Options for Funding Education in Arkansas After the Lake View Case Decision

**Wednesday, July 16, 2003**
**11:30 A.M.**

**Old Supreme Court Room**
**State Capitol Building**
**Little Rock, Arkansas**

1) **Introductory Remarks:**
   - Sybil J. Hampton, Ed.D., President
     Winthrop Rockefeller Foundation
   - Senator Jim Argue
     Chair, Senate Committee on Education
   - Representative Calvin Johnson
     Chair, House Committee on Education

2) **Overview of Report:**
   - Matt Gardner, Senior Policy Analyst
     Institution on Taxation and Economic Policy (ITEP)

3) **Q&A Session:**
   - Matt Gardner

4) **Closing Remarks:**
   - Sybil J. Hampton, Ed.D.
MATTHEW GARDNER


Mr. Gardner has degrees from the University of Maryland and the University of Rochester. He resides in Washington, D.C., and originally hails from Raleigh, North Carolina.
Options for Funding Education in Arkansas  
After the Lake View Decision

Arkansas is at a crossroads. In November of 2002, the Arkansas Supreme Court ruled that the state’s system of public elementary and secondary schools was both inequitable and inadequate. The Lake View decision signals conclusively that Arkansas policymakers must enact unprecedented increases in state spending on elementary and secondary education in order to repair the constitutional violations found by the court.

However, the state’s current tax system is likely to be insufficient to support the sea change in public spending that will be necessary to comply with the Lake View decision’s requirements – raising several vital questions:

- What policy changes will be required in order to provide a constitutionally acceptable level of school funding?
- What will be the implications for tax equity and tax adequacy of the substantial tax reforms that Arkansans may implement in coming years?
- Perhaps most important for the state’s long term vitality, how will these changes in tax and spending policy affect the state’s economy?

The Winthrop Rockefeller Foundation has a long history of research on state and local taxes and a particular interest in the effects of tax systems on funding for public schools as well as the differential impact on citizens of the state. This report, Tax Options for Arkansas: Funding Education After the Lake View Case, is intended to provide policy makers and the public with an understanding of funding alternatives. The Foundation selected three research groups with extensive experience in Arkansas tax analysis to prepare the study: the Institute on Taxation and Economic Policy, Washington, D.C.; HISTECO Associates, Inc., Little Rock; and Arkansas Advocates for Children & Families.
Options for Funding Education in Arkansas - continued
After the Lake View Decision

The report includes an in-depth look at the Lake View state supreme court decision, which set out a vision of the sort of education system Arkansas’s constitution requires.

The report takes a hard look at the virtues and shortcomings of each of the state’s major taxes and assesses the Arkansas tax system as it affects taxpayers at different income levels. It also addresses the implications of various emerging tax policy issues confronting state legislatures across the country, ranging from Internet-based sales tax transactions to the decline of the corporate income tax – with an eye toward developing strategies for increasing the yield of the Arkansas tax system at a time when raising revenue is a priority.

The report builds on this survey by offering a menu of options for tax reform, focusing primarily on revenue raising alternatives but including options for low-income tax relief as well. These options include rate increases as well as base-broadening strategies designed to eliminate costly loopholes. The study provides distributional estimates for each tax option, along with an estimate of the impact on state revenues. Where relevant, the offsetting impact of these options on federal tax revenues are projected as well – an important consideration in assessing the impact of tax changes on Arkansans.

WINTHROP ROCKEFELLER FOUNDATION BACKGROUND INFORMATION

In 1974 the Trustees of Governor Winthrop Rockefeller’s Estate endowed the Winthrop Rockefeller Foundation to continue the work of The Rockwin Fund. Governor Rockefeller setup The Rockwin Fund in 1954 and, on an annual basis from 1956 until his death in 1973, funded projects and programs he believed were important to improving the quality of life in Arkansas.

The Winthrop Rockefeller Foundation is a private, nonprofit foundation whose mission is to improve the lives of Arkansans by funding programs and projects that improve education; economic development; and economic, racial and social justice. During the past 28 years the Foundation has awarded over $62 million in grants.

