



# FISCAL RESEARCH CENTER

## **Georgia's Tax Credit Scholarship Program**

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**ANDREW YOUNG SCHOOL**  
OF POLICY STUDIES

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## **I. Introduction**

In 2008, Georgia adopted legislation that allows tax credits, officially the Qualified Education Tax Credit (QETC), for donations that are used to fund scholarships for students enrolled in private schools. This report presents an overview of this program. We start with some background, including the history, legislation, and data on participation. Next we list the arguments for and against the program and provide a summary of a few existing studies of tax credit scholarship programs. Section VII provides an analysis of the fiscal effects of the program and in Section VIII we turn to an analysis of a proposed second tax credit scholarship program. Finally, we discuss the need for a more extensive evaluation of the program.

### II. History of Tax Credit Scholarship Programs in Georgia and Other States

According to the Friedman Foundation for Educational Choice, as of 2014 there are 14 states that offer tax credit funded scholarship programs; Alabama, Arizona, Florida, Georgia, Indiana, Iowa, Kansas, Louisiana, New Hampshire, Oklahoma, Pennsylvania, Rhode Island, South Carolina, and Virginia. The oldest is Arizona's, having been enacted in 1997, and the most recently enacted programs are in Alabama and South Carolina in 2013 and Kansas in 2014. Several states also offer voucher programs or narrowly-tailored scholarship programs for foster children and children with disabilities, but those programs are beyond the scope of this report.

The scholarship programs differ in many ways, among them the value of the credit (i.e., as a percentage of the amount donated), the maximum allowable credit to any donor, the maximum total credits allowed, the maximum scholarship, and eligibility criteria for scholarship recipients, including means testing. Credit values range from 50 percent of the amount donated in Indiana and Oklahoma to 100 percent in Georgia and five other states. Four states—Florida, Kansas, New Hampshire, and Rhode Island—offer tax credits only to business donors while the remaining ten states offer credits to both businesses and individual taxpayers. Caps on the total tax credits available annually range from \$1.5 million in Rhode Island to \$385 million in Florida; Louisiana has no aggregate limit. Eligibility rules in most states include means-testing, though the criteria vary widely. Two exceptions are Georgia, which does not means-test recipients, and Arizona, which does so only for scholarships funded through its corporate tax credit program. Finally, the programs differ across the states in terms of regulation, particularly governance and reporting requirements for scholarship-granting organizations.<sup>1</sup>

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<sup>1</sup> For detailed surveys of existing programs, see the Friedman Foundation for Educational Choice website, [www.edchoice.org](http://www.edchoice.org), and *Education Tax Credit Programs: An Analysis of Provisions by State* (2013) from the Foundation for Opportunity in Education, available at [www.opportunityined.org](http://www.opportunityined.org).

## III. Current Law and Regulations for Georgia's Tax Credit Scholarship Program

### Tax Credits

Under O.C.G.A. §48-7-29.16, a credit against income taxes is allowed for contributions to qualified student scholarship organizations to fund scholarships for eligible students to attend a qualified school or program. Credits are 100 percent of the amount contributed, subject to preapproval by the Department of Revenue (DOR), with caps for individual taxpayers, corporations, fiduciaries, and pass-through entities as follows:

- Individuals filing as:

Single or Head of Household	\$1,000
Married Filing Joint	\$2,500
Married Filing Separately	\$1,250
  
- Corporations and Fiduciaries                      75 percent of tax liability for the year.
  
- Pass-Through Entity Owner/Partner              6 percent of Georgia income from selected pass through interests, but not more than \$10,000 per taxpayer.

For the latter two categories, limits for preapprovals are based on the above calculations using estimated tax liability or pass-through income, while the final allowed credit amounts are based on actual tax liability or pass-through income. As a result, allowed credits for these taxpayers may be less than preapproved amounts, even if less than the amount of contributions.

Credits are non-refundable, but any portion of the final allowed credit amount that is unused in the tax year of the contribution may be carried forward for up to five years. No credit is allowed if the taxpayer designates his or her contribution for the benefit of any particular individual. No credit is allowed with respect to contributions that are taken as a deduction from taxable income as a charitable contribution; if such a deduction is taken by the taxpayer on his or her federal return, the amount deducted must be added back to Georgia taxable income to qualify for the credit.

The total amount of credits available for any tax year is currently capped under the law at \$58 million, an increase effective for tax year 2013 from \$50 million. Applications for

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credit preapproval must be submitted electronically to the Department of Revenue (DOR) and are approved on a first come, first served basis beginning on the first of each year and continuing until the aggregate annual limit is reached. The DOR must provide notice of preapproval or denial within 30 days of filing of the preapproval request form and, if preapproved, contributions must be made within 60 days of the date of the preapproval notice.

### Scholarships and Scholarship Organizations

O.C.G.A. §20-2A governs student scholarship organizations (SSOs)—the recipients of the donations eligible for the QETC—and the scholarships they award. Among other things, this code chapter defines eligibility of students, regulates the SSOs, and sets reporting requirements.

“Eligible student” is defined to require that scholarship recipients, prior to first receiving such scholarship, be enrolled for six weeks or more in a public primary or secondary school, or are eligible to enroll in a qualified first grade, kindergarten, or pre-kindergarten. The attendance requirement can be waived under certain conditions related to low-performing schools, documented physical violence or threats at school, or home-schooled students.

Beginning in 2012, individual scholarships are limited in any given year to no more than the statewide average of state and local expenditures per student in public primary and secondary schools, as determined by the state Department of Education. For 2014, the maximum scholarship amount is \$8,983, down from \$9,437 in 2012 and \$9,046 in 2013. Scholarships may be used only for tuition and fees at qualified schools or programs, which in general means any Georgia private school that is accredited or in the process of becoming accredited, and which is in compliance with the federal Civil Rights Act and any applicable state laws or regulations.

Qualified SSOs must be 501(c)(3) charitable organizations and must obligate at least 90 percent of their annual donations for scholarships to qualified schools of the parents' choosing; they may not limit their scholarships to only one school. For SSOs with annual donations revenue in excess of \$1.5 million, the minimum percentage of revenue that must be obligated for scholarships rises to 93 percent and to 95 percent for very large SSOs. Under

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the law, SSOs are supposed to consider financial need in awarding scholarships, but there is neither a requirement that scholarships be only need-based nor any limitation on the family income of recipients.

The reporting requirements of SSOs have been expanded since the program began, but remain limited. As initially passed, the program required SSOs to provide audited financial statements to DOR along with i) a report of the total number and dollar value of tax credits approved and contributions received, and ii) a list of donors, including the dollar values of credits approved and contributions received. SSOs were not required to report any information about scholarships or scholarship recipients, and the law prohibited DOR from requiring any additional information from SSOs beyond the items above.

The law was amended in 2011 to, among other things, require that SSO reporting of credits approved and contributions received be broken down by individual versus corporate taxpayers, and also to require that SSOs report the number and dollar amount of scholarships awarded. Additional reporting requirements added in 2013 included summary statistical information about the numbers of families of scholarship recipients that fall in each quartile of Georgia adjusted gross income for the year and the average number of dependents per family for each quartile.



