

**The Way to Education Success in New Mexico: Breaking Free from  
Failed “Reforms”**

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Senior Fellow and Co-Founder, Rio Grande Foundation

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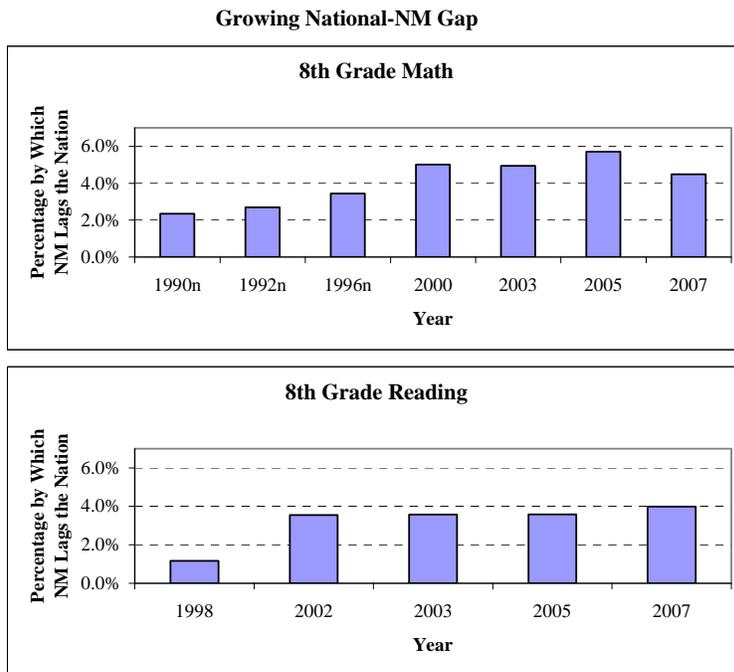
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## Executive Summary

Over the past twenty years New Mexico has undergone “reforms” of its K-12 education system. What are the results of these “reforms?” How can the state actually improve education performance?

The study begins by examining how education performance has changed as a result of the reforms. Unfortunately, the state’s overall performance, as measured by the well-respected National Assessment of Educational Progress (NAEP) (also known as the “Nation’s Report Card”) has remained stagnant. While we have seen some improvement in math scores, reading and science scores have for the most part declined (other subjects did not have enough testing to discern a trend). For example, nearly half of New Mexico’s students failed to achieve “basic level” or above in 4<sup>th</sup> grade reading (42 percent) and 8<sup>th</sup> grade science (54 percent) in 2005. Moreover, we are falling further behind the nation as a whole in all three subjects. Figure 1 gives you a picture of how the national-New Mexico gap has been widening for average 8<sup>th</sup> grade math and reading scores:

**Figure 1: Growing Percentage by which NM lags the nation in average NAEP 8<sup>th</sup> grade math and reading scores**



Overall education performance may be stagnant, but the resources devoted to trying to increase performance have increased dramatically. When adjusted for inflation and population growth general fund<sup>1</sup> spending has increased by 34 percent over the past 19 years. The *average* New Mexican is now paying an extra \$319 each year for no improvement in the education of our children.

Moreover, state spending is supplemented by federal and local dollars. All told per pupil spending from all sources has increased by nearly \$2,700 (in FY 2006 dollars) over the 18 years ending in FY 2005. That is an increase of 52 percent per pupil. Again, what have we gotten for the \$2,700 per pupil increase? Nothing!

That our overall performance is stagnant and lagging the nation by increasing amounts over the time period studied is astonishing. How can this possibly be when taxpayers have been allocating an ever-increasing amount of resources to education and we have been doing so at a faster rate than other states? It is a shameful fact that government schools' productivity in improving educational performance in New Mexico is zero over the past couple of decades. Contrast that with the fact that productivity in most other aspects of our lives has grown by leaps and bounds. Why are New Mexico's government-run schools so seemingly incompetent while everyone else is innovating and improving?

This study attempts to answer that question in part by using regression analysis to conduct a statistical test. I test the hypothesis that the main problem with government-run schools is that incentives are wrong. My years of study of economics and its application to education lead me to conclude that schools perform best when they must compete to satisfy parents. Parental choice creates competition and thus the incentive for schools to be more innovative. The more choice parents have the greater is their *education freedom*.

The regression tested education performance as a function of education freedom across states. States with more freedom were found to have better performance than states like New Mexico. New Mexico could greatly improve performance by encouraging more parents to choose their child's school. In other words, making education more market-like would work.

The final section of the study recommends tuition tax credits targeted to the poor as the specific way to get the job done. Those who are poorer would get more access to help. This could be done with little effect on the state's revenue and budget picture. Other options include increased choice among government-run schools or a system of vouchers, but the author of this study believes that a system of tax credits for needy children is the best immediately-available and politically feasible means of improving New Mexico's education system.

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<sup>1</sup> The "general fund" is the source of state money appropriated by the legislature and governor each year for K-12 education.

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## **New Mexico's Education Performance and the Resources Used to Produce It**

In the private sector and in life, the more effort you make and the more resources you dedicate to a particular task, the more likely you are to succeed. Thus, we see that *more resources usually lead to improved performance*. Think of your garden, for example. If you increase the amount of sweat equity, weed control, and fertilizer you put into it, chances are it will grow better. Or think about how you play an instrument or game of skill. If you increase the amount of time and resources dedicated to studying and practicing playing the guitar, golf or bridge, then you will play better.

The relationship between resources and performance seems so obvious as to not require me to be pedantic. Yet this relationship has not held up for New Mexico's system of primary and secondary education. Since the early 1990s we have been increasing resources that go into education at a *rate greater than other states*. Yet we are not seeing overall improvement in performance, and the amount by which our performance lags the nation is mostly *increasing!*

Evidence of New Mexico's decline in educational achievement relative to other states can be found in tests conducted by the National Assessment of Education Progress (NAEP). These scores are widely accepted as reliable indicators of performance within the education community. As evidence of the ever increasing amount of resources being dedicated to education, we need to look no further than government spending. This paper also documents how the growth of K-12 spending in New Mexico compares to other states.

### ***Performance as measured by National Assessment of Education Progress (NAEP) scores***

We have solid performance data on 4<sup>th</sup> and 8<sup>th</sup> grade mathematics and reading and 8<sup>th</sup> grade science dating back to the 1990s.<sup>2</sup>