Additional information about the Winthrop Rockefeller Foundation can be found on its website, www.wrfoundation.org.
Options for Funding Education in Arkansas
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Q & A's

1. How does the study measure the impact of achieving adequacy on the Arkansas economy?

ITEP used a computer-based general equilibrium model to estimate the impact of these changes on the Arkansas economy. This model, constructed for ITEP by Regional Economic Models, Inc., can be used to estimate the dynamic effects of changes in tax and spending policy. ITEP used the model to forecast the change in personal income, Gross State Product, and employment that would result in Arkansas from a package of spending and revenue increases designed to achieve educational adequacy in compliance with Lake View.

2. Arkansas is hardly the first state to go through a judicially mandated school funding crisis. What lessons can Arkansas learn from the dozens of other states that have attempted education finance reform?

The most important lesson to be learned from the experience of other states is that raising sufficient revenues is a real challenge, and one that some states have not met despite judicial mandates. There are no guarantees that this effort will be successful. An equally important lesson is that the manner in which revenues are raised has important implications for tax equity and for the long-term fiscal health of the state. As Chapter Two of the study shows, Kentucky and Michigan have each enacted revenue-raising tax reform to help fund education equitably—Kentucky enacted a combination of tax increases and credits, including a one-cent sales tax increase, a one percent increase in the corporate income tax. Reforms to Kentucky’s income tax included a low-income tax credit to ensure that the increased state tax burden would not fall primarily on low-income taxpayers. Michigan chose to increase its reliance on slow-growth, regressive cigarette and sales taxes as part of its revenue-raising solution.

3. Couldn’t Arkansas achieve educational adequacy without enacting tax hikes at all, simply by enacting “across the board” budget cuts in other areas, or by consolidating schools?

These non-tax strategies could certainly help on the margin. But studies of school consolidation tend to agree that the most revenue the state could realize from consolidating schools would be around $40 million—far less than the revenues required to ensure an adequate and equitable education system in Arkansas. And while cuts in other budget areas are certainly possible, it’s important to recognize that enormous across-the-board cuts would be required in order to avoid tax hikes entirely. Chapter Three of the Report shows that meeting the Lake View mandate solely through funding cuts would seriously reduce other state funded programs and possibly reduce the amount of federal dollars received by the state through matching programs such as the 3:1 Medicaid match.
4. **What types of revenue-raising options are modeled? Is the ITEP Microsimulation Tax Model’s result sensitive to the choice of tax changes used?**

The results presented in Chapter Eleven of the study are based on a package of tax increases designed to raise state revenues by $839 million—the annual estimated cost of educational adequacy—in 2009. The revenues raised in 2009 are split between sales taxes ($388 million, or 45 percent), a statewide property tax ($128 million, or 15 percent), personal income taxes ($96 million, or 11 percent), a lottery (85 million, or 10 percent), and a number of smaller revenue sources. In other words, it is assumed that Arkansas will meet the Lake View requirements through a broad array of marginal tax increases, rather than a dramatic increase in one particular tax.

ITEP estimated the impact of various packages of revenue-raisers as a test of the robustness of these results. We found that the results are not sensitive to the mix of revenues chosen—the long-term impact remains positive under a variety of tax proposals.

5. **Complying with Lake View will require substantial new state spending—and new revenues. How will these changes affect the Arkansas economy in the long run?**

ITEP estimates that complying with Lake View will increase total Arkansas employment by more than 34,000 by the year 2014, and will increase personal income in the state by $1.9 billion by 2014. As a result of this employment and income growth, state tax revenues will increase by $1.1 billion over the next decade—over and above the tax increases enacted to fund educational adequacy. These issues are addressed in Chapter Eleven of the report.

6. **Most other southern states have landed automotive plants in the past decade—but Arkansas has consistently come in second or third. What can we do to get these corporations to pick Arkansas next time?**

A primary goal of any state’s elected officials should be to make the business climate of their state as attractive as possible. It is incumbent on these officials, however, to recognize that business climate is a function of both the state’s tax system and the set of public services provided by these taxes. A low-tax strategy will make Arkansas seem more attractive to corporations taken on its own, but low taxes can also deplete the important infrastructure needs that improve the quality of life for individuals and corporations.