Under scholarship tax credit programs such as the one created by LB 670, the state would forgo revenue to provide a tax benefit to those who make donations to private school scholarship-granting organizations (SGOs), which in turn, provide scholarships to students in private K-12 schools. LB 670 creates much greater tax benefits for donations to SGOs, as compared to all other nonprofits.

Scholarship tax credits much more lucrative than other types of donations

Tax credits enhance the tax benefit of donating to scholarship-granting organizations, as opposed to tax deductions for other types of charitable donations. For example, under LB 670, an individual, couple, or business can receive a credit equal to 100 percent of their total contributions or 50 percent of their income tax liability, whichever amount is smaller. There are, however, no limits on donation amounts. This means that as long as there are enough credits available, a corporation with an income tax liability of $1 million could make a donation to a private scholarship granting organization of $500,000 and receive a $500,000 tax credit. Or, if a couple has income tax liability of at least $20,000, and they make a donation to a private scholarship granting organization of $10,000, they receive a state tax benefit of $10,000.

On the other hand, if the same couple makes a $10,000 donation to a non-profit private or public school foundation, the potential value of their tax benefit will be the amount of their donation multiplied by their tax rate in the bracket in which that income would have fallen. If that income falls in the state's top income tax bracket of 6.84 percent, the tax savings would be $684. This couple's tax benefit for donating to an SGO would be 14.5 times greater than it would be for donating to the public school foundation.

LB 670's cost could balloon each year

The cost of the tax break is capped at $10 million in the first year, and if 90 percent of the credit is used, the cap will grow by 25 percent the following year. Assuming Nebraska's credit grows by 25 percent each year, the credit would reduce state revenues by more than $93 million by 2030.

New credit would divert public dollars that can be used to lower property taxes, improve public education

Creating a scholarship tax credit now would come at a time when our state's school funding needs are increasing and when state funding of K-12 education has been constrained due to budget shortfalls.[1] This low level of state support leads to a heavy reliance on property taxes to fund schools. Diverting more state resources for scholarship tax credits will make it harder to address state public education needs and increasingly shift the cost of funding K-12 onto property taxpayers.

[1] LB 409 (2017) made changes to the TEEOSA formula to reduce school funding by $123 million by FY 18-19.

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Tax credit scholarships are not targeted to low-income students

Because the eligibility is not targeted to the lowest-income students, the scholarship tax credits would likely subsidize the private education of students who would have attended private schools anyway. Under LB 670, students at 370 percent of the federal poverty level (FPL) would be eligible to qualify for scholarships offered under the program. This means that in 2019, a family of four could make up to $92,870, putting them in the top 40 percent of Nebraska earners, and still qualify for the scholarships. For context, 370 percent of the FPL is double the eligibility level for free and reduced meals, which is the standard that our public school system considers low-income. This eligibility expansion beyond the traditional definition of low-income students is consistent with tax credit programs in some other states. For example, a study of a scholarship tax credit in Arizona found about 76 percent of the scholarships went to students who already had the means to attend private school.[2]

Scholarship tax credits not likely to create savings for the state

It's highly unlikely the credit would sway enough children to switch to private schools to create savings in the public schools. In order to generate savings for the state in reduced public school costs, not only would a significant number of students need to switch from public to private school, but those students who switch would need to be highly concentrated in certain school buildings. A large percentage of public school costs are fixed and not able to be reduced without a large reduction in enrollment. For example, if one or two students in a public school classroom leave and go to private school, the public school must still pay the teacher and maintain the facilities in the same way it would have before the students changed schools.

Bill creates yet another tax credit with no evaluation mechanisms

Like many other state tax credits, LB 670 contains no data collection requirements, so policymakers won't have any information to review whether the measure is achieving the stated goals of improving education or providing savings to the state. This means that, over time, the bill could become a significant drain on revenue that may or may not offer Nebraska a good return on investment.

Conclusion

Scholarship tax credits like the one proposed in LB 670 stand to divert state revenue at a time when we are experiencing revenue struggles. Enacting this measure could force lawmakers to make cuts to vital services such as public K-12 education or shift more of the load of funding our schools on to property taxpayers. In light of these factors, we have serious concerns about creating a new tax credit.

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[2] Glen Wilson, "The Equity Impact of Arizona's Education Tax Credit Program: A Review of the First Three Years," downloaded from http://epsl.asu.edu/epru/documents/EPRU%202002-110/epru-0203-110.htm, on Aug. 7, 2017.