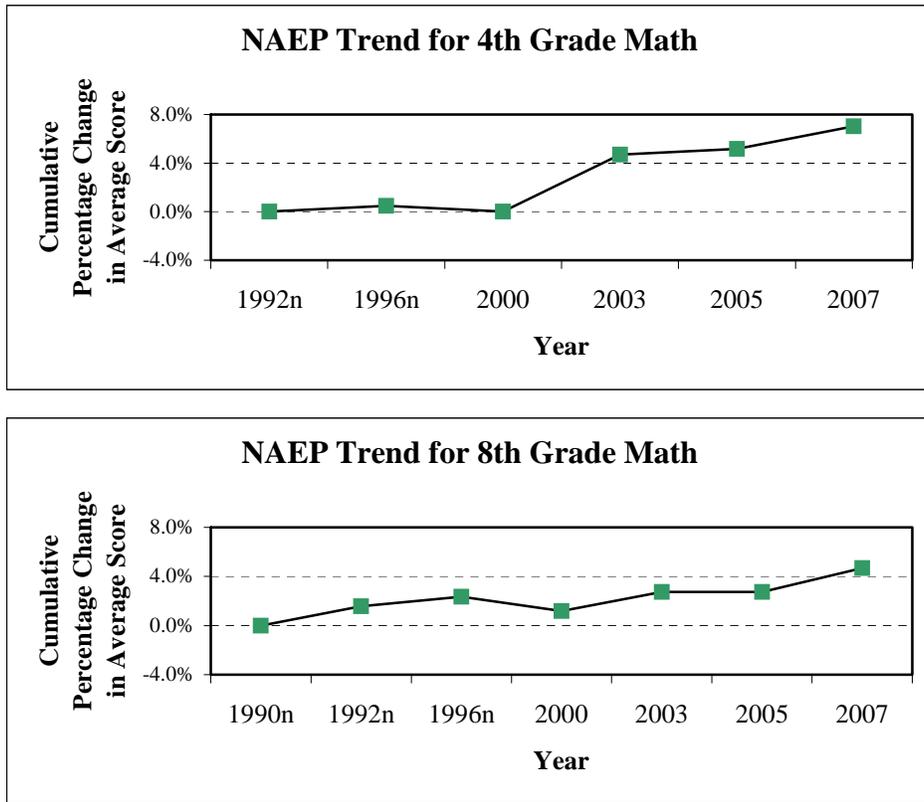
### **No overall improvement in NM's performance since 1990s**

While I will show throughout this paper that overall test scores of New Mexico students have remained stagnant, there is some good news. The good news is that NAEP reports a statistically significant increase in New Mexico students' 4<sup>th</sup> and 8<sup>th</sup> grade math scores since the first year administered. You can get the visual sense of the percentage increase in average scores since 1992 and 1990 in Figure 2.

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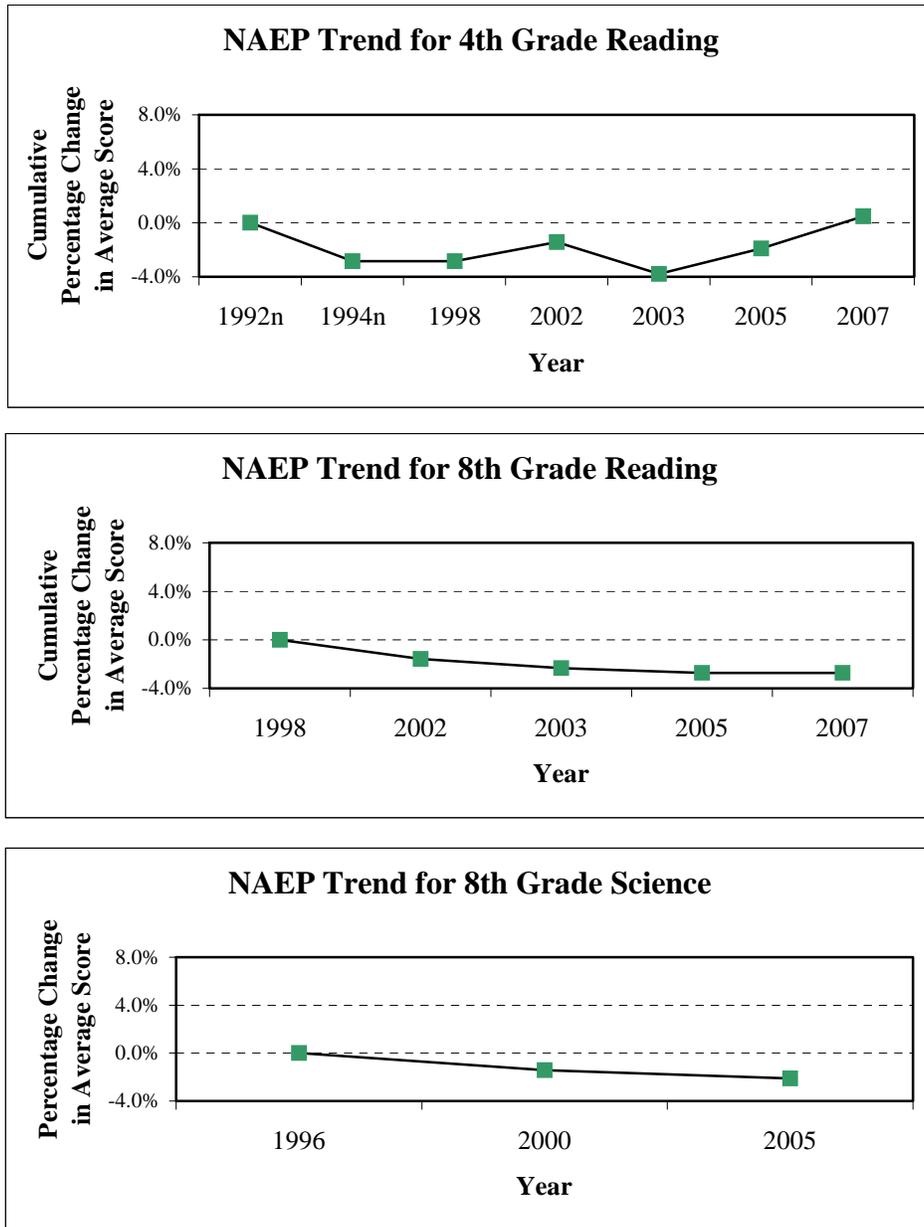
<sup>2</sup> Scores in writing, civics and history do not go back far enough for me to discern a trend.

Figure 2: NAEP trends in Math



Unfortunately, while there is advancement in math, there is bad news for reading and science performance. Figure 3 displays no improvement for 4<sup>th</sup> grade reading since 1992 and downward trends for 8<sup>th</sup> grade reading since 1998 and 8<sup>th</sup> grade science since 1996:

