HB 951

Department of Legislative Services

Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 951 (Delegate Tarlau, *et al.*)

Ways and Means and Appropriations

Higher Education Degree and Job Certification Without Debt Act of 2018

This bill establishes a number of initiatives intended to reduce the costs of attending higher education in the State. Subject to specified limitations, the bill imposes a 19% State income tax on certain income that is attributable to investment management services provided in the State. The revenue generated by the tax is distributed to the new Higher Education Affordability Trust Account (HEATA) and can only be used to pay for the initiatives mandated by the bill. **The bill takes effect July 1, 2018, and applies to tax year 2018 and beyond.**

Fiscal Summary

State Effect: HEATA revenues increase significantly, *potentially* by an estimated $78.0 million in FY 2019 and $58.0 million in FY 2023. HEATA expenditures increase by $55.3 million in FY 2020, increasing to $127.4 million in FY 2022, often relying on available fund balance as shown below. To the extent HEATA revenues are less than estimated, general fund expenditures increase to cover mandated appropriations in the bill. General fund expenditures increase by $172,000 in FY 2019 for one-time expenses and may increase beginning in FY 2022 for funding formulas. **This bill establishes mandated appropriations beginning in FY 2020.**

($ in millions)	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
SF Revenue	$78.0	$75.0	$72.0	$70.0	$58.0
GF Expenditure	$0.2	$0	$0	-	-
SF Expenditure	$0.1	$55.3	$92.4	$127.4	$73.0
Net Effect	$77.8	$19.7	($20.4)	($57.4)	($15.0)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate increase; (-) = indeterminate decrease

Local Effect: State aid to local community colleges increases by an estimated $237,500 beginning in FY 2020 to provide support services to students. To the extent local community college enrollment increases due to the bill, tuition and State aid revenues increase in the out-years; however, this impact cannot be reliably estimated. Capping local community college tuition growth likely has minimal effect on community college revenues, as explained below.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: As described in more detail below, the bill establishes a number of initiatives intended to reduce the costs of attending higher education in the State including the following: (1) the Maryland Community College Promise Program, which phases in a grant to provide specified income-eligible students 100% of tuition at community colleges for an associate's degree or a certificate program, beginning in fiscal 2020; (2) programs for students nearing the completion of a degree; (3) specified tuition caps for public four-year institutions and community colleges; and (4) increases in State funding for need-based scholarships and maximum grant amounts.

Maryland Community College Promise Program

The bill establishes a Maryland Community College Promise Program to provide an opportunity for community college students to earn an associate's degree or certificate debt free. The Maryland Higher Education Commission (MHEC) must administer the program. MHEC must make the program available beginning in the 2019-2020 academic year (fiscal 2020). Grants are provided on a first-come, first-served basis initially; after the first year, prior-year recipients who remain eligible are funded first and then new recipients on a first-come basis. Recipients must agree to reside exclusively in Maryland and be employed in Maryland for a continuous number of years equal to the duration of the grant. Recipients who do not comply with those requirements will have their grant converted into a loan.

To be eligible to receive a grant under the program, a recipient must have a federal adjusted gross income of no more than $150,000. The recipient's income is the combined adjusted gross income of the applicant and the applicant's parents or the applicant and the applicant's spouse, if the applicant is married. A recipient must meet the income limitations for each academic year in which the recipient participates in the program.

Each grant applicant must meet specified eligibility criteria, including enrolling full time and graduating from a Maryland public secondary school or having received a GED (*i.e.*, completed general educational development testing) no more than 12 months before first receiving a grant. The maximum grant for the 2019-2020 academic year is $1,000. Maximum grant amounts increase by $1,000 per year until the 2022-2023 academic year and each year thereafter when the maximum grant amount is 100% of tuition. Except under specified extenuating circumstances, a grant is for up to two academic years of continuous full-time enrollment.

All nonloan aid received by the recipient must be credited to the recipient's tuition before the calculation of the grant amount provided under the program. In general, the grant must be used at the recipient's local community college.

For a recipient enrolled in a program that leads to the issuance of a certificate, a grant under the program is limited to one certificate.

The Governor must include in the State budget the following amounts for the promise program: $32.0 million in fiscal 2020; $40.0 million in fiscal 2021; $45.0 million in fiscal 2022; and $50.0 million in fiscal 2023 and each fiscal year thereafter.

