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Fiscal Impacts of Proposed Educational Tax Credits

Eric Fruits, Ph.D.

Economics International Corp. – www.econinternational.com

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Executive summary

Currently, Oregon parents of public school children who need extra tutoring or other assistance are not reimbursed for that expense. In addition, many low-income parents or parents with children with disabilities cannot find public education alternatives that meet their children's demands and cannot afford educational options available from private schools. In response to these gaps, Cascade Policy Institute proposes two tax credits to help support efforts to make educational opportunities more affordable to Oregon families.

1. The ***Opportunity Scholarship Tax Credit*** is a tax credit for donations made to a tuition scholarship organization that gives scholarships to low-income students or students with disabilities.
2. The ***Oregon Family Education Tax Credit*** is a personal tax credit of $1,000 (per child) for many educational expenses.

The ***Opportunity Scholarship Tax Credit*** would potentially produce a net fiscal gain to the state as it would require a relatively small shift of students to private schools for the tax credit program to pay for itself. The tax credits would be, in effect, exempt from Kicker calculations, thereby increasing the amount of funding retained in the State of Oregon.

The ***Oregon Family Education Tax Credit*** may have an impact on state revenues. Most of the taxpayers who would take advantage of the credit would be infra-marginal taxpayers, meaning that the credit would represent a windfall to the taxpayer and a net cost to the state. On the other hand, if a sufficient number of students transfer to private schools, then per-student public school spending would *increase* by $90 to $730.

Background

Currently, Oregon parents of public school children who need extra tutoring or other assistance are not reimbursed for that expense. Also, parents who homeschool or send their children to private schools do not receive credit for the taxes they pay for public schools.

In addition, many low-income parents or parents with children with disabilities cannot find public education alternatives that meet their demands. Moreover, many of these parents cannot afford educational options available from private schools.

Cascade Policy Institute proposes two tax credits to help support efforts to make educational opportunities more affordable to Oregon families. At the request of Cascade Policy Institute, this report evaluates the potential fiscal impacts of the proposed tax credits, focusing on the "break even" number of students needed for the fiscal benefits of tax credit programs to equal the fiscal cost of the credits.

Proposed tax credits

The ***Opportunity Scholarship Tax Credit*** is a tax credit for donations made to a tuition scholarship organization that gives scholarships to low-income students or students with disabilities. Low-income students are those from a family with a taxable income that does not exceed the income standard for the free or reduced price lunch program. Credits would be limited to a maximum of:

- $1,000 per Oregon taxpayer ($2,000 for married couples filing jointly), and
- $10,000 for Oregon businesses in which the first $2,000 would be 100 percent eligible for the credit and the rest would be 75 percent eligible.

The ***Oregon Family Education Tax Credit*** is a personal tax credit of $1,000 (per child) for any educational expenses including:

- Tuition and fees for educational services, including tutoring,
- Transportation related to educational activities,
- Educational association memberships,
- Testing fees, and
- Educational materials, including books, school supplies, academic lessons, instructional software and academic curricula.

The tax credit cannot be applied to fees or expenses for athletic activities.

Existing education tax credit programs

Many states' tax credit programs have been implemented fairly recently. At the same time, many educational statistics have a lag of several years. Consequently, very little research exists measuring the long-run fiscal impacts of the programs.

Research on Florida's tax credit program finds that the credits for low-income scholarships do not divert funds away from education. Instead, K–12 per pupil state and local revenues in Florida have risen steadily since the inception of the state's tax credit program.[1]

A study prepared in anticipation of Georgia's tax credit program concludes that the program would produce fiscal benefits so long as the scholarships can be sufficiently

[1] Collins Center for Public Policy, Inc. *The Florida Corporate Income Tax Credit Scholarship Program: Updated Fiscal Analysis*. February 2007.

large to attract students from low-income families.[2] Oregon's proposed program has no restrictions on the amount of the scholarships awarded by tuition scholarship organizations. The Georgia study indicates that the state would receive larger fiscal benefits if income restrictions were raised so that some students from middle-income families would be eligible for scholarships.

One criticism of the private school tuition program is that it benefits only those who are already sending their children to private schools.[3] In contrast, one study concludes that most tuition scholarship organizations use financial need as the primary criterion for allocating scholarships to eligible students.[4] The study estimates that 15 to 30 percent of scholarships in the Arizona program were awarded to students that otherwise would have attended public schools. Oregon's proposed program limits scholarships to low-income students and to students with disabilities. As such, the Oregon proposal is designed to attract "new" students to the private education system.

