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Economic Effects of a Universal ESA Program in Texas

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Key Points

- Expanding education choice is a smart and sound investment that Texas can make to grow the state's economy and build a stronger society.
- Creating better matches between students and their education will likely lead to fewer dropouts, which would improve social and labor market outcomes.
- Universal school choice will lead to improvements in the state's human capital and generate economic growth and numerous other benefits.
- Expanding school choice will improve the quality of education for Texas children, lead to higher property values, and spur job creation.
- By creating an education system for the future, Texas can become a leader and set the bar for other states to follow.

Introduction

Education is important for a growing economy and a productive society. Education choice offers a policy that would not only improve the prospects of many Texas students, but it would also improve the state's economy. Research has shown that universal school choice could increase Texas' $1.7 trillion gross domestic product (GDP) by 17 percent to 30 percent over 25 years, or roughly $290 billion to $510 billion each year. If Texas boosted its student achievement to the level of Minnesota, which is the top ranking state in average test scores over the last two decades, then it could grow its GDP over the next 80 years by 199 percent above its current level.

Education choice is about facilitating the best matches between students and providers. It is not about one kind of schooling or product being "superior" to another. In addition, it certainly is not about "dismantling" one kind of education or educational sector in favor of another—this simply has never materialized in any state that has education choice. Just as economic prosperity grows when good matches are made in a labor market, student outcomes will get a boost as better matches are made between students and the kinds of education they receive.

Expanding education choice is a smart and sound investment that Texas can make to grow the state's economy and build a stronger society.

An Education Savings Account (ESA) Program

Texas leaders have indicated an interest in creating a school choice program similar to the universal education savings account program that Nevada passed in 2015 (Hacker). The proposed program would establish education savings accounts for Texas families to exercise greater control over how taxpayer dollars fund their children's education. The Texas Comptroller would administer the program and eligibility would be limited to students who satisfy one of the following conditions:

- Enrollment in a public school during the preceding school year;
- Enrollment in kindergarten or first grade for the first time; or
- Previously established eligibility for the ESA program.

The amount of funds put into an individual's ESA and accessed either online or with a debit card will depend on a child's household income. If a student's family income is above 200 percent of the qualifying level for the federal free and reduced lunch program, then their ESA would receive 60 percent of the state average maintenance and operations (M&O) expenditures per student for the prior fiscal year. If a student's family income is below 200 percent of the same qualifying level, then their ESA would receive 75 percent of the state average M&O expenditures per student for the prior fiscal year. Finally, special needs students would receive an ESA with 90 percent of the state average M&O expenditures per student for the prior fiscal year.

ESA Amounts

The ESA amounts are set to a share of the state and local average per-pupil maintenance and operations (M&O) expenditures. The Texas Education Agency's

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(2016a) data show that the state and local M&O expenditure is $8,330 per student for FY 2015, calculated by dividing $43.3 billion in state and local M&O expenditures by 5.2 million in average daily attendance. Therefore, students in certain situations could receive the following ESA amount the following year: $5,000 in higher-income households who qualify for 60 percent of M&O, $6,250 in lower-income households who could receive 75 percent of M&O, and $7,500 for children with disabilities who would quality for 90 percent of M&O. The average value of these ESA amounts is $6,250 per student. To consider the fiscal effects of an ESA program, we use the assumption by Merrifield and Ginn who use $6,500 for ESAs awarded.

Student Demand and Fiscal Response

To estimate student demand and the fiscal response of the ESA program on state taxpayers, we use the same results reported by Merrifield and Ginn. They use the school choice fiscal notes calculator and input data from the Texas Education Agency and Texas Private Schools Education Association. Their results indicate that the estimated total demand for ESAs in the first school year of the program (2017-18) could be 196,690 students. This estimate reflects past enrollment trends and assumes that 80 percent of the demand will be taken up in the first year, as was the case for the Edgewood Voucher Program and Milwaukee Parental Choice Program. In fiscal year (FY) 2018, estimated fiscal savings split between the relevant public school districts and the state by the ESA program is $165 million. This estimate is based on the difference between the average marginal cost to the state and assumed average ESA amount of $6,500. The ESA amount assumed here represents the amount for students from households with incomes below 200 percent of the qualifying level for the federal free and reduced lunch program. The ESA amount for students from households with income above 200 percent of the qualifying level is $5,000, which would generate greater savings to the state. Thus, the fiscal savings estimate reported here is cautious. It reflects several factors including tuition increases from historical trends and the ESA program, which can influence student transfers from private to public schools, and the likelihood that some students will transfer from private to public schools in order to attain ESA eligibility.

