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In many ways, the legislation recently introduced in Colorado is a refinement and improvement on the Arizona law. King and Hagedorn deserve praise for crafting provisions making the law more equitable and less damaging to public education. Yet substantial concerns remain about the law's effects and legality. This report examines these issues, offers suggestions for additional improve

of contributions) shall not exceed \$3,000,000 initially, increasing to \$10,000,000 by 2010. A key part of the DNO's task is to cut off the allocation of credits after the limit is reached for a given year. Qualified taxpayer donations would be granted on a first-come, first-served basis until the annual limit is reached.

*The Nonpublic-School Component.* Each CNEAO is required to grant from 60% to 75% of its revenue "for the purpose of providing scholarships to income-qualified students who attend eligible schools." Notwithstanding this "scholarship" terminology, the statutory language includes no academic restrictions or guidelines for selecting grant recipients. Instead, the language restricts recipients based on two non-academic criteria: (1) a percentage of the students must have been enrolled in a public school (including a charter school) in the year prior to receipt of his or her first CNEAO grant; and (2) the student's household income must be within 200% of the federal poverty level.

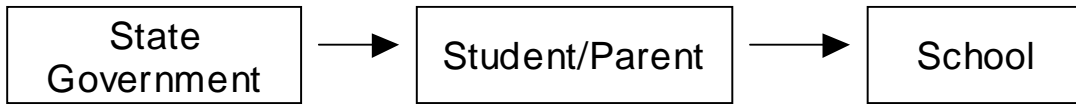
Further, the legislation states that, in order for a student to qualify as a "public-to-private student" (a certain minimum number of grants each year must go to such students), the CNEAO grant to that student must be for at least 30% of the student's annual tuition. For instance, if the student is attending a nonpublic school with annual tuition of \$5,000, the CNEAO grant must be for at least \$1,500. In addition, the nonpublic school, to be eligible to enroll students using the CNEAO grants, must enter into an agreement with the Colorado Commissioner of Education consenting to administer annual tests to the grant-recipient students. The tests shall measure

"academic achievement and growth" using specific approaches set forth in the agreement. (That is, the tests need not be the Colorado Student Assessment Program, or "CSAP", tests required of public school students.) Eligible schools include any nonpublic elementary or secondary school, or a certified "Educational Clinic."<sup>5</sup>

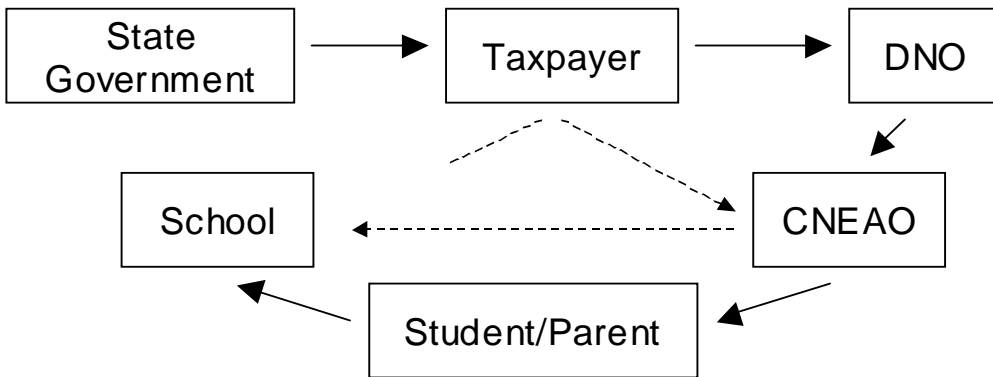
In short, the mechanism proposed in the Colorado legislation tells those who owe state taxes that they may reallocate some of that money from the state general fund to nonpublic schools. Whereas voucher plans entail granting state-allocated funds to schools through the private decisions of parents, the Colorado plan inserts three intermediate steps into the process. First, the grants are issued by privately-created, non-profit CNEAOs, rather than directly by the government. Second, the taxpayers' direct dealings are with a privately-created, non-profit DNO, which then follows the taxpayers' directives in allocating this money to