Table 1: States with education tax credit programs

State	Who Can Claim the Credit	Type of Credit	Maximum Amount	Expenses Allowed
Arizona[5] (1997, 2006)	Individuals, corporations	Tuition scholarship organizations	$500 individual $1,000 joint Total corporate amount capped at $17.28 million	Tuition scholarships
	Individuals	Education expenses	$200 individual $400 joint	Extracurricular activities, character education programs
Florida[6] (2001)	Corporations	Tuition scholarship organizations	Total amount capped at $118 million	Tuition scholarships
Georgia[7] (2008)	Individuals, corporations	Tuition scholarship organizations	$1,000 individual $2,500 joint 75% of corporate income tax liability	Tuition scholarships
Illinois[8] (1998)	Individuals	Education expenses	$250 per child $500 maximum	Tuition, book fees, lab fees
Iowa[9] (1987)	Individuals	Education expenses	$250	Tuition, textbooks

[2] Gottlob, B. *The Fiscal Impact of Tax-Credit Scholarships in Georgia*. Friedman Foundation for Educational Choice, Alliance for School Choice, Georgia Public Policy Foundation, Americans for Prosperity, Black Alliance for Educational Options, and Georgia Family Council. February 2008.
[3] Pathak, A.; Holmes, D.; Mincberg, E.; and Neas, R. G. *A Model To Avoid: Arizona's Tuition Tax Credit Law*. People for the American Way Foundation. 2001.
[4] Lips, C. and Jacoby, J. "The Arizona Scholarship Tax Credit: Giving Parents Choices, Saving Taxpayers Money." *Policy Analysis*. September 17, 2001.
[5] Arizona Revised Statutes 43-1089, 43-1089.01, 43-1183.
[6] Florida Statutes 220.187.
[7] Code of Georgia Titles 20, 48.
[8] Illinois Administrative Code Title 86.

State	Who Can Claim the Credit	Type of Credit	Maximum Amount	Expenses Allowed
Louisiana[10] (2008)	Individuals	Education expenses	$5,000 per child	Tuition, fees and other eligible expenses
Minnesota[11] (1955, 1997)	Individuals	Education expenses	$1,000 per child $200 for computer/software	Tutoring, educational summer camps, textbooks, instructional materials, home computer hardware, educational software
	Individuals	Education expenses	$1,625 per child (K-6) $2,500 per child (7-12)	Private school tuition
Pennsylvania[12] (2001)	Corporations	Tuition scholarship organizations (private schools), educational improvement organizations (public schools)	$150,000 for pre-K programs $300,000 for all other programs	Tuition scholarships
Rhode Island[13] (2001)	Corporations	Tuition scholarship organizations	$100,000 per business Total amount capped at $1 million	Tuition scholarships

Fiscal Analysis

Each state's tax system and educational tax credit programs are unique. Thus, it is impossible to examine another state's program and conclude that the proposed programs for Oregon would have the same experience. Using a range of hypothetical levels and intensities of participation in the proposed programs, this study estimates the potential fiscal impact of the proposed tax credit programs in Oregon.

Opportunity Scholarship Tax Credit

Table 3 presents the potential fiscal impact of the Opportunity Scholarship Tax Credit as a "break-even" analysis. It shows how many students would have to transfer from public schools to private schools for the proposed credit to pay for itself via reduced public school expenditures.

Approximately three percent of personal income tax filers take advantage of Arizona's scholarship tax credit, with an average credit of approximately $700 per filer, for a total of $54 million in 2007.[14] This analysis assumes that Oregon would have the same

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[9] Iowa Code 422.12.
[10] Louisiana Revised Statutes 47:293(9)(a)(xiv), (xv),(xvi); 297.10 through 297.12.
[11] Minnesota Statutes 290.0674.
[12] Pennsylvania Code Article XX-B.
[13] Rhode Island General Laws Title 44-62.
[14] Arizona Department of Revenue. *Individual Income Tax Credit for Donations to Private School Tuition Organizations: Reporting for 2007*. 2008.

participation percentage, but that the average credit would be $1,200 per filer.[15] The higher credit is reasonable because (1) Oregon allows for a larger credit, and (2) Oregon's personal income tax burden is higher than Arizona's. This would amount to approximately $65 million in donations and tax credits.

If every Oregon corporate taxpayer took advantage of the proposed scholarship tax credit, at most approximately $91.5 million in credits would be claimed, representing approximately $116 million in donations to scholarship organizations.[16] This is a very conservative estimate as it would be unreasonable to assume such a high level of participation in the program.

