~~[(11)]~~ when excessive numbers of students eligible to
 23 enroll fail to complete an Algebra II course or any other advanced
 24 course as determined by the commissioner ~~[as distinguishing between~~
 25 ~~students participating in the recommended high school program from~~
 26 ~~students participating in the minimum high school program]~~;

27 (11) ~~[(12)]~~ when resource allocation practices as

1 evaluated under Section 39.0821 indicate a potential for
2 significant improvement in resource allocation;

3 (12) when a disproportionate number of students of a
4 particular demographic group is graduating with a particular
5 endorsement under Section 28.025(c-1);

6 (13) when an excessive number of students is
7 graduating with a particular endorsement under Section
8 28.025(c-1); or

9 (14) [~~(13)~~] as the commissioner otherwise determines
10 necessary.

11 (b) This section applies beginning with the 2014-2015
12 school year.

13 SECTION 49. (a) Section 39.082, Education Code, is amended
14 by amending Subsections (a) and (b) and adding Subsections (d),
15 (e), (f), (g), (h), (h-1), and (i) to read as follows:

16 (a) The commissioner shall, in consultation with the
17 comptroller, develop and implement separate financial
18 accountability rating systems for school districts and
19 open-enrollment charter schools in this state that:

20 (1) distinguish among school districts and
21 distinguish among open-enrollment charter schools, as applicable,
22 based on levels of financial performance; ~~and~~

23 (2) include procedures to:

24 (A) provide additional transparency to public
25 education finance; and

26 (B) enable the commissioner and school district
27 and open-enrollment charter school administrators to provide

1 meaningful financial oversight and improvement; and

2 (3) include processes for anticipating the future
3 financial solvency of each school district and open-enrollment
4 charter school, including analysis of district and school revenues
5 and expenditures for preceding school years.

6 (b) The system must include uniform indicators adopted by
7 ~~the~~ commissioner rule by which to measure the financial
8 management performance and future financial solvency of a district
9 or open-enrollment charter school. In adopting indicators under
10 this subsection, the commissioner shall assign a point value to
11 each indicator to be used in a scoring matrix developed by the
12 commissioner. Any reference to a teacher in an indicator adopted by
13 the commissioner under this subsection means a classroom teacher.

14 (d) The commissioner shall evaluate indicators adopted
15 under Subsection (b) at least once every three years.

16 (e) Under the financial accountability rating system
17 developed under this section, each school district or
18 open-enrollment charter school, as applicable, shall be assigned a
19 financial accountability rating. In adopting rules under this
20 section, the commissioner, in consultation with the comptroller,
21 shall determine the criteria for each designated performance
22 rating.

23 (f) A district or open-enrollment charter school shall
24 receive the lowest rating under the system if the district or school
25 fails to achieve a satisfactory rating on:

26 (1) an indicator adopted under Subsection (b) relating
27 to financial management or solvency that the commissioner

1 determines to be critical; or

2 (2) a category of indicators that suggest trends
3 leading to financial distress as determined by the commissioner.

4 (g) Before assigning a final rating under the system, the
5 commissioner shall assign each district or open-enrollment charter
6 school a preliminary rating. A district or school may submit
7 additional information to the commissioner relating to any
8 indicator on which performance was considered unsatisfactory. The
9 commissioner shall consider any additional information submitted
10 by a district or school before assigning a final rating. If the
11 commissioner determines that the additional information negates
12 the concern raised by the indicator on which performance was
13 considered unsatisfactory, the commissioner may not penalize the
14 district or school on the basis of the indicator.

15 (h) The commissioner shall adopt rules for the
16 implementation of this section.

17 (h-1) The commissioner shall adopt initial rules necessary
18 to implement the changes to this section made by the 83rd
19 Legislature, Regular Session, 2013, not later than March 1, 2015.
20 This subsection expires April 1, 2015.

21 (i) Not later than August 8 of each year, the financial
22 accountability rating of each school district and open-enrollment
23 charter school under the financial accountability rating system
24 developed under this section shall be made publicly available as
25 provided by rules adopted under this section.

26 (b) This section applies beginning with the 2014-2015
27 school year.

1 SECTION 50. (a) Section 39.0823, Education Code, is
2 amended by amending Subsection (a) and adding Subsection (d) to
3 read as follows:

4 (a) If the commissioner, based on the indicators adopted
5 under Section 39.082 or other relevant information, projects a
6 [review process under Section 39.0822 indicates a projected]
7 deficit for a school district or open-enrollment charter school
8 general fund within the following three school years, the agency
9 [district] shall provide the district or school [agency] interim
10 financial reports, including projected revenues and expenditures
11 [supplemented by staff and student count data, as needed], to
12 evaluate the [district's] current budget status of the district or
13 school.

14 (d) The agency may require a district or open-enrollment
15 charter school to submit additional information needed to produce a
16 financial report under Subsection (a). If a district or school
17 fails to provide information requested under this subsection or if
18 the commissioner determines that the information submitted by a
19 district or school is unreliable, the commissioner may order the
20 district or school to acquire professional services as provided by
21 Section 39.109.

22 (b) This section applies beginning with the 2014-2015
23 school year.

24 SECTION 51. (a) Subchapter D, Chapter 39, Education Code,
25 is amended by adding Section 39.0824 to read as follows:

26 Sec. 39.0824. CORRECTIVE ACTION PLAN. (a) A school
27 district or open-enrollment charter school assigned the lowest

1 rating under Section 39.082 shall submit to the commissioner a
2 corrective action plan to address the financial weaknesses of the
3 district or school. A corrective action plan must identify the
4 specific areas of financial weaknesses, such as financial
5 weaknesses in transportation, curriculum, or teacher development,
6 and include strategies for improvement.

7 (b) The commissioner may impose appropriate sanctions under
8 Subchapter E against a district or school failing to submit or
9 implement a corrective action plan required under Subsection (a).

10 (b) This section applies beginning with the 2014-2015
11 school year.

12 SECTION 52. (a) Section 39.083(b), Education Code, is
13 amended to read as follows:

14 (b) The annual financial management report must include:

15 (1) a description of the district's financial
16 management performance based on a comparison, provided by the
17 agency, of the district's performance on the indicators adopted
18 under Section 39.082(b) to:

19 (A) state-established standards; and

20 (B) the district's previous performance on the
21 indicators; and

22 (2) ~~[a description of the data submitted using the~~
23 ~~electronic-based program developed under Section 39.0822, and~~

24 ~~[(3)]~~ any descriptive information required by the
25 commissioner.

26 (b) This section applies beginning with the 2014-2015
27 school year.

1 SECTION 53. (a) Section 39.201(a), Education Code, is
2 amended to read as follows:

3 (a) Not later than August 8 of each year, the commissioner
4 shall award distinction designations for outstanding performance
5 as provided by [under] this subchapter. A distinction designation
6 awarded to a district or campus under this subchapter shall be
7 referenced directly in connection with the performance rating
8 assigned to the district or campus and made publicly available
9 together with the performance ratings as provided by rules adopted
10 under Section 39.054(a).

11 (b) This section applies beginning with the 2013-2014
12 school year.

13 SECTION 54. (a) Section 39.202, Education Code, is amended
14 to read as follows:

15 Sec. 39.202. ACADEMIC ~~[EXCELLENCE]~~ DISTINCTION DESIGNATION
16 FOR DISTRICTS AND CAMPUSES. The commissioner by rule shall
17 establish ~~[a recognized and exemplary rating for awarding districts~~
18 ~~and campuses]~~ an academic distinction designation for districts and
19 campuses for outstanding performance in attainment of
20 postsecondary readiness [under this subchapter]. The [In
21 establishing the recognized and exemplary ratings, the]
22 commissioner shall adopt criteria for the designation under this
23 section [ratings], including:

24 (1) percentages of students who:

25 (A) performed satisfactorily, as determined
26 under the college readiness performance standard under Section
27 39.0241, on assessment instruments required under Section

1 39.023(a), (b), (c), or (1), aggregated across grade levels by
2 subject area; or

3 (B) met the standard for annual improvement, as
4 determined by the agency under Section 39.034, on assessment
5 instruments required under Section 39.023(a), (b), (c), or (1),
6 aggregated across grade levels by subject area, for students who
7 did not perform satisfactorily as described by Paragraph (A);

8 (2) percentages of:

9 (A) students who earned a nationally or
10 internationally recognized business or industry certification or
11 license;

12 (B) students who completed a coherent sequence of
13 career and technical courses;

14 (C) students who completed a dual credit course
15 or an articulated postsecondary course provided for local credit;

16 (D) students who achieved applicable College
17 Readiness Benchmarks or the equivalent on the Preliminary
18 Scholastic Assessment Test (PSAT), the Scholastic Assessment Test
19 (SAT), the American College Test (ACT), or the ACT-Plan assessment
20 program; and

21 (E) students who received a score on either an
22 advanced placement test or an international baccalaureate
23 examination to be awarded college credit; and

24 (3) [~~4~~2] other factors for determining sufficient
25 student attainment of postsecondary readiness.

26 (b) This section applies beginning with the 2013-2014
27 school year.

1 SECTION 55. (a) Section 39.203, Education Code, is amended
2 to read as follows:

3 Sec. 39.203. CAMPUS DISTINCTION DESIGNATIONS. (a) The
4 commissioner shall award a campus a distinction designation for
5 outstanding performance in improvement in student achievement if
6 the campus is ranked in the top 25 percent of campuses in the state
7 in annual improvement in student achievement as determined under
8 Section 39.034.

9 (b) In addition to the distinction designation described by
10 Subsection (a), the commissioner shall award a campus a distinction
11 designation for outstanding performance in closing student
12 achievement differentials if the campus demonstrates an ability to
13 significantly diminish or eliminate performance differentials
14 between student subpopulations and is ranked in the top 25 percent
15 of campuses in this state under the performance criteria described
16 by this subsection. The commissioner shall adopt rules related to
17 the distinction designation under this subsection to ensure that a
18 campus does not artificially diminish or eliminate performance
19 differentials through inhibiting the achievement of the highest
20 achieving student subpopulation.

21 (c) In addition to the distinction designations described
22 by Subsections (a) and (b), a campus that satisfies the criteria
23 developed under Section 39.204 shall be awarded a distinction
24 designation by the commissioner for outstanding performance in ~~[for~~
25 ~~the following programs or the following specific categories of~~
26 ~~performance]~~.

27 [(1)] academic achievement in English language arts,

1 mathematics, science, or social studies[+]

2 [~~(2) fine arts,~~

3 [~~(3) physical education,~~

4 [~~(4) 21st Century Workforce Development program, and~~

5 [~~(5) second language acquisition program~~].

6 (d) In addition to the distinction designations otherwise
7 described by this section, the commissioner may award a distinction
8 designation for outstanding performance in advanced middle or
9 junior high school student achievement to a campus with a
10 significant number of students below grade nine who perform
11 satisfactorily on an end-of-course assessment instrument
12 administered under Section 39.023(c).

13 (b) This section applies beginning with the 2013-2014
14 school year.

15 SECTION 56. (a) Section 39.235(b), Education Code, is
16 amended to read as follows:

17 (b) Before awarding a grant under this section, the
18 commissioner may require a campus or school district to:

19 (1) obtain local matching funds; or

20 (2) meet other conditions, including developing a
21 personal graduation plan under Section 28.0212 or 28.02121, as
22 applicable, for each student enrolled at the campus or in a district
23 middle, junior high, or high school.

24 (b) This section applies beginning with the 2014-2015
25 school year.