Figure 3: NAEP Trends for Reading and Science



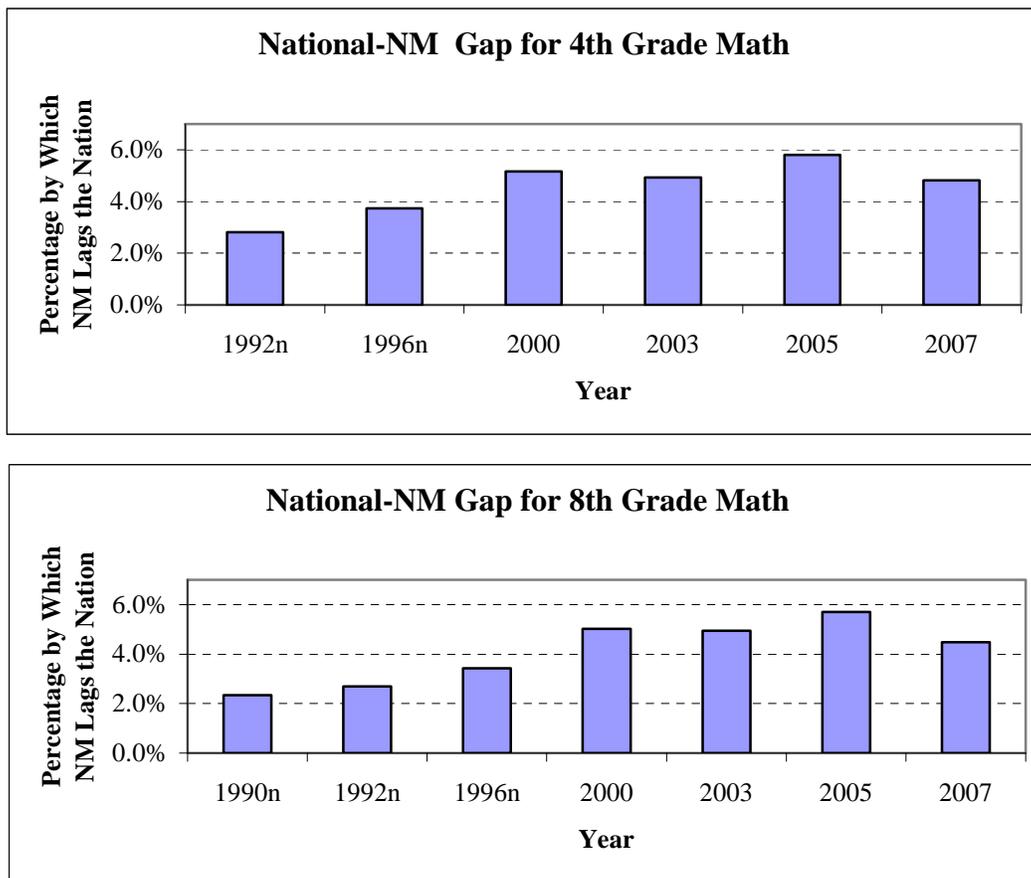
While the trend lines are downward since the first measured year in 8<sup>th</sup> grade reading and science, the NAEP deemed that only in 8<sup>th</sup> grade reading was the decrease “statistically significant.”

From this evidence, it is clear that education performance has stagnated since the tests were first administered some 9 to 17 years ago. Improvements in math have been offset by worsening scores in reading and science.

## New Mexico is falling further behind nation in all measures

As I have just discussed, the overall academic performance of New Mexico's students has been stagnant over the past 9 to 17 years. But New Mexico does not exist in a vacuum. Rather, its citizens and businesses are competing for jobs and economic opportunities with people in other states (not to mention nations). So, how have we done in *average test scores* compared to the rest of the nation? As it turns out, we are not doing so well. In fact, the gap by which the nation leads New Mexico has increased in each of the measured disciplines. You can observe this trend in Figure 4 for math. New Mexico now lags the country by nearly five percent from just over two percent in the early 1990s.

Figure 4: NM lags the nation in math performance by a larger gap since 1992 (4<sup>th</sup> grade) and 1990 (8<sup>th</sup> grade).



Similarly, Figure 5 shows that New Mexico has fallen behind the country in reading by nearly double the gap since 1992 for 4<sup>th</sup> grade reading and roughly four times the gap since 1998 for 8<sup>th</sup> grade reading. New Mexico's performance in reading is downright disgraceful. Forty-two percent of the 4<sup>th</sup> graders failed to perform at the "basic level" for reading in 2007. We are spending thousands of dollars per student yet many of them are turning out to be illiterate.

Figure 5: NM lags the nation in reading performance by a larger gap since 1992 (4<sup>th</sup> grade) and 1998 (8<sup>th</sup> grade)

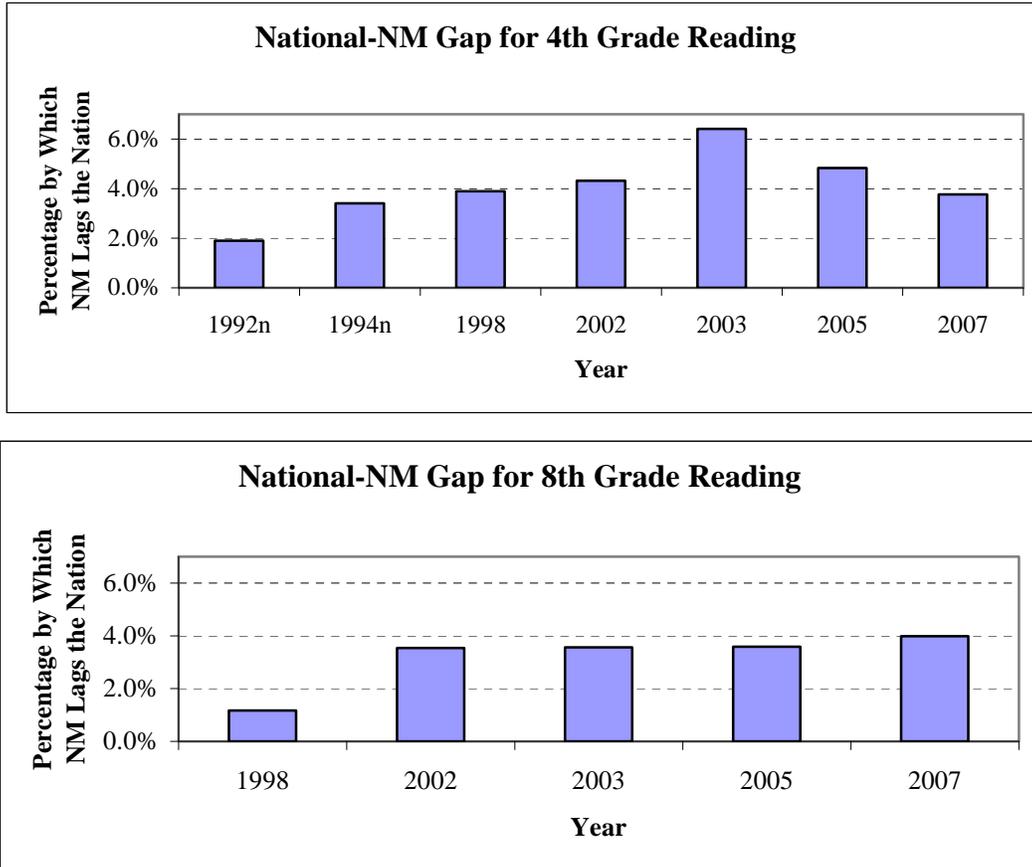
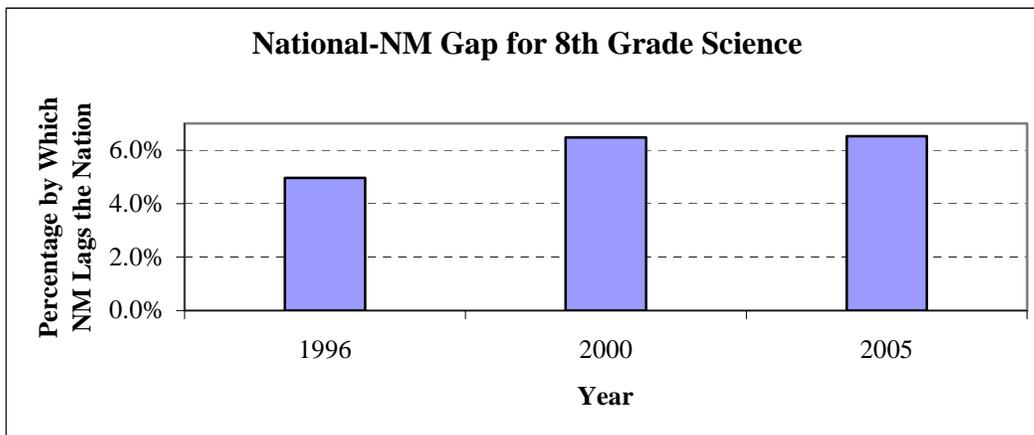


Figure 6: NM lags the nation in science performance by a larger gap since 1996 in 8<sup>th</sup> grade science



It may be hard to believe but over half of New Mexico's 8<sup>th</sup> grade science students scored lower than "basic level" in science in 2005!

