Taxation and Education: Using Educational Research to Inform Coherent Policy for the Public Good

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Abstract

In 2006, following a 30-year trend among the US states to remove the property tax from the revenue for public schools, the South Carolina General Assembly enacted Act 388 which replaced the property tax with a one-cent sales tax. The law decreased the budget capacity of school districts thus impacting educational equity and adequacy. This paper describes key policy makers' and stakeholders' interpretations of the pressure for property tax relief and highlight the importance of policy coherence in education finance, taxation, and accountability.

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Throughout history, the property tax has been the principal source of funding for public education although the percentage of funding for public education that comes from local sources has varied and the reliance on property tax is different in different regions of the country (Kent & Sowards, 2009; McGuire & Papke, 2008). Property taxes have provided a stable revenue source for public schools, yet historically remain vulnerable to challenges on the grounds of equity and adequacy tied to local wealth. Most notably, critics contend that since property wealth is unevenly distributed, the reliance on this source of funding results in uneven tax rates, inconsistent revenues per pupil, and variance in spending across districts (McGuire & Papke, 2008). Nevertheless, California voters approved Proposition 13 over 30 years ago, and since then, other states have removed property taxes from public schools' revenue streams and replaced such taxes with more dynamic and in some cases less predictable funding (Courant, Gramlich & Loeb, 1995; McGuire & Papke, 2008). South Carolina followed these states in 2006.

In the literature on school finance, myriad studies have been conducted to examine the equity and adequacy of revenue allocated in support of public education. Beginning with the seminal work of Berne and Steifel (1984), scholars have both attempted to define and quantify the concepts of horizontal and vertical equity. Due in large part to judicial interpretations of state constitutions regarding the requirement to provide for a system of public education, the debate has evolved from a focus on equity, defined as equal, to one of adequacy, defined as sufficient (Ladd, 2008; Darling-Hammond & Snyder, 2003: Verstegen, 2002; Reschovsky & Imazeki, 2001). Relatively fewer studies exist that examine revenue generation in support of public education. The capacity to budget greatly impacts the ability of educational leaders to deliver an adequate education to children; to do so require both a stable and sufficient source of revenue. Because the competing policy goals of taxpayer equity and the provision of educational services must be balanced, more studies that seek to examine how policy makers deliberate these issues as well as the impact of their decisions must be conducted.

In 2006, South Carolina's General Assembly passed legislation to relieve taxes on owner occupied property valued at more than $100,000 and typically found in attractive locations on waterfronts or in retirement communities. Simultaneously, SC legislators also limited municipalities' and school boards' ability to levy higher rates. The General Assembly removed the property tax on owner occupied property and replaced it with a penny addition to the state's sales tax on specified retail items. With several of Act 388's provisions rolling into implementation from 2007 through 2008, this study took place in 2010 to obtain key policy makers' and stakeholders' perceptions of the consequences of this act on both taxpayers and schools and their political forecast of the next steps in balancing both the tax burden among diverse taxpayers and stabilizing adequate resources for public schools. The research described in this study focused on several questions: What motivated legislators to cut the property tax in South Carolina?; Did the legislators consider the potential impact on the ability to adequately fund the state system of public education by removing the property tax?; In what ways did beliefs about tax burden and ability to pay impact the enacted legislation? This paper further developed answers to these questions: How did the shift in tax impact the capacity of school districts to budget? And, what are the implications for practitioners who must now deliver the same educational program with diminished resources?

Competing Priorities of Equity

According to Dinan (2007) and Guthrie, Springer, Rolle and Houck (2007), scholars have examined the language of the education clause of each state constitution and categorized states according to the duty to provide a system of education. These classifications range from weak clauses that simply establish a school system to clauses mandating a thorough and efficient school system. Furthermore, state education clauses range from containing language regarding the purpose and/or benefit of a quality education to clauses proclaiming education to be a paramount duty or mandating other specific duties. The South Carolina Constitution offers a limited statement (Umpsted, 2007) concerning the operation of schools:

> ... the General Assembly shall provide for the maintenance and support of a system of free public schools open to all children in the State and shall establish, organize, and support other public institutions of learning, as may be desirable. (South Carolina Constitution Article IX, Section 3).