**Figure 1**

Vouchers

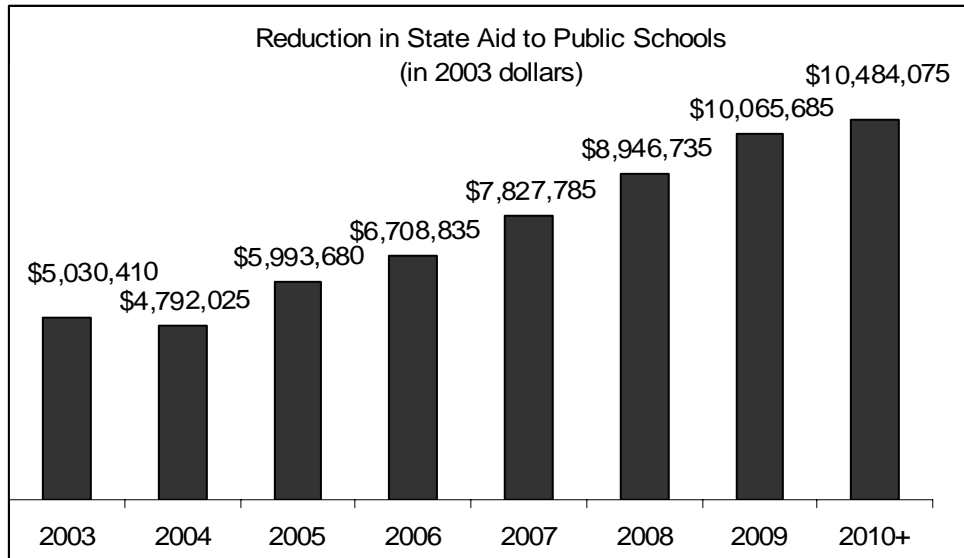


Colorado Tax Credit



(QSDFs) or to assist “income qualified-  
students who attend public elementary  
schools or public secondary schools in  
Colorado in defraying education-related

**Figure 2**

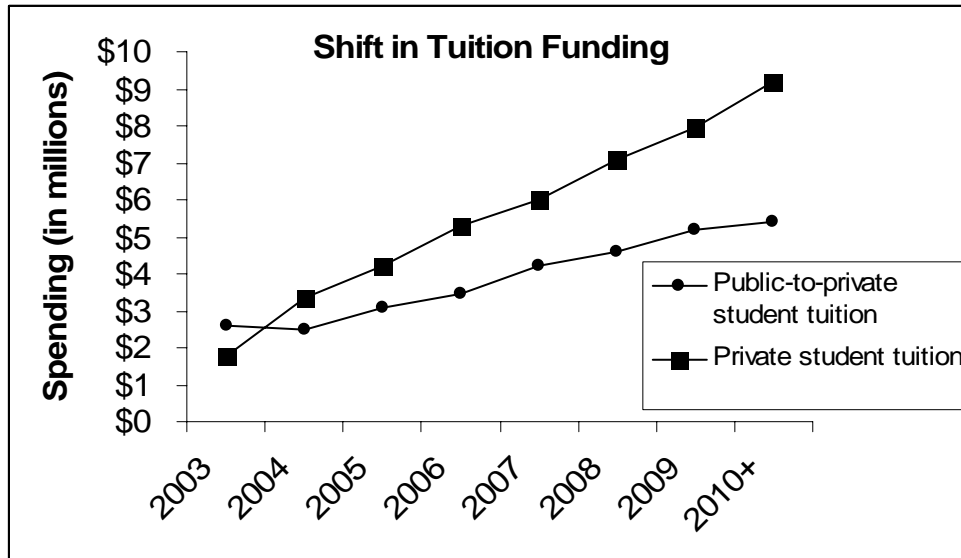


years, one can calculate the approximate reductions in state aid to public schools. This calculation predicts a loss of 84% of per pupil operating revenue for each funded public-to-private student, yielding

**Figure 3**



**Figure 4**



The change in expenditures favoring private student tuition at the expense of public-to-private student tuition can be justified based on t