26 SECTION 57. (a) Section 39.301(c), Education Code, is
27 amended to read as follows:

1 (c) Indicators for reporting purposes must include:

2 (1) the percentage of graduating students who meet the
3 course requirements established by State Board of Education rule
4 for:

5 (A) the foundation ~~[minimum]~~ high school
6 program;

7 (B) ~~[7]~~ the distinguished level of achievement
8 under the foundation ~~[recommended]~~ high school program; ~~[7]~~ and

9 (C) each endorsement described by Section
10 28.025(c-1) ~~[the advanced high school program]~~;

11 (2) the results of the SAT, ACT, articulated
12 postsecondary degree programs described by Section 61.852, and
13 certified workforce training programs described by Chapter 311,
14 Labor Code;

15 (3) for students who have failed to perform
16 satisfactorily, under each performance standard under Section
17 39.0241, on an assessment instrument required under Section
18 39.023(a) or (c), the performance of those students on subsequent
19 assessment instruments required under those sections, aggregated
20 by grade level and subject area;

21 (4) for each campus, the number of students,
22 disaggregated by major student subpopulations, that ~~[agree under~~
23 ~~Section 28.025(b) to]~~ take courses under the foundation ~~[minimum]~~
24 high school program and take additional courses to earn an
25 endorsement under Section 28.025(c-1), disaggregated by type of
26 endorsement;

27 (5) the percentage of students, aggregated by grade

1 level, provided accelerated instruction under Section 28.0211(c),
2 the results of assessment instruments administered under that
3 section, the percentage of students promoted through the grade
4 placement committee process under Section 28.0211, the subject of
5 the assessment instrument on which each student failed to perform
6 satisfactorily under each performance standard under Section
7 39.0241, and the performance of those students in the school year
8 following that promotion on the assessment instruments required
9 under Section 39.023;

10 (6) the percentage of students of limited English
11 proficiency exempted from the administration of an assessment
12 instrument under Sections 39.027(a)(1) and (2);

13 (7) the percentage of students in a special education
14 program under Subchapter A, Chapter 29, assessed through assessment
15 instruments developed or adopted under Section 39.023(b);

16 (8) the percentage of students who satisfy the college
17 readiness measure;

18 (9) the measure of progress toward dual language
19 proficiency under Section 39.034(b), for students of limited
20 English proficiency, as defined by Section 29.052;

21 (10) the percentage of students who are not
22 educationally disadvantaged;

23 (11) the percentage of students who enroll and begin
24 instruction at an institution of higher education in the school
25 year following high school graduation; and

26 (12) the percentage of students who successfully
27 complete the first year of instruction at an institution of higher

1 education without needing a developmental education course.

2 (b) This section applies beginning with the 2014-2015
3 school year.

4 SECTION 58. Subchapter J, Chapter 39, Education Code, is
5 amended by adding Section 39.309 to read as follows:

6 Sec. 39.309. TEXAS SCHOOL ACCOUNTABILITY DASHBOARD. (a)
7 The agency shall develop and maintain an Internet website, separate
8 from the agency's Internet website, to be known as the Texas School
9 Accountability Dashboard for the public to access school district
10 and campus accountability information.

11 (b) The commissioner shall adopt, for use on the Texas
12 School Accountability Dashboard, a performance index in each of the
13 following areas:

- 14 (1) student achievement;
- 15 (2) student progress;
- 16 (3) closing performance gaps; and
- 17 (4) postsecondary readiness.

18 (c) The Texas School Accountability Dashboard developed
19 under Subsection (a) must include:

20 (1) performance information for each school district
21 and campus in areas specified by Subsection (b) and must allow for
22 comparison between districts and campuses in each of the areas;

23 (2) a comparison of the number of students enrolled in
24 each school district, including:

25 (A) the percentage of students of limited English
26 proficiency, as defined by Section 29.052;

27 (B) the percentage of students who are unschooled

1 asylees or refugees, as defined by Section 39.027(a-1).

2 (C) the percentage of students who are
3 educationally disadvantaged; and

4 (D) the percentage of students with
5 disabilities;

6 (3) a comparison of performance information for each
7 district and campus disaggregated by race, ethnicity, and
8 populations served by special programs, including special
9 education, bilingual education, and special language programs; and

10 (4) a comparison of performance information by subject
11 area.

12 SECTION 59. (a) Section 39.332(b), Education Code, is
13 amended by amending Subdivision (23) and adding Subdivision (24) to
14 read as follows:

15 (23) The report must contain an evaluation of the
16 availability of endorsements under Section 28.025(c-1), including
17 the following information for each school district:

18 (A) the endorsements under Section 28.025(c-1)
19 for which the district offers all courses for curriculum
20 requirements as determined by board rule; and

21 (B) the district's economic, geographic, and
22 demographic information, as determined by the commissioner.

23 (24) The report must contain any additional
24 information considered important by the commissioner or the State
25 Board of Education.

26 (b) This section applies beginning with the 2014-2015
27 school year.

1 SECTION 60. (a) Subchapter L, Chapter 39, Education Code,
2 is amended by adding Section 39.363 to read as follows:

3 Sec. 39.363. NOTICE ON AGENCY WEBSITE. Not later than
4 October 1 of each year, the agency shall make the following
5 information available to the public on the agency's Internet
6 website:

7 (1) the letter performance rating assigned to each
8 school district and campus under Section 39.054 and each
9 distinction designation awarded to a school district or campus
10 under Subchapter G;

11 (2) the performance rating assigned to a school
12 district and each campus in the district by the district under
13 Section 39.0545; and

14 (3) the financial accountability rating assigned to
15 each school district and open-enrollment charter school under
16 Section 39.082.

17 (b) This section applies beginning with the 2013-2014
18 school year.

19 [The bill does not contain a SECTION 61.]

20 SECTION 62. (a) Section 51.3062(q-1), Education Code, is
21 amended to read as follows:

22 (q-1) A student who has ~~[completed a recommended or advanced~~
23 ~~high school program as determined under Section 28.025 and]~~
24 demonstrated the performance standard for college readiness as
25 provided by Section 28.008 [39.024] on the postsecondary readiness
26 assessment instruments adopted under Section 39.0238 for Algebra II
27 and English III ~~[end-of-course assessment instruments]~~ is exempt

1 from the requirements of this section with respect to those content
2 areas. The commissioner of higher education by rule shall
3 establish the period for which an exemption under this subsection
4 is valid.

5 (b) This section applies beginning with the 2015-2016
6 school year.

7 SECTION 63. (a) Section 51.3061, Education Code, is amended
8 by adding Subsection (q-2) to read as follows:

9 (q-2) A student who successfully completes a college
10 preparatory course under Section 28.014 is exempt from the
11 requirements of this section with respect to the content area of the
12 course. The commissioner of higher education by rule shall
13 establish the period for which an exemption under this subsection
14 is valid. The exemption applies only at the institution of higher
15 education that partners with the school district in which the
16 student is enrolled to provide the course, except that the
17 commissioner by rule may determine the manner in which the
18 exemption may be applied to institutions of higher education other
19 than the partnering institution.

20 (b) This section applies beginning with the 2013-2014
21 school year.

22 SECTION 64. (a) Section 51.803, Education Code, is amended
23 by amending Subsections (a), (b), and (d) and adding Subsection (m)
24 to read as follows:

25 (a) Subject to Subsection (a-1), each general academic
26 teaching institution shall admit an applicant for admission to the
27 institution as an undergraduate student if the applicant graduated

1 with a grade point average in the top 10 percent of the student's
2 high school graduating class in one of the two school years
3 preceding the academic year for which the applicant is applying for
4 admission and:

5 (1) the applicant graduated from a public or private
6 high school in this state accredited by a generally recognized
7 accrediting organization or from a high school operated by the
8 United States Department of Defense;

9 (2) the applicant:

10 (A) successfully completed:

11 (i) at a public high school, the curriculum
12 requirements established under Section 28.025 for the
13 distinguished level of achievement under the foundation
14 ~~[recommended or advanced]~~ high school program; or

15 (ii) at a high school to which Section
16 28.025 does not apply, a curriculum that is equivalent in content
17 and rigor to the distinguished level of achievement under the
18 foundation ~~[recommended or advanced]~~ high school program; or

19 (B) satisfied ACT's College Readiness Benchmarks
20 on the ACT assessment applicable to the applicant or earned on the
21 SAT assessment a score of at least 1,500 out of 2,400 or the
22 equivalent; and

23 (3) if the applicant graduated from a high school
24 operated by the United States Department of Defense, the applicant
25 is a Texas resident under Section 54.052 or is entitled to pay
26 tuition fees at the rate provided for Texas residents under Section
27 54.241(d) ~~[54.058(d)]~~ for the term or semester to which admitted.

1 (b) An applicant who does not satisfy the curriculum
2 requirements prescribed by Subsection (a)(2)(A)(i) or (ii) is
3 considered to have satisfied those requirements if the student
4 completed the portion of the distinguished level of achievement
5 under the foundation high school program ~~[recommended or advanced]~~
6 curriculum or of the curriculum equivalent in content and rigor, as
7 applicable, that was available to the student but was unable to
8 complete the remainder of the curriculum solely because courses
9 necessary to complete the remainder were unavailable to the student
10 at the appropriate times in the student's high school career as a
11 result of course scheduling, lack of enrollment capacity, or
12 another cause not within the student's control.

13 (d) For purposes of Subsection (c)(2), a student's official
14 transcript or diploma must, not later than the end of the student's
15 junior year, indicate:

16 (1) whether the student has satisfied or is on
17 schedule to satisfy the requirements of Subsection (a)(2)(A)(i) or
18 (ii), as applicable; or

19 (2) if Subsection (b) applies to the student, whether
20 the student has completed the portion of the distinguished level of
21 achievement under the foundation high school program ~~[recommended~~
22 ~~or advanced]~~ curriculum or of the curriculum equivalent in content
23 and rigor, as applicable, that was available to the student.

24 (m) The Texas Higher Education Coordinating Board and the
25 commissioner of education shall jointly adopt rules to establish
26 eligibility requirements for admission under this section as to
27 curriculum requirements for high school graduation under

1 Subsection (a)(2)(A) for students participating under the
 2 recommended or advanced high school program so that the admission
 3 of those students is not affected by their participation in the
 4 recommended or advanced high school program. This subsection
 5 expires September 1, 2020.

6 (b) This section applies beginning with the 2014-2015
 7 school year.

8 SECTION 65. (a) Section 51.805, Education Code, is amended
 9 by amending Subsection (a) and adding Subsection (g) to read as
 10 follows:

11 (a) A graduating student who does not qualify for admission
 12 under Section 51.803 or 51.804 may apply to any general academic
 13 teaching institution if the student:

14 (1) successfully completed ~~[satisfies the~~
 15 ~~requirements of]~~:

16 (A) at a public high school, the curriculum
 17 requirements established under Section 28.025 for the foundation
 18 high school program; or

19 (B) at a high school to which Section 28.025 does
 20 not apply, a curriculum that is equivalent in content and rigor to
 21 the foundation high school program ~~[(1) Section 51.803(a)(2)(A)~~
 22 ~~or 51.803(b), as applicable to the student, or Section~~
 23 ~~51.803(a)(2)(B)]~~; or ~~[and]~~

24 (2) satisfied ACT's College Readiness Benchmarks on
 25 the ACT assessment applicable to the applicant or earned on the SAT
 26 assessment a score of at least 1,500 out of 2,400 or the equivalent
 27 ~~[Sections 51.803(c)(2) and 51.803(d)]~~.

1 (g) The Texas Higher Education Coordinating Board and the
2 commissioner of education shall jointly adopt rules to establish
3 eligibility requirements for admission under this section as to
4 curriculum requirements for high school graduation under
5 Subsection (a)(1) for students participating in the minimum,
6 recommended, or advanced high school program so that the admission
7 requirements for those students under this section are not more
8 stringent than the admission requirements under this section for
9 students participating in the foundation high school program. This
10 subsection expires September 1, 2020.

11 (b) This section applies beginning with the 2014-2015
12 school year.

