



How Public Education Benefits from the Federal Income Tax Deduction for State and Local Taxes and Other Special Tax Provisions

A Background Paper from the Center on Education Policy

Introduction

Discussions about the federal role in education usually focus on the array of federal programs that provide direct funding to educational entities or students. Many citizens do not realize, however, that the U.S. educational system also benefits from a more indirect type of federal support, in the form of special provisions in the tax code that affect the income taxes paid by individuals. These special provisions (which economists refer to as “tax expenditures”) include tax deductions or exclusions that withdraw a portion of personal income from taxation, and tax credits that reduce the actual tax paid by individuals. For example, taxpayers who meet certain criteria may deduct charitable contributions to qualifying educational institutions from their taxable income or may receive a tax credit for college tuition expenses.

For public K-12 education, the individual income tax provision that yields the greatest financial benefit for schools is the federal tax deduction for state and local taxes—the main focus of this paper. Specifically, individuals who itemize deductions on their federal tax returns, rather than taking the standard deduction, may deduct from their taxable income some or all of the amounts they paid for state and local taxes on real estate property, income, personal property (mostly vehicles), and sales (in some states that do not levy income taxes).

The deduction for state and local taxes, as well as the other education-related tax provisions mentioned in this paper, reduces the amount of tax revenues the federal government would otherwise have collected. At the same time, these provisions offer an incentive, in the form of lower federal taxes, for individuals to engage in activities that benefit education and the larger society. For example, taxpayers may be more inclined to save for their children’s college education, continue their own education, or pay state and local taxes for education and other public services if they know these

investments or payments will be offset to some extent by a federal tax break. The willingness of individuals to accept state and local taxation has an enormous impact on public education because the vast majority of revenues for public schools come from local property taxes and other state and local taxes. In this way, state and local tax deductibility and other special tax provisions indirectly subsidize education just as significantly as direct federal program grants.

These special tax provisions are particularly relevant at a time when both taxing and spending policies have come under Congressional scrutiny, and many members of Congress are interested in tax reform. It is important that policymakers and others understand the role of special tax provisions in supporting the nation's educational system so they can make informed decisions about tax policy changes.

This background paper from the Center on Education Policy (CEP) is intended to serve as a companion to the CEP report, *Get the Federal Government Out of Education? That Wasn't the Founding Fathers' Vision* (CEP, 2011). That report discusses the historical foundations and current purposes of the federal role in education. This paper goes into more detail about an issue mentioned briefly in the other report – the financial benefits that education incurs from special federal tax provisions for *individual* taxpayers, particularly the deduction for state and local taxes. Although federal *corporate* tax provisions also affect education, they are beyond the scope of this paper.

Below is a summary of key findings from the analyses done for this paper. Following the key findings is a broad overview of all the special tax provisions for individuals that benefit any level of education and the estimated amount of benefits from each provision. The subsequent sections, which comprise the bulk of the paper, analyze the impact of state and local tax deductibility on public K-12 education.

Key Findings

- ***Special tax provisions indirectly subsidize all levels of education.*** Education receives indirect subsidies from a variety of special tax deductions, exclusions, and credits for individual taxpayers in the federal tax code. Together, these special tax provisions bring benefits to education that total roughly \$42.4 billion to \$47.8 billion, according to our own calculations based on estimates from the Congressional Joint Tax Committee (JTC) and the Office of Management and Budget (OMB). While most of these special provisions target higher education, the greatest financial benefits to education come from the provision that allows taxpayers who itemize their federal deductions to deduct payments made for

state and local taxes. This state and local tax deduction primarily benefits public K-12 education.