In addition, beginning in fiscal 2020 and in each fiscal year thereafter, the Governor must include in the State budget $250,000 to be distributed to the public community colleges in the State proportional to the number of full-time equivalent students (FTES) included in the calculation of the Senator John A. Cade and Baltimore City Community College (BCCC) funding formulas to be used to fund support services for students who have received a grant under the Maryland Community College Promise Program.

MHEC must adopt procedures to administer the program, and the commission may adopt regulations necessary to carry out the Maryland Community College Promise Program.

By December 1, 2019, and each December thereafter, MHEC and each public community college must submit a report to the General Assembly on the implementation of the program, including specified elements.

Near Completers Match and Grant Programs

MHEC must implement a statewide communication campaign for near completers, who are individuals who have completed some college credits but have not received a degree and are no longer enrolled. The Governor must include $250,000 in the State budget in each of fiscal 2020 through 2024 for the communication campaign. MHEC must also develop and implement a centralized web-based match program for near completers that facilitates the matching of a near completer with any institution of higher education at which the near completer would be able to complete the degree. MHEC must encourage each institution of higher education in the State to participate in the match program at no cost to the institution. For fiscal 2020 through 2024, the Governor must include in the State budget $50,000 for the match program.

An institution that participates in the match program must provide MHEC with information regarding near completers who attended the institution, as requested by MHEC and in the format identified by MHEC. On receipt of this information, MHEC must (1) determine any matches between a near completer and institutions and (2) send information to the near completer regarding the matches, any incentives offered for near completers by the State or by the institutions, and any other financial aid available to the near completer.

Individuals must meet specified eligibility criteria to receive a near completer grant including credit hours completed and a minimum grade point average (GPA) of 2.0. Grants are on a first-come, first-served basis, and as provided in the State budget. Maximum grant amounts are specified.

The Governor must include $500,000 for fiscal 2020 and $750,000 for fiscal 2021 through 2024 in the State budget for near completer grants. A near completer grant may be used only for tuition and may not be used for fees or other charges or expenses related to attending an institution of higher education. All nonloan aid received by near completers must be credited to their tuition before the calculation of the grant amount provided.

By December 1, 2019, and every December 1 thereafter through 2025, MHEC must submit a report to the General Assembly on the details of the statewide communication campaign and the match program, including implementation of the campaign and match program and a detailed account of the expenditures under the grant program established in the bill.

Finally, the bill repeals the existing near completer program.

Public Four-year Institutions of Higher Education Tuition Increase Cap and Buy Down

A public four-year institution of higher education may not impose an increase in resident undergraduate tuition of more than 2% over the amount charged for tuition at the institution in the preceding academic year from fall 2019 through fall 2021 (*i.e.*, fiscal 2020 through 2022). For fiscal 2020 through 2022, the Governor must provide in the State budget an appropriation of general funds (or from the Higher Education Investment Fund or HEIF) to the respective governing boards in an amount equal to a 3% increase in the resident undergraduate tuition over the prior fiscal year. For fiscal 2021 and 2022, the amount that was required to be appropriated to the respective governing boards in the prior year must be included when calculating the amount required in the current fiscal year.

Community College Tuition Increase Cap

Beginning in the 2019-2020 academic year (fiscal 2020), a local community college in the State or BCCC may not increase the in-county tuition rate over the prior year by more than the increase in the three-year rolling average of the State's median family income.

Need-based Scholarships

The need-based scholarship programs are specified to be the Delegate Howard P. Rawlings Educational Excellence Awards (EEA) program, the Part-time Grant program, and the Graduate and Professional Scholarship Program.

Subject to the need described below, the Governor must include in the State budget the following amounts for need-based programs: $90.0 million in fiscal 2020; $97.5 million in fiscal 2021; $105.0 million in fiscal 2022; $112.5 million in fiscal 2023; and $120.0 million in fiscal 2024 and each fiscal year thereafter. However, if all students eligible for a need-based program award have received an award in the current fiscal year, the amount required for the following fiscal year must be equal to the amount provided in the current fiscal year.

Educational Assistance Grant

The maximum amount of the Educational Assistance (EA) grant is increased from $3,000 to $3,100 in fiscal 2020, then increasing by $100 per year until the grant is fully phased in at $3,500 in fiscal 2024 and every year thereafter.

Tax on Investment Management Services

"Investment management services" is defined as a service provided by a partner or shareholder to a partnership, an S corporation, or any other entity if the services provide a substantial amount of:

- advising as to the advisability of investing in, purchasing, or selling a specified asset;
- managing, acquiring, or disposing of a specified asset;
- arranging financing with respect to acquiring a specified asset; or
- any activity in support of any of the above services.

