Department of Legislative Services

Maryland General Assembly
2004 Session

FISCAL AND POLICY NOTE
Revised

House Bill 1188 (Delegate Jones, *et al.*)

Appropriations and Ways and Means Budget and Taxation

Higher Education Affordability and Access Act of 2004 - Supplementary Appropriation

This bill establishes a special, nonlapsing Higher Education Investment Fund (HEIF) that contains proceeds from a 10% surcharge on corporate income taxes to be imposed from calendar 2004 to 2006. Funding from HEIF will be used to provide additional support to the University System of Maryland (USM) and Morgan State University (MSU), including supplementary fiscal 2005 appropriations. The bill requires the Governor to include in the fiscal 2006 and 2007 State budgets increases of 5% in aggregate general fund and HEIF support for USM and MSU. If the funding increases in the bill are realized, increases in tuition and fees at USM institutions and MSU are limited to 5% per year from fiscal 2005 to 2007. A commission to study higher education issues is also established.

The bill takes effect July 1, 2004.

Fiscal Summary

State Effect: HEIF revenues would be an estimated $59.5 million in FY 2005 due to the surcharge on corporate income taxes. HEIF expenditures would be $27 million in FY 2005 to pay the supplementary appropriations to USM and MSU. Tuition and fee revenues at USM institutions and MSU would decrease from planned revenue levels by an estimated $13.3 million in FY 2005 due to tuition limitations. General fund expenditures would increase beginning in FY 2006 to provide additional funding to nonpublic universities and community colleges. Compared to current funding projections, general fund expenditures for USM and MSU would decrease in FY 2006 and 2007 as HEIF expenditures supplant general fund appropriations. Future years reflect 5% annual increases for USM and MSU, continued HEIF revenues, and continued tuition and fee limitations through FY 2007. FY 2008 and 2009 estimates reflect the impact of FY 2005 to 2007 funding and tuition mandates.

($ in millions)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
SF Revenue	$59.5	$44.4	$24.5	$0	$0
Higher Ed Rev.	(13.3)	(18.6)	(24.6)	(26.4)	(28.4)
GF Expenditure	0	4.6	(8.7)	58.8	63.1
SF Expenditure	27.0	41.5	59.9	0	0
Net Effect	$19.2	($20.3)	($51.3)	($85.2)	($91.5)

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

Local Effect: Formula State aid to community colleges would increase by an estimated $9.7 million in FY 2006 and by an estimated $15.9 million in FY 2009 due to increased State appropriations to four-year institutions.

Small Business Effect: Meaningful. Small businesses that are corporate entities would be required to pay 10% surcharges on corporate income taxes from 2004 to 2006, effectively raising the corporate income tax rate from 7.0% to 7.7% for three tax years.

Analysis

Bill Summary:

Additional Appropriations to Institutions of Higher Education

From the revenues that are credited to HEIF in fiscal 2005, $1.6 million must be appropriated for MSU and $25.4 million must be appropriated for USM. The amounts must be used to offset reductions in tuition and fees imposed by the bill and for other purposes necessary to provide high-quality and affordable post-secondary education. Any balance remaining in HEIF on June 30, 2007 must be transferred to the State general fund. It is the intent of the General Assembly that any remaining balance be used to support higher education.

For fiscal 2006 and 2007, the Governor must include aggregate annual increases for USM and MSU of at least 5% in the State budget, with HEIF supporting no more than 60% of the cumulative increases from fiscal 2005 to 2007. Increased general fund appropriations must support the rest of the increases. Funding for the Joseph A. Sellinger formula, the Senator John A. Cade formula, and the Baltimore City Community College (BCCC) formula will be based on general fund and HEIF support for the public four-year institutions of higher education.

The additional funding provided through the bill may not supplant funding distributed in accordance with the State's partnership agreement with the U.S. Department of Education, Office of Civil Rights (OCR), for the State's four historically Black institutions. The bill states that it is the intent of the General Assembly to continue support for historically Black institutions in accordance with the State's OCR agreement.

Tuition and Fee Revenues and Policies

For fiscal 2005 to 2007, USM and MSU may not increase resident undergraduate tuition, including mandatory fees, by more than 5% over the rates charged the previous academic year. The 5% limit only applies in fiscal years when the full appropriations required by this bill are provided. The boards of regents of USM and MSU must also establish policies to accommodate projected enrollment growth from the 2004-2005 academic year to the 2006-2007 academic year.

Unless the Board of Regents of USM finds that there is a compelling reason to set the tuition at a lower rate, the board must establish a tuition level for out-of-state undergraduate USM students that is equal to the cost of educating the student, including the costs of facility renewal, equipment for new facilities, academic revenue bond debt expenses, and other expenses related to building and operating State-supported facilities. The Board of Regents of USM must study the out-of-state tuition policies of USM constituent universities and their peer institutions and recommend changes, as appropriate, to USM policies.