13 SECTION 66. (a) Section 51.807(b), Education Code, is
14 amended to read as follows:

15 (b) The Texas Higher Education Coordinating Board, after
16 consulting with the Texas Education Agency, by rule shall establish
17 standards for determining for purposes of this subchapter:

18 (1) whether a private high school is accredited by a
19 generally recognized accrediting organization; and

20 (2) whether a person completed a high school
21 curriculum that is equivalent in content and rigor to the
22 curriculum requirements established under Section 28.025 for the
23 foundation [recommended or advanced] high school program or the
24 distinguished level of achievement under the foundation high school
25 program.

26 (b) This section applies beginning with the 2014-2015
27 school year.

1 SECTION 67. (a) Subchapter A, Chapter 56, Education Code,
2 is amended by adding Section 56.009 to read as follows:

3 Sec. 56.009. ELIGIBILITY BASED ON GRADUATION UNDER CERTAIN
4 HIGH SCHOOL PROGRAMS. To the extent that a person's eligibility to
5 participate in any program under this chapter, including
6 Subchapters K, Q, and R, is contingent on the person graduating
7 under the recommended or advanced high school program, as those
8 programs existed before the adoption of H.B. No. 5, 83rd
9 Legislature, Regular Session, 2013, the Texas Higher Education
10 Coordinating Board and the commissioner of education shall jointly
11 adopt rules to modify, clarify, or otherwise establish for affected
12 programs appropriate eligibility requirements regarding high
13 school curriculum completion.

14 (b) This section applies beginning with the 2014-2015
15 school year.

16 SECTION 69. (a) Section 56.3041, Education Code, is
17 amended to read as follows:

18 Sec. 56.3041. INITIAL ELIGIBILITY OF PERSON GRADUATING FROM
19 HIGH SCHOOL ON OR AFTER MAY 1, 2013, AND ENROLLING IN A GENERAL
20 ACADEMIC TEACHING INSTITUTION. (a) Notwithstanding Section
21 56.304(a), to be eligible initially for a TEXAS grant, a person
22 graduating from high school on or after May 1, 2013, and enrolling
23 in a general academic teaching institution must:

24 (1) be a resident of this state as determined by
25 coordinating board rules;

26 (2) meet the academic requirements prescribed by
27 Paragraph (A), (B), or (C) as follows:

1 (A) be a graduate of a public or accredited
2 private high school in this state who completed the foundation
3 ~~[recommended]~~ high school program established under Section 28.025
4 or its equivalent and have accomplished any two or more of the
5 following:

6 (i) ~~[graduation under the advanced high~~
7 ~~school program established under Section 28.025 or its equivalent,]~~
8 successful completion of the course requirements of the
9 international baccalaureate diploma program~~[,]~~ or earning of the
10 equivalent of at least 12 semester credit hours of college credit in
11 high school through courses described in Sections 28.009(a)(1),
12 (2), and (3);

13 (ii) satisfaction of the Texas Success
14 Initiative (TSI) college readiness benchmarks prescribed by the
15 coordinating board under Section 51.3062(f) on any assessment
16 instrument designated by the coordinating board under Section
17 51.3062(c) ~~[or (e)]~~ or qualification for an exemption as described
18 by Section 51.3062(p), (q), or (q-1);

19 (iii) graduation in the top one-third of
20 the person's high school graduating class or graduation from high
21 school with a grade point average of at least 3.0 on a four-point
22 scale or the equivalent; or

23 (iv) completion for high school credit of
24 at least one advanced mathematics course following the successful
25 completion of an Algebra II course~~[, as permitted by Section~~
26 ~~28.025(b-3),]~~ or at least one advanced career and technical or
27 technology applications course~~[, as permitted by Section~~

1 ~~28.025(b-2)]~~;

2 (B) have received an associate degree from a
3 public or private institution of higher education, or

4 (C) if sufficient money is available, meet the
5 eligibility criteria described by Section 56.304(a)(2)(A);

6 (3) meet financial need requirements established by
7 the coordinating board;

8 (4) be enrolled in an undergraduate degree or
9 certificate program at the general academic teaching institution;

10 (5) except as provided under rules adopted under
11 Section 56.304(h), be enrolled as:

12 (A) an entering undergraduate student for at
13 least three-fourths of a full course load, as determined by the
14 coordinating board, not later than the 16th month after the
15 calendar month in which the person graduated from high school;

16 (B) an entering undergraduate student who
17 entered military service not later than the first anniversary of
18 the date the person graduated from high school and who enrolled for
19 at least three-fourths of a full course load, as determined by the
20 coordinating board, at the general academic teaching institution
21 not later than 12 months after being honorably discharged from
22 military service; or

23 (C) a continuing undergraduate student for at
24 least three-fourths of a full course load, as determined by the
25 coordinating board, not later than the 12th month after the
26 calendar month in which the person received an associate degree
27 from a public or private institution of higher education;

1 (6) have applied for any available financial aid or
2 assistance; and

3 (7) comply with any additional nonacademic
4 requirements adopted by the coordinating board under this
5 subchapter.

6 (b) For purposes of Subsection (a)(2)(A), a student who
7 graduated under the recommended or advanced high school program is
8 considered to have successfully completed the curriculum
9 requirements of Section 51.803(a)(2)(A)(i). This subsection
10 expires September 1, 2020.

11 (b) This section applies beginning with the 2014-2015
12 school year.

13 SECTION 69. (a) Section 61.0517(a), Education Code, is
14 amended to read as follows:

15 (a) In this section, "applied STEM course" means an applied
16 science, technology, engineering, or mathematics course offered as
17 part of a school district's career and technology education or
18 technology applications curriculum and approved, as provided by
19 Section 28.027, by the State Board of Education for purposes of
20 satisfying the mathematics and science curriculum requirements for
21 the foundation ~~[recommended]~~ high school program ~~[imposed]~~ under
22 Section 28.025 ~~[28.025(b-1)(1)(A)]~~.

23 (b) This section applies beginning with the 2014-2015
24 school year.

25 SECTION 70. (a) Section 61.792(b), Education Code, is
26 amended to read as follows:

27 (b) To qualify for a scholarship under this section, a

1 student must:

2 (1) have graduated with a grade point average in the
3 top 20 percent of the student's high school graduating class;

4 (2) have graduated from high school with a grade point
5 average of at least 3.5 on a four-point scale or the equivalent in
6 mathematics and science courses offered under the foundation
7 ~~[recommended or advanced]~~ high school program under Section 28.025
8 ~~[28.025(a)]~~; and

9 (3) maintain an overall grade point average of at
10 least 3.0 on a four-point scale at the general academic teaching
11 institution or the private or independent institution of higher
12 education in which the student is enrolled.

13 (b) This section applies beginning with the 2014-2015
14 school year.

15 SECTION 71. (a) Section 61.852(a), Education Code, is
16 amended to read as follows:

17 (a) A tech-prep program is a program of study that:

18 (1) combines at least two years of secondary education
19 with at least two years of postsecondary education in a
20 nonduplicative, sequential course of study based on the foundation
21 ~~[recommended]~~ high school program adopted by the State Board of
22 Education under Section 28.025 ~~[28.025(a)]~~;

23 (2) integrates academic instruction and vocational
24 and technical instruction;

25 (3) uses work-based and worksite learning where
26 available and appropriate;

27 (4) provides technical preparation in a career field

1 such as engineering technology, applied science, a mechanical,
2 industrial, or practical art or trade, agriculture, health
3 occupations, business, or applied economics;

4 (5) builds student competence in mathematics,
5 science, reading, writing, communications, economics, and
6 workplace skills through applied, contextual academics and
7 integrated instruction in a coherent sequence of courses;

8 (6) leads to an associate degree, two-year
9 postsecondary certificate, or postsecondary two-year
10 apprenticeship with provisions, to the extent applicable, for
11 students to continue toward completion of a baccalaureate degree;
12 and

13 (7) leads to placement in appropriate employment or to
14 further education.

15 (b) This section applies beginning with the 2014-2015
16 school year.

17 SECTION 72. (a) Section 61.855(d), Education Code, is
18 amended to read as follows:

19 (a) A tech-prep program must:

20 (1) be implemented under an articulation agreement
21 between the participants in the consortium;

22 (2) consist of two to four years of secondary school
23 preceding graduation and:

24 (A) two or more years of higher education; or

25 (B) two or more years of apprenticeship following
26 secondary instruction;

27 (3) have a common core of required proficiency based

1 on the foundation [~~recommended~~] high school program adopted by the
2 State Board of Education under Section 28.025 [~~28.025(a)~~], with
3 proficiencies in mathematics, science, reading, writing,
4 communications, and technologies designed to lead to an associate's
5 degree or postsecondary certificate in a specific career field;

6 (4) include the development of tech-prep program
7 curricula for both secondary and postsecondary participants in the
8 consortium that:

9 (A) meets academic standards developed by the
10 state;

11 (B) links secondary schools and two-year
12 postsecondary institutions, and, if practicable, four-year
13 institutions of higher education through nonduplicative sequences
14 of courses in career fields, including the investigation of
15 opportunities for tech-prep students to enroll concurrently in
16 secondary and postsecondary course work;

17 (C) uses, if appropriate and available,
18 work-based or worksite learning in conjunction with business and
19 all aspects of an industry; and

20 (D) uses educational technology and distance
21 learning, as appropriate, to involve each consortium participant
22 more fully in the development and operation of programs;

23 (5) include in-service training for teachers that:

24 (A) is designed to train vocational and technical
25 teachers to effectively implement tech-prep programs;

26 (B) provides for joint training for teachers in
27 the tech-prep consortium;

1 (C) is designed to ensure that teachers and
2 administrators stay current with the needs, expectations, and
3 methods of business and of all aspects of an industry;

4 (D) focuses on training postsecondary education
5 faculty in the use of contextual and applied curricula and
6 instruction; and

7 (E) provides training in the use and application
8 of technology;

9 (6) include training programs for counselors designed
10 to enable counselors to more effectively:

11 (A) provide information to students regarding
12 tech-prep programs;

13 (B) support student progress in completing
14 tech-prep programs;

15 (C) provide information on related employment
16 opportunities;

17 (D) ensure that tech-prep students are placed in
18 appropriate employment; and

19 (E) stay current with the needs, expectations,
20 and methods of business and of all aspects of an industry;

21 (7) provide equal access to the full range of
22 tech-prep programs for individuals who are members of special
23 populations, including by the development of tech-prep program
24 services appropriate to the needs of special populations; and

25 (8) provide for preparatory services that assist
26 participants in tech-prep programs.

27 (b) This section applies beginning with the 2014-2015

1 school year.

2 SECTION 73. (a) Section 61.861(c), Education Code, is
3 amended to read as follows:

4 (c) A course developed for purposes of this section must:

5 (1) provide content that enables a student to develop
6 the relevant and critical skills needed to be prepared for
7 employment or additional training in a high-demand occupation;

8 (2) incorporate college and career readiness skills as
9 part of the curriculum;

10 (3) be offered for dual credit; and

11 (4) satisfy a mathematics or science requirement under
12 the foundation [~~recommended or advanced~~] high school program as
13 determined under Section 28.025.

14 (b) This section applies beginning with the 2014-2015
15 school year.

16 SECTION 74. (a) Section 61.864, Education Code, is amended
17 to read as follows:

18 Sec. 61.864. REVIEW OF COURSES. Courses for which a grant
19 is awarded under this subchapter shall be reviewed by the
20 commissioner of higher education and the commissioner of education,
21 in consultation with the comptroller and the Texas Workforce
22 Commission, once every four years to determine whether the course:

23 (1) is being used by public educational institutions
24 in this state;

25 (2) prepares high school students with the skills
26 necessary for employment in the high-demand occupation and further
27 postsecondary study; and

1 (3) satisfies a mathematics or science requirement for
2 the foundation [~~recommended or advanced~~] high school program as
3 determined under Section 28.025.

