

EDCHOICE
FISCAL IMPACT STATEMENT
2020-2021 REGULAR SESSION

Note Prepared: February 2021

Subject: HB 1371, a bill to establish tax-credit scholarships for students in Arkansas

Impact: State, Local Taxpayers, and School Districts

Effective Data: TBD

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HB 1371 contains components to fund students' education in both public and nonpublic educational settings. The present analysis focuses on the fiscal impact of the nonpublic component only.

FISCAL SUMMARY

Summary of Estimated Fiscal Impacts of the Arkansas Child Academic Opportunity Scholarship and Grant Act

Est. Total Number of Students in Arkansas Public and Private Schools	495,382
Est. Total Number of Students in Arkansas Eligible for Student Scholarships	179,000
Percent of all Arkansas K-12 students eligible for program	36%
Total funding per pupil for public school system, FY 2018	\$12,800
Est. avg. cost of tax credit disbursements per student	\$4,444
Avg. program cost as % of total per-student expenditures for public school system	35%
Amount of funds available for student scholarships (total donations received by SSOs net 10% for admin costs)	
Assumed Average Scholarship Amount	\$4,000
Number of Scholarships Funded	900
Assumed switcher rate	100%
Est. number of scholarship students likely to enroll in public schools without financial assistance from program	900
Total tax credit disbursements for donations to fund nonpublic student scholarships	
	(\$4,000,000)
Total K-12 expenditures for public school system	\$6,104,000,000
Tax credit disbursements as % of total K-12 expenditures	0.1%
State savings from scholarship students no longer enrolled in public schools	\$6,316,000
Net State Impact	\$2,316,000
Net State Impact Per Program Participant	\$2,600
Break-Even Switcher Rate for State	80%
Est. Reduction in Revenue for School Districts After Students Leave District Schools for the Program	
	(\$6,316,000)
Average Variable Educational Cost per Student	\$7,900
Total Cost Burden Relief to School Districts for Students Choosing to Leave District Schools	\$7,090,000
Net School District Fiscal Impact	\$773,000
Net School District Fiscal Impact per Program Participant	\$900

Notes: () denotes a decrease/negative value

Sources: Arkansas Division of Elementary and Secondary Education; U.S. Census Bureau; National Center for Education Statistics, U.S. Dept. of Education; EdChoice

BILL'S PURPOSE: This bill, if enacted, creates the Arkansas Child Academic Opportunity Scholarship and Grant Act, a tax-credit scholarship program where families of eligible students may receive funds to pay for tuition and other approved educational services on behalf of the eligible student. The scholarship amount may not exceed the foundation funding amount.

Students may participate in the program if they meet the following conditions: 1) was enrolled for at least one semester in public school; 2) was not continuously enrolled in a nonpublic school in the state during the school year preceding the first semester for which the student receives a student scholarship; and 3) has a household or family income that is less than 200 percent of the federal poverty limit.

The scholarship tax credit would be available to individual and corporate taxpayers who make donations during a taxable year to one or more qualified scholarship support organizations (SSO) who provide scholarships to students in kindergarten through twelfth grade to attend a nonpublic kindergarten, elementary, or secondary school located within the State.

The tax credit would be equal to 100% of the total donations made to qualified SSOs during the taxable year. The scholarship credit would be capped at \$10,000,000. Of this amount, \$4,000,000 would be allotted for eligible contributions made to fund eligible private school payments and \$6,000,000 would be allotted for eligible contributions made to fund eligible public school payments. If the aggregate value of all credits awarded during the prior fiscal year equals at least 90% of the credit cap available for that year, the credit cap for the next fiscal year shall be increased by 25% over the credit cap amount established for the prior year. SSOs may keep up to 10 percent of donations to cover administration costs.

FISCAL EXPLANATION: This proposal, if enacted, will generate an estimated net benefit for the State General Fund of \$2.3 million for FY 2021. There would be an estimated net fiscal benefit for school districts of \$773,000. There will be no impact on local property taxes.

We estimate that scholarships would be awarded to 900 students.¹ Given the requirements to be enrolled in public school prior to entering the program, the analysis assumes all students would be “switchers” (i.e., students who would enroll in public schools without any financial assistance from the tax-credit scholarship program). These students offset program costs for the state.

State impact: The state would experience an estimated cost to fund tax-credit scholarships equal to \$4.0 million in tax credit disbursements for charitable donations, or 0.1 percent of total expenditures for the state’s public school system. This would be completely offset by \$6.3 million in reduced state expenditures for public schools. After factoring this savings, we estimate a net fiscal benefit to the state of **\$2.3 million, or \$2,600 per student scholarship.**

Impact on local property taxes: Local property tax levies are determined by property value assessments and set independently of the number of students in a school district. Thus, students who use a scholarship and leave their public schools will not affect local property taxes unless they also residentially move out of a district.

School district impact: Local public school districts would experience \$6.3 million in reduced revenue. This reduction would be completely offset by an estimated \$7.1 million in reduced variable costs for students who would have enrolled in district schools without the scholarship program in place.² Thus, there will be an estimated net benefit for district schools of **\$773,000, or about \$900 per student participating in the program.**³

Break-even switcher rate: Switcher is defined as a student who would enroll in a district school if the scholarship program is not in place as opposed to enrolling in private school, home school, or other non-public school settings. Switchers represent fiscal savings for the state and district schools. For the program to generate savings for the state, at least 80% of program participants would need to be switchers.

