

## **Tuition Tax Credits in New Mexico: Saving Money, Creating Educational Opportunities**

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### **Executive Summary**

In an effort to improve education opportunity, several states have enacted tuition tax credit scholarship programs. While the programs vary, they all have provided increased choices for students in their states. The experiences of these states shows that tuition tax credit programs can be revenue neutral for the state and sometimes even provide increased net income, especially at the local levels of government.

This year, New Mexico has an opportunity to embark on the same type of path as these other states. Recently introduced Senate Bill 355 creates a tuition tax credit program to make scholarships available to students who currently qualify for free or reduced-price lunches.

### **Introduction**

A tuition tax credit bill, Senate Bill 355, has been introduced this session. The bill seeks to improve educational choice through a program that provides tax credits to both individuals and businesses that make contributions to a K-12 scholarship program. The scholarships are made available to students who are eligible for free/reduced price lunches.

Several other states have enacted comparable programs and have seen high levels of giving while maintaining revenue neutrality in their states, thus providing more educational choice while offsetting taxpayer costs.

### **States That Have Tax Credit/Deduction Programs**

There are nine states with varying K-12 tuition tax credit programs including: Arizona, Florida, Pennsylvania, Iowa, Rhode Island, Georgia, Illinois, Louisiana, and Minnesota.

In 1997, Arizona created an individual tax credit scholarship program. Within two years the program became revenue neutral and is projected to raise an estimated \$58 million annually by 2015 for scholarship donations.<sup>1</sup> So far more than 27,000 scholarships have been awarded. Arizona's program has been seen as a great success for both providing increased education opportunities as well as being a revenue neutral program for the state.

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<sup>1</sup> Darcy Olsen, "Education Scholarships: Expanding Opportunities for Students, Saving Taxpayers Money," Arizona Issue Analysis 169, March 26, 2002, p. 3.

In 2001, Florida passed a scholarship credit law similar to Pennsylvania's.<sup>2</sup> The Florida program has proven to be a net savings to the state. While it receives less corporate tax revenue because of the credit there is a net savings because "state education spending for students who receive scholarships is reduced by more than the amount of revenue lost."<sup>3</sup> More than 38,000 scholarships have been awarded.

Also in 2001, Pennsylvania started a tax credit program similar to Florida's; it was expanded in 2007. More than 38,000 scholarships have been awarded in Pennsylvania.<sup>4</sup>

Iowa's plan has awarded nearly 8,000 scholarships since being enacted in 2006. It has both a personal deduction for parents of students as well as an individual tax credit for those making donations.

Rhode Island's program is smaller than the other states; it allows small business to donate to a corporate scholarship program for tax credits. Nearly 300 scholarships have been awarded.<sup>5</sup>

Just last year Georgia enacted their program, which allows for both individual and corporate tax credits.<sup>6</sup>

The Illinois program is designed specifically for parents of students; they are able to claim a 25 percent credit on expenses over \$250 (per child), up to \$500.<sup>7</sup>

Louisiana's plan is different in design because it allows for a personal-use tax deduction. Families are allowed to deduct 50 percent of the amount spent, capped at \$5,000 per child.<sup>8</sup>

Minnesota also has a personal-use deduction. More than 200,000 families received deductions in 2008.<sup>9</sup>

### **What the New Mexico Bill Proposes**

Senate Bill 355, introduced in the New Mexico's 2009 legislative session provides a tax credit opportunity for both individuals and businesses. Funds from the credit are to pay for scholarships of students eligible for reduced-price lunches.<sup>10</sup> The scholarship covers all or part of the tuition and fees at a "qualified nonpublic school." The tax credit funds are distributed to "scholarship

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<sup>2</sup> "The Corporate Income Tax Credit Scholarship Program Saves State Dollars," Office of Program Policy Analysis & Government Accountability, Report No. 08-68, December 2008, p. 1.

<sup>3</sup> *Ibid.* p. 4.

<sup>4</sup> "Annual Report 2007," Alliance for School Choice, p. 19, available online at: [http://www.allianceforschoolchoice.org/UploadedFiles/ResearchResources/AnnualReport2007\\_07222008.pdf](http://www.allianceforschoolchoice.org/UploadedFiles/ResearchResources/AnnualReport2007_07222008.pdf).

<sup>5</sup> *Ibid.* p. 20.

<sup>6</sup> "Just the FAQs – Tuition Tax Credits and Tax Deductions," The Center for Education Reform, available online at: <http://www.edreform.com/index.cfm?fuseAction=document&documentID=59>.

<sup>7</sup> *Ibid.*

<sup>8</sup> *Ibid.*

<sup>9</sup> *Ibid.*

<sup>10</sup> Once a student becomes eligible for the scholarship, the student remains eligible until graduating from high school or turning twenty-one.

granting organizations.”<sup>11</sup> In order to qualify, a school must: (1) be non-public; (2) accredited; (3) an elementary or secondary school; (4) non-discriminatory towards students<sup>12</sup>; (5) a non-profit 501(c)(3) organization<sup>13</sup> and (6) require students to take an annual academic test with individual scores provided to the parents.

Individual taxpayers filing a New Mexico tax return can claim a credit for a contribution to a scholarship granting institution up to \$500. The limit is \$1,000 for a married couple filing jointly. Corporate taxpayers filing a New Mexico tax return can claim a credit for a contribution to a scholarship granting institution up to \$50,000, per taxable year.

### **Fiscal Impact of Tax Credits on the State**

The fiscal impact of the tax credit program will depend on how many donations are made by individuals and corporations. Since there is no overall cap on the total amount of credits allowed, the ceiling is completely dependent on the choices made by individuals and corporations.