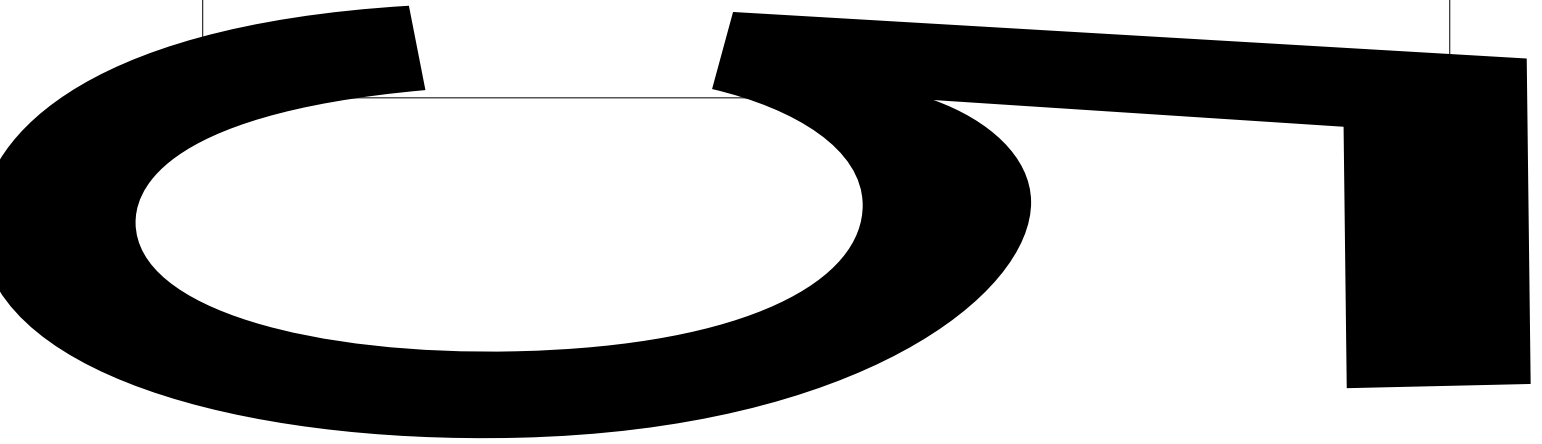
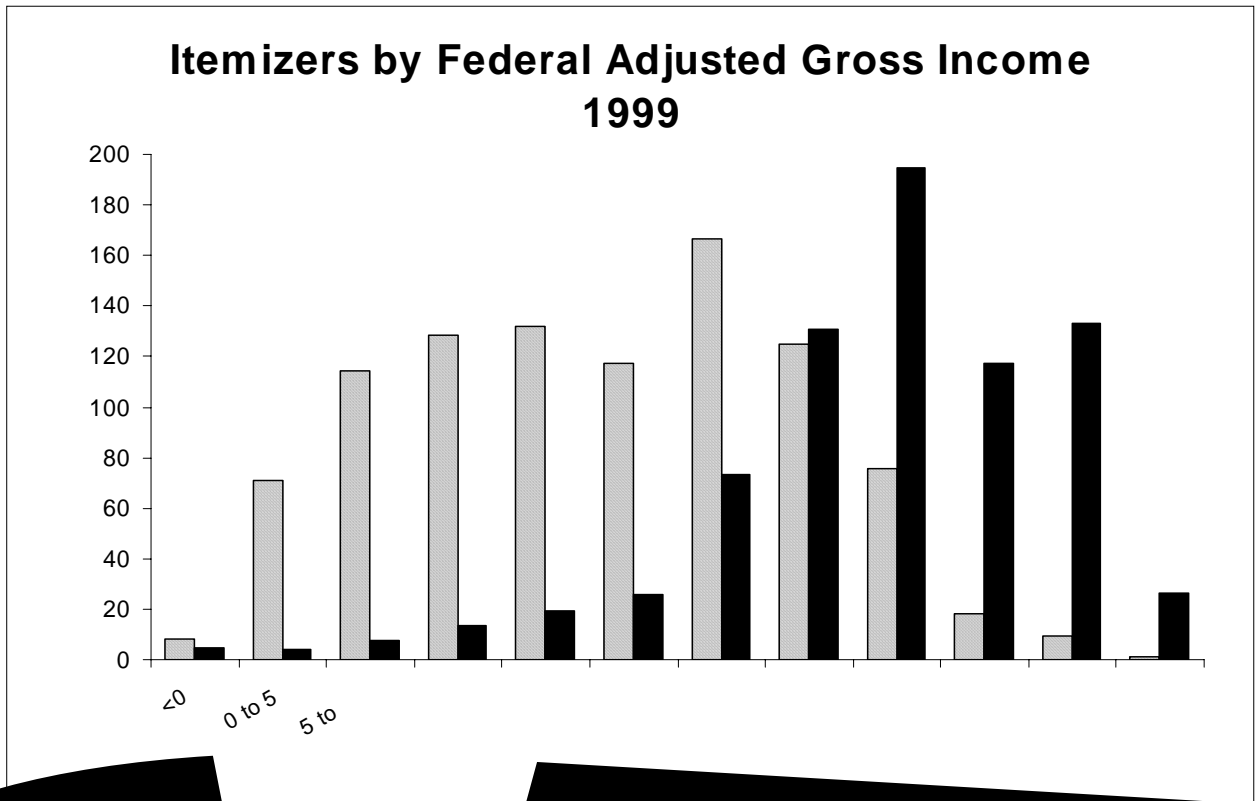
private provision in HB 1137 will therefore cause a somewhat greater amount of grants to be made to these students than would otherwise be expected if the distribution were left completely to the free market. At the beginning of the program, these grants will account for 43%, and they will steadily decrease down to 27%, by the time the program is fully mature.