- *Public K-12 education receives benefits worth billions of dollars through the deductibility of state and local taxes.* The subsidy to K-12 education from this deduction amounted to roughly \$16.5 billion to \$17.1 billion in 2009, according to our estimates based on data from the JTC, OMB, and other federal sources.
- *The federal deduction for state and local taxes has a greater impact in some states than in others.* The impact of this deduction is greatest in states and regions with both a high percentage of taxpayers taking the deduction *and* a high average amount deducted. This group tends to include states with relatively high incomes and high taxes. At the other end of the spectrum, this deduction has a lesser impact in states and regions with a low percentage of taxpayers taking the deduction *and* a low average amount deducted. This latter group tends to include states with relatively low incomes and low taxes.
- *The federal deduction for state and local taxes appears to maximize the ability of states and localities to raise revenues for public K-12 education.* States that benefit to a greater than average extent from this deduction also tend to raise more state and local revenues than average for public K-12 education, with some exceptions. Conversely, states that benefit to a lower than average extent from this deduction tend to raise lower levels of state and local revenues for public K-12 education, with some exceptions.

Overview of Special Tax Provisions That Benefit Education

Table 1 lists all of the individual tax deductions, exclusions, and credits that benefit any level of education, as well as the estimated indirect subsidy to education from each of these provisions. These provisions are categorized by educational level—K-12, postsecondary, or preschool education, or all levels of education. With one exception, the estimates in the table come from the congressional Joint Tax Committee (2010) and the Office of Management and Budget (2010), two federal sources that annually publish estimates of all federal tax expenditures. (In this context, a “tax expenditure” is essentially the amount of tax revenues lost to the federal government or, conversely, the amount of benefit gained by individual taxpayers and/or by various economic activities, such as education.) The exception is the estimate of the value of the state and local tax deduction, which CEP developed using a process described in the next section. All of the estimates in table 1 are for federal income taxes paid by individuals for calendar

year 2009. The JTC and OMB also provide estimates for future years, but these are not included in the table because they are more speculative.

Table 1. Estimated value of education-related special tax provisions for 2009, in billions of dollars

Note: Within each educational level, tax provisions are ordered from highest value to lowest based on JTC estimates.

Type of tax expenditure and level of education affected	Joint Tax Committee estimate	Office of Management and Budget estimate
<i>K-12 education</i>		
Deduction of non-business state and local taxes on real estate property, ^A income, sales, and personal property	\$16.5*	\$17.1*
Exclusion of interest on state and local government bonds for educational facilities	\$2.2	\$1.4
Deduction for teacher classroom expenses	\$0.2	\$0.2
<i>Postsecondary education</i>		
Hope credit for tuition for postsecondary education (including the American Opportunity credit under the American Recovery and Reinvestment Act)	\$6.7	\$5.4
Lifetime Learning credit for tuition for postsecondary education	\$1.9	\$3.9
Exclusion of scholarship and fellowship income	\$1.8	\$2.1
Parental personal exemption for students aged 19-23	\$1.2	\$4.4
Deduction of interest on student loans	\$0.8	\$1.3
Deduction of certain higher education expenses	\$0.7	\$1.8
Exclusion of interest on state and local government qualified private activity bonds for student loans	\$0.4	\$0.4
Exclusion of tax on earnings of qualified college savings programs	\$0.3	\$1.2
Exclusion of tax on earnings of qualified pre-paid tuition programs	< \$0.05	
Exclusion of employer-provided educational assistance benefits	\$0.2	\$0.7
Exclusion of income attributable to the discharge of certain student loan debt and National Health Service Corps educational loan repayments	\$0.1	< \$0.05
Exclusion of interest on education savings bonds	< \$0.05	< \$0.05
<i>Preschool education (primarily)</i>		
Child and dependent care credit	\$4.3	\$4.3
<i>All levels of education</i>		
Deduction for charitable contributions to educational institutions	\$5.0	\$3.6
Exclusion of interest on Coverdell education savings accounts/Education IRAs	\$0.1	< \$0.05
Total value of all special tax provisions for education	\$42.4 billion	\$47.8 billion

Table reads: Public K-12 education benefits from the provision in the federal tax code that allows certain taxpayers to deduct state and local taxes on real estate property, income, sales, and personal property. According to CEP estimates, this deduction provided an indirect subsidy to public K-12 education in 2009 worth roughly \$16.5 billion using baseline data from the Joint Tax Committee or \$17.1 billion using baseline data from the Office of Management and Budget.