The interpretation of the education clause in class action suits heard in 45 of the 50 states has led to recommendations for reform, particularly in the areas of finance and accountability policy (Levine, 1991; Springer, Liu & Guthrie, 2009; Griffith, 2005). At issue in these class action suits are the evolving notions of equity and adequacy. The unit of analysis in these cases is the student with equity being conceptualized as either an input or an output. When measuring equity by the more traditional focus on inputs, an equitable finance system would be measured by what Berne and Steifel (1984) identified as horizontal equity. Under such a system, all students would have access to a similar amount, or “package” or resources (Ladd, 2008 p. 404). Studies that attempt to discern horizontal equity compare expenditures per child. The definition of equity in terms of outputs would, according to Ladd (2008), require that schools be provided sufficient resources to achieve similar outcomes. Because schools are differentially situated, some schools require more or different resources than others. Differential treatment of unequals is termed vertical equity by Berne and Steifel (1984). This concept is especially relevant in the current policy context of schooling that requires equitable outcomes for all children. Some have characterized vertical equity in the ideal as adequacy (King, Swanson, & Sweetland, 2003) while Ladd (2008) made the distinction that adequacy is not just about differential treatment, but rather sufficiency of resources to achieve desired outputs.

Equity may also be viewed through the lens of the taxpayer. Ulbrich (2005) noted that a good revenue system is characterized by adequacy, equity, and efficiency. An adequate revenue system is defined as one that contains a mix of revenue sources that provide a stable foundation so that the revenue grows when the economy does. An equitable tax system distributes tax burden in a fair manner among differential levels of income and between households and businesses. Finally, an efficient system does not distort individual behavior in the market. Tax equity considers issues such as who should pay for government services, ability to pay, and burden.

Policy Coherence, Budgeting, Taxation and the Public Discourse

The seminal work of Smith and O'Day (1991) outlined the need for systemic reform in education policy and advanced the notion that an alignment of policy proposals: standards, testing, teacher licensing, instructional materials, professional development, and sanctions for school performance were required. Recently, finance scholars have advocated the importance of the alignment of funding mechanisms with standards (Adams, 2008; Verstegen, 2002). According to Ryan (2008), the fields of education law and policy have been dominated by the intersection of standards and testing with challenges to school finance distribution systems.

Budgeting may be thought of as comprising three elements: (a) decisions on the amount of funds to be raised, (b) requests for funds, and (c) the allocation of funds. Succinctly stated, budgeting is the process of generating, claiming, and rationing resources (Schick, 1990). The capacity to budget is determined by how well a government or agency can claim and allocate resources in order to produce specified outcome (Schick, 1990). "It is no exaggeration to state that the capacity to govern depends on the capacity to budget" (Schick, 1990, p. 1). By extension, the ability of schools and districts to adequately educate children is impacted by the ability to claim sufficient funds and to align those resources in such a way as to maximize student achievement.

King, Swanson, and Sweetland (2003) noted that taxes serve many purposes including the redistribution of wealth and power, the creation of an economic climate that supports the growth of business, the discouragement of the use of certain products (i.e., tobacco), and the encouragement of various social and economic policies. These issues influence policy choices among the merits of different types of taxes. Tax yield is the amount of revenue that is raised as a result of a tax. Without adequate yield, the government may not be able to provide specific services, balance the budget, and avoid debt. Finally, tax stability or elasticity is a consideration when adopting a tax. Succinctly stated, elasticity refers to the change in revenue based on a change in market conditions or tax rates. According to Odden and Picus (2007), an elasticity of at least 1.0 is highly desirable for revenue generation for schools.

As noted, the property tax has been and continues to be the primary source of local revenues for public schools. McGuire and Papke (2008) noted that 65.3% of local revenues for public education were raised through property taxes in 2003-2004. Scholars have noted that this number is actually an underestimate of the reliance on the property tax for local sources of education funding since additional revenues are distributed from municipal and other parent governments; these revenues are also raised through property taxes. As such, there is agreement that property taxes account for over 80% of all local sources of revenue for public schools (Kent & Sowards, 2009; McGuire & Papke, 2008).