That our overall performance is stagnant and lagging the nation by increased amounts over the time period studied is astonishing. How can this possibly be when we have been increasing resources applied to improving performance, and we have been doing so at a faster rate than any other state? Before attempting to solve that puzzle let's take a look at the magnitude of the resources applied.

***Recent History of Resources Used to Produce K-12 Education in New Mexico***

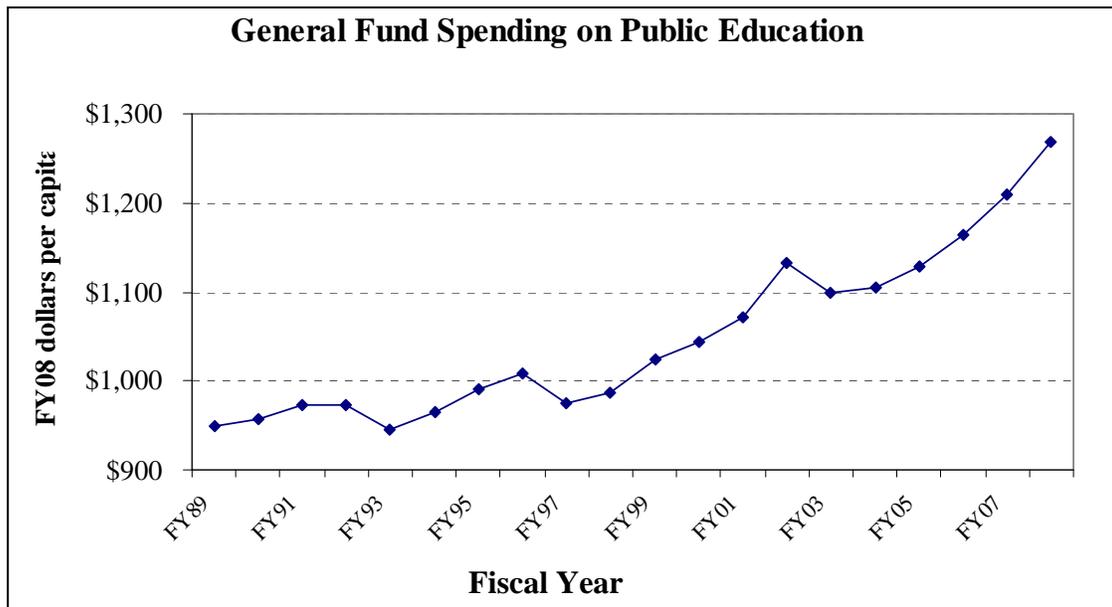
**Thirty-four Percent increase in inflation adjusted, per capita spending from the General Fund over the past 19 years**

Most of what we hear about spending on primary and secondary education comes from the media in their summaries of legislative/executive decisions during each session. Each session deals mostly with the state's "general fund," and education constitutes by far the greatest portion of any line item – roughly 43 percent – of general fund spending.

Since FY 1989, per capita education spending has increased by 34 percent in real terms (that means after being adjusted for inflation and population growth).<sup>3</sup> That means we are spending 34 percent more for each student than we were in 1989. Unfortunately, the 34 percent increase has led to no improvement in performance as I have shown above. That is quite different from the private-sector economy where it is typical that innovation leads to more people being served with a better product, usually at a lower cost than before.

Of course the 34 percent real growth in spending means that New Mexicans pay higher taxes for K-12 education. More explicitly, the per capita tax bill for K-12 education has increased by \$319 since FY 1989 (in FY 2008 dollars). Figure 7 illustrates the spending increase over time:

**Figure 7: Increase in Per capita spending in FY08 dollars**



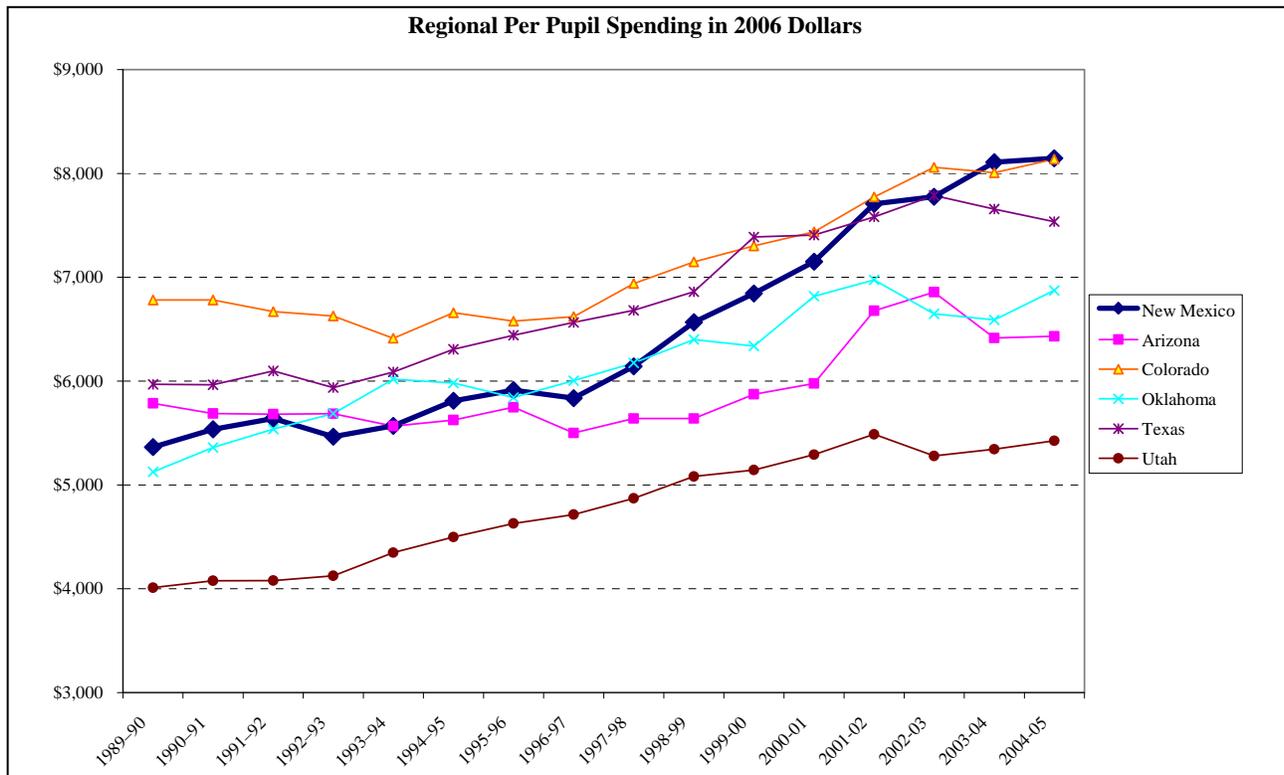
<sup>3</sup> Sources: Legislative Finance Committee, Bureau of Labor Statistics (Consumer Price Index), Bureau of Economic Analysis, Author's calculations

## Growth in inflation adjusted Per Pupil Expenditures have led the nation over the past 15 to 17 years

General fund spending is not the only source of K-12 money. According to data published by the NAEP, the state spent 70 percent of K-12 money in 2005. Federal government (16.5 percent in 2005) and local jurisdictions (13.5 percent in 2005) also added to the spending pot.