*CEP estimated the value of the state and local tax deduction to public K-12 education by using baseline estimates of the total value of this deduction to *all* state and local government services developed by the JTC (\$71.8 billion) and OMB (\$74.3 billion).

^AIncludes real estate property taxes paid by individuals on owner-occupied homes (OMB) or real property (JTC).

Sources: U.S. Congress, Joint Tax Committee, 2010; U.S. Office of Management and Budget, 2010; and Center on Education Policy calculations.

Of all the provisions in table 1, K-12 public education derives the greatest financial benefit from the deduction for state and local taxes. We estimate that in 2009 this deduction provided benefits to public K-12 education worth approximately \$16.5 billion to \$17.1 billion, depending on whether JTC or OMB baseline data are used.

Public K-12 education also benefits to a much lesser extent from tax provisions that exclude from taxation the interest paid on state and local government bonds for educational facilities, and a tax benefit that allows teachers to deduct certain classroom expenses from their taxable income.

As table 1 illustrates, the majority of the special tax provisions that benefit education are directed specifically to postsecondary education. This reflects a trend over the last two decades of supplementing federal grants and loans for college students with various special tax provisions. Among the provisions that bring the greatest financial benefits to postsecondary education are the Hope tax credit for postsecondary tuition, with an estimated value of \$5.4 billion to \$6.7 billion in 2009, depending on whether the OMB or JTC estimate is used; and the Lifetime Learning tax credit, with an estimated value of \$1.9 billion to \$3.9 billion. Other provisions that provide significant indirect subsidies to higher education allow individuals to exclude scholarship and fellowship income from federal taxation or take a personal exemption for dependent students aged 19-23.

Preschool education benefits from the child and dependent care tax credit shown in table 1. This credit subsidizes the costs of child care for children under age 13, as well the cost of public or private preschool education for children below the kindergarten level.

Two of the special tax provisions in table 1 affect all levels of education—the individual tax deduction for charitable contributions by individuals to educational institutions, and the exclusion from taxation of interest on Coverdell education savings accounts. The JTC and OMB provide estimates of the portion of the charitable contribution deduction that is attributable to education but do not further break out the estimated shares for postsecondary or K-12 education. Other data suggest that a large share of these contributions go to postsecondary institutions rather than K-12 education.¹ The

¹According to Giving USA (2010), total charitable contributions for education purposes in 2009 totaled about \$40 billion. Giving USA did not disaggregate this estimate by education level or sector. However, the Council for Aid to Education (2010) estimates that charitable contributions in 2009 to higher education institutions totaled \$27.9 billion, or about 70% of the total education contributions estimated by Giving USA.

Coverdell education savings program, which gives parents an incentive to save for their children's educational expenses, also benefits education at all levels, although the indirect subsidies from this program are relatively low.

Estimated Benefit to K-12 Education from State and Local Tax Deductibility

Using data from various federal sources, CEP developed the estimates in table 1 of the benefits derived by public K-12 education from the state and local tax deduction. This was necessary because the JTC and OMB simply report total estimates of the amount derived from this deduction for *all* state and local government services and do not break out the specific portion attributable to education. For 2009, the total value of this deduction was estimated at \$71.8 billion by the JTC and \$74.3 billion by OMB (JTC, 2010; OMB, 2010).

To approximate the portion of these estimates attributable to K-12 public education, we first divided:

- the current expenditures² of state and local governments for *public K-12 education* in school year 2007-08, totaling about \$465.3 billion³ (U.S. Department of Education, 2010)
- by
- the current expenditures of state and local governments for *all purposes*, totaling approximately \$2,015.2 billion in calendar year 2008 (U.S. Bureau of Economic Analysis, 2009).