"Specified asset" means securities, real estate held for rental or investment, interests in partnerships, commodities, or options or derivatives contracts.

The 19% tax does not apply to the distributive share or pro rata share of a pass-through entity's (PTE) taxable income if, during the taxable year, at least 80% of the average fair market value of the specified assets of the entity consist of real estate. In addition, the tax does not apply to (1) the income attributable to a fee calculated based on reference to the total assets under the management of an entity engaged in investment management services and (2) the income of a small business that conducts investment management services. A "small business" is a business entity that manages assets of less than $25 million; has total assets of $5 million or less; and is not controlled by, does not control, and is not under common control with another person that is not a small business.

Higher Education Affordability Trust Fund

The bill establishes HEATA within HEIF to retain revenues to make higher education more affordable for students. The specified income tax revenues from investment management services must be deposited into HEATA. HEATA funds must be used only to fund the specified higher education purposes.

Current Law:

Near Completer Program

"Near completer" is defined as an individual who has completed some college credits but does not have a college degree and is no longer attending an institution of higher education. MHEC, in collaboration with institutions of higher education, must create a statewide communication campaign to identify near completers in the State and to encourage near completers to re-enroll in an institution of higher education to earn a degree.

Degree Requirements

State regulations contain the following requirements for awarding associate and baccalaureate degrees:

- An associate's degree requires the satisfactory completion of not less than 60 or more than 70 credit hours, representing a planned sequence of learning experiences. The standard number of credit hours required for an associate's degree from a public community college is 60 credit hours. A student must earn at least 15 credit hours at the institution granting the degree.

- For a baccalaureate degree, the standard number of credit hours for a public four-year higher education institution is 120 credit hours. A student must earn at least 30 credit hours, of which at least 15 credit hours are upper divisional credit hours, at the institution awarding the degree.

Need-based Scholarships

The Governor must include in the State budget at least 80% of the funds appropriated in the prior fiscal year for the following need-based programs: EEA; the Part-time Grant; the Janet L. Hoffman Loan Assistance Repayment Program; and the Graduate and Professional Scholarship Program.

Delegate Howard P. Rawlings Education Excellence Award Program

The EEA program consists of two types of awards for full-time undergraduate students: (1) Guaranteed Access (GA) grants that are awarded to the neediest students to ensure that 100% of educational costs are paid and (2) EA grants that are awarded to low- and moderate-income students to assist in paying educational costs.

The GA grant is a need- and merit-based scholarship intended to meet 100% of financial need for full-time undergraduates from low-income households. Qualified applicants must have a cumulative high school GPA of at least 2.5 on a 4.0 scale. MHEC extended the income limits for renewals to 150% of the federal poverty level to prevent a student who may work in the summertime from exceeding the original 130% income cap.

The EA grant is a need-based scholarship intended to meet 40% of financial need at four-year institutions and 60% at community colleges for full-time undergraduates from low- to moderate-income families. The maximum award amount authorized by statute is $3,000. The current maximum amount awarded is $3,000.

An EEA award may be used at a degree-granting institution of higher education, an eligible institution with an associate's degree program that provides transfer credit for an accredited baccalaureate program, or a hospital diploma school for training registered nurses if the curriculum is approved by MHEC.

The award may be used for educational expenses as defined by MHEC, including tuition and fees and room and board.

Part-time Grant

The Part-time Grant program provides grants to undergraduate students taking at least 3 but no more than 11 hours of courses each semester or who are dually enrolled in a secondary school in the State and an institution of higher education. Recipients must be Maryland residents and must demonstrate a definite financial need. Funds for the program are allocated by MHEC to institutions of higher education based on the number of part-time students with demonstrated financial need who are enrolled at the institution. Grants are distributed to students by the institutions based on guidelines established by MHEC.

Graduate and Professional Scholarship Program

The Graduate and Professional Scholarship Program provides financial assistance to full-time and part-time students in the fields of medicine, dentistry, law, pharmacy, nursing, social work, and veterinary medicine at specified institutions of higher education. A recipient of a graduate and professional scholarship must be a Maryland resident, demonstrate a financial need, and attend one of several specified graduate and professional schools. Scholarships range from $1,000 to $5,000 per school year and may not be received for more than eight semesters. MHEC must allocate funds from the Graduate and Professional Scholarship Program to institutions of higher education based on the proportion of State residents enrolled in eligible programs at each institution. Institutions then distribute the scholarship funds to eligible students.