Table 2 shows that, on average, Oregon spends $10,250 per K–12 student.[17,18] Of this, $9,170 represent operating expenditures. Thus, to the extent the tax credits shift students from public education to private schools, public school expenditures would decline by $9,170 per student. Depending on the level and intensity of corporate participation in the tax credit program, so long as 9,400–14,400 students switch to private schools, then the tax credit would "pay for itself."[19] It would be reasonable to expect such levels, because at such levels of participation, the average scholarship would be approximately 20 percent higher than average private school tuition.[20] Average private school tuition is assumed to be $7,200 per year.[21] Moreover, the break-even number of students represents less than 10 percent of the estimated number of students eligible for scholarships under the proposed credit program.[22]

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[15] See Oregon Department of Revenue. *Oregon Personal Income Tax Statistics: Tax Year 2006*. 2008.

[16] Author's calculations based on Oregon Department of Revenue. *Oregon Corporate Excise and Income Tax: Characteristics of Corporate Taxpayers*, 2008 ed. 2008.

[17] Oregon Department of Education. Actual Expenditures by Fund and Function. 2007-2008. See Oregon School Boards Association, *Does Oregon really have $12,000 in revenue per student?*, for a discussion of total versus operating revenues and expenditures.

[18] Some researchers use *revenues* per student rather than *expenditures* per student. Revenues per student can be tracked because they come from identifiable sources and are publicly reported each year. Expenditures per student are more difficult to track because the federal government, state legislatures, and local school boards use different spending criteria on the revenues, making it difficult to verify and track true costs. See Collins Center for Public Policy, Inc. *The Florida Corporate Income Tax Credit Scholarship Program: Updated Fiscal Analysis*. February 2007. In Oregon, revenues per student are $11,790.

[19] In the long-run, districts could adjust capital expenditures to account for declining enrollment. Thus, in the long-run a smaller number of transfers to private schools would be needed for the tax credit program to "break even."

[20] U.S. Department of Education, National Center for Education Statistics, Schools and Staffing Survey (SASS), "Private School Questionnaire," 1999–2000 and 2003–04. 2006. Inflation adjustments from Oregon Office of Economic Analysis. Historical Annual and Quarterly Data Tables, 1990-2015. 2008.

[21] See *supra* note 20.

[22] Oregon Department of Education. Students Eligible for Free/Reduced Lunch. 2007–2008. U.S. Department of Education, Office of Special Education and Rehabilitative Services, Annual Report to Congress on the Implementation of the Individuals with Disabilities Education Act, selected years, 1977 through 2005; and Individuals with Disabilities Education Act (IDEA) database, retrieved on September 22, 2006, from http://www.ideadata.org/PartBdata.asp. National Center for Education Statistics, Statistics of Public Elementary and Secondary School Systems, 1977; Common Core of Data (CCD), "State Nonfiscal Survey of Public Elementary/Secondary Education," 1981–82 through 2004–05; and Projections of Education Statistics to 2015. 2006.

Table 2: Oregon Education Per Student Actual Revenue and Expenditures by Fund and Source, 2007–2008

	General Fund	Special Revenue Funds	Debt Service Funds	Trust & Agency Funds	Enterprise Funds	Total
Revenues						
State sources						
State School Fund	$4,490	$10	$10	$20	$ -	$4,530
Other sources	310	170	-	-	-	480
Local sources	2,440	400	790	40	10	3,680
Federal sources	70	780	-	-	-	850
Other sources	1,090	580	490	80	10	2,250
Total	$8,400	$1,940	$1,290	$140	$20	**$11,790**
Expenditures						
State sources						
State School Fund	$4,050	$10	$10	$10	$ -	$4,080
Other sources	280	130	-	-	-	410
Local sources	2,200	310	660	20	10	3,200
Federal sources	60	610	-	-	-	670
Other sources	980	460	410	30	10	1,890
Total	$7,570	$1,520	$1,080	$60	$20	**$10,250**
Memo: Operating Expenditures = Total *minus* debt service						$9,170

Source: Oregon Department of Education; Oregon School Boards Association

The State of Oregon is required by law to refund excess tax revenue when revenues collected for the biennium are more than 2 percent higher than forecast at the time the budget was adopted. "Kicker" refunds are made in the form of a credit on the tax return for the second year of the biennium. Beginning in 2009, the corporate kicker will be calculated based on tax liability *after* credits, as opposed to how it was calculated for tax year 2005, using before-credit tax liability.[23] Thus, corporate donations under the proposed program would not be eligible for Kicker refunds. In this way, the proposed credits increase the amount of corporate expenditures in the state.

[23] See Oregon Department of Revenue. *Oregon Corporate Excise and Income Tax: Characteristics of Corporate Taxpayers*, 2008 ed. 2008.

