



## Testimony by Martin Lueken on North Dakota SB 2288

February 9, 2021

My name is Marty Lueken, and I am the director of the Fiscal Research and Education Center at EdChoice. Thank you for inviting me to speak today on the potential fiscal impact of SB 2288.

In general terms, the fiscal impact of an education choice program is the difference between savings accrued from students who use the choice program to switch from a public school to a private school and the total cost of the program.

The cost of the Education Scholarship Tax Credit (ESTC) Program would be capped at \$3 million in scholarship tax credits available to taxpayers who make donations to scholarship granting organizations (SGOs).

A very common argument made by school choice critics is that these programs somehow “siphon” or “drain” resources from public schools. This is not the case under SB 2288 as the cost of the tax-credit scholarship program represents just 0.2% of the total funding for North Dakota’s public school system (\$3.9 billion). Based on the experiences of 24 operation tax-credit scholarship programs nationwide, I estimate that the average cost of tax credit disbursements would be around \$3,300, or just 23% of total spending per student for the public school system.

An important question is: Can we expect this program to have a negative fiscal impact on North Dakota school districts, and will students be harmed? The answer I believe, based on the long history of experiences of current school choice programs, and informed by the substantial body of rigorous research, is “no.”

First, funding of K-12 public schools in North Dakota is not completely based on students – when students leave a district, the district loses most state funds but still retains most federal funds plus about 15-20% of state funds for various grants because these funds are not enrollment-based.

Second, when students leave, it costs less to educate fewer students. Costs go down. Some costs are fixed, and some costs are variable. In the short run, districts have fixed costs such as building maintenance, debt service, and utilities. Variable costs are costs that can be reduced. Variable costs might include textbooks, software licenses, and personnel costs. In the long run, all costs are variable, meaning that over time districts can fully adjust operations to a change in enrollment.

Third, choice programs in states that already have them (including the oldest and largest programs) have not led to an exodus of students, and the public system still remains the dominant provider to this day. Overall, about 2% of K-12 students participate in education choice programs today. I estimate that the program under SB 2288 would provide scholarships for 900 students if the donation cap is met. This is less than 1% of all students enrolled in the state’s public school system.

And research demonstrates that students benefit from these programs, both those who participate and those who remain in public schools. There are 27 studies that examine the effects of education choice programs on the outcomes of students who remain in public schools. Of these, 25 found positive and modest improvements in learning gains by public school students, 1 documented a negative program

effect, and one could not detect any effect. In addition, a recent meta-analysis on the competitive effects of choice programs concluded:

*“In general, competition resulting from school-choice policies does have a small positive effect on student achievement. The lack of an overall negative impact on student outcomes might ease critics’ concerns that competition will hurt those students ‘left behind’ due to school-choice policies.”* (Jabbar et al., 2019, *Education Policy*)

Another study examined the effects of scaling up a choice program in Florida and found that not only did the program increase learning for students who remained in public schools in response to competitive pressure, but it also led to lower absenteeism and lower suspension rates.

These programs not only facilitate better matches between students and the education they receive, but they also result in arrangements that teachers and parents often care about, such as smaller class sizes.

I conducted a fiscal analysis of SB 2288 (appended to the present testimony). The tax-credit scholarship program under this bill could generate net savings for the state. Based on the experiences of states that currently have tax-credit scholarship programs, I estimated that about 900 scholarships would be awarded to students in the program’s first year. Of this group, about 770 students would enroll in the public school system without financial assistance from the program.

When students use a tax-credit scholarship to switch from public schools to private schools, the state experiences savings because it would no longer have to fund that child’s education in the public school system. Thus, these students would offset some or all of the costs of the program, depending on the proportion of scholarships given to this groups of students.

The cost to the state for tax credit disbursements would be completely offset by reduced state expenditures for students no longer in public schools, resulting in an estimated net fiscal benefit of \$1.9 million, or \$2,100 for each ESTC student.