*Which Taxpayers Will Take the Credit?*

An individual taxpayer cannot take the tax credit if he or she does not itemize deductions. Lower-income Colorado families can benefit from the tax credit policy, as recipients of CNEAO grants, but they are cannot play a part in the earlier, decision-making (directing donations to a particular CNEAO) process unless they owe state taxes and itemize deductions in their tax returns.

Less than 44% of Colorado's returns in the year 1999 (the last year for which I found data) were itemized. This means that more than half the state's taxpayers would be effectively barred

**Figure 5**



Alliance for Choice in Education, as reported in a recent story in the *Rocky Mountain News*. The alliance grants scholarships to low-income Denver families, comparable to the main activity that HB 1137 proposes for CNEAOs. According to the *News*, “At the inner-city schools many alliance scholarship



contributions received by many CNEAOs would likely be devoted to the affiliated nonpublic school or schools. In this regard, it is important to note that the legislation places no express limitations on the “education-related costs” to be defrayed by the CNEAO grants. The education provided could relate to core academic subjects or could be religious education. The discretion is left with the CNEAO and the school.

The above discussion assumes that the vast majority of CNEAOs will be created to serve nonpublic schools. Another alternative would involve the creation of CNEAOs to serve public schools. Each CNEAO could devote up to 40% of their received contributions to assist low-income students, either directly defraying education-related costs or indirectly passing on the money to a QSDF. Yet such a CNEAO would also be required to use 60% of their received contributions to facilitate student movement from public to nonpublic schools – an unlikely goal for a CNEAO created to serve public schools. Consider the situation faced by a taxpayer considering a donation to such a CNEAO. For each dollar donated, the taxpayer is effectively paying 50 cents (the state pays the other 50 cents, through the tax credit). As a result of that 50 cent investment, approximately 40 cents will benefit public schools. If the taxpayer instead makes a charitable donation of one dollar to a given school and treats the donation as a regular tax deduction, it will cost the taxpayer about 70 cents (assuming a 30% marginal tax rate), but the public school receives the full dollar. For a supporter of public schools, this latter option is clearly preferable: a 79% greater return on the taxpayer’s investment.

Based on this rationale, one would expect few successful public-school

oriented CNEAOs. One would also expect that the distribution range of 60%-75% is superfluous; CNEAOs affiliated with nonpublic schools will focus as much as possible on defraying tuition costs. Finally, one would expect that any money that does reach a QSDF would not be distributed equally or according to overall need. That is, the fund-raising ability of a QSDF would likely be greater for some school districts than for others, and these differences may not reflect actual school need.

#### Comparing the Arizona Experience

Colorado’s legislation follows in the wake of similar laws enacted in Arizona and, more recently, in Pennsylvania and Florida. The Arizona law, passed in 1997, provides a 100% tax credit of up to \$625 per taxpaying couple. This credit is available to individuals, but not corporations, and the donations must be made to school tuition organizations (STOs),<sup>19</sup> rather than directly to the schools. The Pennsylvania and Florida laws were recently passed (in 2001) and therefore have no significant track record, but they differ from the Colorado legislation in that they provide credits only to corporations, not individuals. Similarly, Arizona differs in that only individuals – not corporations – are included. Like the Colorado proposal, the laws in all three of these states include provisions designed to benefit public schools as well as nonpublic schools.<sup>20</sup>

The Arizona law places only two notable limitations on its tuition tax credit system. The tax credit “is not allowed if

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<sup>19</sup> Arizona’s “School Tuition Organizations” play a role similar to Colorado’s proposed CNEAOs.