The NAEP publishes total per pupil spending from all three sources. With few exceptions<sup>4</sup> New Mexico has far outpaced the nation in the growth of per pupil expenditures since the early 90's.<sup>5</sup> As you can readily see from Figure 8,, we have gone from middle of the pack to the most lavish spending state in the region when it comes to K-12 education.<sup>6</sup>

**Figure 8: Growth of Per Pupil Spending in New Mexico Compared to States in the Region**



Comparing New Mexico to the nation, inflation adjusted, per pupil spending growth from FY90 to FY05 is 52 percent contrasted with 24 percent for the nation as a whole. New Mexico still trails the nation in average per pupil spending, but it rose to 90 percent of the national average in

<sup>4</sup> States that have kept pace with New Mexico are Kentucky, Idaho and West Virginia.

<sup>5</sup> Source: NAEP. Available data are not as recent (last year for good interstate comparisons is FY04) as for those for the general fund. The general fund trend pictured in Figure 7 indicates that there has been no slow down in New Mexico's rush to throw money all over education in the last few budget years.

<sup>6</sup> Source: NAEP.

FY05 from 71 percent in FY90. More recent data, when they become available, will likely show New Mexico closing in on the national average.<sup>7</sup>

The fact that New Mexico spends less than the national average on education may give the impression that we still need to “catch up” to others. But it is important to note that labor costs and other expenses are lower in New Mexico and other western states than they are in New York and New Jersey just to name two high-cost states.

## **Two Problems Identified**

As documented above, New Mexico is now devoting some 52 percent more resources to improving education performance relative to 1990, a percentage increase that puts it at the top (tied with three other states) for the rate of growth of spending. We have also seen that New Mexico’s educational performance is stagnant. That leaves us with two problems to understand and solve in the remainder of the study:

**Contrary to what we would expect (with everything else being equal), significant additional resources have produced no additional performance as measured by widely accepted test scores**

**New Mexico’s performance is falling farther behind the rest of the nation.**

## **Analysis of the Problems: What Is It That Is Not Equal?**

Seen through the eyes of an economist, the total lack of productivity<sup>8</sup> in government schools leads to an examination of the incentives within the system. Unfortunately, the incentives that have been created by New Mexico’s K-12 system are quite different from those that would otherwise be found in a market setting. That is the “what is not equal” part—the part that generates the increasing productivity we enjoy just about everywhere else in our lives but which is absent in K-12 education. Let’s examine the incentives of parents as the consumers of their kids’ schooling and the incentives of those who provide the schooling to satisfy those consumers.

### ***What are the options of parents as consumers of K-12?***

In the United States, in most spheres of our everyday lives, we are used to selecting from a wide range of alternatives with every purchase we make. Such is the benefit of the substantial economic freedom with which we are blessed. If I am unhappy with a product or service, then I am free to obtain a similar product or service elsewhere. Only those businesses that satisfy me get my business.

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<sup>7</sup> Per capita general fund spending alone has increased by 15 percent since FY04 in today’s dollars.

<sup>8</sup> Economists define productivity as the additional output (performance) obtained from additional resources. In New Mexico we have added well over 50 percent additional resources since 1990 but we have obtained zero additional performance.

That freedom is greatly reduced when it comes to primary and secondary education. Simply put, most parents, especially those who are less well to do, cannot afford the option of moving their kids to another school when they are unhappy with their current school. After all, if they had the means they could easily move their kids to a private school or relocate to another school district.<sup>9</sup> Like it or not, however, most low-income adults have to pay taxes to support, and ultimately send their kids to, government schools.

We often hear education officials lament that “parents should be more involved in their schools.” But parents have virtually no say in how their kids are schooled, and thereby have very little incentive to “be involved.” In New Mexico (even more-so than in other states due in part to the state’s statewide funding regime) schools are governed from the top down. Decisions about how children are to be schooled are made in Santa Fe and Washington. The result is a one-size-fits-all product. If the shoe doesn’t fit, the consumer still has to wear it.

The recent principle shuffling at the Albuquerque Public Schools is a perfect example of parents’ lack of influence. Between the end of the 2006-2007 and the start of the 2007-2008 school years 16 principals and several assistant principals were shifted as a result of dictates coming from the central offices of the public schools.<sup>10</sup> Theoretically designed to shift better principles to underperforming schools (and presumably shift worse principles to better schools), the principle shuffle is just another example of bureaucratic meddling and ignoring parent concerns.<sup>11</sup>

### ***What are the incentives within government schools to improve performance?***

Another reason for the lack of improvement in our educational system is the Soviet style command and control system under which our schools operate. Since parents essentially have no clout if they are dissatisfied with their kids’ current school, there is no incentive on the part of those in charge to adapt to their wishes or compete for schooling their kids. They have a government sponsored monopoly on schooling, and we as consumers suffer the zero productivity consequences.

### ***How much do lack of parental options and teachers’ incentives to innovate in government schools affect K-12 performance?***

Blaming a lack of choice in today’s educational system is not enough. These assertions must be backed up with hard evidence. I test that assertion empirically by analyzing educational performance as a function of resources (as measured by per pupil spending) and freedom of choice by education consumers (as measured by the proportion of spending that is provided at the local level). We would expect that more resources put into education leads to greater performance. The freedom of choice measure requires a bit more explanation.

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<sup>9</sup> The so called “No Child Left Behind” federal law supposedly allows parents to move their kids to another school from a “failing” school. In practice the law has not been effective in allowing even that kind of choice.

<sup>10</sup> Susie Gran, “District Planning Principal Shuffle,” *Albuquerque Tribune*, May 8, 2007, <http://www.abqtrib.com/news/2007/may/08/district-planning-principal-shuffle/> .

<sup>11</sup> Susie Gran, “Principal Reassignments Rile Parents, Teachers,” May 26, 2007, <http://www.abqtrib.com/news/2007/may/26/principal-reassignments-rile-parents-teachers/> .

We would like to measure how much freedom of choice education consumers have in each state. Unfortunately we have no such direct measure. But we have a proxy measure. In other words, we have a measure that should vary directly with the degree of freedom of choice available to education consumers in each state. That measure is the proportion of state education spending that comes from the local level.

Federal and state money comes to localities only with strings attached (more regulations, certification requirements, standards and so forth). The greater the proportion of local funding, the fewer the number of strings attached to that funding. Greater proportion of local funding should mean more choice. More choice is a result of greater local autonomy, thus making it less costly for consumers to move from a district they don't like to a district they like better. And the threat of outmigration helps discipline school administrators to provide what consumers want. After all, no administrator likes to see an exodus from her district.