It is possible that the program’s actual experience deviates from some of assumptions employed in the analysis. This is where the break-even switcher rate can provide additional information about the potential fiscal impact of the program. The program has a break-even switcher rate of up to 70%, meaning that if at least 70% of the students in the program switch from public schools to private schools, the program will generate a net savings for the state.

This 70% switcher rate is lower than switcher rates observed in education choice programs in other states. Therefore, if the switcher rate with the program under consideration is in line with switcher rates observed in programs in other states, then the program will save state taxpayers money.

The actual switcher rates of these out-of-state choice programs are observed because they have caps on the number of scholarships, many more students apply for the scholarships than the number available, and the scholarships are awarded by a random lottery. Researchers have collected data on families who apply for, but are not chosen in a random lottery, for a scholarship and recorded whether they enrolled their children in a public or private school after losing the lottery.

Researchers tend to find that around 90% of students who participate in educational choice programs switch from public schools. Therefore, the ESTC Program under SB 2288 will likely generate net fiscal savings for the state.

Thank you again for inviting me to be here today to testify to the data of SB 2288.

**EDCHOICE**  
**FISCAL IMPACT STATEMENT**

**Note Prepared:** February 2020

**Subject:** Education Scholarship Tax Credit

**Impact:** State & Local

**Effective Data:** TBD

**Prepared by:** Martin F. Lueken, Ph.D., Director of Fiscal Research and Education Center

**MEASURE'S PURPOSE:**

If enacted, this bill would create the Education Scholarship Tax Credit (ESTC) Program, a program to expand educational opportunities for North Dakota families of K-12 age children by providing scholarships to attend private school. Taxpayers may receive tax credits, worth 75% of the contribution amount, for contributions made to organizations that provide educational scholarships to eligible students.

To qualify for the program, a student must be a resident of the state who is age 5 or older by September 10 of the year the scholarship is disbursed, and under 19 years of age.

The amount of tax credit disbursements under the ESTC is limited to \$3 million during the first year. This limit may be increased by 10% in future years where the amount of allowable credits are claimed in a given year. Scholarship granting organizations (SGOs) must use at least 90% of contributions they receive for scholarship disbursements. Scholarship amounts cannot exceed 80% of the state's share of the per student payment made to a public school for the applicable year (equal to about \$6,000 on average).

**FISCAL SUMMARY**

**Summary of estimated fiscal impacts of North Dakota Education Scholarship Tax Credit (ESTC) Program**

Total number of students in North Dakota eligible for an ESTC scholarship	120,300
Percent of all North Dakota K-12 students eligible	100%
Total per-student expenditures for North Dakota public K-12 school system	\$14,330
Average cost of ESTC Program (tax credit disbursements for each participating student)	\$3,330
Avg. cost of ESTC Program per student as percentage of total per-student cost for public school system	23%
Number of scholarships funded	900
Est. switcher rate	85%
Est. number of ESTC students likely to have enrolled in public schools without a scholarship	770
Total State Expenditures for ESTC Program	(\$3,000,000)
Total K-12 expenditures for public school system	\$1,624,670,800
ESTC expenditures as % of total K-12 expenditures	0.2%
State Savings from ESTC students likely to enroll in public schools	\$4,926,000
<b>Net State Impact</b>	<b>\$1,930,000</b>
<b>Net State Impact Per Program Participant</b>	<b>\$2,100</b>
<b>Break-Even Switcher Rate for State</b>	<b>44%</b>
Est. Reduction in State Aid Revenue to School Districts for ESTC Students Switching from Public Schools	(\$4,926,000)
Average Variable Educational Cost per Student	\$8,100
Total Cost Burden Relief to School Districts for ESTC Students Switching from Public Schools	\$6,230,000
<b>Net Local School District Savings</b>	<b>\$1,300,000</b>
<b>Net Local School District Savings Per Program Participant</b>	<b>\$1,400</b>