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### IV. Participation in Georgia's Tax Credit Scholarship Program

The tax credit funded scholarship program has been increasingly popular since its inception in 2008. The annual cap on tax credits, which was reached for the first time in 2011, was \$50 million initially and increased to \$58 million effective for tax year 2013. Since 2011, the cap has been reached earlier each year and this year it was reached on January 22. Table 1 below summarizes the numbers and amounts of credits approved each year, and for 2011-2014, the date the cap was reached each year. The amounts of actual contributions made to SSOs, and thus eligible for the credit, are also shown for 2010-2013. Over the last three years, contributions received averaged about 94 percent of the amounts preapproved.

**TABLE 1. TAX CREDIT PREAPPROVALS AND SSO CONTRIBUTIONS**

(\$ thousands)	2008	2009	2010	2011	2012	2013	2014
Tax Credits Preapproved	\$7,077.5	\$26,578	\$38,152	\$50,000	\$51,500	\$58,000	\$58,000
Number of Applications	2,779	10,577	17,186	17,238	18,519	19,086	18,217
Date Cap Reached				7-Nov	13-Aug	9-May	22-Jan
Contributions Received	NA	NA	\$37,664	\$47,359	\$48,118	\$54,915	NA

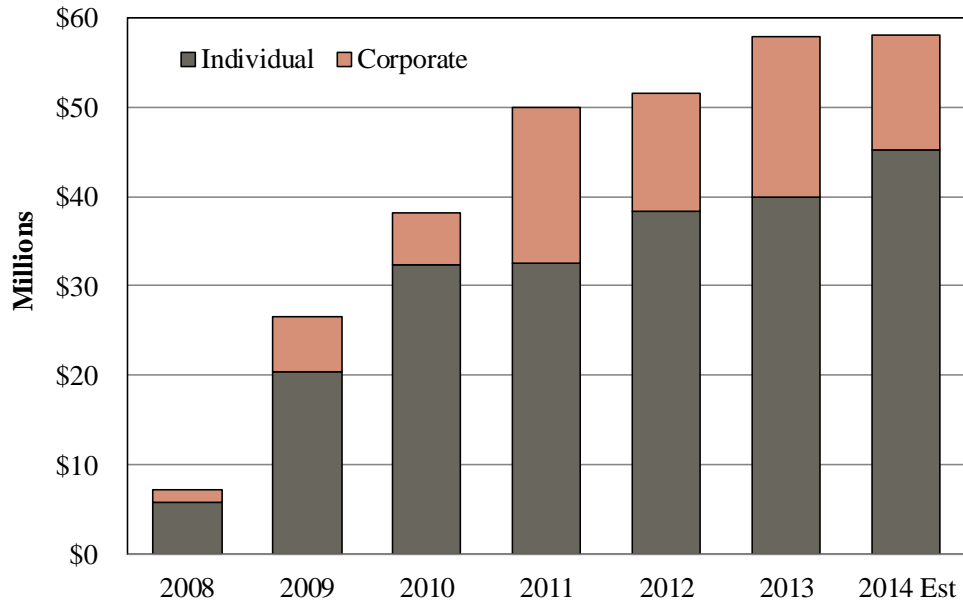
Source: Georgia Department of Revenue. NA: not available.

Figure 1 breaks down the preapprovals by taxpayer type, individual versus corporate (including pass-through entities). Corporate donors amount to between 1.1 and 1.3 percent of all donors each year, but between about 15 and 35 percent of preapprovals and contributions. While individual preapprovals have grown each year since 2008, corporate preapprovals have been more volatile and fell sharply in 2014 as the window for filing for preapprovals shortened to the first three weeks of January, at which point the cap was reached.

From the inception of the program through 2012, the average credit preapproval amount for individual donors was fairly stable, between \$1,911 and \$2,099, but has since risen to \$2,514 in 2014, according to DOR estimates. Over the entire period, corporate preapprovals averaged about \$58 thousand per donor, but this amount has also varied widely from year to year. Table 2 shows the number and average amount of preapproved credits by taxpayer type since inception of the program.

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**FIGURE 1. TAX CREDIT PREAPPROVALS BY TAXPAYER TYPE**



Source: Georgia Department of Revenue.

**TABLE 2. TAX CREDIT PREAPPROVALS BY TAXPAYER TYPE**

	2008	2009	2010	2011	2012	2013	2014
Number of Applications Approved:							
Individual	2,746	10,437	16,971	17,042	18,272	18,856	18,020
Corporate	33	140	215	196	247	230	197
Average Amount Approved:							
Individual	\$2,093	\$1,949	\$1,911	\$1,914	\$2,099	\$2,120	\$2,514
Corporate	\$40,284	\$44,541	\$26,608	\$88,693	\$53,249	\$78,274	\$64,467

Source: Georgia Department of Revenue.

**TABLE 3. SCHOLARSHIP AWARDS**

	2011	2012	2013
Number of Scholarships	11,292	13,285	13,268
Total Awarded (\$ thousands)	\$39,457	\$45,006	\$46,660
Average Scholarship Award	\$3,494	\$3,388	\$3,517

Source: Georgia Department of Revenue.

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The number and amount of scholarships awarded have only been reported since 2011, and 2014 figures are not yet available, but for the years where data are available, Table 3 shows these figures as well as the average scholarship amount. Since part of the donations made by tax payers goes to cover administrative expenses of SSOs and part may also be reserved for multi-year scholarship commitments, the value of the contributions determine the tax credits, but will be larger than the scholarship amounts. For 2013, for example, scholarship awards amounted to 85.0 percent of contributions. The average scholarship amount has been fairly stable over the three years reported and well below the maximum allowed. The number of SSOs participating in the program also grew sharply from 10 in 2008 to 39 in 2011, but the number fell to 33 by mid-2013 and presently stands at 32.<sup>2</sup>

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<sup>2</sup> Counts are from lists of participating Student Scholarship Organizations published online periodically by the Georgia Department of Education.

### V. Pros and Cons of Tax Credit Scholarship Programs

Proponents and opponents of publicly funded vouchers or tax credit scholarships make several arguments in support of and in opposition to tax credit scholarship programs.

Proponents argue that:

- Giving parents a choice of schools will allow them to choose the school that is best suited for their child and that the child will benefit from this better fit.
- If parents have a choice, public schools will be driven to increase the quality of their education in the same way that for-profit companies behave in the market place.
- Vouchers and tax credit scholarships allow children of low-income households to escape having to attend poor performing public schools.
- By allowing tax credits, the state allows taxpayers to determine the nature of the scholarships to be awarded.

On the other hand, opponents argue that:

- Funds should be used to improve the quality of public education rather than to experiment with school choice.
- Vouchers and tax credits scholarships will benefit private schools at the expense of public schools.
- Vouchers and tax credit scholarships are a way of allowing public funds to go to private schools, including religious schools.
- School choice programs do not combat the problems of public schools and actually make public schools worse off.

Evaluating each of these arguments is beyond the scope of this report.