Senator John A. Cade Funding Formula

The State's annual contribution for the Senator John A. Cade Funding Formula, the largest community college aid program, is determined by enrollment at local community colleges and the level of funding received by public four-year institutions. The Cade formula bases per pupil funding on a set statutory percentage of current-year State appropriations per FTES at selected public four-year institutions of higher education. The resulting community college per student amount is multiplied by the number of FTES enrolled in the colleges in the second preceding fiscal year to identify a total formula amount. Specifically, the number of FTES is calculated as the number of student credit hours produced in the fiscal year two years prior to the fiscal year for which the State share is calculated, divided by 30. "Student credit hours" are defined as student credit hours or contact hours which are eligible, under the regulations issued by MHEC.

Baltimore City Community College

Like the local community colleges, annual State funding for BCCC is determined by a formula that bases per pupil funding for the college on a set statutory percentage of the current-year State appropriations per FTES at selected public four-year institutions of higher education. The resulting BCCC per student amount is multiplied by the number of FTES enrolled in the college in the second preceding fiscal year to identify a total formula amount. The number of FTES is calculated in the same manner as it is for the local community colleges, and "student credit hours" are defined the same.

Background: According to the Project on Student Debt, about 54% of the Class of 2016 who graduated from public and private nonprofit colleges in Maryland had student loan debt. These borrowers owed an average of $27,455.

Promise Programs

The Mayor of Baltimore City recently announced a promise scholarship program for students who graduate from Baltimore City Public Schools to attend BCCC tuition free as the Mayor's Scholars Program. Four counties in Maryland also have promise programs. For more information on those programs in Maryland and similar programs nationwide, please see the **Appendix – Promise Programs.**

Community College Tuition and Fees

As shown in **Exhibit 1**, the average statewide in-county tuition and fees for Maryland's community colleges was $4,324 in fall 2017. However, tuition and fees are only part of the costs associated with attending a community college. For example, students must obtain books and other educational materials in addition to room and board.

Exhibit 1
In-county Tuition and Fees at Community Colleges, based on 30 Credit Hours per Year
Fall 2017

College	In-county
Allegany	$3,940
Anne Arundel	4,100
Baltimore City*	3,196
Baltimore County	4,606
Carroll	4,884
Cecil	3,660
Chesapeake	4,760
College of Southern Maryland	4,613
Frederick	4,385
Garrett	4,230
Hagerstown	3,990
Harford	4,553
Howard	4,848
Montgomery	4,974
Prince George's	4,700
Wor-Wic	3,750
Statewide	**$4,324**

*Baltimore City Community College has one rate for in-state students.

Source: Maryland Association of Community Colleges

Financial Aid

The State's largest financial aid program, the Delegate Howard P. Rawlings Educational Excellence Awards Program, is available to students with financial need who are enrolled in community college full time in credit courses. Students may receive up to $3,000 in awards. However, there is a waiting list for the EEA program. Federal financial aid, like Pell grants, is generally *not* available to students who take noncredit courses except in limited circumstances. Most State scholarships are limited to programs that lead to a degree, although a few (including the senatorial and delegate scholarships) may be used to earn a certificate from a private career school, and the new Workforce Development Sequence Scholarship can be used at community colleges. Without access to financial aid, even relatively inexpensive certificate programs can remain out of reach to low-income individuals.

Beginning with the 2018-2019 award year, EEA award recipients are required to successfully complete 30 credits at the end of their sophomore year to receive their maximum renewal award. A student who fails to meet the 30-credit completion requirement but completes between 24 and 29 credits is eligible for a prorated renewal award.

The Governor's proposed budget for fiscal 2019 includes $84.7 million for the EEA program, $1.2 million for the Graduate and Professional Scholarship program, and $5.1 million for the Part-time Grant program. Thus, a total of $91.0 million is provided for these need-based award programs.

Near Completers

According to the U.S. Census Bureau, approximately 19.4% of Marylanders have completed some college, but they do not have an associate's or bachelor's degree. Not all of those who have begun college will qualify as a near completer, but many will. Many community college students are tempted to transfer to a four-year institution prior to completing their associate's degree. However, for various reasons many of those students never complete their bachelor's degree and are, thus, left without any degree for their effort. These students are then only able to present an accumulated number of college credits to a potential employer rather than being able to state on their resume that they have earned an associate's degree despite generally having acquired the credits and knowledge required for an associate's degree. In addition, sometimes credits without a degree may be deemed obsolete when presented later in life, either to employers or when returning to school to obtain a bachelor's degree.