4 (b) This section applies beginning with the 2014-2015
5 school year.

6 SECTION 75. (a) Section 78.10(~~b~~), Education Code, is
7 amended to read as follows:

8 (b) The Texas Academy of Mathematics and Science is a
9 division of The University of Texas at Brownsville and is under the
10 management and control of the board. The academy serves the
11 following purposes:

12 (1) to provide academically gifted and highly
13 motivated junior and senior high school students with a challenging
14 university-level curriculum that:

15 (A) allows students to complete high school
16 graduation requirements[~~, including requirements adopted under~~
17 ~~Section 28.025~~] for the foundation [~~advanced~~] high school program
18 and the distinguished level of achievement under the foundation
19 high school program and earn appropriate endorsements as provided
20 by Section 28.025, while attending for academic credit a public
21 institution of higher education;

22 (B) fosters students' knowledge of real-world
23 mathematics and science issues and applications and teaches
24 students to apply critical and computational thinking and
25 problem-solving skills to those issues and problems;

26 (C) includes the study of English, foreign
27 languages, social studies, mathematics, science, and technology;

1 and

2 (D) offers students learning opportunities
3 related to mathematics and science through in-depth research and
4 field-based studies;

5 (2) to provide students with an awareness of
6 mathematics and science careers and professional development
7 opportunities through seminars, workshops, collaboration with
8 postsecondary and university students including opportunities for
9 summer studies, internships in foreign countries, and similar
10 methods; and

11 (3) to provide students with social development
12 activities that enrich the academic curriculum and student life,
13 including, as determined appropriate by the academy, University
14 Interscholastic League activities and other extracurricular
15 activities.

16 (b) This section applies beginning with the 2014-2015
17 school year.

18 SECTION 76. (a) Section 87.505(b), Education Code, is
19 amended to read as follows:

20 (b) The Texas Academy of International Studies is a division
21 of Texas A&M International University and is under the management
22 and control of the board. The academy serves the following
23 purposes:

24 (1) to provide academically gifted and highly
25 motivated junior and senior high school students with a challenging
26 university-level curriculum that:

27 (A) allows students to complete high school

1 graduation requirements[, ~~including requirements adopted under~~
2 ~~Section 28.025~~] for the foundation [~~advanced~~] high school program
3 and the distinguished level of achievement under the foundation
4 high school program and earn appropriate endorsements as provided
5 by Section 28.025, while attending for academic credit a public
6 institution of higher education;

7 (B) fosters students' knowledge of real-world
8 international issues and problems and teaches students to apply
9 critical thinking and problem-solving skills to those issues and
10 problems;

11 (C) includes the study of English, foreign
12 languages, social studies, anthropology, and sociology;

13 (D) is presented through an interdisciplinary
14 approach that introduces and develops issues, especially issues
15 related to international concerns, throughout the curriculum; and

16 (E) offers students learning opportunities
17 related to international issues through in-depth research and
18 field-based studies;

19 (2) to provide students with an awareness of
20 international career and professional development opportunities
21 through seminars, workshops, collaboration with postsecondary
22 students from other countries, summer academic international
23 studies internships in foreign countries, and similar methods; and

24 (3) to provide students with social development
25 activities that enrich the academic curriculum and student life,
26 including, as determined appropriate by the academy, University
27 Interscholastic League activities and other extracurricular

1 activities generally offered by public high schools.

2 (b) This section applies beginning with the 2014-2015
3 school year.

4 SECTION 77. (a) Section 130.008, Education Code, is
5 amended by amending Subsection (d) and adding Subsection (f) to
6 read as follows:

7 (d) ~~A [Except as provided by Subsection (d-1), a]~~ public
8 junior college may enter into an agreement with a school district,
9 organization, or other person that operates a high school to offer a
10 course as provided by this section regardless of whether the high
11 school is located within the service area of the junior college
12 district.

13 (f) Except as provided by this section, a student may not
14 enroll in more than three courses under this section at a junior
15 college if the junior college does not have a service area that
16 includes the student's high school. A student enrolled at an early
17 college high school may enroll in a greater number of courses to the
18 extent approved by the commissioner of education.

19 (b) This section applies beginning with the 2013-2014
20 school year.

21 SECTION 78. (a) Effective September 1, 2013, the following
22 sections of the Education Code are repealed:

- 23 (1) Sections 29.190(b), (d), and (e);
24 (2) Sections 39.024(b), (c), (d), (e), (f), (g), and
25 (h);
26 (3) Section 39.0241(a-2);
27 (4) Section 39.0242;

1 (5) Sections 39.025(a-2) and (a-3); and

2 (6) Section 130.008(d-1).

3 (b) Effective September 1, 2014, the following provisions
4 of the Education Code are repealed:

5 (1) Section 28.002(q);

6 (2) Sections 28.0212(e) and (g);

7 (3) Sections 28.025(b-6), (b-8), and (g);

8 (4) Section 39.0822; and

9 (5) Sections 39.0823(b) and (c).

10 SECTION 79. (a) Except as provided by Subsection (b) of
11 this section, Section 39.025, Education Code, as amended by
12 Sections 35 and 36 of this Act, as related to reducing end-of-course
13 testing requirements, applies only to students who have entered or
14 will enter the ninth grade during the 2011-2012 school year or a
15 later school year.

16 (b) Students who have entered the ninth grade during or
17 after the 2011-2012 school year and before the 2013-2014 school
18 year may be administered only those end-of-course assessment
19 instruments that would have been administered to those students
20 under Section 39.025, Education Code, as amended by Section 35 of
21 this Act, and Section 39.025, Education Code, as amended by Section
22 35 of this Act, is continued in effect for purposes of satisfying
23 those end-of-course testing requirements.

24 (c) The commissioner of education may by rule adopt a
25 transition plan to implement the amendments made by this Act
26 relating to end-of-course testing requirements during the
27 2013-2014 and 2014-2015 school years.

1 SECTION 80. Not later than October 1, 2013, the
2 commissioner of education shall adopt rules to administer Section
3 39.025(a-1), Education Code, as amended by this Act.

4 SECTION 81. Section 39.027(a-2), Education Code, as added
5 by this Act, applies to a student regardless of the date on which
6 the student initially enrolled in a school in the United States.

7 SECTION 82. If, on September 1, 2013, a person is serving on
8 a committee or panel that advises the commissioner of education or
9 the Texas Education Agency who would not be eligible for
10 appointment under Section 39.038, Education Code, as added by this
11 Act, the person's position on the committee or panel becomes vacant
12 and shall be filled in accordance with applicable law.

13 SECTION 83. (a) The Texas Education Agency, in
14 collaboration with the Texas Higher Education Coordinating Board
15 and the Texas Workforce Commission, shall, through an external
16 evaluator at a center for education research authorized by Section
17 1.005, Education Code, evaluate the implementation of the changes
18 made by this Act to the curriculum requirements for high school
19 graduation. The evaluation must include an estimation of this
20 Act's effect on high school graduation rates, college readiness,
21 college admissions, college completion, obtainment of workforce
22 certificates, employment rates, and earnings.

23 (b) The commissioner of education shall submit an initial
24 report regarding the review to the governor, lieutenant governor,
25 and members of the legislature not later than December 1, 2015. The
26 commissioner of education shall submit a final report regarding
27 the review to the governor, lieutenant governor, and members of the

1 legislature not later than December 1, 2017.

2 SECTION 84. Except as otherwise provided by this Act:

3 (1) this Act takes effect immediately if it receives a
4 vote of two-thirds of all the members elected to each house, as
5 provided by Section 39, Article III, Texas Constitution; and

6 (2) if this Act does not receive the vote necessary for
7 immediate effect, this Act takes effect September 1, 2013.

H.B. No. 5

President of the Senate

Speaker of the House

I certify that H.B. No. 5 was passed by the House on March 27, 2013, by the following vote: Yeas 147, Nays 2, 1 present, not voting; that the House refused to concur in Senate amendments to H.B. No. 5 on May 10, 2013, and requested the appointment of a conference committee to consider the differences between the two houses; that the House adopted the conference committee report on H.B. No. 5 on May 26, 2013, by the following vote: Yeas 147, Nays 0, 1 present, not voting; and that the House adopted H.C.R. No. 224 authorizing certain corrections in H.B. No. 5 on May 27, 2013, by the following vote: Yeas 144, Nays 1, 1 present, not voting.

Chief Clerk of the House

H.B. No. 5

I certify that H.B. No. 5 was passed by the Senate, with amendments, on May 6, 2013, by the following vote: Yeas 31, Nays 0; at the request of the House, the Senate appointed a conference committee to consider the differences between the two houses; that the Senate adopted the conference committee report on H.B. No. 5 on May 26, 2013, by the following vote: Yeas 31, Nays 0; and that the Senate adopted H.C.R. No. 224 authorizing certain corrections in H.B. No. 5 on May 27, 2013, by the following vote: Yeas 31, Nays 0.

Secretary of the Senate

APPROVED: _____

Date

Governor

SUBJECT: Public school accountability and graduation program changes

COMMITTEE: Public Education — committee substitute recommended

VOTE: 10 ayes — Aycock, Allen, J. Davis, Deshotel, Dutton, Farney, K. King, Ratliff, J. Rodriguez, Villarreal

0 nays

1 absent — Huberty

WITNESSES: *(On original bill:)*
For — David Anthony, Raise Your Hand Texas; Jennifer Bergland, Texas Computer Education Association; Nancy Blackwell, Macarthur Senior High School; Eddie Bland, Texas Association of Community Schools; Reece Blincoe, Brownwood ISD; Portia Bosse, Texas State Teachers Association; Keith Bryant, Texas Association of Mid-Size Schools; Barbara Cade, Paul Clore, Gregory-Portland ISD; HD Chambers, Barbara Guidry, Alief ISD; Jesus Chavez, Texas School Alliance; David Dominguez, Shelley Wells, Killeen ISD; Sandy Farris, Bryan ISD; Carol Fletcher, Texas Association of School Boards; Robert Floyd, Texas Music Educators Association and Texas Coalition For Quality Arts Education; Bruce Gearing, Dripping Springs ISD; Buck Gilcrease, Texas Rural Education Association; Eric Haugeberg, Belton ISD; Alexis Hernandez, Manor High School; Linda Holcombe, Texas Industrial Vocational Association; Sharon Kollaja, Corpus Christi Chamber of Commerce and Sterling Personnel; Ted Melina Raab, Texas American Federation of Teachers; Wayne Morren, Floydada ISD; Mike Motheral, Texas Association of Community Schools; Randy Reid, Keller ISD; Hector Revero, Texas Chemical Council; Christy Rome, Texas School Coalition; Gonzalo Salazar, Los Fresnos CISD and South Texas Association of Schools; Michael Sandroussi, Craft Training Center of the Coastal Bend; Sara Solomon, Texas PTA; Haylee Uptergrove; Jim Van Zandt, Texas Music Administrators Conference; Thomas Wallis, Bryan ISD; Mary Ann Whiteker, Texas Association of School Administrators; Randy Willis, Central Texas School Board Association; and 19 individuals; (Registered, but did not testify: David D. Anderson, Arlington ISD; Kris Andrews, Center for Educator Development in Fine Arts; Kathy Barber, National Federation of Independent Business in Texas; Charles Chadwell, Round