### VI. Existing Evaluations of Tax Credit Scholarship Programs

There has been very little analysis of any of the tax credit funded scholarship programs other than analyses of their fiscal effects. Though there is a vast literature that explores the effects of other school choice programs such as voucher programs and charter schools, there has been no analysis of the effect of tax credit scholarship programs on academic performance. A review of the literature on performance effects of school choice programs is beyond the scope of this report.

As to fiscal impact, Gottlob (2008) conducted an analysis of the potential impact of a tax credit scholarship program in Georgia before Georgia had implemented the program. He first develops an estimate of the reduction in expenditures per student if public school students transfer to a private school. Gottlob then estimates the number of public school students that would be expected to transfer to private school for different values of scholarships. He refers to this as the demand for scholarships. He estimated this demand for different levels of income, measured by percent of poverty level. If the scholarship amount is low, few students would take a scholarship, i.e., would transfer from the public schools to a private school. If eligibility is limited to lower income students, even fewer students would transfer.

Given the expected donations, he calculates the number of scholarships that could be offered for different values of the scholarship. He refers to this as the supply of scholarships. Then for each scholarship level he calculates the minimum of the demand and supply, which is the actual number of scholarships that would be taken. He then calculates the difference between the total scholarship funds and the reduction in total public school spending due to students transferring from a public to a private school. If the number of students who transfer is small, for example if the scholarship value is small, the state would provide more in tax credits than the reduction in school expenditures. Gottlob assumes that all scholarship recipients would have gone to the public school in the absence of the scholarship. This is an assumption that is made in most other fiscal analysis studies for other states; as we note below, that assumption is probably incorrect.

Lips and Jacoby (2001) conducted a fiscal evaluation of Arizona's tax credit scholarship program for the CATO Institute. They report that 70 to 80 percent of the scholarships are distributed to low-income families. The average scholarship was \$846.

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They also explored the percentage of scholarship students who were previously enrolled in public schools or would probably have to leave private school if they did not receive a scholarship. They concluded that between 15 and 30 percent of the scholarships were dedicated to students who would have otherwise attended public school. They estimate that the scholarship program was “essentially revenue neutral.”

In addition to Gottlob, the only other report that provides any evaluation of Georgia's tax credit scholarship program was done by the Southern Education Foundation (SEF, undated). In the report, SEF first presents a brief history of the program as of 2012 and then details the various ways that the operation of the program is, according to SEF, in violation of the law and associated regulations. For example, SEF presents evidence that some SSOs allow a parent to earmark their donation to fund a scholarship for a particular child.<sup>3</sup> The SEF report also raises questions as to whether the schools participating in the program are actually eligible and whether the SSOs have allocated the required percentage of the donations to scholarships. Finally, the report provides data on the likely characteristics of the students, such as income, race, and religion, and on student performance. However, since state law restricts the information that can be collected on the program and that can be made available publicly, the SEF report had to rely on more general data to draw any conclusions.

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<sup>3</sup> In January 2013, the SEF submitted a document to the Georgia Department of Revenue that contains the evidence the SEF collected regarding this issue and requested an investigation.

### VII. Fiscal Effects of Georgia's Tax Credit Scholarship Program

This section presents an analysis of the fiscal impact of the tax credit scholarship program, which depends on the amount of tax credits taken and the reduction in spending on public education. The value of tax credits taken is the gross reduction in state revenue. However, if scholarship students switch from a public to a private school, the state and the local school system can each reduce their spending by the amount of the variable cost of educating that student. Thus, the net fiscal effect of the tax credit scholarship on the state's budget equals the value of the tax credits that are taken less any reduction in state education grants due to the scholarship program.

There are four variables that determine the fiscal impact: the tax credits per scholarship recipient, the number of recipients, the reduction in spending on education if a student switches from public school to private school as a result of the scholarship, and the share of scholarship recipients who switch. We discuss each of these variables in turn.

Consider first the tax credits per scholarship recipient. The legislation caps the amount of tax credits that can be taken and preapproved credits reached the cap in each of the last four years. However, taxpayers apply to take the tax credit and subsequently make the donation, so some taxpayers who have been approved for the tax credit may not actually make the donation (see Table 1) and thus do not get a tax credit. In addition, credits earned in a given year may not be fully used to offset tax liability in the same year; some may be carried forward to subsequent years. For these reasons, we would ideally use the actual tax credit taken, and not the credits approved or donations received by SSOs, in calculating the revenue loss to the state.

Additionally, some of the donations are used for administrative expense, and thus on a per scholarship recipient basis, the cost to state revenue is the total tax credits taken per scholarship recipient, not the value of the scholarship per recipient. For simplicity, we assume for the analysis that follows that tax credits taken equals \$50 million. Note that the number of scholarships times the tax credit per scholarship thus equals \$50 million.

The third variable is the reduction in public school education expenditures if a student leaves the public school system. We first discuss the fiscal effect on just the state government, and thus consider the reduction in the state education grant to the local school

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system. There are several factors that have to be considered in determining the value of this change in state education grant.

First, state grants for K-12 education are based largely on a per student (full time equivalent) basis, and thus the reduction in the state grant if the school system loses a student is approximately equal to the average grant per student. Only the categorical grants in the Quality Basic Education (QBE) program are not based on full time equivalent (FTE) counts and these are a very small percentage of the total grant.<sup>4</sup> Thus, while the average grant per FTE may overstate the reduction in state expenditure, it is very close to the actual reduction.

Second, the reduction in the state grant for K-12 education depends on which school system the student is from and the grade or programs the student is in. State grants vary across school systems due to variations in property tax wealth for two reasons: the QBE grant to a school system is reduced by the amount of property taxes that 5 mills will raise, and the equalization grant depends on the property wealth per student.

Third, the state grant also depends on the experience and education of the teachers in the system. A system with more experienced teachers and with teachers holding higher academic degrees will get more revenue from the state, so the savings to the state from a student shifting from public to private school will be larger for these systems than for those with less experienced and less highly educated teachers.

Fourth, under QBE the size of the state grant per student depends on the program or grade the student is in. A student in basic high school courses earns the school system the smallest grant, while a student in special education earns the school system a larger grant.

Table 4 and Figure 2 provide information on how the size of the state grant per student (FTE) varies across school systems, and across grade levels and programs. As can be seen, there is substantial variation in the size of the grant per student; mean values, weighted by FTE students, range from \$3,223 for high school grades to \$6,580 for special education, gifted, ESOL, and other programs. For all programs, the FTE weighted mean is \$4,066 while the low and high for all districts are \$1,458 and \$7,098, respectively.

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<sup>4</sup> While not calculated based on FTE, the grant for school busing is related to enrollment.