Effects of Fewer High School Dropouts on Savings and Economic Growth

The best available evidence on the effect of education choice on high school attainment comes from a study of the District of Columbia Opportunity Scholarship Program, a school voucher program that serves low-income families (Wolf et al., 2013). This study is based on random assignment, widely regarded as the "gold standard" of research methods because the only difference between the comparison and control groups is that one group received vouchers and the other group received "business as usual" (i.e., returning to their public school). Students who were randomly selected to receive vouchers were 12 percentage points more likely to graduate high school than students not randomly selected to receive vouchers. More remarkably, this effect increases to 21 percentage points for the group of students who actually used vouchers.

Cowen et al. compared various outcomes between students who participated in the Milwaukee Parental Choice Program (MPCP) and a matched group of peers who remained in the Milwaukee Public School District. They found some evidence that the program increased graduation rates among students, such as an increase of 7.1 percentage points for one cohort of students. The estimate for a second cohort was positive but statistically insignificant.

Increasing education options for families in Texas, which would likely happen with this universal ESA program, would facilitate matches between students and the education they receive. These better matches would in turn keep students in school longer and reduce the number of dropouts. The cost of dropping out of high schools has been documented. Sum et al. find that dropping out of high school is associated with higher incarceration rates and worse labor market outcomes. It stands to reason that creating better matches between students and their education will likely lead to fewer dropouts and subsequently improve social and labor market outcomes.

We can also estimate the break-even share of ESA students who must be redirected from public schools in order for the program to have a neutral effect on the state. This is simply the ratio of the per-student cost of the program to the savings generated by each redirected student (Lueken). In order for the program to be cost-neutral, 82 percent of all ESA students must otherwise have attended public schools. This implies that if less than 18 percent of ESA students would enroll in private schools absent the ESA program, then the program will generate savings for the state government.

Effect of ESAs on Public Schools

The originating public schools would no longer receive funding for students enrolled elsewhere. On average, public school district revenue would decline by the ESA amount based on the factors above. Public schools, however, will concurrently realize variable cost savings from not having to educate those students. The ESA amount from the Foundation School Program (FSP) is within a cautious range of estimates by economists of short-run variable cost savings in K-12 education to be roughly 55 to 75 percent. The Texas Education Agency reports annually the "Instructional Expenditure Ratio," which is defined as instructional and related expenditures divided by total expenditures, which is 63.8 percent—well within the range found by Scafidi. In addition, Bifulco and Reback estimated variable costs for Albany and Buffalo are, respectively, 66.3 percent and 54.6 percent of expenditures. Moreover, school districts will retain all interest and sinking (I&S) funds, in addition to other miscellaneous funds, when students are diverted from public schools. I&S funds retained by school districts for each diverted student range from $0 to $17,117 per student, with the average being $1,190 per student diverted.[1]

To be clear, variable cost savings are not reflected by a direct reduction in school expenditures. As with all other facets of the economy, schools must make active decisions to cut costs commensurate to declining enrollment. District officials' options for what to do with cost savings include reinvesting these savings in students remaining in public school. If schools choose not to cut costs, then they will be passively passing on these savings to expenditures on their remaining students. In other words, while total revenue will decrease, spending on a per-pupil basis will actually increase because schools will still receive some funding associated with students that they no longer educate.

A concern often voiced by education choice critics is that these programs will lead to a mass exodus of students from public schools. There are currently 61 private school choice programs that have been enacted in the United States, and none of them led to a mass exodus of students from public schools (EdChoice, 2017a). Ignoring any benefits associated with school choice, the harm school choice may inflict on the public school model is questionable when resources devoted to private choice programs comprise just less than 1 percent of total spending on public K-12 education in states that currently have school choice programs (EdChoice, 2017b). The reality is that many public schools perform well for many students, but it is unrealistic to expect that they are the best fit for all students. This was the reality in Edgewood, where many students were not served well and chose to transfer when afforded the opportunity. However, many families were satisfied with their current schools—over the 10-year life of the voucher program, the average percentage of students who chose to remain in public schools, despite the opportunity to use a voucher to enroll in private schools, was 90.5 percent (Aguirre et al.).

Economic Effects of ESAs

Several economists have examined the economic effect of school choice programs and proposals in Texas. Researchers extensively studied the effects of the Horizon voucher program in the Edgewood District (Aguirre et al.). This program was privately funded and provided vouchers for all students. Vouchers could be used to attend both private schools and public schools that agreed to participate in the program. Residency in Edgewood was the only requirement. Thus, this program provides a microcosm of what a universal statewide education program in Texas might look like.

School Choice's Effect on Economic Growth in Texas

A recent Texas Public Policy Foundation report by the renowned economist Arthur Laffer examines the economic effects of a universal education choice program in Texas. Notably, the proposed program he analyzes is very similar to the current program being proposed. Laffer estimates that universal school choice could increase Texas' $1.7 trillion gross domestic product (GDP) by 17 percent to 30 percent over 25 years, or roughly $290 billion to $510 billion each year. He also estimates that such growth could contribute to between 560,000 and 985,000 new jobs.