In 2017, MHEC advised that, in fiscal 2016 under the current near completer program, staff from the 16 participating institutions identified a total of 8,140 near completers, successfully contacted 5,864 near completers, and re-enrolled 1,012.

Investment Management Services – Carried Interest

Investment funds – such as private equity and hedge funds – are often organized as partnerships. These partnerships typically have two types of partners: general partners; and limited partners. General partners manage the fund, while limited partners typically only contribute capital to the partnership. General partners normally receive two types of compensation for managing a fund: a management fee tied to some percentage of the fund's assets and a profit share; or "carried interest," tied to some percentage of the profits generated by the fund. In a common compensation agreement, general partners receive a management fee equal to 2% of the invested assets plus a 20% share in profits as carried interest.

The management fee, less the fund's expenses, is subject to ordinary income tax rates (the top federal income tax rate for individuals in 2018 is 37%) and self-employment tax on the federal level and is subject to the State individual income tax. However, taxation of the carried interest is deferred until profits are realized on the fund's underlying assets, when at such time the carried interest is taxed in the same manner as the investment income received by the limited partners. Thus, if the investment income consists solely of capital gains, the carried interest is taxed only when those gains are realized and at the lower capital gains rate on the federal level (the top capital gains tax rate in 2018 is 20%). The Maryland income tax is based, after specified adjustments, on the federal adjusted gross income of the taxpayer, so taxation on the carried interest is deferred, but both forms of income are taxed at the same rate under the State income tax.

Taxation of Pass-through Entities

A PTE is a business structure that avoids the double taxation imposed on an ordinary corporation. A corporation's income generally is taxed at the corporate level and taxed again at the individual level when income is distributed as dividends (cash) to the owners or shareholders. Unlike for a corporation, income recorded by a PTE flows through and is allocated to the owners of the entity. The owners of the PTE pay income tax at the individual level on this amount. Owners may choose the type of entity to form for a variety of reasons, including the number of owners, liability protection, profit distribution, ease of formation, and tax treatment.

In order for a business to be treated as a PTE, the entity must organize under State law and make an election to do so on the entity's federal income tax return.

State Fiscal Effect:

HEATA Revenues: HEATA revenues increase significantly as a result of taxing income attributable to investment management services at 19%. While the bill will increase State revenues, the total fiscal impact cannot be reliably estimated at this time. The overall impact depends on the number of taxpayers who file in Maryland and have income attributable to investment management services.

The U.S. Department of the Treasury (Treasury) recently estimated that taxing carried interest as ordinary income would generate approximately $2.6 billion of federal tax revenue in the near term and $1.9 billion in fiscal 2022. Based on the Treasury estimate, the Department of Legislative Services estimates that State tax revenues would increase by $79.0 million in fiscal 2019 and by $58.0 million in fiscal 2023 from taxing investment management services at a 19% tax rate, as shown in **Exhibit 2**.

Exhibit 2
Revenue Impact under the Bill
Fiscal 2019-2023
($ in Millions)

	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
Revenue Estimate	$78.0	$75.0	$72.0	$70.0	$58.0

Source: U.S. Department of the Treasury; Department of Legislative Services

Using estimates by the Congressional Budget Office (CBO) on taxing carried interest at ordinary federal income tax rates, the Comptroller's Office estimates State tax revenues could increase by $60.0 million annually beginning in fiscal 2019.

The CBO and Treasury estimates reflect the likelihood of some partnerships responding to a federal policy change by restructuring their compensation agreements so that the general partner's 20% share of profits continues to be taxed at the lower capital gains tax rates. If carried interest was taxed as ordinary income, CBO expects some limited partners to provide an amount equivalent to 20% of the fund to the general partner as an interest-free loan, with the requirement that the borrowed capital be invested in the fund. The foregone interest on the loan would be taxed at ordinary income tax rates and, thus, generate new tax revenue, but if the general partner sells the assets of the investment fund for a profit, the gains realized by the general partner would still be taxed at the lower tax rates.

State Expenditures: General fund expenditures increase in fiscal 2019 for one-time tax form changes and computer programing modifications at the Comptroller's Office, as discussed below, and may increase beginning in fiscal 2020 for community college funding formulas. Otherwise, HEATA is assumed to be used to implement the bill and comply with the mandated appropriations.