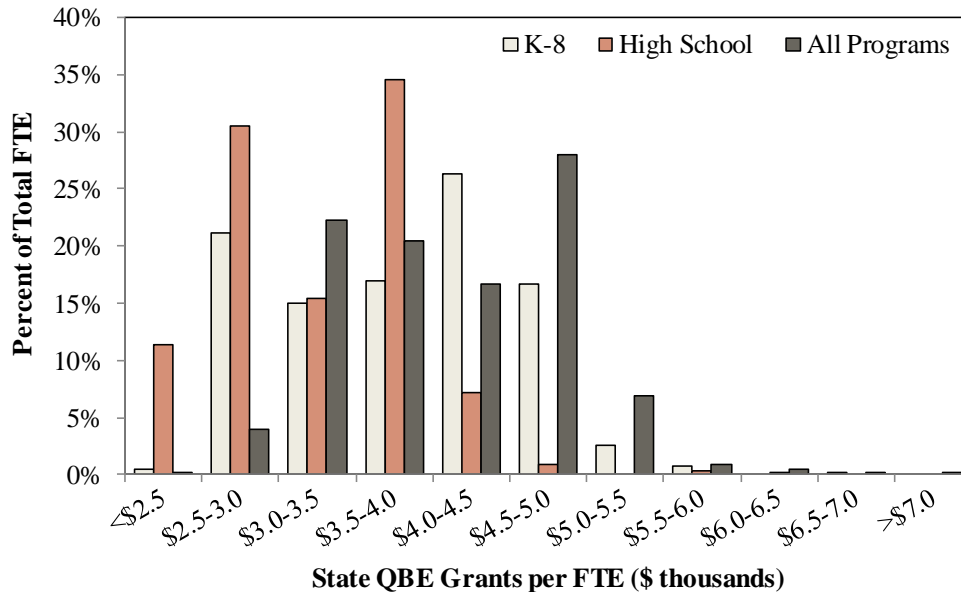
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**TABLE 4. TOTAL STATE GRANT PER FTE BY SCHOOL DISTRICT (FY2013)**

Grades/Programs:	K-8	High School	Sp. Ed./Other	All Programs
Mean (unweighted)	\$4,265	\$3,561	\$7,122	\$4,490
Median	\$4,268	\$3,590	\$7,483	\$4,552
Minimum	\$1,361	\$1,202	\$2,406	\$1,458
Maximum	\$6,696	\$6,060	\$12,941	\$7,098
FTE Weighted Mean	\$3,804	\$3,223	\$6,580	\$4,066

Source: Georgia Department of Education.

**FIGURE 2. DISTRIBUTION OF STATE EDUCATION GRANTS PER FTE (FY2013)**



Source: Georgia Department of Education.

Thus, to determine how much the state saves from a student switching from public to private school, it is necessary to know from what school system and program the student was switching. The Southern Education Foundation (undated) reports that Cobb, DeKalb, Fulton, and Gwinnett counties in metropolitan Atlanta are home to 43.5 percent of the private schools that enroll scholarship program students; these four counties have 28 percent of public school students. Since these school systems tend to have higher wealth per student, their grant per student are less than the average for the state; the weighted average QBE grant to these counties in 2013 was \$3,587, compared to the state average of \$4,066. For our

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calculations we assume that the state would save \$4,066 per student, on average, but we test the sensitivity of the fiscal effects using the lower QBE grant average for these Metro Atlanta counties.

Finally, in addition to knowing how much the state would save from a student transferring from public to private school, we need to know the percentage of scholarship students who in the absence of the scholarship would have attended public schools. For convenience we call this percentage the switching rate. That information is not available, nor do we have the data necessary to estimate it.<sup>5</sup> Consequently, we rely on estimates presented in other studies, though the literature is limited.

Lips and Jacoby (2001) suggest that for Arizona's program, which like Georgia's is not restricted to low-income students, the switching rate ranges from 15 percent to 30 percent of scholarship recipients, with a breakeven fiscal impact (revenue loss from 1999 tax credits equal to cost savings in 2000-2001 school year) at about 20 percent. Their range estimate of switching rates, however, is derived from interviews with the private schools rather than from hard data.

Among the literature on voucher programs, Ferreyra (2007) develops a general equilibrium model of school choice in the Chicago area based on 1990 Census and other data. Absent a voucher program, she estimates equilibrium private school enrollment at about 16 percent of households with children in school. With a \$1,000 voucher (a little more than 1/8 of the public school per student spending in her model) that can be used for either religious or non-religious schools, her model predicts that an additional 6 percent of households will shift to private schools, bringing the private share to 22 percent. This equates to about 27 percent of voucher recipients being public-to-private switchers. This switching rate assumes that all families of students already enrolled in private schools would utilize the vouchers, which results in a much larger cost than would be the case when those already enrolled in private schools are not eligible. To the extent that scholarships are awarded on a need basis, the switch rate would likely be higher and the cost from subsidizing students who would have attended private schools even in the absence of a scholarship would be lower. In general, the switching rate will be higher the more restrictions the state imposes on scholarship eligibility.

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<sup>5</sup> Theoretically, one could compare the change in the public school enrollment to the number of scholarships. However, public school enrollment is not a constant and the number of scholarships is small, and thus it would be nearly impossible to estimate that relationship.

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Other studies of the fiscal effects of tax credit scholarship programs such as Gottlob (2008) assume a switching rate of 100 percent, but they present no evidence regarding the veracity of the assumption. However, there are several reasons why the switching rate would not be 100 percent even with a prior public school enrollment requirement. Parents might simply enroll their child in a public school for the sole purpose of making him or her eligible for a scholarship, and thus in the absence of the scholarship would not have attended public school. Some parents may also have intended to enroll their children in public schools for the lower grades and move them to a private school later, regardless of the availability of scholarships. These students would be eligible for a scholarship, but would not count as switchers. In addition, the public school enrollment restriction on scholarship eligibility does not apply to private school students who start private school by the first grade. As a result, those qualifying at that stage will include those who would have enrolled in private school anyway, in addition to those who would have gone to public school if not for the scholarship. We have been unable to find data on when private school students tend to first enroll, but if these students receive scholarships the actual switching rate will be lower. In addition, home schooled children are also eligible for scholarships in Georgia if they have been home schooled for at least a year. The probability that such a child would switch from home school to a public school is likely to be small. Thus, providing a scholarship for such a student is not likely to reduce enrollment in public schools.

In the analysis presented in Table 5, we use switching rates of 30 percent or higher to illustrate the sensitivity of the fiscal impact to differences in this and other parameter values. For higher levels of assumed tax credits per scholarship student, we calculated the switching rate that would be required for the state to break even, that is to have a zero or small positive net fiscal effect. For simplicity, we assume \$50 million of tax credits for all calculations and vary the tax credits per scholarship student, the switching rate, and the state grant per student. For the state grant, again, we use the overall (all grades/programs) weighted mean grant per full-time equivalent student for the high and the mean grant for students in four metropolitan Atlanta county systems for the low, that is, \$4,066 and \$3,587, respectively. For tax credits per scholarship student, we use a low of \$1,500 and higher levels up to \$4,000.