Notes: ( ) denotes a decrease/negative value

Sources: North Dakota Department of Public Instruction; U.S. Census Bureau; National Center for Education Statistics, U.S. Dept. of Education

### **FISCAL EXPLANATION:**

Based on the experiences of other states that have private educational choice programs, an average award amount of \$4,000 would fund 900 scholarships for students.<sup>1</sup> Of this group, 770 students would be “switchers” from public schools.<sup>2</sup>

“Switchers” are students using a scholarship to enroll in a nonpublic school who, in the absence of the educational choice program, would have enrolled in a public school. These students will offset program costs for the state and reduce educational costs for public schools when they leave via the ESTC program. “Non-switchers” are students who, in the absence of the educational choice program, would have enrolled in a nonpublic school setting even without the program. The analysis assumes a non-switcher rate about twice the enrollment rate of K-12 students in nonpublic school settings, which implies that 85% of scholarship students would likely have been enrolled in public schools without the ESTC program in place.

This program, if enacted, is expected to have a positive estimated net fiscal impact of \$1.9 million on the state General Fund and a positive estimated net fiscal impact of \$1.3 million on school districts. There will likely be no impact on local property taxes.

*State impact:* The state’s cost to fund the ESTC Program would be \$3.0 million (0.2% of total K-12 expenditures). This cost would be completely offset by \$4.9 million in reduced state expenditures. After factoring this savings, we estimate a net fiscal benefit to the state of **\$1.9 (or \$2,100 per ESTC student)**.

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

*School district impact:* Local public school districts would experience \$4.9 million in reduced state aid revenue. This reduction would be completely offset by an estimated \$6.3 million in reduced variable costs for students who would have enrolled in district schools without the ESTC program in place.<sup>3</sup> Thus, there will be a net positive local impact of **\$1.3 million, or \$1,400 per ESCT student**.<sup>4</sup>

*Break-even switcher rate:* Switcher is defined as a student who would enroll in a district school if the EEA program is not in place as opposed to enrolling in private school, home school, or other non-public school settings. Switchers represent fiscal savings for the state and district schools. For the program to be fiscally neutral for the state, 44% of ESTC program participants would need to be switchers.

### **KEY ASSUMPTIONS AND CAVEATS**

- The analysis cautiously assumes a switcher rate of 85% (i.e., 85% of ESTC students would likely to enroll in public schools without the ESTC program). This assumption is likely cautious based on empirical research on school choice.<sup>5</sup>
- The analysis assumes that taxpayer contributions will be made to reach the \$3.0 million credit limit.
- It also assumes the average scholarship amount will be \$4,000.<sup>6</sup>
- The analysis assumes that SGOs will use 10% of contributions for administration costs.
- Although most state funding is determined by student enrollment, districts receive some state grants for certain educational areas (e.g., special education and transportation). These grants, which represent about 15% of total state general fund expenditures, are independent of student enrollment.<sup>7</sup> Therefore, districts will retain a portion of the state’s per-pupil funding when students leave, in addition to revenue from the federal government, which is largely based on factors other than student enrollment. These revenues do not change when enrollment changes. Therefore, a district’s per-student funding will increase when students leave for any reason. These fiscal benefits are not reflected in this fiscal note.
- North Dakota also has “hold harmless” provisions designed to protect school districts from significant drops in student enrollment. This funding is benchmarked to funding that districts received in 2012-13,

meaning that districts are guaranteed the same level of funding they received for that school year. Furthermore, because funding is determined by a district's student enrollment in the prior year, the district will have at least one year to adjust its operations to any changes to student enrollment.

**DATA SOURCES:** North Dakota Department of Public Instruction; U.S. Dept. of Education, National Center for Education Statistics; U.S. Census Bureau

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

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<sup>1</sup> Under the proposed program, \$3.0 million in tax credits would generate \$4.0 million in donations to scholarship organizations. If scholarship organizations keep the maximum amount allowed for administrative costs, then they will have \$3.6 million for awarding scholarships.