Rock ISD; Melody Chatelle, United Ways of Texas; Frank Coachman, Texas Bandmasters Association; John Craft, Robert Muller, Killeen ISD; Walter Dansby, Hank Johnson, Fort Worth ISD; Harley Eckhart, Texas Elementary Principals and Supervisors Association; Terry Green, Family and Consumer Sciences Teachers Association of Texas; Caroline Hammond, Texas Cultural Trust; Sharon Lutz, Texas Choral Directors Association; Peter Martindell, Fort Bend ISD; Louann Martinez, Dallas ISD; Mike Meroney, Huntsman Corp. and Sherwin Alumina Co.; Gerald Mooney, Nancy Mooney, Jim Ramage, Banquete ISD, Scott Norman, Texas Association of Builders; Sheryl Pace, Texas Taxpayers and Research Association; Robin Painovich, Career and Technology Association of Texas; Beverly Schlegel, Texas Orchestra Directors Association; Rod Schroder, Amarillo ISD; Debbie Seeger, Corpus Christi ISD; Michael Willard, Goodwill Industries of Central Texas; Columba Wilson)

Against — Bill Hammond, Texas Association of Business; Drew Scheberle, Greater Austin Chamber of Commerce; Douglas Torres-Edwards

On — Yannis Banks, Texas NAACP; Jennifer Collier, Spring Branch ISD; Holly Eaton, Texas Classroom Teachers Association; Monty Exter, Association of Texas Professional Educators; Luis Figueroa, Mexican American Legal Defense and Educational Fund; John Fitzpatrick, Educate Texas; Sharon Karnas, Science Teachers Association of Texas; Duncan Klussmann, Spring Branch ISD; Janna Lilly, Texas Council of Administrators of Special Education; Sandra West, Science Teachers Association of Texas; Laura Yeager, Texans Advocating for Meaningful Student Assessments; and nine individuals; (Registered, but did not testify: Fidel Acevedo, League of United Latin American Citizens Council 4227; Priscilla Aquino Garza, Stand For Children Texas; Teresa Bosworth Green, Texas Science Education Supervisors Association; Kevin Brackmeyer, Manor ISD; Renee Byas, Houston Community College; Paul Gray, Texas Association of Supervisors of Mathematics; Patricia D. Lopez, Ph.D., Texas Center for Education Policy; Tom Pauken, Texas Workforce Commission; Robyn Shapiro, Texans Advocating for Meaningful Student Assessments; Angela Valenzuela, Texas Center for Education Policy; and seven individuals)

BACKGROUND: **Student assessment.** In 1986, the Texas Education Agency (TEA) implemented the Texas Educational Assessment of Minimum Skills (TEAMS), the first statewide assessment that students were required to pass to be eligible to receive a high school diploma.

In 1990, the state adopted the Texas Assessment of Academic Skills (TAAS), which was designed to shift the assessment focus from minimum skills to academic skills. Passing the exit level tests in reading, writing, and mathematics at grade 10 was a requirement for students seeking to graduate from a public high school.

The Texas Assessment of Knowledge and Skills (TAKS) replaced TAAS as the primary statewide assessment program in 2003. TAKS was designed to measure more of the state-mandated curriculum. Students were required to pass exit-level tests in English language arts, mathematics, science, and social studies to graduate.

The 80th Legislature in 2007 enacted SB 1031 by Shapiro, replacing the TAKS assessments in grades 9-12 with 15 end-of-course (EOC) assessments in 12 different courses, beginning with the class entering grade 9 in the fall of 2011. Those courses are: algebra I and II; geometry; biology; chemistry; physics; English I, II, and III; world geography; world history; and U.S. history.

The 81st Legislature in 2009 enacted HB 3 by Eissler, which requires TEA to develop assessments in a manner that allows the measurement of performance across grades, culminating in college readiness performance standards in algebra II and English III. In order to graduate, students must achieve a cumulative score corresponding to satisfactory performance in each core subject (English, mathematics, science, and social studies) on all administered EOC exams. For example, scores for biology, chemistry, and physics must average to a satisfactory score to meet the science requirement. A student must achieve a minimum score determined by the commissioner for an EOC exam score to count toward a cumulative score.

A student who does not perform satisfactorily on an end-of-course exam must retake the exam. If the student's performance does not meet college readiness performance standards on the algebra II or English III EOC exam, the student may take the exam again.

In 2012, following the requirements of HB 3, the State of Texas Assessments of Academic Readiness (STAAR) EOC exams were administered under initial passing standards slated to increase with subsequent administrations.

High school graduation programs. There are three high school graduation plans under current law: minimum, recommended, and advanced. The minimum plan has the fewest requirements in terms of courses and EOC exams that students must successfully complete for graduation. Students following the recommended and advanced programs must complete four years of mathematics, science, English language arts, and social studies. Students need two credits of a language other than English to graduate under the recommended program and three under the advanced program. Students need six elective credits to graduate under the recommended program and five under the advanced program. A student must achieve at least the minimum score determined by the commissioner of education for English III and algebra II EOC exams to graduate under the recommended or advanced programs.

Public school accountability. In 1993, the Legislature mandated the creation of the public school accountability system to rate school districts and evaluate schools. The system relied on an existing student data collection system, the state-mandated curriculum, and the TAAS assessment system. The accountability standards were designed to phase in increasingly higher expectations for districts and campuses. The state raised expectations for acceptable performance each year between 1995 and 2001.

This accountability system remained in place through the 2001-02 school year. A new rating system based on the TAKS was developed during 2003. Districts were rated as exemplary, recognized, academically acceptable, or academically unacceptable. Campuses were rated as exemplary, recognized, acceptable, or low-performing.

There were no accountability ratings in 2012 as the state transitioned to STAAR. The commissioner of education is developing a new accountability system for the 2012-13 school year.

DIGEST:

CSHB 5 would institute a new standard course of study for high school students and reduce the number of EOC exams public high school students were required to pass in order to graduate. The bill also would establish a

new accountability ratings system evaluating schools on academic performance, financial performance, and community and student engagement.

CSHB 5 would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2013.

High school graduation programs. CSHB 5 would replace the minimum, recommended, and advanced high school program with a 24-credit foundation high school program, beginning with the 2014-15 school year. The curriculum requirements for the foundation program would be:

- four credits in English language arts, including English I, II, and III, and one other advanced English course;
- three credits in mathematics, including algebra I, geometry, and an advanced mathematics course;
- three credits in science, including biology, an advanced science course, integrated physics and chemistry, or an additional advanced science course;
- three credits in social studies, including U.S. history, one-half credit in government, one-half credit in economics, and world geography or world history;
- two credits in a foreign language;
- seven elective credits;
- one fine arts credit; and
- one physical education credit.

A student could satisfy the foreign language requirements by substituting two credits in computer programming. A student served by special education could satisfy the foreign language requirements by substituting credits in other specified coursework.

A student would be allowed to participate and receive credit in a fine arts program not provided by the school district.

Students could earn endorsements on their diplomas in any of five areas: STEM (science, technology, engineering, and math), business and industry, public services, arts and humanities, and multidisciplinary studies.

Students could earn a distinguished level of achievement designation by completing the requirements of the foundation program and at least one endorsement, while also earning four credits of science and four credits of math, including algebra II. Students also could earn an acknowledgment for outstanding performance in a dual-credit course; on a college advanced placement test or international baccalaureate exam; on the PSAT, the ACT-Plan, the SAT, or the ACT; or for earning a nationally or internationally recognized business or industry certification or license. The distinguished level of achievement, endorsement, and performance acknowledgment would be listed on diplomas and transcripts.

The commissioner of education would be required to adopt a transition plan for implementing the foundation high school program. Students who entered the ninth grade before the 2014-15 school year would be allowed to choose the foundation plan or remain on the current minimum, recommended, or advanced plans.

All high school graduates would be eligible to apply for admission to Texas public four-year universities, and those who met additional academic achievement requirements would be eligible to receive a TEXAS grant. Only students completing the distinguished level and graduating in the top 10 percent of their class would be eligible for college admission under the top 10 percent automatic admissions law.

CSHB 5 would require the State Board of Education (SBOE) to designate the specific courses required under the new foundation program and would set out the specific number of completed credits for various subjects and the number of elective credits. The SBOE also would develop the curriculum requirements for each endorsement with the participation of educators and business and industry representatives.

Districts would have local flexibility to develop courses outside the required curriculum without obtaining SBOE approval if certain conditions were met, which include partnering with an institution of higher education and local business and community leaders. The courses would have to prepare students for technical training or college readiness. One credit in a local course could be substituted for the required physical education credit by a student who could not participate in physical activity because of disability or illness.

Beginning in the 2014-15 school year, counselors at elementary, middle school, and high school levels would be required to provide students and their parents information about preparing for postsecondary education and financial aid availability. Students in their first year of high school would receive information from counselors about the advantages of earning a diploma endorsement, performance acknowledgement, and distinguished level of achievement.

Student assessment. For students entering grade 9 during the 2011-12 school year or later, CSHB 5 would reduce from 15 to five the number of STAAR EOC tests that students had to pass to graduate. Students would be able to meet their graduation requirements by passing English II (both reading and writing), algebra I, biology, and U.S. history.

The bill would eliminate EOC testing in geometry, chemistry, physics, English I, world geography, and world history. TEA would be required to adopt EOC exams for algebra II and English III, which students could opt to take. The Texas Higher Education Coordinating Board (THECB) would have to ensure those tests were capable of measuring college readiness. Scores from those tests would not be used in determining graduation eligibility or in the accountability system.

CSHB 5 would eliminate the requirement that EOC test scores count for 15 percent of a student's overall grade and allow districts to adopt local policies for factoring test scores in final course grades. It also would eliminate the requirement that students earn a cumulative score corresponding to satisfactory performance in all EOC exams in each core subject area. Instead it would require a student to earn a score on a 100-point scale corresponding to satisfactory performance. Students who failed to achieve a score requirement on an EOC test could retake the test but would not be required to do so.

Students would be allowed to satisfy EOC test performance requirements through satisfactory performance on nationally recognized norm-referenced assessments such as advanced placement, SAT, and ACT exams. A student who failed to perform satisfactorily on one of those exams could retake the test or take the appropriate EOC exam. The commissioner of education would be required to determine a method by which a student's satisfactory performance on the PSAT or the ACT-Plan could satisfy the EOC exam requirements. However, a student who failed the PSAT or ACT-Plan would have to take the appropriate EOC exam.

The admission, review, and dismissal committee of a student served by special education would determine whether the student was required to achieve satisfactory performance on EOC tests to be eligible to receive a high school diploma.

Students who completed grade 11 but were unlikely to pass the required exams would have to enroll in a corresponding content area college preparatory course. Students could use their scores on the EOC exam for the college preparatory course to satisfy the graduation requirement.

Public school accountability. CSHB 5 would establish a new three-category rating system evaluating schools on academic performance, financial performance, and community and student engagement.

Schools and districts would be rated using letter grades of A, B, and C to reflect acceptable performance, and F to reflect unacceptable performance. TEA would be required to release all three ratings at the same time each year by August 8. Each year by August 31, TEA would be required to post online the various letter performance ratings, financial accountability ratings, and distinction designations awarded to each district and open-enrollment charter school.

Academic performance. The accountability system for academic performance would have to include at least three additional indicators of student achievement beyond certain test results, dropout rates, and high school graduation rates, with weight given to non-test-based indicators to the greatest extent possible.

Districts and campuses could earn academic distinction designations for outstanding performance in attaining postsecondary readiness based on several factors, including the number of students who perform satisfactorily or show annual improvement on EOC exams. Campuses also could earn several different academic distinction designations associated with being in the top 25 percent in the state in annual improvement, closing achievement gaps, or high performance in core content areas.

The percentage of graduating students who meet the foundation course requirements, the distinguished level of achievement, and each diploma endorsement would serve as additional performance indicators for reporting purposes.

CSHB 5 would require the commissioner to conduct special accreditation investigations when excessive numbers of eligible students failed to complete an advanced mathematics or other advanced course.

Financial performance. The financial accountability rating system for school districts and open-enrollment charter schools would be developed by the commissioner of education in conjunction with the comptroller by March 1, 2015. It would assign a point value to each indicator to be used in a scoring matrix. One indicator would measure future financial solvency of a district or charter school. The commissioner would be required to evaluate the financial indicators at least once every three years. Before assigning a final rating, the commissioner would be required to assign a preliminary rating and consider additional information submitted by a district or charter school. Districts or charter schools assigned a failing rating under the financial accountability rating system would be required to submit a corrective action plan.