Although school year 2007-08 covers a slightly different time period than calendar year 2008, these figures were sufficient to enable us to determine that roughly 23% of the current expenditures of state and local governments go toward public K-12 education. We then applied this 23% figure to the above-mentioned JTC and OMB estimates of the total value of the state and local tax deduction. Through this process, we estimated that in 2009 this deduction provided indirect subsidies to public K-12 education of about \$16.5 billion using JTC baseline data or about \$17.1 billion using OMB data.

The federal deduction for state and local taxes has both price and income implications for taxpayers who itemize deductions. This deduction in effect reduces the price of state

²Current expenditures do not include expenditures for construction and related costs.

³This figure was calculated by applying the state and local government share (91.8%) of total public K-12 education revenues to the total current expenditures by public K-12 education systems.

and local government services for itemizing taxpayers by a percentage equivalent to their marginal federal income tax rate, or tax bracket. In other words, if a taxpayer's income reaches the 28% tax bracket, the availability of the state and local tax deduction reduces the price of state or local taxes by up to 28%. In addition, taxpayers who qualify for this deduction end up with more net income than they would if the deduction were not allowed. With higher net income, they may be willing and able to spend more for state and local government services, as well as any other goods and services, than they otherwise would. Thus, both the price and income effects of this deduction encourage increased spending on all types of state and local government services, including public K-12 education.

If the individual income tax deduction for state and local taxes were to be reduced or eliminated, state and local government expenditures for public K-12 education would likely decrease over time. Taxpayers who itemize would perceive an increase in the net "cost" of their state and local tax payments because a portion of these payments would no longer be offset by the federal deduction. The result might well be increased resistance to state and local taxation among some taxpayers, although this resistance might be focused primarily on proposed *increases* in the amount and rate of state and local taxes.

Differences among States in the Impact of State and Local Tax Deductibility

The impact of the federal deduction for state and local taxes differs among states. This is because the percentage of federal income taxpayers who itemize their deductions varies significantly among the states, as does the average amount deducted based on state and local tax payments. **Table 2** includes data from the Tax Policy Center of the Urban Institute and Brookings Institution (2010) on the percentage of returns claiming this deduction and the amounts claimed. Nationwide, an average of 33.0% of all individual federal income tax returns included an itemized deduction for state and local taxes in 2007. Within specific states, however, this percentage ranged from 16.4% in West Virginia to 47.6% in Maryland. In other words, almost three times as many taxpayers in Maryland as in West Virginia took advantage of this deduction. Since individuals with higher incomes are more likely to itemize their deductions, the percentage of taxpayers taking the deduction for state and local taxes is greatest in states with high average incomes, such as Maryland, New Jersey, and Connecticut, and lower in states with low average incomes, such as West Virginia, Mississippi, and Louisiana.

The average amount claimed by taxpayers who took advantage of this deduction also varied, ranging from \$3,933 in Alaska and \$4,385 in Tennessee, to \$16,322 in New Jersey

and \$16,685 in New York. States with the highest average amounts deducted tended to be in the Northeast, Mid-Atlantic, or Pacific Coast regions, while those with the lowest average amount deducted tended to be in the South or Rocky Mountain regions.

The final column of table 2 includes a “tax deduction impact index” developed by CEP. Using baseline data from the Tax Policy Center (2010), we calculated these figures by multiplying each state’s percentage of taxpayers taking the deduction by its average amount deducted, then comparing the result to the national average (set a 1.00).