Education finance reform, starting in the 1970s, saw a move away from the use of property taxes to support public education. These reforms shifted the percentage of funds that were received from local sources to the state. Public data on education finance reveal that the percentage of revenues for public education from local sources dropped from approximately 62% in 1957 to approximately 40% today (NCES, 2010). Concurrently, the percentage of total revenues for public education raised from the property tax has declined. Although the total percent of revenue raised from property taxes has declined over time, one cannot underestimate the importance of the tax. The literature points to the fact that decreases to the property tax have often been accompanied by restrictions on the locality to raise additional sources of revenue (Downes & Figlio, 2008; Kent & Sowards, 2009; McGuire & Papke, 2008). These restrictions have resulted in losses in efficiency for localities to administer services.

Changes to the education finance systems and the reduced reliance on the property tax were largely a part of class action suits brought in state supreme courts that challenged the finance systems in the respective states. Concurrent with the court action for greater equity and adequacy in school finance has been public demand for decreased property taxes (Blankenau & Skidmore, 2002; Downes & Figlio, 2008). Yinger (2006) found that increased state aid resulted in reductions to property taxes in 75% of the cases. Changes to the tax code have been seen across the United States. For example, both Michigan and California have both capped the ability of local education agencies to use the property tax and have instead implemented a state property tax to raise revenues for public schools. Other states, such as New Hampshire, have included a local provision as part of their foundation system which is labeled a statewide property tax. Still other states, such as Massachusetts have adopted laws that limit the amount of annual increases to property taxes. Despite the historical reliance on this revenue source to fund education and other services, the property tax is perhaps the most unpopular tax in the United States. According to Dornfest (as cited in Kent & Sowards, 2009), “the public continues to express resentment toward this tax and politically empowered groups whittle it away through demand for exemption or other favored treatment” (p. 34).

Criticisms of the property tax abound. It is largely seen as inefficient, inequitable, and difficult to administer. Property taxes are multifaceted. They include a tax on land, tax on the improvements to the land, and a tax on personal property. These multiple dimensions invariably lead to criticisms of valuation. Research on the criticism of the property tax shows clear themes in attempting to explain inefficiency, inequity, and administrative difficulties. These themes include: the impact on consumer behavior as a result of the tax (inefficiency), the burden imposed or incidence of the tax (inequity), and the degree to which the system is fairly administered. Specific to this inquiry are questions of burden and property valuation. These stakeholder concerns largely drove the tax revolt in South Carolina.

In a review of the impact of tax and expenditure limits, Downes and Figlio (2008) noted that while tax and expenditure limits slowed the growth of property tax revenue, they found no evidence that there was not a significant decline in revenues available to local governments. The authors stated that these findings were in the aggregate for all functions of local government and that this finding was likely the result of three factors: increased state aid funded through increased state taxes, provisions in the law that allowed voters in localities to choose to continue historical levels of spending patterns, and an increase in other local taxes or user fees. In South Carolina, Act 388 included an increase in state sales taxes to offset the lost local revenue, but lost sales tax revenue due to the economic downturn coupled with strict limits on localities to limit tax increases has limited the amount of both state and local revenue to school districts. Downes and Figlio (2008) concluded their review by considering the impact of tax and expenditure limitations on student achievement. They suggested that it is difficult to discern how tax and expenditure limitations will impact student performance because one must examine changes to spending patterns to see if districts are spending efficiently. It has long been argued that school spending patterns have not changed over time. Because districts are not aligning resources to achieve intended outcomes, there may be no reason to believe that decreased availability of revenues will impact student performance at all. On the other hand, schools are serving an increasingly heterogeneous population of students. Research tells us that it is more costly to educate diverse populations because all students have different levels of need. Reduced funding could be catastrophic for student achievement given the current need.

Despite calls for change and the politically unpopular nature of the property tax, the literature suggests that the property tax will continue, in some form, to fund public education (Augenblick, 2008). Research seems to conclude that the ability to fund public education has been eroded by efforts to enact exemptions and other forms of tax relief (Kent & Sowards, 2009). Further, scholars have stated that it is imperative that the property tax be administered properly so as to achieve both horizontal and vertical equity. Because it is believed that property taxes will not be completely eliminated, Poole (2007) introduced steps to include in the political discourse surrounding the use of property taxes to fund local government. Specifically, he noted the need to educate politicians and taxpayers about property tax reform, the benefits of the property tax, the economic consequences of change to property taxes, and the need to demystify property tax and valuation processes.