Community and student engagement. Each school district would evaluate its own performance and the performance of its campuses based on criteria developed by the commissioner of education in conjunction with a local committee at each school district. This new evaluation category would include measures related to:

- fine arts;
- wellness and physical education;
- community and parental involvement;
- the 21st Century Workforce Development program;
- the second language acquisition program; and
- compliance with statutory reporting and policy requirements.

SUPPORTERS
SAY:

CSHB 5 would bring needed balance to excessive state-mandated testing. The current system costs too much in time, money, and resources that should be dedicated to classroom instruction rather than test preparation. Over-testing threatens the futures of high school students, most of whom now must pass 15 EOC exams to be eligible to graduate, as opposed to four exit-level tests under the TAKS program.

The bill also would make changes to the high school curriculum that maintain rigor while providing students flexibility to pursue college or career interests. This would meet the growing need of Texas employers for

skilled workers ready to enter technical trades, such as welding, pipefitting, and computer animation. Finally, the bill would broaden the accountability system to lessen reliance on test scores and provide a better understanding of overall school performance.

While the commitment of Texas to public school accountability has certainly yielded gains in student achievement over the years, the burden created by excessive testing has grown too large. CSHB 5 would address the excesses of the state's testing and accountability system while maintaining high standards and expectations for Texas students.

Student assessment. CSHB 5 would reduce the high-stakes nature of EOC exams in several ways. It would lower the number of tests a student must pass to graduate from 15 to five. Even under these reduced requirements, the bill would maintain strict assessment requirements for graduation compared to other states, 42 of which require three tests or fewer and 25 of which require none.

By ending the requirement that EOC exam scores count for 15 percent of a student's grade, the bill would give districts local control over how to incorporate EOC scores into course grades. Last spring, in response to outcry from parents and school boards across the state, TEA allowed districts to delay the implementation of the "15 percent requirement," a policy retained by the current commissioner of education. CSHB 5 appropriately would remove this requirement from statute, which currently threatens the class ranks and grade point averages of high-achieving students if they perform poorly on any of the 15 EOC tests.

The emphasis on testing in the STAAR program narrows the curriculum and dampens the joy of learning with "drill-and-kill" exercises. Teachers and students are losing valuable instruction time taking practice tests to prepare for the high-stakes exams. CSHB 5 would allow schools to spend more of that time on classroom discussions and hands-on projects, which would spark students' curiosity and enrich their learning experiences.

At a time when the state is attempting to increase the rigor of academic work in high schools, the current testing regime contains a perverse incentive for students to switch to the minimum plan because it does not require satisfactory performance on all 15 EOC exams as a requirement for graduation. The initial round of STAAR testing in 2012 placed about 30 percent of sophomores at risk of not graduating. In addition, only 46

percent of ninth-grade students would have passed their English I reading exams and only 39 percent would have passed their algebra I exams if the state had not delayed implementing passing standards for the first year of STAAR. CSHB 5 would move the state assessment program away from policies that encourage test-fatigued students to take less demanding courses of study or even to drop out altogether.

The bill would save millions of dollars in testing costs. Texas is spending \$468 million over four years with its testing contractor, far more than other states. That money would be better used to hire more teachers and offer stronger academic programs. By reducing or making optional the number of EOC exams TEA had to develop and administer, CSHB 5 would result in savings of \$12.1 million annually, according to the fiscal note.

High school graduation programs. The bill would place all students on one foundation plan for graduation while allowing multiple pathways for students to pursue their career interests. Students are more engaged when they can tailor their studies to their interests and take courses that apply to their career choices.

The growing Texas economy needs skilled workers to work in the energy industry and other sectors that offer high-paying jobs that do not require a college degree. Not all students will go to college and they should be informed about other options for financially rewarding work. By eliminating the minimum graduation plan, the bill would ensure that all graduates were ready for postsecondary education, including community college, technical training, or four-year colleges and universities. CSHB 5 also would allow school districts to partner with community colleges and local businesses to develop local courses that meet area workforce needs.

The overall credit requirement for graduation would increase from 22 to 24 credits, and students could choose to take more challenging courses and earn endorsements in any of five areas, including multidisciplinary studies. By requiring that students earn a distinguished level of achievement designation to be eligible for college admission under the top 10 percent law, CHSB 5 would prevent students from taking less rigorous coursework in an attempt to rank in the top 10 percent of their graduating classes.

Current requirements that students on the recommended plan take four years of mathematics, science, English and social studies — known as the “4x4 plan,” — are inflexible. Career-training classes such as engineering, robotics, computer animation, and accounting can be just as rigorous as traditional academic courses. While many students struggle to pass algebra II, not all need to master this discipline for success in their post-high school lives. Students who wished to take algebra II still could do so under CSHB 5, and it would remain a required course for students to earn a distinguished achievement designation on their diplomas.

Public school accountability. The approach to accountability under CSHB 5 would paint a fairer, more comprehensive picture of campus and district performance while reducing the emphasis on testing. The current system puts too much focus on the worst performing subgroup, allowing a few students to potentially affect the rating of an entire campus. Using the familiar letter grades of A, B, C, and F would make it easier for the public to understand how a district or campus was performing.

The new accountability system under CSHB 5 would rate district and campus academic performance on many factors besides test scores. The new rating categories of financial accountability and community and student engagement would give the public a much better overall understanding of how schools and districts were performing. The bill would strengthen public investment in the system by involving local groups of parents and community and business leaders in decisions about what criteria should be used to evaluate their schools.

OPPONENTS
SAY:

CSHB 5 would reduce academic rigor and lower expectations for Texas students. Texas has been at the vanguard of public school accountability for decades, a commitment that has raised academic performance and narrowed achievement gaps among student groups. The performance of Texas students continues to improve compared to their peers nationally in eighth grade math, and graduation rates have increased steadily to almost 86 percent in 2011.

Nevertheless, too many high school graduates are not ready for college-level courses or the highly technical jobs of the future. Texas needs a skilled workforce to meet the demands of the 21st-century economy, and rigorous academic standards are the best way to prepare the state’s workforce for this challenge. By watering down the 4x4 curriculum and

STAAR EOC assessments that are designed to increase college and workforce readiness, CSHB 5 would take a step in the wrong direction.

Student assessment. Barely one year after the implementation of STAAR, it is too soon to retreat from the higher-level critical thinking skills that the new tests are designed to measure. The EOC exams are being phased in, and teachers already are using the results to better prepare students for future tests. Each time the state has adopted new assessments, the initial scores were low, but the data show students have improved their performance over time.

The EOC exams in CSHB 5 are designed for freshman- and sophomore-level courses, and would not be good measures of college readiness. Without a requirement that students pass advanced courses such as algebra II and physics, there would be little incentive for students to study these challenging subjects.

High school graduation programs. Rigorous graduation requirements are critical to helping more students enter and succeed in college and career. Challenging coursework in high school is the best predictor of student success at the community college and university levels. The 4x4 graduation plan ensures that all students are pursuing a course of study that should prepare them for success in college or the workforce.

The Higher Education Coordinating Board has estimated that 2,652 additional students would not be college-ready because of the graduation plan changes in CSHB 5. The cost in state higher education funding to remediate these students is estimated at \$1 million, not to mention the further \$1.8 million those students are projected to incur in additional tuition and fees.

Loosening graduation standards to allow students to pursue more career training could lead to minority students being steered disproportionately into the career option and away from the college track. This could have a long-term impact for these students and for the state because minority students constitute the majority of the state's public school student population. Studies have shown that people with college degrees earn significantly more over their lifetimes than those without a degree.

The state's default curriculum should include algebra II, while allowing some students to opt out of it. Many jobs of the future will require high-

level mathematics skills, and now is not the time to undo the requirement that students take four years of mathematics. A course such as algebra II teaches higher-order thinking and critical reasoning skills that prepare students for postsecondary education, regardless of what they decide to pursue after high school.

Public school accountability. The existing accountability system is designed to ensure that public schools are fulfilling their core mission of teaching the state-mandated curriculum. Most parents are familiar with the district and campus rating system and use the designations to hold local school officials responsible.

OTHER
OPPONENTS
SAY:

EOC exams should be limited to three in the core subjects of mathematics and English language arts. Better yet, Texas should do away with all EOC exams and rely on national tests such as the SAT and ACT. Student gains on the TAKS over the past decade have not translated into similar improvements on national norm-referenced exams such as the SAT and ACT. There is no reason to believe that tweaking the new STAAR program would have better results.

Reducing the testing burden on Texas high school students is a good idea, but over-testing in grades 3 through 8 also should be addressed.

NOTES:

CSHB 5 differs from the bill as introduced in several ways. Unlike HB 5 as filed, the committee substitute would:

- add a third science course for the foundation diploma;
- reduce the number of electives from eight to seven;
- allow world geography or world history for the third social studies credit;
- allow students to receive credit in a fine arts program not provided by the school district;
- add a distinguished level of achievement graduation program and make those students eligible for automatic admissions under the top 10 percent law;
- make students who completed the foundation diploma and certain other requirements eligible for TEXAS grants;
- drop the letter grade D from the accountability ratings; and
- require three indicators in addition to STAAR results and graduation rates for evaluating school performance.

According to the Legislative Budget Board (LBB), CSHB 5 would result in a savings of \$25.1 million in fiscal 2014-15. The state would save money from eliminating EOC exams but would face higher costs for collecting financial data and for additional students needing college remedial courses. In its analysis of the bill as introduced, the LBB projected savings of \$27.9 million in fiscal 2014-15, but has since increased its estimate of how much data collection for the financial accountability system would cost.

Unofficial copy Travis Co. District Clerk Velda L. Price

LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 83RD LEGISLATIVE REGULAR SESSION

May 25, 2013

TO: Honorable David Dewhurst, Lieutenant Governor, Senate
Honorable Joe Straus, Speaker of the House, House of Representatives

FROM: Ursula Parks, Director, Legislative Budget Board

IN RE: HB5 by Aycock (Relating to public school accountability, including assessment, and curriculum requirements; providing a criminal penalty.), **Conference Committee Report**

Estimated Two-year Net Impact to General Revenue Related Funds for HB5, Conference Committee Report: a positive impact of \$11,376,839 through the biennium ending August 31, 2015.

The bill would make no appropriation but could provide the legal basis for an appropriation of funds to implement the provisions of the bill.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2014	\$6,593,905
2015	\$4,782,934
2016	\$5,390,981
2017	\$5,672,081
2018	\$7,882,281

All Funds, Five-Year Impact:

Fiscal Year	Probable Savings/(Cost) from <i>General Revenue Fund</i> 1	Probable Savings/(Cost) from <i>Foundation School Fund</i> 193
2014	(\$2,056,095)	\$8,650,000
2015	(\$3,867,066)	\$8,650,000
2016	(\$3,259,019)	\$8,650,000
2017	(\$2,977,919)	\$8,650,000
2018	(\$767,719)	\$8,650,000

EXHIBIT
6533

Fiscal Year	Change in Number of State Employees from FY 2013
2014	2.0
2015	2.0
2016	2.0
2017	2.0
2018	2.0

Fiscal Analysis

The bill would eliminate the Minimum, Recommended, and Advanced High School graduation programs, and would create the Foundation High School Program. The bill would create endorsements on a student's diploma and transcript if the student completes certain courses. The endorsements would include science, technology, engineering, and mathematics; business and industry; public services; arts and humanities; and multidisciplinary studies. The bill would require four credits in mathematics to earn any endorsement and would require each student to identify an endorsement the student intends to earn upon entering the ninth grade.