Good data are available from NAEP in the late 90's to measure performance, per pupil spending and the proxy measure for freedom of choice in 43<sup>12</sup> states.

### **Education performance in the states**

We are interested in how performance is affected by resources (measured by per pupil spending) and education freedom (proxy measurement by percentage of local spending). Our measure of performance is based on NAEP test scores from the 43 states that participated in at least two of the exams during the period studied. The score for each exam for each state is converted to estimated standard deviations from the mean. Then the scores are combined into an overall performance measure for each state with the result from each exam receiving equal weight. The results are displayed in

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<sup>12</sup> Seven states did not participate in at least two exams for NAEP testing, so their performance measures are unavailable.

Table 1.

**Table 1: Measures of Education Performance by State**

**Performance in standard deviations from the US mean (blank cells indicate no test)**

<i>STATE</i>	<i>4th grade NAEP reading (1998)</i>	<i>8th grade NAEP reading (1998)</i>	<i>8th grade NAEP writing (1998)</i>	<i>4th grade NAEP math (1996)</i>	<i>8th grade NAEP math (1996)</i>	<i>8th grade NAEP science (1996)</i>	<i>Equally Weighted Average</i>
Alabama	-0.79	-1.63	-1.07	-1.64	-1.51	-1.13	-1.30
Alaska				0.18	0.96	0.50	0.55
Arizona	-1.11	-0.49	-0.46	-0.91	-0.69	-0.50	-0.69
Arkansas	-0.95	-1.31	-1.69	-1.28	-1.37	-0.63	-1.20
California	-1.42	-1.47	-0.61	-1.64	-0.82	-0.88	-1.14
Colorado	0.79	-0.16	0.46	0.37	0.27	0.63	0.39
Connecticut	2.69	1.79	3.07	2.01	1.10	1.13	1.96
Delaware	-0.63	-0.98	-0.31	-0.73	-0.55	-0.75	-0.66
Florida	-0.95	-1.31	-0.77	-0.91	-0.82	-0.75	-0.92
Georgia	-0.79	-0.98	-0.15	-1.28	-0.96	-0.75	-0.82
Hawai'i	-1.90	-1.96	-1.38	-0.73	-0.96	-1.50	-1.40
Indiana				0.73	0.14	0.38	0.41
Iowa	0.95			0.37	1.10	1.13	0.88
Kansas	0.79	0.65					0.72
Kentucky	0.00	-0.33	-0.46	-0.73	-0.96	-0.50	-0.50
Louisiana	-1.58	-2.12	-1.84	-2.19	-2.20	-1.75	-1.95
Maine	1.11	1.79	1.23	1.28	1.10	1.75	1.38
Maryland	0.00	0.00	-0.15	0.37	0.14	-0.25	0.02
Massachusetts	1.26	0.82	1.07	0.73	0.69	1.25	0.97
Michigan	-0.16			0.55	0.69	0.63	0.43
Minnesota	1.11	0.98	0.15	1.64	1.51	1.25	1.11
Mississippi	-1.74	-1.96	-1.99	-2.19	-2.20	-1.88	-1.99
Missouri	0.00	-0.33	-1.07	0.00	-0.14	0.13	-0.24
Montana	1.26	1.14	0.15	0.37	1.24	1.75	0.99
Nebraska				0.73	1.10	1.00	0.94
Nevada	-1.26	-1.14	-1.07	-1.10			-1.14
New Mexico	-1.11	-1.14	-0.92	-1.28	-1.24	-1.00	-1.11
New York	0.00	0.49	-0.46	0.00	-0.14	0.00	-0.02
North Carolina	-0.16	0.00	0.46	0.18	-0.41	-0.38	-0.05
North Dakota				0.73	1.37	1.75	1.29
Oklahoma	0.16	-0.33	0.15				0.00
Oregon	-0.16	0.33	0.46	0.18	0.41	0.63	0.31
Rhode Island	0.47	-0.16	0.15	-0.55	-0.41	-0.13	-0.10
South Carolina	-1.11	-1.47	-1.38	-1.46	-1.24	-1.25	-1.32
Tennessee	-0.63	-0.82	0.00	-0.55	-1.10	-0.63	-0.62
Texas	0.00	-0.49	1.07	0.91	-0.27	-0.50	0.12
Utah	-0.16	0.00	-0.46	0.55	0.14	0.63	0.12
Vermont				0.55	0.55	0.88	0.66
Virginia	0.16	0.33	0.46	-0.18	-0.27	0.00	0.08
Washington	0.00	0.16	0.15	0.18	0.41	0.00	0.15
West Virginia	0.00	-0.65	-0.92	-0.18	-1.24	-0.75	-0.62
Wisconsin	0.79	0.33	0.61	1.28	1.24	1.50	0.96
Wyoming	0.16	-0.33	-0.15	-0.18	-0.14	0.88	0.04

## Per Pupil Spending and Education Freedom Proxy

Table 2: Per pupil spending and education freedom proxy (measured by percentage of spending under local control) data from NAEP for academic year 1999-2000:

<i>STATE</i>	<i>Per Pupil Spending</i>	<i>Proxy for Education Freedom</i>
Alabama	\$ 5,626	30.5%
Alaska	\$ 6,744	29.8%
Arizona	\$ 4,679	51.1%
Arkansas	\$ 5,596	34.8%
California	\$ 5,235	36.3%
Colorado	\$ 5,832	54.3%
Connecticut	\$ 8,097	62.6%
Delaware	\$ 7,508	31.3%
Florida	\$ 6,008	47.2%
Georgia	\$ 6,278	41.3%
Hawai'i	\$ 6,020	2.6%
Indiana	\$ 7,156	49.6%
Iowa	\$ 7,126	46.7%
Kansas	\$ 6,639	41.1%
Kentucky	\$ 6,678	31.6%
Louisiana	\$ 6,052	42.3%
Maine	\$ 7,012	53.4%
Maryland	\$ 6,795	59.1%
Massachusetts	\$ 6,747	54.4%
Michigan	\$ 6,997	29.3%
Minnesota	\$ 7,384	42.9%
Mississippi	\$ 5,243	36.2%

<i>STATE</i>	<i>Per Pupil Spending</i>	<i>Proxy for Education Freedom</i>
Missouri	\$ 5,674	47.8%
Montana	\$ 6,552	47.9%
Nebraska	\$ 6,967	65.1%
Nevada	\$ 5,717	33.3%
New Mexico	\$ 5,866	16.2%
New York	\$ 8,174	57.8%
North Carolina	\$ 5,934	32.8%
North Dakota	\$ 6,486	54.8%
Oklahoma	\$ 6,120	34.1%
Oregon	\$ 6,584	44.0%
Rhode Island	\$ 7,191	58.3%
South Carolina	\$ 6,179	42.8%
Tennessee	\$ 5,508	47.2%
Texas	\$ 6,034	53.4%
Utah	\$ 4,049	33.2%
Vermont	\$ 7,408	76.0%
Virginia	\$ 7,068	56.8%
Washington	\$ 5,826	28.7%
West Virginia	\$ 8,322	31.6%
Wisconsin	\$ 7,847	42.5%
Wyoming	\$ 7,853	47.9%

## Regression Results

I ran the following ordinary least squares regression:

1. Dependent variable: education performance as displayed by the last column in

Table 1.