Table 2. State and local tax deduction by state for tax year 2007

State	% of returns in state claiming deduction	Amount of deduction (in billions of dollars)	Average amount claimed (in dollars)	Tax deduction impact index
<i>U. S. total</i>	33.0%	<i>\$494.1 billion</i>	\$9,686	1.00
Alabama	27.7%	\$3.2	\$4,984	.43
Alaska	25.3%	\$0.4	\$3,933	.31
Arizona	36.7%	\$7.1	\$6,670	.77
Arkansas	22.6%	\$2.2	\$6,849	.48
California	36.9%	\$86.5	\$13,333	1.54
Colorado	39.7%	\$7.9	\$8,089	1.01
Connecticut	42.4%	\$11.8	\$14,918	1.98
Delaware	35.6%	\$1.2	\$7,236	.81
District of Columbia	39.6%	\$1.7	\$13,791	1.71
Florida	30.6%	\$18.6	\$6,265	.60
Georgia	36.9%	\$13.1	\$7,765	.90
Hawaii	32.2%	\$1.6	\$7,150	.72
Idaho	33.5%	\$1.7	\$7,052	.74
Illinois	34.4%	\$21.9	\$9,701	1.05
Indiana	29.0%	\$6.4	\$6,783	.62
Iowa	30.0%	\$3.3	\$7,188	.67
Kansas	30.1%	\$3.6	\$8,608	.81
Kentucky	27.6%	\$4.4	\$7,370	.64
Louisiana	21.7%	\$2.5	\$5,436	.37
Maine	28.9%	\$1.9	\$9,014	.82
Maryland	47.6%	\$16.1	\$11,509	1.71
Massachusetts	38.9%	\$15.8	\$11,779	1.43
Michigan	34.4%	\$13.1	\$7,612	.82
Minnesota	39.7%	\$9.8	\$9,043	1.13
Mississippi	22.1%	\$1.7	\$5,418	.37
Missouri	30.0%	\$7.2	\$7,960	.75
Montana	29.6%	\$1.0	\$6,889	.64
Nebraska	29.6%	\$2.3	\$8,585	.80
Nevada	35.3%	\$2.8	\$5,972	.66
New Hampshire	34.8%	\$2.0	\$7,766	.85
New Jersey	42.8%	\$32.0	\$16,322	2.19
New Mexico	25.4%	\$1.4	\$5,676	.45

State	% of returns in state claiming deduction	Amount of deduction (in billions of dollars)	Average amount claimed (in dollars)	Tax deduction impact index
New York	35.5%	\$58.8	\$16,685	1.86
North Carolina	33.8%	\$13.3	\$8,587	.91
North Dakota	19.3%	\$0.4	\$6,357	.38
Ohio	31.6%	\$16.4	\$8,481	.84
Oklahoma	27.1%	\$3.1	\$6,433	.55
Oregon	38.1%	\$8.1	\$11,180	1.33
Pennsylvania	30.0%	\$18.2	\$9,069	.85
Rhode Island	35.0%	\$2.0	\$10,193	1.12
South Carolina	29.9%	\$4.8	\$7,169	.67
South Dakota	19.1%	\$0.4	\$4,492	.27
Tennessee	23.7%	\$3.3	\$4,385	.33
Texas	24.1%	\$17.9	\$6,577	.50
Utah	39.5%	\$3.3	\$6,955	.86
Vermont	29.7%	\$1.0	\$9,336	.87
Virginia	39.1%	\$14.5	\$9,218	1.13
Washington	35.2%	\$8.3	\$7,028	.77
West Virginia	16.4%	\$1.1	\$6,992	.36
Wisconsin	36.3%	\$10.1	\$9,378	1.07
Wyoming	23.8%	\$0.3	\$4,997	.37

Table reads: In Alabama, 27.7% of the individual income tax returns filed for 2007 claimed the deduction for state and local taxes; the total claimed statewide for this deduction was \$3.2 billion. The amount of this deduction claimed averaged \$4,984 per tax return in Alabama. On the tax deduction impact index developed by CEP, Alabama has an index number of 0.43, well below the national average of 1.00.

Sources: Tax Policy Center (2010); and Center on Education Policy calculations.

