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Under scholarship tax credit programs such as the one created by LB 364, the state would forgo a large and growing amount of revenue to provide a dollar-for-dollar tax credit to those who make donations to private school scholarship-granting organizations (SGOs), which in turn, provide scholarships to students in private K-12 schools. LB 364 would be one of the most generous programs in the nation and creates much greater tax benefits for donations to SGOs, as compared to all other nonprofits.

Scholarship tax credits much more lucrative than other types of donations

Tax credits enhance the tax benefit of donating to SGOs, as opposed to tax deductions for other types of charitable donations. For example, under LB 364, an individual, couple, or business can receive a credit equal to 100 percent of their total contributions or 50 percent of their income tax liability, whichever amount is smaller. There are, however, no limits on donation amounts. This means that as long as there are enough credits available, a corporation with an income tax liability of $1 million could donate to a private scholarship granting organization of $500,000 and receive a $500,000 tax credit. Or, if a couple has income tax liability of at least $20,000, and they donate $10,000 to a private scholarship granting organization, they receive a state tax benefit of $10,000.

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

LB 364 would create one of the most generous programs of its kind

While 18 states currently have scholarship tax credit programs, only 11 of them offer credits to individual taxpayers in the manner that LB 364 does. Ten of these states either offer credits at a lower percent of the contribution[1] or have a stricter limitation on the maximum credit that a taxpayer can receive in any given year.[2] Only in one other state – Louisiana – could the couple in the previous example receive a $10,000 tax benefit for their donation.

LB 364's cost could balloon each year

The cost of the tax break is capped at $10 million in the first year, and if 90 percent of the credit is used, the cap will grow by 25 percent the following year. Assuming

[1] Indiana and Oklahoma offer a tax credit equal to 50% of the contribution. Iowa, South Carolina, and Virginia offer a tax credit equal to 65% of the contribution. Illinois offers a tax credit equal to 75% of the contribution.

[2] Montana caps credits at $150 per taxpayer. Arizona caps credits at $500 for individual taxpayers and $1,000 for joint filers. Georgia caps credits at $1,000 for single filers and $2,500 for joint filers. Alabama caps credits at the lesser of 50% of taxable income and $7,500.

Nebraska's credit grows by 25 percent each year, the credit would reduce state revenues by more than $90 million annually by 2032.

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

Creating a scholarship tax credit now would come at a time when our state's school funding needs are increasing and when state funding of K-12 education has been constrained.[3] This low level of state support leads to a heavy reliance on property taxes to fund schools. Diverting more state resources for scholarship tax credits will make it harder to address state public education needs and increasingly shift the cost of funding K-12 onto property taxpayers.

Scholarship tax credits not likely to create savings for the state

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

Bill creates yet another tax credit with no evaluation mechanisms

Like many other state tax credits, LB 364 contains no data collection requirements, so policymakers won't have any information to review whether the measure is achieving the stated goals of improving education or providing savings to the state. This means that, over time, the bill could become a significant drain on revenue that may or may not offer Nebraska a good return on investment.

Conclusion

Scholarship tax credits like the one proposed in LB 364 stand to divert state revenue at a time when we are navigating the economic effects of COVID-19 and have recently committed to more than $4.6 billion in new spending over the next 11 years.[4] Enacting this measure could force lawmakers to make cuts to vital services such as public K-12 education or shift more of the load of funding our schools on to property taxpayers. In light of these factors, we have serious concerns about creating a new tax credit.

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[3] LB 380 (2021) reduces TEEOSA funding by roughly $19 million, or 1.8%, from FY21 to FY22.
[4] Nebraska Legislature, "LB 1107 Fiscal Note," accessed at https://nebraskalegislature.gov/FloorDocs/106/PDF/FN/LB1107_20200811-160649.pdf on Jan. 25, 2021.