KEY ASSUMPTIONS AND CONSIDERATIONS

- The analysis assumes that the state disburses the maximum amount of tax credits (\$4 million for nonpublic schools) for tax-credit scholarship donations. It’s plausible that the impact on the state will be less if some donors reduce contributions to other tax credit programs in order to make contributions to the scholarship program. The analysis takes a cautious approach by assuming the scholarship program will have no effect on charitable giving for other tax credit programs.
- The analysis assumes the average scholarship amount equals to \$4,000.⁴
- The bill includes strong requirements for prior enrollment in public schools. Thus, the analysis assumes that all scholarship students will be switchers.
- The analysis assumes that SGOs retain 10 percent of donations to cover administrative costs.
- Arkansas public schools are mostly funded by a combination of state and local monies. The amount of state and local funding is based on foundation funding for each student and determined by a funding matrix. The state’s funding formula first determines the total amount of funding needed. Districts must raise a portion of these funds via property tax, and the state provides the remainder to meet the foundation amount. When a student leaves a district, total revenue will decrease by the foundation amount, plus any add-ons associated with the student. Because local revenue is fixed, the revenue reduction will take the form of savings for the state equal to the foundation funding for that student.

- For each student who switches from a public school into the scholarship program, the analysis assumes reduced state costs equal to the foundation amount (\$7,018).⁵ This is a cautious approach because, in addition to the foundation base amount, the state provides extra funding for students with certain backgrounds and characteristics, including students with special needs, students from low-income families, and students who are English language learners. Given that the program targets low-income families, the estimated fiscal savings for the state, as stated in the present analysis, will likely be higher.
- The analysis assumes that districts will lose the full foundation funding amount for students who leave, or \$7,018.

DATA SOURCES: Arkansas Division of Elementary and Secondary Education; National Center for Education Statistics, U.S. Department of Education; U.S. Census Bureau; EdChoice

DISCLAIMER: The contents of this fiscal note are intended to provide information and should not be construed as lobbying for any position related to any legislation. EdChoice is committed to research that adheres to high scientific standards and matters of methodology and transparency are taken seriously at all levels of the organization. We are committed to providing high-quality information in a transparent and efficient manner. We welcome any and all questions related to methods and findings.

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NOTES

¹ The analysis assumes that \$4.0 million in tax credits would generate \$4.0 million in donations to SSOs. If scholarship organizations keep the maximum amount allowed for administrative costs, then they will have \$3.6 million for awarding scholarships. The 900 scholarship students estimated to participate in the program represents about 0.5 percent of the estimated total number of students eligible for the program.

² Estimates for short-run variable costs were constructed from data from the Arkansas Division of Elementary and Secondary Education (DESE) and the 2018 Annual Survey of School System Finances reported by the U.S. Census Bureau. We estimate that the average variable cost per student is almost \$8,000. Using federal data, we first estimated that 61.4 percent of total costs are variable. We then applied this rate to more recent expenditure data from the state's DESE. Our estimate for variable costs includes expenditures for Instruction, Student Support Services, and Instruction Support Services and excludes all other costs such as capital, debt services, administration, food services, and transportation. Two studies on education costs suggest that variable costs are even higher than what is estimated in this fiscal note (Scafidi, 2012; Bifulco & Rebeck, 2014). Thus, savings that offset revenue reductions for Arkansas school districts from the tax-credit scholarship program may be higher.

Arkansas Division of Elementary and Secondary Education, *Annual Statistical Report of the Public School of Arkansas and Education Service Cooperatives: 2019-2020*, retrieved from: https://dese.ade.arkansas.gov/Files/20210212122345_2019-2020%20Annual%20Statistical%20Report.pdf; U.S. Census Bureau, *2018 Annual Survey of School System Finances*, retrieved from: <https://www.census.gov/data/tables/2018/econ/school-finance/secondary-education-finance.html>; Benjamin Scafidi (2012), *The Fiscal Effects of School Choice Programs on Public School Districts*, Friedman Foundation for Educational Choice, retrieved from EdChoice website: <https://www.edchoice.org/research/the-fiscal-effects-of-school-choice-programs-on-public-school-districts>; Robert Bifulco and Randall Reback (2014), Fiscal Impacts of Charter Schools: Lessons from New York, *Education Finance and Policy* 9(1), pp. 86–107, http://dx.doi.org/10.1162/EDFP_a_00121.

³ To be clear, this \$773,000 net fiscal benefit represents a \$7.1 million reduction in cumulative school variable costs, which outweighs the \$6.3 million cumulative net revenue reduction for 900 students who would enroll in district schools without the scholarship program in place. It is not a direct reduction in school expenditures. The public schools will still have to make decisions to cut costs as enrollment declines. However, they now have \$7.1 million in available cost burden relief from which to find at least \$6.3 million in spending reductions to match their net revenue reduction.

⁴ This assumption is slightly greater than the weighted average for scholarship amounts awarded by SGOs in other states with tax-credit scholarship programs, or \$3,852. In practice, SGOs are unlikely to award scholarships worth full tuition given that tax-credit scholarship programs are incentivized to maximize private schools' enrollment (Lueken, 2018). Martin F. Lueken (2018), The Fiscal Effects of Tax-Credit Scholarship Programs in the United States, *Journal of School Choice*, 12(2), pp. 181–215, <https://dx.doi.org/10.1080/15582159.2018.1447725> “School Choice in America,” EdChoice, last modified February 4, 2020 <http://www.edchoice.org/school-choice/school-choice-in-america> (accessed 1/26/2021).

⁵ This estimate is based on total state revenue from all sources for districts and charter schools.

Arkansas Division of Elementary and Secondary Education, *Annual Statistical Report of the Public School of Arkansas and Education Service Cooperatives: 2019-2020*, retrieved from: https://dese.ade.arkansas.gov/Files/20210212122345_2019-2020%20Annual%20Statistical%20Report.pdf