Efficiency, Effectiveness, and Accountability

The bill states that it is the intent of the General Assembly that USM and MSU improve their effectiveness and efficiency and reduce their cost structures to provide world class education, research, and public service. The bill requires USM to continue its effectiveness and efficiency initiative and to attain effectiveness and efficiency savings of at least $17 million in fiscal 2005. MSU must implement an effectiveness and efficiency initiative.

The boards of regents of USM and MSU are required to submit reports detailing management strategies for improved efficiency, strategies for managing enrollment growth effectively, and efforts to improve access and affordability through the use of need-based financial aid. USM must also report on entrepreneurial efforts, including the development and expansion of institution-based research parks. Nonpublic institutions of higher education that receive State funds are required to report annually to the Maryland Higher Education Commission (MHEC) on the scholarships and grants they award to Maryland students.

Commission to Study Higher Education in Maryland

The bill requires the General Assembly and Governor to establish a 22-member commission to study the coordination, funding, educational delivery, and State commitment to higher education in Maryland. The commission must engage the services of the Education Commission of the States (ECS) to conduct a study of current and future funding needs for USM constituent institutions. The commission must review options and make recommendations relating to the establishment of a consistent and stable funding mechanism that will allow Maryland institutions of higher education to ensure accessibility and achieve national eminence. A report on its findings and recommendations is due by December 1, 2005. The Department of Legislative Services, the Department of Budget and Management, MHEC, and USM will provide staff for the commission.

Current Law: Funding for USM and MSU are as provided in the annual State budget. It is the intent of the General Assembly, however, that, barring unforeseen economic conditions, the Governor include in the annual budget submission an amount of general fund State support for higher education equal to or greater than the amount appropriated in the prior fiscal year. The goal of the State, as noted in statute, is that State support for higher education operating and capital expenditures comprise 15.5% of general fund revenues.

Subject to the authority and policies of the Board of Regents of USM, the president of each USM constituent institution sets tuition and fees for the institution. The Board of Regents of MSU fixes tuition for the university.

The corporate income tax rate is 7% of Maryland taxable income. There is no surcharge on this amount.

Background: The bill codifies many of the recommendations of the Special Committee on Higher Education Affordability and Access. The committee was formed to respond to concerns about recent reductions in State support for higher education and subsequent increases in tuition rates at the State's public institutions of higher education. The committee found that fiscal 2004 is the first year that tuition and fee revenues in the aggregate exceed State support at USM institutions. The fiscal 2005 State budget further widens the difference between tuition and fee revenues and State support at USM institutions. The committee's final report indicates that fiscal 2005 tuition and fee revenues per full-time equivalent student ($9,478) are more than $1,700 higher than the fiscal 2005 State support per full-time equivalent student ($7,767).

Many of the concerns that led to the committee's creation began when students at USM institutions endured tuition and fee increases that averaged 18% between fall 2002 and fall 2003. The fiscal 2003 USM budget as proposed in fall 2002 assumed an initial 4% tuition increase. After cost containment reductions in winter 2003, USM adopted an unusual 5% mid-year increase to help offset reduced general fund support. At the beginning of fiscal 2004, following the outcome of the legislative session and actions taken by the Board of Public Works, USM raised fall 2003 tuition rates by an additional 10% or more at several institutions.

The combined actions of the General Assembly and the Board of Public Works reduced the USM budget $67 million in fiscal 2003 and $54.7 million in fiscal 2004. However, the tuition and fee increases brought in $74 million in additional revenues, offsetting 61% of the reduced general funds. The fiscal 2005 State budget provides the same level of State support for USM and MSU that was provided in fiscal 2004, but additional resident undergraduate tuition and fee revenues of $88.6 million are assumed in the proposed fiscal 2005 State budget. **Exhibit 1** shows the fall 2002, fall 2003, and proposed fall 2004 tuition rates at USM institutions and MSU.