Other notable economists have examined the economic effect of improving the quality of providing education. Hanushek et al. estimate the economic effect for each state in the U.S. and find that "differences in student achievement and educational attainment account for 20 to 35 percent of the current variation in per-capita GDP among states" (54). If all states could raise their students'

[1] District-level I&S data were based on a Public Information Request to the TEA. Data were delivered on May 18, 2016. The request provided data for 851 school districts but was missing for 176 school districts.

level of achievement (knowledge accumulation) to the level of Minnesota, which is the top ranking state in average test scores over the last two decades, then the overall gains from these improvements over 80 years is projected to be $76 trillion. Hanushek et al. also estimated the economic effect of improving school quality in Texas under three scenarios:[2]

- If Texas and all other states increased their student achievement to the level of Minnesota (the level of the best performing state), then Texas GDP could grow over the next 80 years by 343 percent over its current level (worth about $66 trillion in present value terms).
- If just Texas boosted its student achievement to the level of Minnesota (and other states in the region do not commit to reforms to improve their schools), then it could grow its GDP over the next 80 years by 199 percent over its current level (worth $3.2 trillion in present value terms).
- If Texas and all other states improved their performance so all students are at least NAEP basic (what No Child Left Behind was designed to accomplish), then Texas could grow its GDP by 91 percent (worth $1.5 trillion in present value terms).

At least half (55 percent) of state residents were born in their current states. According to U.S. Census Bureau American Community Survey data, this rate for Texas is about 60 percent. One reason why states gain a lot from improving schools is that, on average, over half of their workers come from their own state; Texas can come out ahead if it improves its own schools, but it can come out "more ahead" if other states improve their schools because of interstate migrations that occur—part of Texas' workforce is comprised of people educated in other states. By creating an education system for the future, Texas can become a leader and set the bar for other states to follow. Doing so now would also give Texas a first-mover advantage, allowing the state to maximize the benefits initially gained from a universal education choice program. It may also have positive spillover effects by incentivizing neighboring states to pursue similar education reforms in the future aimed at improving their K-12 education systems. This would be a win-win for Texas.

School Choice's Effect on Property Values

Research points to a clear link between the quality of schools and property values, whereby parents are willing to pay more for housing where their children have access to a higher quality education (Black; Shapiro and Hassett). This was the case with the Horizon program, where Edgewood's property values more than doubled by the program's ninth year, which was more than 1.5 times greater than property values in neighboring San Antonio ISD over the same period (Aguirre et al.). For each percentage point increase in test scores, property values increased by about 5 percent. This is lower than estimates by Shapiro and Hassett that in the New York counties of Nassau and Westchester a one percent increase in ELA and math test scores was associated with roughly an 18 to 20 percent increase in those districts' housing prices. Laffer estimates that a universal choice program in Texas could raise property values by 20 percent. Assuming these estimates give a good ballpark, a universal school choice program would likely be associated with property values increasing between 5 and 20 percent.

School Choice's Effect on Job Creation

Laffer estimates that a universal school choice program could create between 560,000 and 985,000 new jobs for the state. By virtue of creating better matches between Texas children and the education they receive, the ESA program will lead to improvements in the state's human capital and substantially reduce the incidence of dropping out of school. Improvements in human capital will improve productivity and output, which in turn leads to more jobs and higher wages.

Conclusion

Expanding education choice is a smart and sound investment that Texas can make to grow the state's economy and build a stronger society. Texas' own past experiences with school choice policies have provided numerous benefits for students and its citizens.

Estimated total demand for ESAs in the first school year of the program (2017-18) could be 196,690 students, and estimated fiscal savings split between the budgets of relevant public school districts and the state by the ESA program is $165 million. Moreover, creating better matches between students and their education will likely lead to fewer dropouts, which would improve social and labor market outcomes.

[2] See "State-Specific Projections of Economic Gains from Education Reform," *Education Next*, 2016; "Economic Impact of Student Performance Improvement," *Education Next*, 2016; "Texas: Economic Future With Educational Reform," *Education Next*, 2016.

A universal ESA program will lead to improvements in the state's human capital and generate more economic growth and other benefits. Economists have estimated the economic effect of improving the quality of education in states such as Texas. A universal school choice could increase Texas' $1.7 trillion gross domestic product (GDP) by 17 percent to 30 percent over 25 years, or roughly $290 billion to $510 billion each year. If Texas boosted its student achievement to the level of Minnesota, which is the top ranking state in average test scores over the last two decades, then it could grow its GDP over the next 80 years by 199 percent above its current level (worth $3.2 trillion in present value terms). Moreover, school choice will increase property values and spur job creation.

Texas can become a leader and set the bar for other states to follow by creating an education system for the future. And doing so now would give Texas a first-mover advantage over its neighboring states and allow the state to maximize the benefits initially gained from a universal education choice program.

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