The impact of the deduction for state and local taxes is greatest in states and regions with both a high percentage of taxpayers taking the deduction *and* a high average amount deducted. These states, which have an index figure in table 2 that is substantially above 1.00, include California, Connecticut, Maryland, New Jersey, and New York, plus the District of Columbia. At the other end of the spectrum, the impact of this deduction is the least in states and regions with a low percentage of taxpayers taking the deduction *and* a low average amount deducted. These states, which have an index number substantially below 1.00, include Alabama, Alaska, Arkansas, Louisiana, Mississippi, New Mexico, North Dakota, South Dakota, Tennessee, West Virginia, and Wyoming. Again, we see a general pattern of contrast between relatively high-income and high-tax states in the Northeast, Mid-Atlantic, and Pacific Coast areas, and relatively low-income and low-tax states in the South and Rocky Mountain regions.

Other research suggests that in some states, public K-12 education may benefit more from the indirect subsidy provided through the deductibility of state and local taxes than it does from direct federal grant aid. A study published in the *Economics of Education Review* attempted to measure the value of this indirect subsidy and to

compare it with direct grant aid (Loeb & Socias, 2004). The study estimated that in 31 states, the value of the indirect aid to K-12 education associated with the state and local tax deduction was greater than the value of direct grant aid. This was especially the case in relatively high-income states, such as Connecticut, Massachusetts, New Jersey, and New York. Conversely, the direct aid was greater than the indirect aid from taxes in low-income states, such as Alabama and Mississippi, and in states like Alaska that benefitted from federal minimum grant provisions for small-population states and other special aid provisions.

At the school district level, Loeb and Socias found that indirect subsidies provided through state and local tax deductibility favored districts with higher average income levels. Thus, the deductibility provisions contributed to funding disparities between districts in the same state, both by providing greater indirect aid to districts with higher average income levels and by increasing the willingness of taxpayers in these districts to pay state and local taxes.

State and Local Tax Deductibility and State Revenues for Public Education

We also sought to determine whether there was a relationship between the significance of the benefits a state receives through the state and local tax deduction, and the amount of state and local revenues raised within a state to support public education. As an indicator of the significance of the deductibility provisions in each state, we used the tax deduction impact index discussed above in connection with table 2. As an indicator of revenues, we developed a state and local K-12 per capita revenue index. This was determined by dividing:

- the amount of revenues from state and local sources for public K-12 education in school year 2007-08 for each state (U.S. Department of Education, 2010)
by
- the estimated state total population as of July 1, 2008 (U.S. Census Bureau, 2009).

The resulting number for each state was then compared with the national average (set at 1.00). A state with a revenue index greater than 1.00 is raising more revenues per person for public K-12 education than the national average, while a state with a lower index is raising fewer revenues than the national average.

Table 3 shows both the tax deduction index and the state and local revenue per capita index for each state, ranked from highest to lowest according to the revenue index.

Table 3. Comparison of tax deduction impact index with state and local revenue per capita index

Note: States are ordered from highest to lowest according to the state and local revenue per capita index.

State	Tax deduction impact index	State and local K-12 revenue per capita index
<i>U. S. total</i>	1.00	1.00
Alaska	.31	1.63
Wyoming	.37	1.59
New Jersey	2.19	1.56
Connecticut	1.98	1.46
New York	1.86	1.44
Vermont	.87	1.29
Maryland	1.71	1.24
Massachusetts	1.43	1.20
District of Columbia	1.71	1.16
Rhode Island	1.12	1.10
New Hampshire	.85	1.06
Minnesota	1.13	1.05
Pennsylvania	.85	1.05
Ohio	.84	1.04
Illinois	1.05	1.03
Kansas	.81	1.03
Maine	.82	1.02
Michigan	.82	1.02
Delaware	.81	1.01
Indiana	.62	1.01
California	1.54	1.00
Georgia	.90	1.00
Virginia	1.13	.99
Wisconsin	1.07	.99
Hawaii	.72	.98
Texas	.50	.96
Nebraska	.80	.95
Iowa	.67	.93
New Mexico	.45	.90
South Carolina	.67	.89
Nevada	.66	.88
Washington	.77	.88
West Virginia	.36	.88
Colorado	1.01	.87
Missouri	.75	.86
Alabama	.43	.84
Utah	.86	.84
Louisiana	.37	.83
Oregon	1.33	.83
Arkansas	.48	.82
Florida	.60	.82
Arizona	.77	.80