**TABLE 5. SENSITIVITY OF NET STATE AND LOCAL FISCAL EFFECTS TO PARAMETER VALUES**

<b>Tax Credits per Scholarship Student</b>	<b>Number of Scholarship Students</b>	<b>Percent Switching from Public Schools</b>	<b>State Grant per Public School Student</b>	<b>Net State Fiscal Effect per Scholarship Student*</b>	<b>Net State Fiscal Effect, Total</b>	<b>Local Marginal Cost per Student</b>	<b>Avg Local Fiscal Effect per Scholarship Student*</b>	<b>Net Local Fiscal Effect, Total</b>	<b>Combined Net Fiscal Effect, Total</b>
\$1,500	33,333	30%	\$3,587	(\$424)	(\$14,130,000)	\$1,272	\$382	\$12,720,000	(\$1,410,000)
\$1,500	33,333	42%	\$3,587	\$7	\$218,000	\$1,272	\$534	\$17,808,000	\$18,026,000
\$1,500	33,333	30%	\$4,066	(\$280)	(\$9,340,000)	\$1,272	\$382	\$12,720,000	\$3,380,000
\$1,500	33,333	37%	\$4,066	\$4	\$147,333	\$1,272	\$471	\$15,688,000	\$15,835,333
\$2,000	25,000	30%	\$3,587	(\$924)	(\$23,097,500)	\$1,272	\$382	\$9,540,000	(\$13,557,500)
\$2,000	25,000	42%	\$3,587	(\$493)	(\$12,336,500)	\$1,272	\$534	\$13,356,000	\$1,019,500
\$2,000	25,000	56%	\$3,587	\$9	\$218,000	\$1,272	\$712	\$17,808,000	\$18,026,000
\$2,000	25,000	30%	\$4,066	(\$780)	(\$19,505,000)	\$1,272	\$382	\$9,540,000	(\$9,965,000)
\$2,000	25,000	38%	\$4,066	(\$455)	(\$11,373,000)	\$1,272	\$483	\$12,084,000	\$711,000
\$2,000	25,000	50%	\$4,066	\$33	\$825,000	\$1,272	\$636	\$15,900,000	\$16,725,000
\$3,000	16,667	30%	\$3,587	(\$1,924)	(\$32,065,000)	\$1,272	\$382	\$6,360,000	(\$25,705,000)
\$3,000	16,667	62%	\$3,587	(\$776)	(\$12,934,333)	\$1,272	\$789	\$13,144,000	\$209,667
\$3,000	16,667	84%	\$3,587	\$13	\$218,000	\$1,272	\$1,068	\$17,808,000	\$18,026,000
\$3,000	16,667	30%	\$4,066	(\$1,780)	(\$29,670,000)	\$1,272	\$382	\$6,360,000	(\$23,310,000)
\$3,000	16,667	57%	\$4,066	(\$682)	(\$11,373,000)	\$1,272	\$725	\$12,084,000	\$711,000
\$3,000	16,667	74%	\$4,066	\$9	\$147,333	\$1,272	\$941	\$15,688,000	\$15,835,333
\$3,500	14,286	73%	\$3,587	(\$881)	(\$12,592,714)	\$1,272	\$929	\$13,265,143	\$672,429
\$3,500	14,286	98%	\$3,587	\$15	\$218,000	\$1,272	\$1,247	\$17,808,000	\$18,026,000
\$3,500	14,286	66%	\$4,066	(\$816)	(\$11,663,429)	\$1,272	\$840	\$11,993,143	\$329,714
\$3,500	14,286	87%	\$4,066	\$37	\$534,571	\$1,272	\$1,107	\$15,809,143	\$16,343,714
\$4,000	12,500	83%	\$3,587	(\$1,023)	(\$12,784,875)	\$1,272	\$1,056	\$13,197,000	\$412,125
\$4,000	12,500	100%	\$3,587	(\$413)	(\$5,162,500)	\$1,272	\$1,272	\$15,900,000	\$10,737,500
\$4,000	12,500	75%	\$4,066	(\$951)	(\$11,881,250)	\$1,272	\$954	\$11,925,000	\$43,750
\$4,000	12,500	99%	\$4,066	\$25	\$316,750	\$1,272	\$1,259	\$15,741,000	\$16,057,750

Note: Total tax credits taken are assumed to be \$50 million for all calculations. \*Given the assumed switching rate, this is the fiscal effect per student who switches.

## Georgia's Tax Credit Scholarship Program

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If the average QBE grant is \$4,066, the tax credit scholarship program would have a negative net fiscal effect at the state level at a switching rate of 30 percent and tax credits per student of \$1,500, but would break even at the state level with a switching rate of 37 percent. If scholarships awarded are 90 percent of contributions received, this implies that the average scholarship would be about \$1,350 for a 37 percent switching rate to result in a net positive budget effect at the state level. If tax credits per scholarship recipient were \$2,000, the switching rate would have to be 50 percent for the program to be budget neutral at the state level, assuming an average QBE state grant of \$4,066, and 56 percent if the average QBE grant was \$3,587. If tax credits per scholarship recipient were \$3,500, which is a little less than the average scholarship in 2013, the breakeven switching rates rise to 87 percent and 98 percent, respectively, for the high and low QBE grant assumptions. Given published estimates of the switching rate, an 87 percent breakeven switching rate raises doubts that the program is fiscally neutral for state government.

However, the above analysis considers only the net fiscal effect on the state government. Reducing the number of public school students may also reduce expenditures funded by the local school system. The amount of revenue per student provided by local school systems varies widely, as shown in Table 6 and Figure 3.

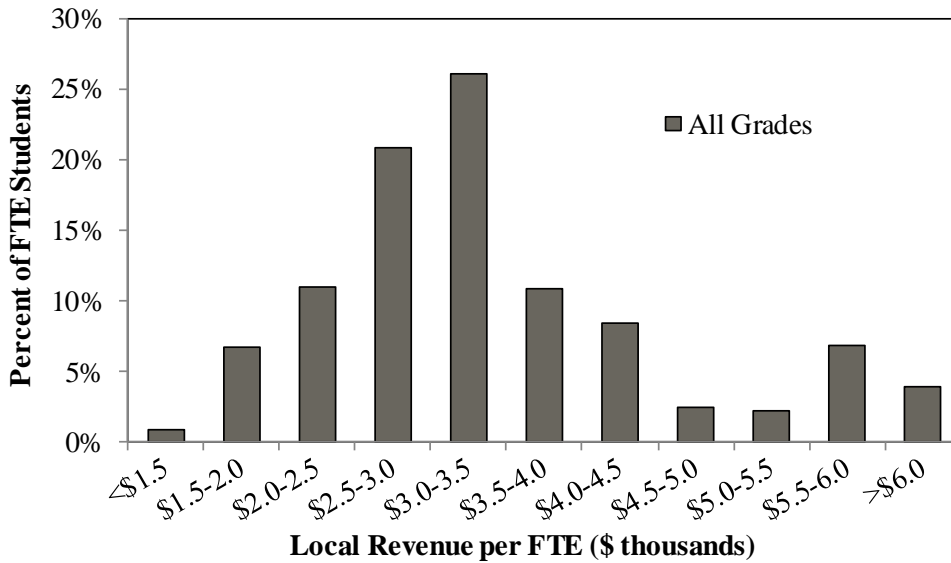
**TABLE 6. LOCAL SOURCE REVENUE  
PER FTE (FY2013)**

	<b>All Grades</b>
Median	\$2,872
Minimum	\$648
Maximum	\$10,902
FTE Weighted Mean	\$3,477

Source: Georgia Department of Education.