The bill would require the Commissioner of Education to develop a transition plan to implement the bill with respect to replacing the Minimum, Recommended, and Advanced High School graduation programs with the Foundation High School Program beginning with the 2014-15 school year.

The bill would require the Texas Education Agency (TEA) to redevelop assessment instruments administered to students with significant cognitive disabilities in alignment with federal law.

The bill would limit end-of-course assessments to Algebra I, Biology, English I, English II, and United States History. The bill would require the English I and II end-of-course assessments to assess both reading and writing in the same assessment. The bill would eliminate the requirement that a student's performance on an end-of-course assessment shall account for 15 percent of the student's final grade for the course.

The bill would require TEA to administer post-secondary readiness assessment instruments for Algebra II and English III at a district's option.

The bill would require the release of questions and answer keys to certain assessment instruments in fiscal years 2014-2017.

The bill would modify the terms of payment for the Instructional Materials Allotment.

The bill would exclude a student who is reported as a dropout, reenrolls, and drops out again in computing dropout and completion rates.

The bill would require TEA to develop and maintain an internet website known as the Texas School Accountability Dashboard which would provide performance indexes on certain criteria for each campus.

The bill would require TEA, in collaboration with the HECB and the Texas Workforce Commission, to evaluate, through an external evaluator, the implementation of the changes to the curriculum requirements for high school graduation that would be required by this bill.

Methodology

The bill would reduce the number of end-of-course assessments from 15 to 5.

Reducing the number of end-of-course assessments would result in savings of \$8.7 million annually.

The estimated savings for eliminating the Geometry, Chemistry, Physics, World Geography, and World History end-of-course assessments would be \$1.15 million per fiscal year, per end-of-course assessment. The estimated savings of combining the reading and writing end-of-course assessments into one assessment each for English I, English II, would be \$0.9 million annually.

This analysis assumes that the July and December administrations of the Algebra II and English III assessments would be eliminated. The estimated savings from eliminating the July and December administrations of the Algebra II assessment would be \$300,000 per fiscal year, and the estimated savings from eliminating the July and December administrations of the English III assessment would be \$1.7 million annually.

Based on information provided by TEA, the modification to PEIMS to collect information required by the bill would cost \$87,050 in fiscal year 2014.

Based on information provided by TEA, changes would be required to the educational materials system related to the modified terms of payment from the Instructional Materials Allotment at an estimated cost of \$5,000 in fiscal year 2014.

Based on information provided by TEA, the cost to develop assessment instruments administered to students with significant cognitive disabilities would be \$550,000 in fiscal year 2014 and \$550,000 in fiscal year 2015.

This analysis assumes the cost to release the questions and answer keys to certain assessment instruments would be \$2.4 million in fiscal year 2015, fiscal year 2016, and fiscal year 2017.

Based on information provided by TEA, one FTE would be required to calculate the non-cohort based graduation rate required by the modification to the calculation of completion and dropout rates. The estimated cost of this FTE, including salary, benefits, and other operating expenses, would be \$95,471 in fiscal year 2014 and \$87,471 in subsequent years.

Based on information provided by TEA, one FTE would be required to develop and maintain the Texas School Accountability Dashboard. The estimated cost of this FTE, including salary, benefits, and other operating expenses, would be \$112,161 in fiscal year 2014 and \$104,161 in subsequent years.

Based on information provided by TEA, the estimated cost to study the implementation of the changes to the curriculum requirements for high school graduation required by this bill would be \$0.3 million in fiscal year 2016 and \$0.2 million in fiscal year 2018.

To the extent that as a result of the bill, students will take additional developmental education classes at public institutions of higher education, there could be formula funding costs beginning in fiscal year 2016. The institutions may also realize additional tuition revenue tied to these students.

Technology

TEA estimates \$0.1 million in fiscal year 2014 to amend PEIMS.

Local Government Impact

The bill would create a Class B misdemeanor. A Class B misdemeanor is punishable by a fine of not more than \$2,000, confinement in jail for a term not to exceed 180 days, or both. Costs associated with enforcement, prosecution, and confinement could likely be absorbed within existing resources. Revenue from fines imposed and collected is not anticipated to have a significant fiscal impact.

A school district might experience savings from the reduced number of end-of-course assessments, although a district might incur some additional costs related to implementing the provisions of the bill.

Source Agencies: 320 Texas Workforce Commission, 701 Central Education Agency, 781 Higher Education Coordinating Board

LBB Staff: UP, JBi, JSc, AH, GO

~~28.002(c). [Not later than December 1, 2010, the agency shall provide to the legislature a report regarding the pilot program, including the feasibility of expanding the pilot program statewide.]~~

Amendment No. 29 was adopted.

Amendment No. 30

Representative Patrick offered the following amendment to **CSHB 5**:

Floor Packet Page No. 68

Amend **CSHB 5** (house committee printing) as follows:

- (1) On page 11, line 21, immediately following the semicolon, insert "and".
- (2) On page 11, line 23, strike "; and" and substitute an underlined period.
- (3) On page 11, lines 24-25, strike "(4) the curriculum requirements for at least one endorsement under Subsection (c-1)."

AMENDMENT NO. 30 - STATEMENT OF LEGISLATIVE INTENT

REPRESENTATIVE S. KING: Representative Patrick, have you heard from members on this floor from their school districts on how the endorsement component would affect their districts?

REPRESENTATIVE PATRICK: Yes. There are a number of small and rural districts represented by this body in which it has been reported to me that they have, for example, only one agriculture and business teacher. Another school district, one high school, two teachers and one teacher for business and accounting. Another high school reported that they have a pathway of agriculture, livestock production advanced animal sciences, and so forth. So, for the students that are seeking the distinguished level, which translates to eligibility for top 10 percent, they're going to have to go through the pathways that exist in their school district.

S. KING: So, are you saying that if they do not have an endorsement either, one, that they're interested in or, two, that's available, they would no longer be considered for the top 10 percent?

PATRICK: They would not be eligible for the top 10 percent if they do not complete an endorsement, as proposed by **HB 5**. What this amendment does is say that all students who complete the foundation program and, in addition, Algebra II and one advanced science, would be eligible for the top 10 percent.

S. KING: And that is without an endorsement. Is there anything in this bill that has an option for the endorsement, or is that the whole purpose of your bill—or your amendment?

PATRICK: The amendment does not do away with endorsements.

S. KING: Correct.

PATRICK: The amendment simply says you do not have to have an endorsement to be eligible for the top 10 percent.

S. KING: So, does that mean that students that, prior to this bill, without passing your amendment, would no longer be available or qualified to seek the top 10 percent designation if they could not comply with this endorsement? Is that correct?

PATRICK: That is correct.

S. KING: How many students do you think that might include—you mentioned over half the school districts are rural, or not metropolitan, so they would, perhaps, not have the capacity for the amendment—I mean the endorsements. Is that correct?

PATRICK: Yes, the majority of school districts in the State of Texas have less than 1,000 pupils in the whole school district. Some high schools have 200 or fewer students, and because of that they are not able to provide the array of endorsements that we have suggested are required. We're talking about the majority of districts—we're not talking about the majority of students. The majority of students are in our urban areas and they have access to these things, but we're talking about the majority of districts represented by this body.

S. KING: So, in your opinion—one last question. Does this have a negative impact on the rural students of the State of Texas in regard to them being able to be qualified for the top 10 percent admission to a public university?

PATRICK: The rural and small districts do not have the endorsement pathways that would be available to give students in those districts the choices that they deserve, to pick the areas that are described in the bill, for example, STEM. That's not widely available. The most popular pathway in the state is agriculture, at the present time.

REPRESENTATIVE ANDERSON: Let me ask you a question that may have already been dealt with here, but—so, you're saying that currently there's a number of schools, particularly in rural areas, that do not have access to endorsement options as far as pathways?

PATRICK: That's correct. Because of the limited number of courses that they are able to offer, they can afford to offer, and, more importantly, they have the teachers to teach the classes, they all report back to me that they struggle with finding teachers, presently.

ANDERSON: Okay, and so that would make it a much higher hurdle for those students in rural school districts to be able to attain the top 10?

PATRICK: That's correct. The endorsements are required, one endorsement or more, to be eligible for the top 10 percent. What my amendment simply does is say that you would be eligible for the top 10 percent if you have completed the foundation programs and attained distinguished level by completing Algebra II and an advanced science. It gives students the option of adding endorsements, and also in the bill, the performance acknowledgement options are mentioned. We haven't talked much about that today, but if a student completed dual credit, AP or IB, PSAT, ACT, SAT, etc., this performance acknowledgement option and

the endorsement options are yet to be established by the SBOE. We do not know what courses those will involve, but it will be approximately six courses, which would take away all the electives that a student would have.

ANDERSON: These options would actually increase the flexibility of **HB 5** as far as its ability to reach more school districts?

PATRICK: That would be the goal, yes. Thank you.

ANDERSON: You bet. In your opinion—and this may be a difficult question—how long do you think it would take, say the average community under 1,000 population, to be able to offer the endorsement options both either in teachers or in space—classroom space or in curriculum?

PATRICK: If **HB 5** passes and it's not amended per my amendment, I would hope that they could do that quickly. Whether that's actually going to occur I'm not sure, because it's also a matter of cost to the district, and so, as Chairman Aycock mentioned, there would be cost involved for the district.

ANDERSON: So, it may be a year, it may be two years, it may be five years—those youngsters in those rural communities may not have access to this, consequently would be denied access to the top 10 for five or 10 years—for their whole high school career.

PATRICK: Or for some period of time, until they were able to add these courses to their curriculum, and until that time comes they will be limiting their students to the endorsements or pathways that they currently have.

Representative Aycock moved to table Amendment No. 30.

The motion to table prevailed by (Record 99): 113 Yeas, 28 Nays, 2 Present, not voting.

Yeas — Allen; Alvarado; Ashby; Aycock; Bell; Bohac; Bonnen, G.; Branch; Burkett; Button; Callegari; Capriglione; Carter; Clardy; Cook; Craddick; Creighton; Crownover; Dale; Darby; Davis, J.; Davis, S.; Deshotel; Dutton; Elkins; Fallon; Farney; Farrar; Fletcher; Flynn; Frank; Frullo; Geren; Giddings; Goldman; Gonzales; Guerra; Harless; Harper-Brown; Herrero; Hilderbran; Huberty; Hughes; Hunter; Isaac; Kacal; Keffer; King, K.; King, P.; King, T.; Kleinschmidt; Klick; Kolkhorst; Krause; Kuempel; Larson; Laubenberg; Lavender; Leach; Lewis; Longoria; Lozano; Lucio; Martinez; McClendon; Menéndez; Miles; Miller, D.; Miller, R.; Moody; Morrison; Murphy; Nevárez; Orr; Otto; Paddie; Parker; Perez; Perry; Phillips; Pickett; Pitts; Price; Raney; Ratliff; Raymond; Riddle; Ritter; Sanford; Schaefer; Sheets; Sheffield, J.; Sheffield, R.; Simmons; Simpson; Smith; Smithee; Springer; Stephenson; Stickland; Taylor; Thompson, E.; Thompson, S.; Toth; Turner, C.; Turner, E.S.; Turner, S.; Villalba; Villarreal; White; Workman; Zedler; Zerwas.

Nays — Alonzo; Anderson; Burnam; Coleman; Collier; Cortez; Davis, Y.; Eiland; Farias; González, M.; Gonzalez, N.; Gooden; Guillen; Gutierrez; Hernandez Luna; Howard; Johnson; King, S.; Márquez; Martinez Fischer; Muñoz; Naishtat; Patrick; Rodriguez, J.; Rose; Strama; Walle; Wu.

Present, not voting — Mr. Speaker; Bonnen, D.(C).

Absent, Excused — Reynolds.

Absent — Anchia; Canales; Dukes; Oliveira; Rodriguez, E.; Vo.