Funding Public Education in South Carolina

Funding for the system of public education in South Carolina was established in the Education Finance Act of 1977 (EFA). The EFA is a foundation program that includes a weighting system designed to equitably distribute funds among districts based on local property wealth (Flanigan & Richardson, 1993). The goals of the EFA were to guarantee each student in the public schools in South Carolina the availability of at least a minimum educational program, appropriate to the needs of each student and substantially equal to that which is available to other students in the state with similar need without regard to geographic location of socioeconomic status (South Carolina Code of Laws, Title 59, Chapter 20, § 30). The law required that 70% of the cost of the program would be borne by the state with the remaining 30% of funding to be raised locally (Flanigan & Richardson, 1993; Tetrault & Chandler, n.d.). The EFA required each locality to raise funds according to their taxpaying ability which is calculated to be a measure of local wealth. The EFA placed the determination of a per pupil cost each fiscal year based on revenue projections. The base student cost, initially provided to all students to ensure horizontal equity, is then weighted based on grade level, handicapping condition, homebound instruction, and vocational education as a means to provide a degree of vertical equity. This calculation provides a cost of the educational program for each district. Local districts must raise a portion of the total cost of the program in order to be eligible for state matching funds.

A second component of education funding in South Carolina is the Education Improvement Act (EIA) of 1984. While this component of education funding does not have an explicit requirement for local funding, it's worth briefly examining the provisions of the law since the loss of fiscal capacity due to changes in tax policy coupled with the current economic climate has implications for how school districts can use their limited funds. The EIA was an attempt to raise and distribute additional funds for education to improve the quality of the system of public education in South Carolina. EIA raised the state sales tax from 4% to 5% and allocated funds for improved academic standards, the teaching and testing of basic skills, improvements in leadership, management and fiscal efficiency, increases in teacher salaries, the creation of effective partnerships between schools, parents, communities, and businesses, and school construction (Tetrault & Chandler, n.d.).

The ability to raise local funds for education in South Carolina varies. Of the 85 school districts in South Carolina, 23 have fiscal autonomy, 36 school districts have authority to set millage rates within parameters established by statute, referenda, legislative action, or county council action, and 26 districts must call upon the legislative delegation or county governments to establish millage. Fiscally autonomous school districts have the authority to establish a millage rate for the operation of schools. Local funds are used to satisfy the local effort requirements of the EFA, to provide supplements to state and federal funds deemed appropriate by local communities, and to provide school facilities or to offer special initiatives or services with costs beyond the constitutional debt limit.

Act 388

In Fiscal Year (FY) 2006, the SC Legislature passed Act 388, also known as the *Property Tax Relief Act*, which changed the means by which localities could raise funds in support of public education. Until then, property taxes had been the main source of local funding for public education in South Carolina. That changed to a reliance on ad valorem taxes, revenue transfers from the state in lieu of taxes, and revenues from fees. Localities were given the legislative authority to determine fees as necessary. Three major components of this act pertained directly to public school finance (Schunk, 2006). The first included a sales tax increase from 5% to 6%. According to the law, the revenue generated by this increase flowed into the newly created Homestead Exemption Fund. Secondly, all owner-occupied residential property became exempt from property taxes for school operations. By FY 2008, money in the Homestead Exemption Fund became the source for reimbursements to school districts for the lost property tax revenue. The last component of Act 388 imposed millage caps for all local governing bodies including school districts. The millage cap limited local governments to a percentage less than or equal to the percentage increase in local population plus the rate of inflation of the Consumer Price Index (CPI) (Schunk, 2006). The projections for FY 2008 were that Act 388's allocations of the property tax relief funds were distributed to districts as a direct reimbursement for the funds that would have been collected by each district through property tax collections. Each subsequent year, the property tax fund was supposed to grow by the percent of state population growth plus the prior year CPI, or 4% whichever was greater. Beginning in FY 2009, districts were projected to receive the base amount set in FY 2008 plus the growth funds, distributed by Weighted Pupil Units (WPU) and a poverty factor.