## Georgia's Tax Credit Scholarship Program

**FIGURE 3. DISTRIBUTION OF LOCAL REVENUE PER FTE (FY2013)**



Source: Georgia Department of Education.

In the short run and for small reductions in the number of students, it is not likely that local expenditures would decrease by the average expenditures per student if a student switched to a private school. Consider, for example, a reduction of one student, i.e., 5 percent of a class of 20. The local school system would not be able to reduce the number of teachers or classrooms. A reduction of one student may in fact result in an increase in expenditures from local funds because of the reduction in the state QBE grant. Since the school system will have to retain the teacher, the school system will have to cover a larger share of the salary because the state contribution will be reduced by 5 percent. Of course, the remaining 19 students may get more attention from the teacher and other local resources will likewise be spread across fewer students. On the other hand, if a larger number, say 20 or 30 students or more from a given school, were to transfer to private schools, then the local system may be able to reduce staffing and other variable costs and, in the long run for the district as a whole, reduce facilities costs as well.

In recent years, the number of scholarships awarded under the existing scholarship program has been about 13,000 each year. While not a trivial number, it is small relative to the total number of students in public schools. Considering just Cobb, DeKalb, Fulton, and

## Georgia's Tax Credit Scholarship Program

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Gwinnett, scholarship program students statewide are about 3 percent of the students in those school systems.

Gottlob (2008) estimates a regression equation relating the change in total expenditures per student to changes in the number of students between 1999-2000 and 2006-07 for Georgia. He finds that the total expenditure per student changes, on average, by \$6,299 for a marginal change of one student. This change in expenditures equals the change in state grant, federal grants, and local revenue. In 2006-07, state revenue per student was \$4,352. Federal aid is comprised of a number of programs, the largest of which is Title I; we assume that Federal Aid would decrease by the per student average, which was \$628 in 2006-07. Thus, the marginal decline in local spending as a result of a reduction of one student in 2006-07 would be, on average, about \$1,319. This represents 36.6 percent of the average local revenue per student at the time. We apply this percentage to the 2012-13 local revenue per student as reported in Table 6, and thus assume that local school systems will save, on average, \$1,272 for each student who switches from the public schools to a private school. We refer to this figure as the local marginal cost per student. The net fiscal effects at the local level are also dependent on the switching rate, just as at the state level, so this amount is multiplied by the switching rate to estimate the local fiscal effect per scholarship student.

Local, and combined state and local fiscal effects for the various combinations of parameter values are shown in the final four columns of Table 5. Switching rates necessary for combined state and local budget neutrality are also estimated. For example, with tax credits per scholarship student at \$2,000 and state grants per student at \$4,066, a switching rate of 38 percent would result in an \$11.4 million net fiscal cost at the state level, but a \$12.1 million net fiscal gain at the local level. At the lower level of tax credits per scholarship, \$1,500, and the 37 percent switching rate necessary to break even at the state level, the combined fiscal effect is a \$15.8 million budget gain. At the \$3,500 level of tax credits per scholarship student and \$4,066 for state QBE grants, the combined state and local budget effect would be slightly positive at a switching rate of 66 percent. A switching rate of 66 percent is greater than the 30 percent switching rate reported by Lips and Jacoby (2001), but we do not have the information to determine how likely or unlikely it is that the actual switching rate is at least 66 percent.

### VIII. Proposal for an Additional Tax Credit Scholarship Program

Recently, a draft legislative proposal has been developed that would be a new tax credit scholarship program in Georgia, referred to as the BEST (Business and Education Succeeding Together) program, which would be in addition to the existing program. The proposed new program is similar in many ways to the existing QETC program, but differs from the current program in the following ways:

- Only C-corporations would be eligible to take the tax credit.
- Limit the aggregate amount of BEST tax credits to \$25 million.
- Donations from individual corporations would be limited to \$2.5 million each.
- Scholarships would be restricted to students eligible for free or reduced lunch (FRL), namely a household income of less than 185 percent of the poverty level.

These differences will affect the fiscal impact of the BEST program relative to the existing program. First, the tax credit cap of \$25 million means that for any switching rate, the net fiscal impact will be half as large as the amounts shown in Table 5 for any given set of other parameter values. However, the switching rate that results in zero net fiscal impact is the same as those reported in Table 5.

Second, the switching rate will likely be higher given the income requirement. In its analysis of the fiscal effect of the Florida tax credit scholarship program, which is limited to low-income students, the Florida Office of Program Analysis and Government Accountability (OPAGA) assumed that students eligible for free and reduced lunch would be very unlikely to enroll in private schools in the absence of a scholarship. OPAGA used a switching rate of 90 percent in their analysis, but do not explain how they arrived at that assumption.

The notion that low-income students do not enroll in private school is not correct. Using Census data, we find that there are 36,025 FRL students in Georgia private schools, which is more than 4.7 percent of Georgia children who are eligible for free and reduced lunch. This compares to 15.6 percent for K-12 students from families with incomes above 185 percent of the poverty level who are in private school. Of course some of these low-



## Georgia's Tax Credit Scholarship Program

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income students in private schools may have tax credit funded scholarships or other financial aid now, in the absence of which they would not attend private school, but this number is almost three times the total number of scholarships awarded under the current QETC scholarship program. Note further that only 17.9 percent (44.2 percent) of families with scholarship students are in the first (first and second) quartile of Georgia adjusted gross income.

While we believe that the switching rate will be higher for the proposed new program than for the existing program, we do not have a way of independently estimating what it might be. There are several studies that find that the likelihood of private school attendance increases with increases in income and decreases in tuition, although Buddin, Cordes, and Kirby (1998) find no effect of marginal changes in tuition on private school enrollment. This leads to the concern that if scholarship amounts are too low, few students will switch and the program will not have the desired impact.

Gottlob (2008) estimates that the total number of Georgia FRL students who would take a \$2,000 scholarship is 5,567 students (and assumes that all of these students would be switchers from public to private school), but \$2,000 would cover only a small portion of tuition to most private schools, even where need-based tuition discounts are offered. Nationally, private school tuition averaged \$10,740 in 2011-2012, though it was lower on average for religious schools (National Center for Education Statistics, undated).

Ferreira (2007), though she does not give a baseline for low-income households in private schools absent the vouchers, reports 13 percent low-income household enrollment in private schools for a \$1,000 universal voucher and 53 percent for a \$3,000 universal voucher. If the voucher program is restricted to nonsectarian private schools, the low-income enrollment rate drops to 3 percent for the \$1,000 voucher, but rises to 20 percent if the voucher is increased to \$3,000. The higher response by low-income households to universal than to nonsectarian vouchers may be an artifact of the market, Chicago, where the majority of private school enrollments at the time were to Catholic schools, which are usually subsidized by a parish or diocese of the church, and thus charge significantly lower tuition. In 1993-1994, around the time covered by her data, average tuition at Catholic parochial and diocesan schools nationally were \$1,610 and \$1,913, respectively, compared to \$3,084 for all private schools and \$6,822 for nonsectarian schools (National Center for Education Statistics

## Georgia's Tax Credit Scholarship Program

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1997). Achieving similar private school enrollment rates for low-income families in Georgia may be difficult if scholarship amounts are too small relative to tuition costs.