Table 3: Break-even Fiscal Analysis of Opportunity Scholarship Tax Credit

	25% Corporate Participation	50% Corporate Participation	75% Corporate Participation
Donations to tuition scholarship organizations			
Corporate	$28,625,000	$57,250,000	$85,875,000
Personal	63,000,000	63,000,000	63,000,000
Total	$91,625,000	$120,250,000	$148,875,000
Tax credits claimed			
Corporate	$22,900,000	$45,800,000	$68,700,000
Personal	63,000,000	63,000,000	63,000,000
Total	$85,900,000	$108,800,000	$131,700,000
Operating expenditures per public school student	$9,170	$9,170	$9,170
Minimum number of students to "break even"	**9,400**	**11,900**	**14,400**
Memo: Percent of eligible students	4.8%	6.1%	7.4%
Memo: Private school enrollment as percent of total enrollment	10.2%	10.6%	11.0%

Source: Author's calculations

Oregon Family Education Tax Credit

Table 4 shows the estimated cost of the Family Education Tax Credit under assumptions that the average credit claimed is $100, $250, $500, or $750 per student. Table 4 presents the potential fiscal impact of the Family Education Tax Credit as a "break-even" analysis. It shows how many students would have to transfer from public schools to private schools for the proposed credit to pay for itself via reduced public school expenditures.

Oregon has approximately 637,800 K–12 students:

- 563,100 in public schools,[24]
- 54,300 in private schools,[25] and
- 20,400 home-schooled.[26]

It is assumed that 80 percent of families with students would take advantage of the tax credit. This assumption is both reasonable and conservative. For example, among Oregon taxpayers, the personal exemption credit is the most widely claimed credit, with approximately 90 percent of the amount claimed being used because the

[24] Oregon Department of Education. District Profile. 2005-2006.

[25] U.S. Department of Education, National Center for Education Statistics, Private School Universe Survey (PSS), various years, 1997-98 through 2003–2004. 2006.

[26] Oregon Department of Education. 2003–2004 Home Schooling Statistics. 2005.

remaining 10 percent is associated with filers whose credits claimed exceed their pre-credit tax liability.[27]

As noted above, Oregon has an average of $9,170 in operating expenditures per K–12 student. Table 4 shows the number of students that would have to transfer to private schools for the Family Education Tax Credit program to "break even," in that the amount of the tax credit would equal the reduced demand for public school spending. Depending on the average tax credit taken, the break-even number of transfers to private school would be between 5,600 and 41,700 or an increase of 10 percent to 77 percent.[28]

It would be reasonable to assume that state and local governments would *not* reduce K–12 spending in the face of declining enrollment. Table 4 shows that if current levels of funding are maintained, then the break-even number of transfers would increase per-student public school spending by $90 to $730. Alternatively, per-student spending could be held constant and spending on other programs could be increased.

Table 4: Potential Fiscal Impact of Oregon Family Education Tax Credit

	$100 Average Credit	$250 Average Credit	$500 Average Credit	$750 Average Credit
Total number of students taking credit	510,200	510,200	510,200	510,200
Total credit	$51,020,000	$127,550,000	$255,100,000	$382,650,000
Operating expenditures per public school student	$9,170	$9,170	$9,170	$9,170
Minimum number of transfers to private school to "break even"	5,600	13,900	27,800	41,700
Memo: Percent increase in private school enrollment to "break even"	10%	26%	51%	77%
Operating expenditures per public school student, after credit	$9,260	$9,400	$9,650	$9,900
Increase in operating expenditures per public school student, after credit	$90	$230	$480	$730

Source: Author's calculations

[27] See Oregon Department of Revenue. *Oregon Personal Income Tax Statistics: Tax Year 2006*. 2008.

[28] The break-even number of transfers is much larger than would be expected under the credit. Existing peer-reviewed research indicates that the price elasticity of demand for private school education is 1.1. In other words, a 10 percent reduction in the price of private school education would be associated with an 11 percent increase in the quantity demanded. Thus, the range of hypothetical average tax credit would result in a 1.4 percent to 10.4 percent increase in private school enrollment. See Anderson, P. L.; McLellan, R.; Overton, J. P.; and Wolfram, G. *The Universal Tuition Tax Credit: A Proposal to Advance Parental Choice in Education*. Mackinac Center for Public Policy. 1997.

Conclusions

The ***Opportunity Scholarship Tax Credit*** potentially would produce a net fiscal gain to the state as it would require a relatively small shift of students to private schools for the tax credit program to pay for itself. The tax credits would be, in effect, exempt from Kicker calculations, thereby increasing the amount of funding retained in the State of Oregon.

The ***Oregon Family Education Tax Credit*** may have an impact on state revenues. Most of the taxpayers who would take advantage of the credit would be infra-marginal taxpayers, meaning that the credit would represent a windfall to the taxpayer and a net cost to the state. On the other hand, if a sufficient number of students transfer to private schools, then per-student public school spending would *increase* by $90 to $730.