According to the U.S. Census Bureau’s data on 2006 public school funding per-pupil spending in New Mexico is around \$8,086<sup>14</sup> State aid to schools for 2010 will be around \$7,200 (based on historical trends).<sup>15</sup> Since there is no cap on total amount collected, theoretically all students who qualify for reduced/free lunches (more than 156,000) could receive a scholarship. If so that would save state  $\$7200 \times 156,000 = \$1.1$  billion. Number of kids who qualify for reduced lunches in the state 156,401 in 2003-2004 school year.<sup>16</sup> More than half the students enrolled in public schools in New Mexico qualify for free or reduced lunches.<sup>17</sup>

The impact on the state budget depends on the amount of individual and corporate tax revenue lost because of the credit, the number of students who leave public schools as a result of the scholarships, and the reduction of state aid payments to public schools. Previous studies have shown that less than 4,000 students need to move from public schools to nonpublic schools for the credit to have a net positive fiscal effect.<sup>18</sup>

Studies also indicate that by year 3 of the program there would be around \$24 million in scholarships available. That study shows that there may be an initial outlay cost of up to \$1

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<sup>11</sup> To qualify it was demonstrate that it is qualified as a 501(C)(3), that it provides financial assistance in the form of educational scholarships or tuition grants to attend nonpublic schools, spends a minimum of ninety percent of tax credit revenue for scholarships or tuition grants, and provide all scholarships and grants to children who qualify for reduced-price lunches.

<sup>12</sup> “Non-discriminatory” includes discrimination on the basis of a student’s race, national origin or ethnicity.

<sup>13</sup> Also includes organizations in the process of applying for the tax status.

<sup>14</sup> State per-pupil spending available online at: <http://www.ppinys.org/reports/jtf/pupilspending.htm>.

<sup>15</sup> For the 2002-2003 school year state aid was about \$5,300 per pupil and at a 4% increase per year it increases to more than \$7,000.

<sup>16</sup> National Center for Education Statistics (IES) available online at: [http://74.125.47.132/search?q=cache:qMpl7kw4BBsJ:nces.ed.gov/ccd/TableDisplay.asp%3FTablePath%3Dtables/table\\_07.asp+total+students+new+mexico+free+lunch&hl=en&ct=clnk&cd=4&gl=us&client=firefox-a](http://74.125.47.132/search?q=cache:qMpl7kw4BBsJ:nces.ed.gov/ccd/TableDisplay.asp%3FTablePath%3Dtables/table_07.asp+total+students+new+mexico+free+lunch&hl=en&ct=clnk&cd=4&gl=us&client=firefox-a)

<sup>17</sup> Brian J. Gottlob, “The Fiscal Impact of Tuition Tax Credits in New Mexico,” Friedman Foundation, April 22, 2005, p. 9.

<sup>18</sup> *Ibid.* p. 16.

million for the state for the first two years but by the third year the program will result in savings between \$1 million and \$12 million.<sup>19</sup> The net impact of savings on local school districts will vary but savings can be immediate. A 2005 study indicates that in the first year local districts will see a savings of more than \$1 million, which will increase to more than \$8 million within 10 years.<sup>20</sup>

The Fiscal Impact Report for SB 355 projects an estimated personal income tax revenue loss of \$3.5 million for the first year of the program and \$1.6 million in corporate income tax revenue loss.<sup>21</sup> The report, however, fails to take into account any offset costs to the state or local governments resulting from the tuition tax credit program. As students leave the public schools, the state and local governments will save money that would have been spent to send that student to a public school.

While the Legislative Fiscal Impact Report looked at Arizona and Ohio they did not take into account other states' experiences. In Florida, for example, corporate income tax revenues have actually increased since the program started.<sup>22</sup>

### **Educational Impact of Tax Credits on the State**

For many families in New Mexico, there is no choice when it comes to their children's education. The only option for them is their local public school; they cannot afford anything else. Tuition tax credits change this. It provides better education opportunities for those who cannot afford it on their own.

Other states that have created scholarships through tuition tax credits, similar to what SB 355 proposes, have experienced an outpouring of support and gratitude from their communities. One student in Florida commented, "The last five years have completely changed my life...If it weren't for the scholarship program, I might have been one more student who drops out of school and just another statistic. My school ended up being a perfect fit for me. It was the first time in my life that I actually believed in myself."<sup>23</sup>

Instead of forcing students to attend whatever public school they are closest to, these scholarships provide them the opportunity to find a good fit for them. Finding that good fit is an integral component to ensuring that more students in New Mexico not only graduate but graduate with the potential to achieve either in the workplace or in a higher education setting.

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<sup>19</sup> *Ibid.*

<sup>20</sup> *Ibid.* p. 20.

<sup>21</sup> "Fiscal Impact Report," Legislative Finance Committee for standing finance committees of the New Mexico Legislature, February 8, 2009, p. 2.

<sup>22</sup> "The Florida Corporate Income Tax Credit Scholarship Program: Updated Fiscal Analysis," Collins Center for Public Policy, Inc., February 2007, p. 8.

<sup>23</sup> Jullian Metz, "Crist Celebrates Florida Scholarship Program," *School Reform News*, The Heartland Institute, Vol. 13, No. 2, February 2009, p. 13.

## **Conclusion**

Tuition tax credits provide increased educational opportunities for those who could not otherwise afford it. Instead of costing the state money, however, a tuition tax credit program can be revenue neutral and may eventually save the state money by decreasing the amount of funds it has to provide directly to public schools. Nine states have already enacted similar programs which have benefited students, families, and taxpayers, perhaps New Mexico should do the same.