<sup>20</sup> Most notably, Arizona concurrently created a tax credit for donations to public schools, to support extracurricular activities (A.R.S. § 43

the taxpayer designates the taxpayer's donation to the school tuition organization for the direct benefit of any dependent of the taxpayer." Also, the law prohibits the recipient schools from discriminating "on the basis of race, color, handicap, familial status or national origin." The Colorado proposal includes a stronger version of this first limitation but, as noted earlier, excludes the second. With regard to discrimination, while it is surprising that the proposed law includes no express provision purporting to prohibit recipient nonpublic schools from, e.g., overtly rejecting applications from students of color and students with disabilities, Colorado or federal civil rights laws may nonetheless impose such restrictions upon the CNEAOs as well as upon nonpublic schools once they accept public funding.<sup>21</sup>

By including a stronger version of the first limitation – concerning the earmarking of a donation for the benefit of the taxpayer's dependent – the authors of Colorado's bill have avoided one of the most glaring problems with the Arizona law. Although Arizona bars the earmarking of a donation to one's own dependant, there is no prohibition against designating the schoolmate or neighbor of one's child. And, in fact, according to an article in the *artie wring*

based on the federal constitution's establishment clause, to the constitutionality of school vouchers – one might expect privatization advocates to be actively introducing voucher legislation from coast to coast. Yet, while experts do expect an increase in such legislation and while several vouchers bills were recently introduced in Colorado, many proponents



these two provisions. The program, the court held, did not amount to constitutionally significant aid to a sectarian educational institution.<sup>27</sup> Yet the court's decision identified two factors that likely distinguish this case from k-12 voucher and tax credit situations. The court focused on the Blaine Amendment's intent to avoid any ideological control

money ever enters the state's control as a result of this tax credit. Nothing is deposited in the state treasury or other accounts under the management or

the state to require students who receive CNEAO grants “to be annually tested by a recognized testing firm to measure academic achievement and growth in a manner specified in the agreement.” But this requirement is a bit misleading.

The requirement does not obligate the nonpublic school to participate in Colorado’s CSAP state assessment. CSAP is not generally administered by a recognized testing firm. Moreover, the provision only requires the testing of students receiving a CNEAO grant – not the entire student body. Since the requirement will mo

7. Require recipient private schools to teach to state curriculum standards, administer the CSAP test, and hire only certified teachers. As noted earlier, Americans overwhelmingly favor requiring schools receiving vouchers to meet a variety of requirements, such as following state curriculum standards (88%) and hiring only certified teachers (86%). Given the firm Colorado (and national) policy favoring standards-based accountability, nonpublic schools choosing to benefit from public financial backing should be brought within this system.
8. Remove the eligibility of “educational clinics,” unless they agree to comply with the same state curriculum standards.
9. Require more and better data gathering and reporting, regarding such matters as the family income and residence of recipients and donors, and the prior public school of recipient students, the distribution of CNEAO grants, the admission policies of participating nonpublic schools, the specific “education-related” costs defrayed pursuant to the public-school aspect of the grants, and the rules and procedures CNEAOs use to determine grants. Paragraph (7) of HB 1137 contains an auditing requirement, but the provision fails to require the auditor specifically to include any of this crucial information.

#### Conclusion

As a means of providing equity and improving achievement for impoverished students currently enrolled in the state’s public education systems,

Colorado’s educational tax credit proposal is fundamentally flawed. While possible changes in the legislation may make it more equitable, such amendments cannot rescue the policy from its inherent inability to accomplish the stated goal of its architects: improving education for impoverished students. Only policies that improve all public schools – where the vast majority of those students will continue to be enrolled – can do so.

Even assuming that the plan would yield a better education for participating students, is it proper for the state to accomplish this goal through a policy that requires low-income parents to pay 30-50% of the education’s cost? Why would Colorado want to move poor families from a system that covers the entire cost of their education into one where only about half is covered? In public schools, families are not asked to pay tuition, and students cannot be turned away because they are too poor, too disabled, or of the wrong religion. Before seriously considering this policy option, must the state have already concluded that it cannot realistically provide a quality education, through the free public school system, to all children? Answers to these questions are beyond the scope of this report, but they raise important issues to be considered by any policy maker considering the tuition tax credit legislation.