As shown in **Exhibit 3,** HEATA expenditures increase by $60,000 in fiscal 2019, increasing to $55.3 million in fiscal 2020 and $127.4 million in fiscal 2022 due to mandated appropriations to implement the bill. HEATA expenditures increase further in fiscal 2024; some mandated funding ends after fiscal 2024. Using the assumptions on revenue explained above, in particular, that individuals do not alter behavior to avoid the tax, HEATA revenues and the fund balance from the tax established by the bill exceed HEATA expenditures. However, to the extent HEATA revenues are less that estimated, general fund expenditures increase due to the mandated and assumed costs of the programs established by the bill. The assumptions and information below were used in this expenditures estimate.

Exhibit 3
Total Estimated HEATA Revenues and Expenditures
Fiscal 2019-2023
($ in Thousands)

	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
Estimated HEATA Revenue	$78,000	$75,000	$72,000	$70,000	$58,000
HEATA EXPENDITURES					
NC Communications Campaign		$250	$250	$250	$250
NC Match Program		50	50	50	50
NC Grants		500	750	750	750
Promise Program		32,000	40,000	45,000	50,000
CC Support		250	250	250	250
Need-based Aid		-	6,530	14,030	21,530
Tuition Buy Downs		22,104	44,419	66,949	-
MHEC	$60	139	133	138	143
Total HEATA Expenditures	**$60**	**$55,293**	**$92,383**	**$127,418**	**$72,974**
Net HEATA Revenue	$77,940	$19,707	($20,383)	($57,418)	($14,974)
HEATA Year-end Fund Balance[1]	$77,940	$97,647	$77,264	$19,846	$4,873

[1] To the extent HEATA expenditures exceed revenues from the tax established by the bill, general fund expenditures increase.

CC: community college
HEATA: Higher Education Affordability Trust Account
MHEC: Maryland Higher Education Commission
NC: near completer

Notes: Additional general fund impacts due to the community college funding formulas from new students are likely under the bill. Numbers may not sum to total due to rounding.

Source: U.S. Department of the Treasury; Department of Legislative Services

Maryland Community College Promise Program

The bill mandates that the Governor include the following amounts for the Maryland Community College Promise Program: $32.0 million for fiscal 2020; $40.0 million for fiscal 2021; $45.0 million for fiscal 2022; and $50.0 million for fiscal 2023 and each fiscal year thereafter.

Beginning in fiscal 2020, HEATA expenditures increase by $250,000 annually to fund support services for students who have received promise grants. The grants are to be distributed to the public community colleges in the State proportional to the number of FTES who have received a promise grant. According to the estimated number and distribution of promise grant recipients, BCCC receives an estimated $12,500, and the local community colleges receive the remaining $237,500.

Senator John A. Cade Funding Formula

Due to the Senator John A. Cade Funding Formula for community colleges, general fund expenditures increase for each FTES who attends a local community college due to the promise scholarship established by the bill. This impact cannot be reliably estimated. *For illustrative purposes,* for each FTES who attends a local community college due to the bill in the 2019-2020 academic year (fiscal 2020), general fund expenditures increase by an estimated $3,633 in fiscal 2022.

Baltimore City Community College

The promise program established by the bill is assumed to have negligible impact on the (revenues and) expenditures of BCCC due to the existing Mayor's Scholars Program, meaning that students who are motivated to enroll in community college by a promise program would already have decided to enroll as a result of the mayor's program. However, if the Mayor's Scholars Program is discontinued, then State expenditures for the BCCC formula (and BCCC revenues and expenditures) increase, potentially significantly.

BCCC receives an estimated $12,500 in support grants for promise students annually beginning in fiscal 2020.

In addition, limiting the increase in tuition at BCCC to the increase in the three-year rolling median family income is not anticipated to significantly decrease BCCC tuition revenues because community colleges are generally price sensitive and have limited the increases in tuition during periods when salaries stagnate. However, anomalous periods do occur. BCCC tuition increased 7% from fall 2015 to fall 2017. The increase in the three-year rolling median family income was 2.1% for the period between 2014 through 2016. Thus, BCCC is limited to increasing tuition by 2.1% for fall 2019 (fiscal 2020).

Near Completers Programs

HEATA expenditures increase by an estimated $800,000 in fiscal 2020 increasing to more than $1.0 million in fiscal 2021 through 2024 due to the mandated appropriations in the bill, as shown in Exhibit 3. MHEC staffing for the program is accounted for in the positions below.