Method

The study relied heavily on oral histories from key participants in the 2006 legislative process (Kvale & Brinkman, 2009; Marshall & Rossman, 2006) as well as data detailing tax revenues as published by the South Carolina Department of Revenue and the South Carolina Budget and Control Board. These recounts of personal roles and discussions with others were triangulated with participants' documents and media accounts of the time (Corbin & Strauss, 2008). Sixteen people representing state legislators, media and public analysts, and grassroots taxpayer organizations participated in the study. Key political elites, including around 10 legislators and media representatives, were identified prior to the study. Then, additional participants were nominated by the initial participants in a technique known as snowballing (Marshall & Rossman, 2006).

The theoretical framework provided the structure for interview questions, which appear as an appendix. All of the interviews were conducted by one member of the research team; 12 over the phone and 4 in face-to-face settings. All of the interviews were audio-recorded and transcribed into documents for the analysis. The analysis began with a set of start-codes derived from the theoretical framework and attached to specific interview questions. However, these codes proved too fine-grained and orthogonal for the complexity and density of the participants' narratives. Instead, the researchers used a reiterative coding process to access findings among the responses.

To discern the impact of the policy change, descriptive statistics were collected on tax revenues (Table 1) as well as the base student cost expenditures (Table 2) for each the past ten years. The tax elasticity for each tax, income, state sales and use tax, as well as the property tax was calculated. For the purposes of this study, tax elasticity was defined as the change in revenue given the change in income.

Findings

Two findings are presented: first stakeholder perceptions of the efforts to change the tax policy as recorded during the oral histories as well; second, descriptive statistics on tax revenues and the elasticity calculations. The oral histories yielded results including six categories that illustrated the political contrasts over Act 388: (a) equity for taxpayers, (b) shift in tax burden, (c) adequacy of resources, (d) Act 388 effects on education in South Carolina, (e) local control of schools, and (f) possible changes to Act 388. In the paper, quotes from transcripts are cited with participants' surnames (their own or their selected pseudonym) and the date of the interview with the page number of the transcript.

Participants' perceptions regarding taxpayer equity was examined prior to and following the passage of Act 388 and from two different equity perspectives - taxpayer equity and educational equity for children. One of the interviewees described taxpayer equity features of Act 388 as follows:

> ... the guys that owned the $10 million-dollar homes along the battery in Charleston, they are the ones that saw the big break. The wealthiest of the wealthy saw the biggest property tax break. The average person in South Carolina did not see much of a property tax break unless their home was valued at more than $100,000, then you got a little bit of a break (Anthony, March 7, 2010, p. 2).

Educational equity fared even worse in the Act 388 design. Most of the participants admitted that the legislative focus was on taxpayers, not on education. Although some saw the discourse over Act 388 as a bait-and-switch con game.

"It has nothing to do with education. Absolutely nothing. Part of the rhetoric to sell the idea was the concept to separate the pitting of the homeowner against the local education community" (Jones, March 19, 2010, pp. 3-4).

"It was sold that way but it really had nothing to do with education; it was all about taxation. It doesn't have anything to do with education. It has nothing to do with education" (Read, February 25, 2010, pp. 5, 8).

Thus, the strongest perspective among the responses focused on the purpose of Act 388 as a means of resetting the tax burden from one set of constituents to others. "... in some cases, the lower income people do not have to pay those taxes because they get food stamps. They said this was much better for us" (Doe, March 8, 2010, p. 7). This particular participant rationalized the removal of the higher value home property from tax rolls with the notion that the passage of the additional penny sales tax was fairer since poor people do not own homes. Essentially, the shift of the tax burden moved from property of owner-occupied homes to consumers, which calculated as a 20% sales tax increase on goods and services. However, the business community also reacted to the shift as a 6% increase in tax devolved to manufacturing and industry when high-valued homes were removed under Act 388.

The research examined the participants' perceptions of adequacy of resources for education. Although some participants cited waste in schools, others identified a reduction in funding since the economic decline, beginning in 2008. The 2008 recession immediately affected consumer sales, and thus dropped sales tax revenues. Sales tax collections in South Carolina experienced deficient collections of 6.3% in fiscal year 2008, or $165 million. These lower-than-projected revenues had a simultaneously impact on school resources as noted by one of the participants:

> So you're just screwed in terms of your [school] operating revenues. That's hard to come by these days. ... It's just staggering. ... Personally I don't like to pay property taxes but there are certain things that we have to do to make the world work. One of [then-Governor] Mark Sanford's efforts was to reduce the size of government and one way to do that was to bankrupt government. ... To bankrupt the government! I don't know if it was intended or it was just a byproduct (Miley, March 9, 2010, pp. 3-4).