State	Tax deduction impact index	State and local K-12 revenue per capita index
Montana	.64	.80
North Dakota	.38	.80
Kentucky	.64	.77
Oklahoma	.55	.75
Idaho	.74	.73
South Dakota	.27	.72
Mississippi	.37	.71
North Carolina	.91	.69
Tennessee	.33	.67

Table reads: On the tax deduction impact index developed by CEP, Alaska had an index number of .31, below the national average of 1.00. This indicates that the state has a low percentage of taxpayers taking the deduction for state and local taxes and a low average amount deducted for this purpose. On the state and local K-12 revenue per capita index, Alaska had an index number of 1.63, above the national average, which indicates a high level of state and local revenues raised per person for public K-12 education.

Sources: Center on Education Policy calculations, based on data from the Tax Policy Center (2010); the U.S. Department of Education (2010); and the U.S. Bureau of the Census (2009).

As table 3 shows, states with a tax deduction impact index above 1.00—in other words, those that benefit more than average from this deduction—also tend to have a state and local revenue per capita index above 1.00, meaning that they are raising more revenues than average for public K-12 education. At the same time, most states with figures below 1.00 on one of these indices also tend to be below 1.00 on the other. In general, it appears that the states where taxpayers make the most use of the state and local tax deduction are best able to raise revenues for public K-12 education.

There are exceptions to this general pattern, however. States tend to fall into four groups:

- **States where both indices are substantially above 1.00.** These include several states with relatively high incomes, high percentages of taxpayers who itemize and/or high average amounts deducted by itemizers, and high levels of revenues for public K-12 education. This group includes New Jersey, Connecticut, New York, Maryland, Massachusetts, and the District of Columbia.
- **States where both indices are substantially below 1.00.** These include several states with relatively low incomes, low percentages of taxpayers who itemize and/or low average amounts deducted by itemizers, and low levels of revenues for public K-12 education. This group includes Tennessee, Mississippi, South Dakota, Idaho, Oklahoma, Kentucky, North Dakota, Montana, Arizona, Florida, Arkansas, Louisiana, and Alabama.

- *A small group of states with a relatively high tax deduction impact index but an average or below-average revenue per capita index.* These states benefit substantially from the tax deduction yet their revenues per capita for public K-12 education are not high. This group includes California and Oregon.
- *States with a relatively low tax deduction impact index but a higher than average revenue per capita index.* These states benefit to a somewhat lesser extent from the tax deduction but are raising greater than average level of revenues per capita for public K-12 education. This group includes Alaska, Wyoming, Vermont, New Hampshire, Pennsylvania, Ohio, Kansas, Maine, Michigan, Delaware, and Indiana.

Conclusion

As this paper has shown, a host of special federal deductions, exclusions, and credits for individual taxpayers have an important impact on funding for education. The indirect subsidies to education derived from all of the relevant special tax provisions amounted to roughly \$42 billion or more in 2009.

For public K-12 education, the most significant of these tax provisions is the deduction for state and local taxes. This deduction provided an estimated \$16 billion or more in indirect subsidies to public K-12 education in 2009. Data presented in this paper also suggest that the states in which taxpayers make the most use of the state and local tax deduction are able to raise the highest levels of state and local revenues for education. At the same time, the impact of this deduction varies by state and is generally greater in states with higher incomes and higher taxes.

The deduction for state and local taxes and the other education-related special tax provisions are particularly relevant as Congress looks closely at taxing and spending policies. State and local governments have depended on federal deductibility for many decades to bolster their ability to raise revenues. If this policy were changed or terminated, state and local governments could suddenly find it much harder to raise revenues for public education. This is a particular concern in the current economic climate because state and local governments have been hit especially hard. Over time, a change in special tax provisions, particularly the deduction for state and local taxes, could end up eroding funding for public education as much as a direct cut in federal, state, or local budgets.

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