Public Four-year Tuition Buy Down

Public four-year tuition is anticipated to increase by approximately 5% annually. The bill limits the increase in in-state tuition for fiscal 2020 through 2022 to 2% and mandates the 3% tuition buy down for public four-year institutions for fiscal 2020 through 2022. Based on current in-state tuition and enrollment, in fiscal 2020 the tuition buy down is anticipated to cost $21.1 million for the University System of Maryland; $678,437 for Morgan State University; and $321,674 for St. Mary's College of Maryland. For fiscal 2021 and 2022, the amount required to be appropriated to the respective governing boards in the prior year must be included when calculating the amount required in the current fiscal year.

Need-based Scholarships

Mandating the appropriation for the EEA program, the Part-time Grant, and the Graduate and Professional Scholarship Program by the amounts specified in the bill is estimated to **not** affect general fund or HEATA expenditures in fiscal 2020 as the Governor's proposed fiscal 2019 budget includes approximately $91.0 million for those programs. However, due to the mandated amounts, HEATA expenditures increase by $6.5 million in fiscal 2021; $14.0 million in fiscal 2022; and $21.5 million in fiscal 2023; (and $29.0 million in fiscal 2024 and beyond). This estimate is based on the assumption that the specified need-based aid programs are level funded in future years under current law.

It is assumed that phasing in an increase in the maximum grant amount for the EA grant to $3,500 by fiscal 2024 has no fiscal impact on the State since the EA grant is distributed based on the amount of money available for the program. However, it is assumed that, despite the increase in the maximum award amount, all eligible students will receive an award due to the increase in funding for all the need-based scholarship programs.

Maryland Higher Education Commission

This estimate assumes that MHEC administrative and operating expenditures are allowable HEATA expenditures. To the extent that these expenses are not allowable, general fund expenditures increase by an equivalent amount.

HEATA expenditures increase by $60,000 in fiscal 2019 for one-time programing costs to program the MDCAPS scholarship system for the promise grant. Beginning in fiscal 2020, the estimate reflects the cost of hiring one full-time staff specialist and one full-time program specialist to implement the bill. The full-time staff specialist will implement the near completer programs, including overseeing the development of the near completer web-based match program and outreach to near completers. This position may not be necessary after fiscal 2024 when funding for near completer programs is no longer mandated. The full-time program specialist will implement the promise grant and assist with reporting requirements.

	FY 2019	FY 2020
Positions	0	2
Salaries and Fringe Benefits	$0	$128,380
Programming for MDCAPS	$60,000	0
One-time Start-up and Other Operating Expenses	0	11,030
Total HEATA Administrative Expenditures	**$60,000**	**$139,410**

Future year expenditures reflect full salaries with annual increases and employee turnover and ongoing operating expenses.

Comptroller's Office

The Comptroller's Office reports that it will incur a one-time general fund expenditure increase of $172,000 in fiscal 2019 to add a new line to the individual, PTE, and corporate income tax returns. This includes data processing changes to the SMART income tax return processing and imaging systems and systems testing.

Local Fiscal Effect: The impact of the bill on local community colleges is described below. The most significant impact will be due to new students enrolling in community colleges; however, as explained below, this impact cannot be reliably estimated.

Maryland Community College Promise Grant

There is no immediate impact on local community college revenues due to promise grants likely going to current community college students, as discussed above. However, tuition and other revenues increase for each *new* student attending community college up to the full amount of tuition and fees. Due to the Senator John A. Cade Funding Formula for community colleges, State aid increases for each FTES who attends a local community college due to the promise scholarship established by the bill. This impact cannot be reliably estimated. *For illustrative purposes,* for each FTES who attends a local community college due to the bill in the 2019-2020 academic year (fiscal 2020), State aid increases by an estimated $3,633 in fiscal 2022.

As explained above, beginning in fiscal 2020, local community college revenues increase by up to a total of $250,000 annually to fund support services for students who have received promise grants. According to the estimated number and distribution of promise grant recipients, the local community colleges receive $237,500 of the grant.

Capping Community College Tuition Growth

Limiting the increase in tuition at local community colleges to the increase in the three-year rolling median family income is not anticipated to significantly decrease local community college tuition revenues because community colleges are generally price sensitive and have limited the increases in tuition during periods when salaries stagnate. However, *for informational purposes*, the increase in the three-year rolling median family income was 2.1% for the period between 2014 through 2016. Thus, local community colleges are limited to increasing tuition by 2.1% for fall 2019 (fiscal 2020).