To explore the fiscal implication of the proposed BEST program, consider first the case in which no current FRL private school student gets a BEST scholarship, meaning that the actual switching rate is 100 percent. In this case, the state breaks even if 6,149 scholarships are awarded, resulting in \$25 million of reduced QBE funding grants (\$4,066 times 6,149). At the lower QBE grant level of \$3,587, the breakeven number of scholarships would be 6,970. In the event that SSOs are unable to place the requisite number (or more) of scholarship students, the savings in QBE funding would be less than the total credits allowed. This could occur, for example, if the scholarships offered are too small relative to private school tuition costs to attract enough FRL-eligible students. Alternatively, if the average scholarship is too large, the \$25 million of donations would be absorbed by fewer than the breakeven 6,149 students and again the savings to the state would fall short of the cost in credits.

To support 6,149 students while being budget neutral at the state level, tax credits per scholarship cannot be more than \$4,066 since a larger amount would result in a net negative budget impact for the state. If 90 percent of donations fund scholarships, this would equate to a maximum average scholarship amount of about \$3,659 for the state to break even.

This breakeven number of scholarships, 6,149, would represent about a 17 percent increase in the number of FRL-eligible students in private schools, and is about 0.6 percent of the total number of Georgia's FRL-eligible public school students. It is also only 582 students or about 10.5 percent larger than the number of FRL students that Gottlob (2008) estimated would switch to private school in response to a \$2,000 scholarship. If we include the reduction in local education expenditures (the local marginal cost per student in public schools), the breakeven number of scholarships, counting both state and local fiscal effects, would be 4,683.

Second, consider the case in which not all of the scholarship recipients are switchers from public school. As noted above, there are far more FRL-eligible students currently in private school than can be explained by the QETC scholarship program, so it cannot be assumed that 100 percent of BEST scholarship recipients would not attend private school in the absence of the BEST program. In this case, to break even the BEST program would still need to fund 6,149 true switchers (or 6,970 if the lower average QBE grant is assumed).

## Georgia's Tax Credit Scholarship Program

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However, because some scholarship recipients would have enrolled in private school anyway, the total number of scholarships awarded out of the \$25 million of donations would have to be larger than 6,149 and the average scholarship amount must be smaller. As in the case of the QETC program, at \$3,000 per scholarship student and an average QBE grant of \$4,066, the state level breakeven switch rate would be 74 percent (6,149 switchers out of 8,333 scholarship recipients). The required switching rate would be 57 percent if the reduction in local education expenditures is also considered. Lower average scholarship amounts, as before, result in lower breakeven switch rates, but lower average scholarship amounts also may make it more difficult to attract sufficient new FRL students to reach breakeven. Nevertheless, a 74 percent switch rate is more likely in a means-tested program than in a program that is not means-tested, and is below what OPAGA and others have assumed in evaluating means-tested programs in other states.

### **IX. Evaluating the Efficacy of the Tax Credit Scholarship Program**

Other than attempts to measure the fiscal impact, there has not been a thorough evaluation of the effectiveness of tax credit scholarship programs in meeting other goals, either in Georgia or elsewhere. There are many questions that such an evaluation might want to address, including:

- What percentage of scholarships go to students who switch from low-performing public schools?
- Do the scholarships result in improved student performance?
- What is the income, gender, race/ethnicity, grade level of scholarship recipients?
- What is the quality of the private schools that the scholarship recipients attend?

However, with the limited data that is available, it is not feasible to conduct an evaluation that addresses these questions for Georgia. We recognize the desire to maintain confidentiality of scholarship recipients, but with appropriate precautions and controls, additional data could be made available that would be useful to policymakers in understanding the costs and benefits of the program.

The data that would be necessary, or at least very useful, to conduct an evaluation include:

- The public schools attended by scholarship recipients prior to award of the scholarship. These data would be used to estimate the switching rate and to evaluate the quality of the public schools the students are leaving.
- To explore the improvement in student performance, it would be useful to have scores on comparable standardized tests for the private and previously attended public schools. Private schools are not required to use the same standardized tests that public schools use, but available performance information could be used to judge the benefits in terms of quality of the private schools relative to the public schools the scholarship students had been attending.
- The characteristics of scholarship recipients is an important aspect of any evaluation of the program. Thus, the distribution by race, gender, family income, and age (grade) of the scholarship recipients would be important data to report.

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Regarding income, SSOs currently report the number of families receiving scholarships, but not the total number or amount of scholarships, by quartile of Georgia adjusted gross income. This reporting provides little detail regarding the income distribution of scholarship recipients and no information on the distribution of scholarship dollars. Reporting by decile, and including the numbers of scholarship students and the total amounts awarded for each decile, would provide a better understanding of the distribution and would not require any additional effort. In addition, a broader income measure than Georgia AGI would be preferable as it is a much narrower income definition than is used in delineating the poverty level or in determining eligibility for FRL and other income-based programs. However, the household income measure used to determine eligibility for FRL has many components and it would be difficult to collect that much information for children who are not likely to apply for FRL. A simple alternative is to report by total income from the federal income tax return; that is, income on line 22 of the 2013 Form 1040. It would be reasonable to assume that total income from Form 1040 is approximately equal to the income used to measure poverty.

The federal poverty threshold, and thus the eligibility threshold for free or reduced price lunch, varies by the number of adults and children in the household, but using total income does not allow a differentiation by size of the family. Information on the numbers of parents and of children under 18 years of age in the household would allow reporting by income groups defined as a percent of the poverty threshold, perhaps corresponding to FRL eligibility levels and then higher multiples of poverty level income.

### **X. Summary and Conclusions**

In 2008, Georgia adopted legislation that allows tax credits for donations that are used to fund scholarships for students enrolled in private schools. Georgia is one of 14 states that offer a tax credit funded scholarship program. In this report we first present an overview of this program, including its history, legislation, and data on participation, and a summary of the arguments for and against the program. However, the main focus of the report is an analysis of the fiscal effects of the current program and of a proposed second tax credit scholarship program.

The fiscal impact of the tax credit scholarship program depends on the amount of tax credits taken and the reduction in spending on public education. The value of tax credits taken is the gross reduction in state revenue. However, if scholarship students switch from a public to a private school, the state and the local school system can each reduce their spending by the amount of the variable cost of educating that student. Thus, the net fiscal effect of the tax credit scholarship on the state's budget equals the value of the tax credits that are taken less any reduction in state education grants due to the scholarship program. Local savings may partially offset or even exceed any net cost at the state level.

There are four variables that determine the fiscal impact: the tax credits per scholarship recipient, the number of recipients, the reduction in spending on education if a student switches from public school to private school as a result of the scholarship, and the share of scholarship recipients who switch, which we refer to as the switching rate. While the reduction in spending on education depends on several factors, we are able to identify the mean reduction within a small range.