The notion that government should be diminished was also a feature of Act 388 in that it capped the ability of both school districts and municipalities in raising revenues through property taxes. The Act limits the ability to raise millage by the consumer price index plus the rate of inflation. South Carolina and local school districts have historically clung to local control of schools. The curtailing of local control appeared to be the policy intent of one supporter of Act 388:

...the wild, reckless spending... reign them in some to get them where… they had no respect for a person's home. They thought that a retired person's life savings was their piggy bank. We could no longer afford them to have free access to our savings account (Bowen, March 7, 2010, p. 5).

The study sought to determine if participants believed there would be any changes to Act 388. Some participants advocated for comprehensive tax reform - a broad based tax base with low rates. Those advocating for reform were concerned with both the imbalance in tax burden on businesses and consumer as well as those who recognized the instability for local government and school revenues. Others, among who were those depending on continued support among retirees and realtors/developers with investments in with high value waterfront property, felt that efforts to reverse Act 388 would fail.

Descriptive statistics in Tables 1 & 2 illustrate the impact of the changed tax policy. Tax estimates, actual collections, and the difference between the two are displayed in Table 1 as is the mean household income in the state and tax elasticity calculations. Several patterns emerge. First, the property tax was by far the most stable tax. The property tax was the only tax that resulted in actual collections above the estimate. Both the income and sales taxes were below the projection in six of the ten years of study with the largest deficit taking place in a year of declining income (FY 08-09). Conversely, property taxes remained stable and actually grew in nine of the ten years of study. Both income and sales tax revenues declined in years when the state and country were experiencing recession (2000-2003 and FY 2007-2010) while property taxes performed above expectations. Elasticity calculations were impacted by flat and declining median household income in the state. Recalling the standard of 1.0 for elasticity for revenue generation in schools, the income tax was the least reliable tax in terms of generating sufficient income to fund public education. The income tax only met the standard three times (FY 03-04, FY 04-05, and FY 08-09). The property tax met the standard a total of four times while the sales tax met the standard a total of five times.

The impact on revenue allocations to public schools as a result of a change to a reliance on a less stable source of revenue has been drastic. These data appear in Table 2. The base student cost in South Carolina is allocated based on revenue projections. In examining the data in Tables 1 & 2, it appears that the greatest surplus in funds occurred in FY 05-06. Coincidentally, that is the same year that Act 388 was signed in to law. Based on increased revenues, the base student cost rose from $2290 in FY 06 to $2367 in FY 07 and $2476 in FY when the law was fully implemented. Unfortunately, the housing market crash in 2008 coupled with the ensuing recession resulted in huge revenue shortfalls. The base student cost decreased to $2191 in FY 08-09 and $1756 in FY 09-10. That allocation in FY was a cut of over $900 per student below the budget and control board estimate of the cost of educating a student in South Carolina.

Discussion

Balancing tax equity and funding education has been an elusive goal in South Carolina. Coherent education policy is premised on the systemic reform of standards, accountability policy as well as the means by which to system is funded. The oral histories recorded as part of this study clearly reveal that the goal of the proponents of Act 388 was to reduce the tax burden on the elites. Although the impact of Act 388 was exacerbated by the 2008 recession, the coincidence of the Act's provisions and the economic downturn provided a dynamic illustration of the issues with replacing a relatively stable revenue stream with a volatile one, the sales tax. The responses from the political elites in this study revealed that the enactment of the law was not merely shortsighted economically, but also in terms of taxpayer equity. The proponents of

Act 388 were primarily retirees, realtors, and developers with high-value waterfront properties intended for owner-occupancy. The taxpayers who lost in the burden shift were consumers and other businesses with large property sites for manufacturing and other purposes. The biggest losers were public schools and students along with local municipalities whose ability to raise revenues was curtailed by Act 388.