STATEMENTS OF VOTE

When Record No. 99 was taken, I was in the house but away from my desk. I would have voted yes.

Canales

I was shown voting no on Record No. 99. I intended to vote yes

S. King

HR 1134 - ADOPTED (by Dutton)

Representative Dutton moved to suspend all necessary rules to take up and consider at this time **HR 1134**.

The motion prevailed.

The following resolution was laid before the house:

HR 1134, In memory of Frank Thompson, Jr., of Houston.

HR 1134 was unanimously adopted by a rising vote.

On motion of Representative Dutton, the names of all the members of the house were added to **HR 1134** as signers thereof.

CSHB 5 - (consideration continued)

Amendment No. 31

Representative Branch offered the following amendment to **CSHB 5**:

Floor Packet Page No. 69

Amend **CSHB 5** (house committee printing) on page 12 by striking lines 23-26 and substituting the following:

(c-2) In adopting rules under Subsection (c-1), the State Board of Education shall:

(1) require a student in order to earn any endorsement to successfully complete four credits in mathematics, which must include:

(A) the courses described by Subsection (b-1)(2); and

(B) an additional advanced mathematics course authorized under Subsection (b-2) or an advanced career and technology course designated by the State Board of Education as containing substantively similar and rigorous academic content to such an advanced mathematics course; and

(2) develop additional curriculum requirements for each endorsement with the direct participation of educators and business and industry representatives.

Amendment No. 31 was adopted.

(3)~~(2)~~] other factors for determining sufficient student attainment of postsecondary readiness.

(b) This section applies beginning with the 2013-2014 school year.

(13) In the recital to amended Section 51.3062, Education Code, and strike "by amending Subsection (i) and adding Subsections (q-2) and (q-3)" and substitute "by adding Subsection (q-3)".

(14) Strike amended Section 51.3062(i), Education Code.

(15) Strike added Section 51.3062(q-2), Education Code.

(16) In amended Section 56.3041(a)(2)(A)(ii), Education Code, strike "Section 51.3062(p) or [] (q) [~~or (q-1)~~]" and substitute "Section 51.3062(p), (q), or (q-1)".

(17) Add the following appropriately numbered SECTION to read as follows:

SECTION _____. (a) Effective September 1, 2013, the following provisions of the Education Code are repealed:

(1) Sections 29.190(b) and (e); and

(2) Section 39.025(a-3).

(b) Effective September 1, 2014, the following provisions of the Education Code are repealed:

(1) Section 28.002(q);

(2) Section 28.0212(e) and (g);

(3) Sections 28.025(b-6), (b-8), and (g);

(4) Section 39.0822; and

(5) Sections 39.0823(b) and (c).

Amendment No. 3 was adopted.

HB 5 - STATEMENT OF LEGISLATIVE INTENT

REPRESENTATIVE HERRERO: I supported **HB 5** yesterday, and I intend to do that today, as well, on third reading. In knowing that there are certain implementations, if you will, through **HB 5** that affect public schools, I think that's part of the equation, if you will, in helping improve our public schools and our neighborhood schools. The other part, in my opinion, deals with the funding for our public schools. And so, when we look at today's calendar, for example, we have, obviously, **HB 5** that deals with accountability and assessment with respect to public schools, and then, we also have **HB 4**, then, that deals with water and the funding structure for water projects. And so, my question is, when will we, as a body, be able to discuss public school finance, where we, as a body, can do what we can to advocate for our constituents and our neighborhood schools, our children, our teachers, that are faced with circumstances, where, because of cuts that were made last legislative session, are having now overcrowded classrooms, student-teacher ratios that are not what we would want under ideal circumstances. And my question to you is, will we, and, if so, when will we have the opportunity to address school finance as a body?

REPRESENTATIVE AYCOCK: I think there are two parts to your question, actually. The first deals with the amount of money we will put into the system. I think that discussion will occur very quickly. As we come to the budget, I think

people will have an opportunity, as always, to discuss that amount of money and move money around within that budget. We'll have a long day, as you know, that day that discusses that amount. I think the harder question is what I call the distribution model, some people call it the formula, but it's really a distribution model of which schools get the money, how it's distributed. Thus far, it's my understanding, and I'm not on the Appropriations Committee, but it's my understanding that the amount of money that has been put in, so far, is substantial, perhaps not adequate in many people's minds, but substantial. And that money has been directed to, at first, removing that RPAF. I think when we come to the budget, you will see that RPAF goes back to 1, is the plan, and that is my understanding, as I understand it presently. I'm not going to speak for the Appropriations Committee. I might not ought to be having this discussion even, but I think the question will be, do we restore that and where does the rest of the money go? And I think most of it will go to raise the lower tier of schools, and I hope that the body will, in fact, move the bottom up, as we say, and try to move that bottom up.

HERRERO: And I think that is a step in the right direction, and I guess, the first part of your answer was, how much money. And I think we heard yesterday, if I understood correctly, Chairman Pitts, in answering questions from Representative Burnam, that the budget in 2014-15 does not restore the \$5.4 billion cuts to public education, and that the amount in the supplemental budget also would not fully restore the cuts that were made to public education. And so, there's that discussion, and I know that you indicated that it depends on what we think is adequate, and it may depend on who we're talking about, and the districts that we each respectively represent, but that's part of why I'm bringing this up, because we each have different opinions on what that amount may be and how we think we can better structure a school-funding formula that allows for there to be equality, if you will, across the state. And, to your knowledge, is there a time when we, as a body, will be able to address public school funding on the house floor during this regular session?

AYCOCK: My committee does not have a bill before it that we are considering to that end, and beyond that, I do not know of a vehicle that is likely to be considered, at this time, regarding that distribution formula. Quite candidly, when the legislature has attempted, in the past, to model and craft a distribution formula ahead of a court order, it has not been very successful, historically. It has always had to come back and say, "Well, the court didn't like what we did." To that end, I think many in the body will probably propose that we wait for that court order, and say, "Judge, what do you want us to do, with the distribution model in particular?" That court case will also, as you well know, address adequacy; it will address equity; it will address a number of issues that are before the court, and there will be litigance in that issue. And I understand the argument about, we need to decide the issue independent of the courts, but historically, that has not been a real successful operation. And so, I'm one of those guys that would probably say, "Let's get a court order before we know what we're going to do, before we do the distribution model." To that end, I will also be one of those guys that say, "If there's money available, we need to put it in public schools."

HERRERO: And thank you for saying that, and I respectfully disagree with the approach on waiting for the judicial branch to dictate to the legislature something which, by constitution, is a responsibility of the legislative body.

AYCOCK: I understand the frustration.

HERRERO: And part of the frustration that compounds it is the fact that we're not, at this point, instead of addressing the issue up front and funding public education first, as a priority, as I think it should be, the monies that we do have, that we obviously know are limited, but the monies that we do have, we're spending it elsewhere, not in public education. And that's where the frustration, in my opinion, gets compounded, because, let's assume that the court comes back and tells us, "You need some X amount of money," but we've already appropriated it somewhere else. And I think we're digging ourselves in a hole that we may not be able to get ourselves out of, and this is where I think the priorities of the legislature should be such that we make public education the number one priority, and that we fully restore the cuts to public education so that teachers are in better circumstances to ensure that our children, no matter who they are, are able to achieve the highest potential that they can, whether it be going into a trade or a four-year university. And this is where I think it is creating a situation where we may want there to be success in public education through these assessments and accountability standards, but unless we provide the resources and the tools to accomplish that goal, we may fall short. And it's not due to any direct result of your efforts, because, as I mentioned before, you've done an outstanding job as it pertains to accountability and assessment, but I would urge you, as well as the speaker and every member here, to make sure that we make public education a priority. Because we have to make sure that we meet our constitutional obligation and that we provide an equal education to every student, so that, no matter what their dreams are, that they are achieved and we have success when it comes to public education.

AYCOCK: And I pledge to join you on trying to find adequate resources for all our children, in every program, in every district in the state, and I will join you in that effort.

PARLIAMENTARY INQUIRY

HERRERO: Mr. Speaker, if I'm an individual that wishes to make public education a priority, specifically, public school finance a priority, and given that there isn't currently a bill within the public education committee, what would be the avenue for me, as a member, to bring public education—public school finance to the forefront, so that we as members can decide where public education falls within the spending priorities of the state?

SPEAKER STRAUS: Mr. Herrero, you can either introduce another bill or you can speak with the chairman of Appropriations.

HERRERO: In order to file the bill, would I need to get permission from the body to file the bill after the filing deadline?

SPEAKER: That's correct.

HERRERO: And would that be—would that request require recognition from the speaker or would it be a motion that I'm able to make pursuant to the rules?

SPEAKER: Mr. Herrero, the chair has recognized everyone who has made that request.

REMARKS ORDERED PRINTED

Representative Herrero moved to print remarks between Representative Aycock and Representative Herrero and between Speaker Straus and Representative Herrero.

The motion prevailed.

HB 5, as amended, was passed by (Record 116): 147 Yeas, 2 Nays, 1 Present, not voting.

Yeas — Allen; Alonzo; Alvarado; Anchia; Anderson; Ashby; Aycock; Bell; Bohac; Bonnen, D.; Bonnen, G.; Branch; Burkett; Burnam; Button; Callegari; Canales; Capriglione; Carter; Clardy; Coleman; Collier; Cook; Cortez; Craddick; Creighton; Crownover; Dale; Darby; Davis, J.; Davis, S.; Davis, Y.; Deshotel; Dukes; Dutton; Eiland; Elkins; Fallon; Farias; Forney; Farrar; Fletcher; Flynn; Frank; Frullo; Geren; Giddings; Goldman; Gonzales; González, M.; Gooden; Guerra; Guillen; Gutierrez; Harless; Harper-Brown; Hernandez Luna; Herrero; Hilderbran; Howard; Huberty; Hughes; Hunter; Isaac; Johnson; Kacal; Keffer; King, K.; King, P.; King, S.; King, T.; Kleinschmidt; Klick; Kolkhorst; Krause; Kuempel; Larson; Laubenberg; Lavender; Leach; Lewis; Longoria; Lozano; Lucio; Márquez; Martinez; Martinez Fischer; McClendon; Menéndez; Miles; Miller, D.; Miller, R.; Moody; Morrison; Muñoz; Murphy; Naishtat; Nevárez; Oliveira; Orr; Otto; Paddie; Parker; Patrick; Perez; Perry; Phillips; Pickett; Pitts; Price; Raney; Ratliff; Raymond; Reynolds; Riddle; Ritter; Rodriguez, E.; Rodriguez, J.; Rose; Sanford; Schaefer; Sheets; Sheffield, J.; Sheffield, R.; Simmons; Simpson; Smith; Smithee; Springer; Stephenson; Stickland; Taylor; Thompson, E.; Thompson, S.; Toth; Turner, C.; Turner, E.S.; Turner, S.; Villalba; Villarreal; Vo; Walle; White; Workman; Wu; Zedler; Zerwas.

Nays — Gonzalez, N.; Strama.

Present, not voting — Mr. Speaker(C).

HB 281 ON THIRD READING

(by Lucio, Carter, and Alvarado)

HB 281, A bill to be entitled An Act relating to the right of one immediate family member of certain deceased peace officers to make an oral statement regarding the terms of a plea bargain agreement.

HB 281 was passed by (Record 117): 149 Yeas, 0 Nays, 1 Present, not voting.

Yeas — Allen; Alonzo; Alvarado; Anchia; Anderson; Ashby; Aycock; Bell; Bohac; Bonnen, D.; Bonnen, G.; Branch; Burkett; Burnam; Button; Callegari; Canales; Capriglione; Carter; Clardy; Coleman; Collier; Cook; Cortez; Craddick; Creighton; Crownover; Dale; Darby; Davis, J.; Davis, S.; Davis, Y.; Deshotel;