<sup>2</sup> This analysis assumes that 85 percent of participating scholarship students will be “switchers.” Because scholarship organizations are likely to prefer awarding scholarships to public school students than students already enrolled in private schools, our estimates are likely cautious (Lueken, 2018).  
Lueken, M. F. (2018). The fiscal effects of tax-credit scholarship programs in the United States. *Journal of School Choice*, 12(2), 181-215.

<sup>3</sup> The North Dakota Department of Public Instruction reports all expenditures annually to the U.S. Department of Education. The analysis uses these data to derive estimates for short-run variable costs and considers Instruction, Instruction Support Services, and Student Support Services as short-run variable costs. Based on these data, the analysis estimates that 57% of total costs for public schools are variable in the short run. All other costs are considered fixed in the short run. This rate is then applied to the most recent educational cost data available from North Dakota Department of Public Instruction to estimate average short-run variable costs per student. This approach is more cautious than what other economists employed to estimate short-run variable costs for public schools. For instance, Scafidi used data from the U.S. Department of Education and estimated that the average variable cost rate for ND public schools was 65.6%.

Benjamin Scafidi (2012), *The Fiscal Effects of School Choice Programs on Public School Districts*, Friedman Foundation for Educational Choice, retrieved from EdChoice website: <http://www.edchoice.org/wp-content/uploads/2015/07/The-Fiscal-Effects-of-School-Choice-Programs.pdf>.

North Dakota Department of Public Instruction, Office of School Finance, “2020 Finance Facts,” retrieved from <https://www.nd.gov/dpi/sites/www/files/documents/SFO/Downloadable%20Data%20File/Fnfct20%20hard%20code.d.xlsx>.

<sup>4</sup> To be clear, this \$1.3 million net fiscal benefit represents a \$6.2 million reduction in cumulative short run school variable costs, which outweighs the \$4.9 million cumulative net revenue reduction for 900 students who would enroll in district schools without the ESTC program in place. It is not a direct reduction in school expenditures. The public schools will still have to make decisions to cut costs as enrollment declines. However, they now have \$6.2 million in available cost burden relief from which to find at least \$4.9 million in spending reductions to match their net state revenue reduction.

While strategies for managing costs represent local determinations, numerous resources are available to help financial officials with cost management. The New Hampshire Department of Public Instruction provides strategies

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from some of these resources. For instance, please see pp. 8-10 in: New Hampshire Department of Education (2020). *Long-term Comprehensive Modeling Analysis: New Hampshire Charter School Grant*, February 13, retrieved from <https://www.education.nh.gov/sites/g/files/ehbemt326/files/inline-documents/sonh/long-term-comprehenisve-model-charter-school-grant.pdf>

<sup>5</sup> A body of empirical evidence on private school voucher programs based on random assignment provides information to help infer switcher rates. In these studies, researchers observed the percentage of families who lost a lottery after applying for a choice program and enrolled their children in public schools. Thus, these students would have attended a private school only if they had received a scholarship from a school choice program. Lueken (2020) summarized this body of research from six different school choice programs across the nation. He identified 27 estimates of switcher rates from this research and estimated lower bound and upper bound weighted average switcher rates – estimates that ranged from 84% to 90%.

Lueken, Martin F. (2020). The Fiscal Impact of K-12 Educational Choice: Using Random Assignment Studies of Private School Choice Programs to Infer Student Switcher Rates, *Journal of School Choice*, published online at <https://www.tandfonline.com/doi/abs/10.1080/15582159.2020.1735863>.

<sup>6</sup> This estimate is close to the average scholarship amount of \$3,852 for 24 operational tax-credit scholarship programs nationwide.

“School Choice in America Dashboard,” *EdChoice*, last modified February 4, 2020 <http://www.edchoice.org/school-choice/school-choice-in-america>.

<sup>7</sup> SB 2013 DPI Appropriation Bill, retrieved 1/21/2020 from <https://www.legis.nd.gov/assembly/66-2019/documents/19-0226-04000.pdf>