2. First independent variable: per pupil spending as displayed by the first column in Table 2. Expected regression result is that more resources should result in better performance.
3. Second dependent variable: proxy for education freedom (percentage of spending controlled at the local level) as displayed in the second column of Table 2. Expected regression result is that more education freedom should result in better performance.

The results were quite good for cross section data. The regression explained 36 percent of the variation<sup>13</sup> among states. Both dependent variables had the expected influence on performance and were statistically significant.<sup>14</sup>

### Interpretation of results

The estimates for the regression coefficients were as follows:

Independent Variable	Estimated Coefficient
Resources as measured by per pupil spending	$3.712 \times 10^{-4}$
Education freedom as measured by percentage of spending controlled locally	2.712

These estimates help us understand why New Mexico has been unable to improve its performance despite the significant increase in resources documented in Figure 8 . As New Mexico has been adding resources, its “reforms” have been reducing education freedom. Each so called “reform” seems to add more regulation, more certification, and more centralization. These policies are exactly the opposite of what would make the education system more responsive to parents and thereby improve performance.

There is an easy way to improve performance. The magnitude of the estimated coefficient for education freedom suggests that an increase of education freedom of 41 percentage points would put New Mexico on par with the rest of the nation.

This achievement would be no trivial matter. If New Mexico caught up to the national average we would see 80 percent of 4<sup>th</sup> grade math students perform at the “basic level” or better compared to 65 percent in 2005. Similarly 69 percent of 8<sup>th</sup> grade math students would perform at the basic level or better compared to 53 percent in 2005. For reading students 4<sup>th</sup> graders would improve their performance to 64 percent at basic or better (compared to 51 percent in 2005), and 8<sup>th</sup> grade students would improve their performance to 73 percent at basic or better (compared to 62 percent in 2005).

Of course there are many ways we can go about increasing education freedom and, since we were using a proxy for education freedom to estimate its effect, saying we should increase

<sup>13</sup> As measured by adjusted R-Squared.

<sup>14</sup> The “t-statistics” were 2.83 for per pupil spending were and 3.00 for the education freedom proxy.

education freedom by a specific number of percentage points is overly vague.<sup>15</sup> Exactly how we can improve performance considering the political hurdles involved is the subject of the next section.

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<sup>15</sup> In an attempt to remove this vagueness the Cato Institute has recently completed a study of how well existing school systems resemble free markets. See Coulson, Andrew J. *The Cato Education Market Index*, Policy Analysis No. 585 of December 14, 2006.

## Parental Choice Is The Solution

There is enormous room for improvement in our educational system. Hardly any activity in the United States is technically more backward. We essentially teach children the same way we did 200 years ago: one teacher in front of a bunch of kids in a closed room. The availability of computers has changed the situation but not fundamentally. Computers are being added to public schools, but they are typically not being used in an imaginative and innovative way.

Milton Friedman 1995<sup>16</sup>

There are many ways to improve the incentives of parents, teachers and school administrators so that they interact in ways that lead to better education performance. Unfortunately, in recent years New Mexico has been weakening these incentives, not strengthening them.

We have seen over the past 20 years, in the guise of one reform after another, increased requirements for certification, more command and control by the state, and more regulation of what is taught and how it is taught. States, including New Mexico, have been further hampered by the so-called “No Child Left Behind” onerous federal requirements and paperwork.<sup>17</sup> The bottom line is that more centralization and bureaucracy reduce the ability of parents to seek alternative schooling.

On the plus side, however, a bipartisan task force of the National Governor’s Association has recently issued a report<sup>18</sup> recommending that states expand the range of educational choices available to families. Our own Governor Richardson was one of the governors issuing the report.<sup>19</sup> The report recommends charter schools, virtual schools and tuition assistance for private schools as specific ways to improve the choices available to families.

The counterproductive direction toward more centralization in New Mexico over the past couple of decades does not bode well for the likelihood of redirecting authority and decision making back to the local level.

Thus, rather than directly battling an entrenched education bureaucracy to remove or alter regulations that have been imposed at both the federal and state levels, it might make sense first to target low-income students who tend to get stuck in the worst performing schools with no way around it. One way to do this is to offer the parents of lower-income students tuition assistance that can be used to attend private schools.

The “tax credits” approach was just one of the approaches recommended by the National Governors Association in their report. I, for one, agree that such a move would provide needed

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<sup>16</sup> *Washington Post*, February 19, 1995 reprinted in *An Education Agenda: Let Parents Choose Their Children’s School*, Pete du Pont, project chairman, John C. Goodman and Fritz F. Steiger, eds., National Center for Policy Analysis, 2001

<sup>17</sup> States may opt out of this federal law, but they have to give up the money if they wish to release the strings that are attached to it. Bureaucracies are loathe to give up money.

<sup>18</sup> *Providing Quality Choice Options in Education*, report of the National Governors Association, undated (released about August 29, 2005) <http://www.nga.org/Files/pdf/EDUCATIONCHOICE.PDF> .

<sup>19</sup> The others were Janet Napolitano (Arizona), Tim Pawlenty (Minnesota), Haley Barbour (Mississippi), Mark Sanford (South Carolina) and Jon Huntsman (Utah).

innovation outside of the public school system, without diverting resources from existing public schools. An overview of how that might be done is the focus of the remainder of this report.

### ***Tuition Tax Credits: Assisting New Mexico's Neediest Children***

Tuition tax credits are an excellent way to introduce parental choice and an element of competition into the New Mexico education system. Here are the basic characteristics of tuition tax credits<sup>20</sup>:

1. Tuition tax credits allow taxpayers to donate money for scholarships so that poor children may attend independent schools.
2. Unlike vouchers, the money for the scholarships is contributed by taxpayers and does not come from the government. Taxpayers eligible to take the credit (at no personal financial benefit) can be individuals, corporations or both.
3. Limits are often placed on the amount individuals and companies may contribute as well as an overall limit on the amount that may be diverted to tax credits.
4. Each donation is made to a scholarship granting organization of the donor's choice. Scholarship granting organizations determine who gets scholarships and how much they get based on criteria in the enabling legislation.
5. Each scholarship granting organization should be registered with the IRS as a non-profit organization under section 501(c)(3) of the tax code and be subject to audit requirements. Other than that regulations should be minimal. By having the ability to opt out, parents themselves become the primary regulators. Since the entire system relies on individual and corporate taxpayers for funding, yet another watchdog is added.

Tuition tax credits may be politically viable. They do not conflict with the interests of the teaching establishment except to add an element of competition. Similar legislation has passed in Iowa, Arizona, Pennsylvania, and Florida, usually with bi-partisan support. New York Governor Eliot Spitzer (a Democrat), supports tax credits, but not vouchers for education.<sup>21</sup>

It is the poor by far who are the biggest losers in New Mexico's education system. Scholarships for the poor would give those parents more freedom to escape demonstrably failing schools. By structuring the scholarships so that most of the benefits go the poor, tuition tax credits should get political traction in New Mexico. Operationally this can be done by constraining scholarship granting organizations so that the poorer the recipient the bigger the scholarship. Specifically, scholarships could be granted based on the grantees federally determined poverty level. For example, the scholarships might be granted as shown in Table 3.