More alarming was the total disregard for the impact that the removal of revenues would have on the system of public education in the state. Indeed, the proponents of the Act did not even consider the systemic ramifications of the removal of the most stable source of revenue for public education. The result was a decrease by over one-third in the base student cost resulting in furloughs, layoffs, and a reduction in the number of days in the school year. Each of these resources has been proven to have a positive impact on student achievement in the literature. Interviewees expressed the belief that there was waste in education funding and that shifting the tax burden would decrease the size of government. Wasteful spending and inefficiency are frequent criticisms of public education. Two definitions have emerged in the literature for inefficiency in education finance. Scholars attempting to discern the adequate cost of an education have defined inefficiency as the difference between required costs and actual expenditures. Critics contend that the adequacy calculations are flawed in part because there are multiple goals of public education and that the use of minimum proficiency targets may actually underestimate the true cost of educating children. Economists define efficiency as the allocation of inputs to achieve maximum levels of outputs. Using this argument, it is possible to have underperforming schools that are efficient because output is maximized given inadequate inputs. Inefficiency, as defined by economists, is found in schools where costs exceed outputs. Both groups agree that there are increased costs for educating students in schools with high concentrations of poverty and other indicators of risk.

Given the findings that stakeholders saw little need to make revisions to Act 388, even given the decrease in revenue to support education, we believe that there is greater need for educational leaders to become involved in advocating for more coherent policies. If the ability to implement a system of public education that meets the needs of all students and provides them with the opportunity to achieve proficiency targets inherent in accountability policy, leaders must be given the capacity to budget. This requires an adequate source of revenues from multiple sources so as to ensure stability. Educational leaders must be willing to work with policymakers and to inform them of the impact of changes to revenues in support of public education. Lastly, educational leaders must be willing to reflect on current resource allocation practices and to advocate for change. Years of production function research have identified school level resources that most impact student achievement. Further inquiries have identified that these resources tend to be concentrated in the least needy schools. An emerging body of research on *x-efficiency* has described the impact that school policies, practices, and culture can have on student achievement (Addonizio, 2009; Leibenstein, 1966). Leaders must be willing to make the difficult choice of reallocating resources to the neediest schools, a decision that few have been willing to make to date, while working to improve the process by which we educate our children. In so doing, perhaps we can create greater understanding of the resources and practices required to better educate all children and move toward greater policy coherence in school finance and taxation policy.

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Appendix - Interview Protocol

1. Since enacting the 2006 legislation known as Act 388, what two or three issues have you heard about from your constituents?

    Follow up questions (if necessary)

    a. How did Act 388 impact the business community? Do you know of any fiscal impact studies about the effects of the Act on the business community? (Burrup, Brimley, & Garfield, 1993)

    b. How did the Act affect homeowners? Do you believe homeowners prefer to be taxed in the form of a sales tax rather than a property tax? (Martin, 2006; Slade, 2007; 2009)

2. As you think about Act 388, do you see it as primarily a tax law or an education law? (Picus, Odden, & Fermanich, 2001)

3. What consideration of tax burden led to the development of Act 388 in 2006? (Burrup et al., 1993)

    a. Do you recall any discussion about the reactions of corporations or manufacturers to a shift from property taxes to sales taxes? If so, what was the nature of that discussion?

        i. Was there any discussion of the possibility that corporations and manufacturers could shift the tax burden onto consumers in the form of higher prices? If so, what was the nature of that discussion? (Odden & Picus, 2007)

        ii. What about speculation on corporations and manufacturers shifting the tax burden backward to workers in the form of lower wages? If so, what was the nature of that discussion? (Odden & Picus, 2007)

        iii. Do you recall any discussion about corporations and manufacturers shifting the tax burden backward to suppliers in the form of lower prices for raw materials? If so, what was the nature of that discussion? (Odden & Picus, 2007)

        iv. To what extent was there any speculation about owners of rental property increasing monthly rent on tenants? (Odden & Picus, 2007)

4. To what extent did escalating assessed values influence the passage of Act 388? (Burrup et al., 1993)

    a. What kinds of estimates about real estate sales surrounded discussions about the Point of Sale price for the purposes of taxation? (Burrup et al., 1993)

        i. Did the property valuation system need overhauling? (Picus et al., 2001) Is there further overhauling of the tax system in South Carolina?

        ii. Are there any repercussions from instituting a tax reassessment cap at 15% (Scoppe, 2008)

    b. How were the exemptions to sales taxes determined? (Burrup et al., 1993)