Small Business Effect: Small businesses that provide investment management services or receive income that is attributable to investment management services may be adversely affected by paying a 19% tax on that income. However, the bill exempts from the tax an independent business that manages assets of less than $25 million and has total assets of $5 million or less. The American Investment Council reported that there were 69 private equity firms headquartered in Maryland in 2015. It is unknown how many of these private equity firms are small businesses and would incur a 19% tax on their services.

Additional Information

Prior Introductions: None.

Cross File: SB 317 (Senator Pinsky, *et al.*) **-** Education, Health, and Environmental Affairs and Budget and Taxation.

Information Source(s): Comptroller's Office; Maryland Higher Education Commission; Baltimore City Community College; University System of Maryland; St. Mary's College of Maryland; Maryland Association of Community Colleges; U.S. Department of the Treasury; U.S. Census Bureau; *The New York Times*; *The Atlantic*; tennesseean.com; Project on Student Debt; Congressional Budget Office; Department of Legislative Services

Fiscal Note History: First Reader - February 7, 2018
nb/rhh

Analysis by: Caroline L. Boice

Direct Inquiries to:
(410) 946-5510
(301) 970-5510

Appendix – Promise Programs

In 2014, the Tennessee General Assembly passed legislation establishing a program, beginning with the class of 2015, offering two years of tuition-free education at 1 of the state's 13 community colleges or 27 technical schools. The program, known as Tennessee Promise, is a last-dollar scholarship, meaning it covers costs of tuition and mandatory fees not met by federal Pell scholarships, the Tennessee HOPE scholarship, or the Tennessee Student Assistance Award Program. To be eligible, a student must meet a number of requirements, including completing the federal Free Application for Federal Student Aid, enroll in a college full time for up to five consecutive semesters, maintain a 2.0 grade point average (GPA), and complete eight hours of community service per semester.

To pay for the program, the state created an endowment of $361.1 million using state lottery reserves. Because community college is relatively affordable, and the Tennessee program is a "last dollar" program, meaning existing financial aid grants are applied first before the Promise award is received, the average Tennessee Promise award in the first year was only $1,020. The total cost to the state was $10.6 million in fiscal 2016, but this is expected to scale up to about $36.0 million when fully implemented. In the first couple years, community college enrollment in Tennessee increased about 10%. In January 2017, Tennessee's governor announced a plan to expand the program to all adults in the state.

In 2015, Oregon became the second state to enact legislation to provide free community college. Among other requirements, to be eligible, students must have at least a 2.5 GPA. Under the program, all eligible students will receive a minimum grant of $1,000, even if their tuition and fees are covered by other financial aid. Any money remaining after tuition and fees can be used for transportation, books, and other expenses. A report on the first year of the program revealed that it reached approximately 1,000 more students than projected and fewer students are eligible for a Pell grant than projected, which has increased the cost of the program for the first year from a projected $10.0 million to $13.5 million. The cost of the program is projected to double in the second year. Enrollment of Oregon's high school graduates in the state's public universities declined slightly (by less than one percentage point) in 2016.

In January 2017, New York's governor announced a plan called the Excelsior Scholarship, which ensures free tuition at New York's public two- and four-year institutions to students whose families make up to $125,000 per year once the program is fully phased in in 2019. Nearly a million families in the state will qualify for the scholarship. According to *The New York Times*, which first reported the plan, initial cost estimates of the Excelsior Scholarship are anticipated at $163.0 million a year when fully funded.

Five jurisdictions in Maryland already offer Promise-like programs (Baltimore City and Allegany, Garrett, Somerset, and Wicomico counties). The program in Allegany County is unique in that it provides a scholarship to residents to attend the community college or Frostburg State University, the public four-year institution located in the county. In fall 2017, the Mayor of Baltimore City announced a promise scholarship program for students who graduate from Baltimore City Public Schools to attend Baltimore City Community College (BCCC) tuition free as the Mayor's Scholars Program. There is also a two-year pilot program for Mayor's Scholars Program recipients who graduate from BCCC; they will be eligible for four semesters of tuition waivers to attend Coppin State University. Additionally, Chapter 647 of 2016 created a task force to study establishing a program in Prince George's County.

An article in *The Atlantic* reported that, even with free tuition, some of the poorest students are still finding attending community college a challenge because they need to work 30 to 40 hours a week to afford books and meet basic living expenses, which can cost between $5,000 and $10,000 per year.