The variable about which we have very little information is the share of scholarship recipients who, in the absence of the scholarship, would attend public schools. That information is not available, nor do we have the data necessary to estimate it. There are several reasons why the switching rate would not be 100 percent even with a prior public school enrollment requirement. For example, parents might simply enroll their child in a public school for the sole purpose of making him or her eligible for a scholarship, and thus in the absence of the scholarship would not have attended public school. In addition, the public school enrollment restriction on scholarship eligibility does not apply to private school students who start private school by the first grade.

## Georgia's Tax Credit Scholarship Program

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Since we don't know the percentage of scholarship recipients who would have switched from public schools, we determine the switching rate required for the state government to break even. For example, if tax credits per scholarship recipient were \$3,500, which is a little less than the average scholarship in 2013, breakeven requires that 87 percent of the scholarship recipients would not have been in private school in the absence of the scholarship, assuming each switcher saved the state the average per student QBE grant. If savings in local education spending is included, the required rate of switching is 66 percent.

Recently, a new tax credit scholarship program has been proposed. The proposed new program, BEST, is similar in many ways to the existing QETC program, but differs from the current program in that only C-corporations would be eligible to take the tax credit, total tax credits would be capped at \$25 million, and scholarships would be restricted to students eligible for free or reduced price lunch (FRL). If the actual switching rate was 100 percent, then at least 6,149 scholarships would have to be awarded to FRL-eligible students eligible in order for the total reduction in QBE funding to be at least equal to the total of \$25 million in tax credits. This breakeven number of scholarships, 6,149, would represent about a 17 percent increase in the number of FRL-eligible students in private schools and is about 0.6 percent of the total number of Georgia's FRL-eligible public school students. We are unable to predict whether at least 6,149 scholarships would be taken, but note that this number is comparable to the 5,567 Georgia FRL students that Gottlob (2008) estimated would switch to private school in response to a \$2,000 scholarship.

We cannot assume that 100 percent of BEST scholarship recipients would not attend private school in the absence of the program. But regardless of the switching rate, to break even the BEST program would still need to fund 6,149 true switchers. However, because some scholarship recipients would have enrolled in private school anyway, the total number of scholarships awarded out of the \$25 million of donations must be larger than 6,149 and the average scholarship amount must be smaller than would be possible if the switch rate was 100 percent. Lower average scholarship amounts result in lower breakeven switch rates, but also may make it more difficult to attract sufficient new FRL students to reach breakeven. Nevertheless, achieving the breakeven switch rate is more likely in a means-tested program than in a similar program that is not means-tested.

## Georgia's Tax Credit Scholarship Program

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***Geographic Dispersion of SNAP Enrollment in Georgia (Peter Bluestone).*** This brief, with the aid of maps, illustrates the variations in SNAP enrollment as a share of county population as well as the changes that have occurred in those shares from 2000 to 2012. [FRC Brief 267](#) (February 2014)

***Trends in Georgia School Staffing 2001-2012 (Nicholas Warner).*** This brief examines the changes in teacher and administrator education, experience, and compensation over the last 10 years with a focus on the possible effect of the Great Recession. [FRC Brief 266](#) (January 2014)

***School District Education Expenditures in Response to the Great Recession (Nicholas Warner and Carolyn Bourdeaux).*** This report examines the structure of school district expenditures between 2001 and 2012 with a particular focus on changes in instructional expenditures during the recession. [FRC Report 265](#) (January 2014)

***Georgia's Taxes: A Summary of Major State and Local Government Taxes, 20th Edition (Carolyn Bourdeaux, Robert Buschman, and Richard Hawkins).*** A handbook on taxation that provides a quick overview of all state and local taxes in Georgia. [FRC Annual Publication A\(20\)](#) (January 2014)

***Geographic Dispersion of Federal Funds in Georgia and Its Major Urban Regions (Peter Bluestone).*** This brief examines the geographic distribution of federal spending in Georgia. [FRC Brief 264](#) (October 2013)

***Population, Employment, and Income Trends for Georgia and Atlanta (David L. Sjoquist).*** This report explores the growth in population, employment, and income over the previous 50 years in Georgia and Atlanta. [FRC Report 263](#) (September 2013)

***Georgia's High-Technology Industry and Innovation Capacity (Cathy Yang Liu).*** This report describes the demographic composition of the high-technology industry workforce and the innovation capacity of Georgia in comparison to peer Southeastern states between 2000 and 2011. [FRC Report 262](#) (September 2013)

## Georgia's Tax Credit Scholarship Program

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***The Department of Defense Budget Cuts: Economic Impact on Georgia and Selected Counties (Peter Bluestone)***. This brief examines the economic impact Department of Defense procurement contracts, grants, and civilian wages have on the state of Georgia as well as selected counties. [FRC Brief 261](#) (February 2013)

***Zero-Base Budgeting for the 21<sup>st</sup> Century Public Administrator (Ron Shelby)***. This report discusses the history of Zero-Base Budgeting (ZBB) reform, how to implement classic 1970s style ZBB reform and strengths and weaknesses of the reform. [FRC Report 260](#) (March 2013)

***The Structure and History of Georgia's Job Tax Credit Program (David L. Sjoquist and Laura Wheeler)***. This report describes the provisions of Georgia's job tax credit program and how the program has evolved since its inception in 1990. [FRC Report 259](#) (February 2013)

***The Incentives Created by the Tax-Benefit System Facing Low-Income Families in Georgia (Chelsea Coleman, Kendon Darlington, Mark Rider, and Morgan Sinclair)***. This report describes the incentives created by the major taxes and public assistance programs facing low income-families in Georgia. [FRC Report/Brief 258](#) (February 2013)

***Georgia Taxpayers and Federal "Pease" Limitations on Itemized Deductions (Robert Buschman)***. This brief analyzes the effects of federal limits on itemized deductions and the state income tax liabilities of Georgia taxpayers. [FRC Brief 257](#) (January 2013)

***Lessons for Georgia: Telecommunications Tax Reform in Some of the Other Southeastern States (Richard Hawkins)***. This report reviews telecommunications tax reform in other states, discusses four major policy issues and looks at the health of the industry in the other states after reform. [FRC Report 256](#) (January 2013)

***Property Tax and Education: Have We Reached the Limit? (David L. Sjoquist and Sohani Fatehin)***. This report explores changes over the past decade in property taxes used to fund K-12 education and discusses the future of the property tax for education. [FRC Report 255](#) (January 2013)

***Georgia's Revenue and Expenditure Portfolio in Brief, 1989-2010 (Carolyn Bourdeaux, Nicholas Warner, Sandy Zook, and Sungman Jun)***. This brief uses Census data to examine how Georgia ranks in terms of spending and revenue by functions and objects and examines how Georgia's portfolio has changed over time compared to national peers. [FRC Brief 254](#) (January 2012)

(All publications listed are available at <http://frc.gsu.edu> or call the Fiscal Research Center at 404.413.0249.)