5. To what extent did the deliberations over Act 388 include consideration of centralized state authority over resources and quality and the tradition of local control of schools? (Guthrie, Rolle, Springer & Houck, 2007)
6. By removing local property taxes from revenue generation for local school districts, did the General Assembly consider who or what agency would oversee the spending of the state tax dollars? In other words, was the loss of local control considered in developing the Act? (Burrup et al., 1993)

7. How did equity of resources play into the development and eventual passage of Act 388? (Picus et al., 2001)
    i. At this point, what do you think the General Assembly will do about Act 388?
    ii. Do you think the response will be primarily a new taxation policy or a new education policy?
    iii. Which constituents likely will be satisfied with the General Assembly’s response?
    iv. Which constituents likely will be dissatisfied with the General Assembly’s response?

Table 1
South Carolina Tax Revenues, Household Income and Tax Elasticity

	FY 00-01	FY 01-02	FY 02-03	FY 03-04	FY 04-05	FY 05-06	FY 06-07	FY 07-08	FY 08-09	FY 09-10
Individual State Income Taxes										
Estimate	2,284,249,442	2,353,988,655	2,307,230,914	1,964,484,931	1,979,363,905	2,158,416,916	2,599,913,486	2,927,383,170	2,969,672,332	2,469,023,143
Actual	2,127,286,899	1,920,136,736	1,859,125,469	1,973,635,422	2,215,376,042	2,608,227,193	2,881,930,422	2,863,839,126	2,326,707,698	2,170,909,624
Over/ (Under)	(156,962,543)	(433,851,919)	(448,105,445)	9,150,491	236,012,137	449,810,277	282,016,936	(63,544,044)	(642,964,634)	(298,113,519)
State Sales and Use Taxes										
Estimate	2,092,964,644	2,178,000,237	2,150,685,980	2,151,994,915	2,249,617,591	2,396,065,472	2,495,764,823	2,599,400,000	2,698,853,250	2,192,353,185
Actual	2,000,208,479	2,026,514,449	2,041,704,530	2,181,357,756	2,318,474,848	2,544,065,472	2,631,222,230	2,463,274,765	2,247,876,029	2,190,976,127
Over/ Under	(92,756,165)	(151,485,788)	(108,981,450)	29,362,841	68,857,257	148,000,000	135,457,407	(136,125,235)	(450,977,221)	(1,377,058)
Property Taxes County, City, and School District Level										
Estimate	2,771,124,427	3,086,707,524	3,242,461,172	3,429,329,344	3,495,878,573	3,829,662,904	4,166,080,985	4,065,064,529	4,360,090,649	4563199593
Actual	2,796,638,298	3,110,484,500	3,267,014,852	3,448,756,640	3,515,806,273	3,846,831,188	4,184,451,598	4,082,471,168	4,377,601,963	4590179930
Over/ Under	25,513,871	23,776,976	24,553,680	19,427,296	19,927,700	17,168,284	18,370,613	17,406,639	17,511,314	26,980,337
Median Household Income										
Estimate	37,736	37,812	38,479	38,691	40,230	39,617	44,213	42,155	41,101	41,699

	FY 00-01	FY 01-02	FY 02-03	FY 03-04	FY 04-05	FY 05-06	FY 06-07	FY 07-08	FY 08-09	FY 09-10
Tax Elasticity										
Income		-48.35	-1.80	11.18	3.08	-11.64	.90	.13	7.50	-4.60
Sales		6.53	.42	12.41	1.58	-6.39	.30	1.37	3.50	-1.74
Property		60.81	2.85	10.10	.49	-6.18	.76	.52	-2.89	3.34

* Source: South Carolina Budget and Control Board, Historical Analysis, US Census Bureau

Table 2

South Carolina Base Student Cost

FY	Budget & Control Board BSC Estimate	General Assembly BSC Proviso	Funded BSC
00-01	2012	2012	2002
01-02	2073	2073	1881
02-03	2133	2033	1770
03-04	2201	1701	1754
04-05	2234	1852	1852
05-06	2290	2290	2290
06-07	2367	2367	2367
07-08	2476	2476	2476
08-09	2578	2578	2191
09-10	2687	2034	1756

Source: South Carolina Department of Education