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<sup>20</sup> More detail may be found in the publication Forster, Greg, *Funding School Choice: a Road Map to Tax-Credit Scholarship Programs and Scholarship Granting Organizations* dated June 1, 2006 at <http://www.friedmanfoundation.org/friedman/research/ShowResearchItem.do?id=10076> .

<sup>21</sup> Eliot Spitzer, "Statement by Attorney General Eliot Spitzer Regarding Education Tax Credits," NY Department of Law, January 19, 2006, [http://www.oag.state.ny.us/press/2006/jan19c\\_06.html](http://www.oag.state.ny.us/press/2006/jan19c_06.html) .

Eligible families are those from zero percent to 400 percent of the federal poverty level. Families at zero percent poverty would qualify for \$4000 scholarship. The scholarship amount would phase out at the rate of \$10 per percentage point increase in the poverty level until it reaches zero at 400 percent of poverty.<sup>22</sup> The scholarship amounts should be adjusted annually for inflation just as is the federally determined poverty level. The specific schedule shown is easily amendable to accommodate a different zero percent of poverty scholarship threshold or phase out rate. I am not wedded to this particular one, but I do think it would work well to achieve the desired results.

**Table 3: Proposed Schedule of Scholarship Grants**

Percent of Poverty	Scholarship Amount
0%	\$4,000
25%	\$3,750
50%	\$3,500
75%	\$3,250
100%	\$3,000
125%	\$2,750
150%	\$2,500
175%	\$2,250
200%	\$2,000
225%	\$1,750
250%	\$1,500
275%	\$1,250
300%	\$1,000
325%	\$750
350%	\$500
375%	\$250
400%	\$0

### ***Budget Impact***

The next obvious question is how would this scholarship schedule affect the state's budget?<sup>23</sup> Once the scholarships are implemented we can expect most parents of the roughly 21,000 students who are eligible and already attending independent schools to apply for them. That means the state will lose the tax revenue that goes to fund those scholarships (parents were previously footing the bill without scholarship assistance).

The main issue is how will those currently in government schools respond to the availability of scholarships? Each student who migrates from a government school to an independent school saves the state money because the scholarship amount (which represents lost tax revenue for the

<sup>22</sup> Annual income for a family of four at the 100% level of poverty is \$20,650.

<sup>23</sup> A well done prior budget analysis of tax credits focused on another scheme for providing the scholarships. See *The Fiscal Impact of Tuition Tax Credits in New Mexico* by Brian J. Gottlob dated April, 22, 2005. That study may be found at <http://www.friedmanfoundation.org/friedman/research/ShowResearchItem.do?id=10016> .

state) is more than offset by the reduced cost of having to school the student who chose to migrate.

Fortunately, it is relatively simple to estimate the expected budgetary impact a tax credit program would have on the state budget. This is based on observed behavior of parents in deciding whether or not to send their children to independent schools in New Mexico. Based on data from a 2000 Census Bureau sample,<sup>24</sup> it is easy to see that parental decisions are quite responsive to changes in income.

In the poverty level range from zero to 400 percent the income elasticity of demand for independent schools has been found to be approximately 1.4. That means a one percent increase in income tends to trigger a 1.4 percent increase in migration to independent schools within that population. Say, for example, that there were 1000 children of parents who earn \$40,000 per year attending independent schools. If all parents earning that amount receive an income increase of \$400 per year (one percent increase), then we would expect 14 additional children to attend independent schools (a 1.4 percent increase from 1000).

The potential scholarship offer is in essence an increase in income for the family should they choose to accept it. If scholarships are based on the schedule in Table 3 and they are fully funded (that is if everyone eligible gets their prescribed scholarship), it would reduce state tax collections net of expenditures for scholarships by approximately \$33 million per year in current dollars.<sup>25</sup> Assuming that one-third of all scholarship applicants are approved in each of the first three years of the program, it would cost the state about one-third of that amount each year to fund it. Since new scholarship granting organizations cannot form overnight, that is the likely scenario.<sup>26</sup>

Beyond the one-third of applicants per year for each of the first three years criterion, the estimate does not limit scholarships for eligible students currently attending independent schools. To do so would, in my opinion, not be fair. The parents of those students have already sacrificed their tax dollars and their tuition money to educate their kids; and they have saved the state money by not sending their kids to government schools. How could we penalize them by less favorable treatment than those who have not so sacrificed? Penalizing them would save only six-tenths of one percent of the general fund budget.<sup>27</sup>

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<sup>24</sup> I thank Brian J. Gottlob for giving me access to the Census data.

<sup>25</sup> The estimate was obtained by application of the state's STATE EQUALIZATION GUARANTEE COMPUTATION, annual per pupil estimates for capital outlays, updating student population estimates in proportion to increase in state population since 2000, a ten percent overhead cost for scholarship granting organizations and the author's calculation of income elasticity of demand for independent schools. RGF will be happy to provide details by separate correspondence on request.

<sup>26</sup> The actual supply of independent school space is unlikely to be a problem. There is space available in existing independent schools; and start-ups or existing independents have flexibility in obtaining space since they are not constrained by necessity of capital outlays as is the case for government schools.

<sup>27</sup> Legislators in other states have not shared my sense of fairness. They have limited scholarships going to existing independent school students so that the predicted fiscal effect would be zero.

More detailed fiscal estimates can be made once the legislature and governor agree to specific structures on the demand and supply side of the credits. The good news is that tuition tax credits in other states have actually resulted in fiscal benefits.<sup>28</sup>

## Conclusion

New Mexico's K-12 schools' overall performance has not improved during the last two decades. Worse, while there is no doubt that large numbers of teachers and administrators may care deeply about the children they are attempting to educate, New Mexico's educational system is falling behind the rest of the country. Incredibly this has occurred despite the dedication of over 50 percent more resources per student over that time. Unfortunately, more resources alone are not enough to improve results. Systemic changes need to be made; changes that will motivate parents and teachers to get better results.

Giving parents more say in how and where their kids are schooled will alter the incentives inherent in the current system, giving the system an element of competition and thereby encouraging innovation and improved performance. Tuition tax credits that are directed to the poor are the way to achieving success.

Doing for the next 20 years what we have done for the last 20 years risks allowing New Mexico students to fall even further behind their peers throughout the country.



## About the Author

**Harold C. “Harry” Messenheimer** is senior fellow with the Rio Grande Foundation. He holds a Ph.D. in economics from George Mason University and has taught at George Mason University, Troy State University and the University of Richmond. Among the studies he has authored for the Rio Grande Foundation are *Reform This!: Coherent Tax Strategies for New Mexico*; *Tax Policy Briefing: Why Does New Mexico's Economy Underperform Compared to Its Neighbors?*; *Lower Taxes – Period: The Right Way to End the Food Tax*; and *Solutions to the Medicaid Crisis in New Mexico* (with Kenneth M. Brown, Ph.D.). All these studies and more are available at [www.riograndefoundation.org](http://www.riograndefoundation.org).

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<sup>28</sup> See *Saving Money and Improving Education: How School Choice Can Help States Reduce Education Costs* by David Salisbury, Policy Analysis No. 551, Cato Institute, October 4, 2005. This study omits analysis of the supply side of independent schools; and that tends to increase savings resulting from school choice.