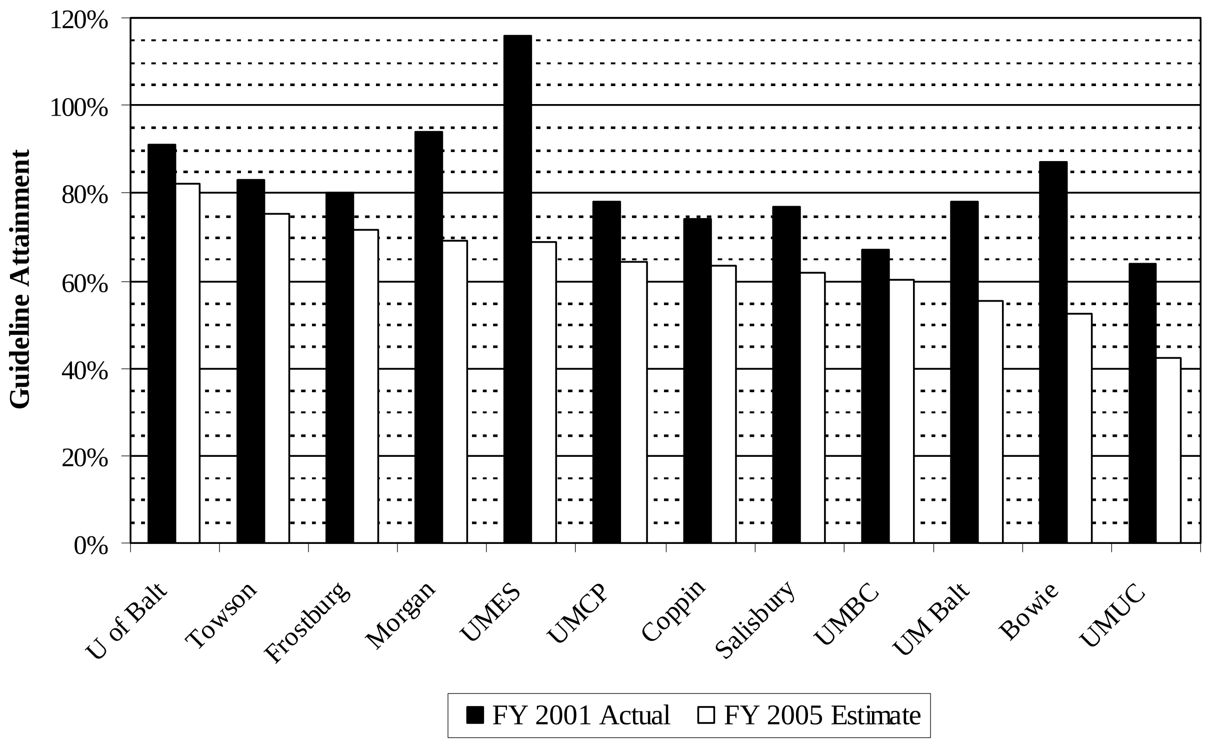
Exhibit 1
Annual Tuition and Mandatory Fees at USM Institutions
For Full-time Resident Undergraduate Students
Fall 2002 to 2004

University	Fall 2002	Fall 2003	Increase 02 to 03	Proposed Fall 2004	Increase 03 to 04
Bowie State	$4,064	$4,853	19.4%	$5,218	7.5%
Coppin State	3,959	4,240	7.1%	4,454	5.0%
Frostburg State	4,618	5,342	15.7%	5,830	9.1%
Salisbury	4,804	5,564	15.8%	5,976	7.4%
Towson	5,401	6,226	15.3%	6,672	7.2%
U of Baltimore	4,996	5,913	18.4%	6,448	9.0%
UM Baltimore*	5,096	6,224	22.1%	6,626	6.5%
UM Baltimore County	6,362	7,388	16.1%	8,020	8.6%
UM College Park	5,670	6,759	19.2%	7,426	9.9%
UM Eastern Shore	4,461	5,105	14.4%	5,558	8.9%
UM Univ College**	6,180	6,660	7.8%	6,780	1.8%
Morgan State	4,698	5,078	8.1%	5,578	9.8%

* Based on tuition and fees for the School of Nursing, the largest undergraduate program at UMB.
** Based on 30 credit hours per year.

Funding guidelines attempt to calculate an appropriate level of general fund support for Maryland's public institutions of higher education using per student spending at identified peer institutions. MHEC calculates the guidelines and, accounting for different tuition rates at the peer institutions, calculates a recommended State appropriation for each institution. **Exhibit 2** shows that estimated funding guideline attainment for fiscal 2005 is below actual fiscal 2001 attainment for every institution.

Exhibit 2
Funding Guideline Attainment
Fiscal 2001 and 2005



Source: Maryland Higher Education Commission

State Revenues: Two revenue sources would be affected by the bill. The three-year surcharge on corporate income taxes would establish a revenue source for HEIF. In addition, assuming the bill's funding requirements are met, tuition and fees at USM institutions and MSU would be limited to 5% annual increases for three years, reducing potential tuition and fee revenues.

Surcharge on Corporate Income Taxes

The corporate income tax surcharge would be imposed from calendar 2004 through 2006. The surcharge would increase revenues by an estimated $59.5 million in fiscal 2005 when, in effect, six quarterly payments would be made, including four in the first half of the fiscal year (to account for all of calendar 2004) and two in the last half of the fiscal year (to account for the first half of calendar 2005). In fiscal 2006, estimated annualized revenues of $44.4 million would be collected from the surcharge. In fiscal 2007, when only half a year of revenues would be generated, collections are estimated at $24.5 million. All of the proceeds from the surcharge would be placed into HEIF. Any remaining funds in HEIF at the end of fiscal 2007 would revert to the general fund.

Tuition and Fee Reductions

Assuming the supplementary appropriations specified in the bill are granted, fiscal 2005 tuition and mandatory fees for resident undergraduate students attending USM institutions and MSU would be limited to 5% increases over fiscal 2004 tuition and fee rates. This would decrease tuition and fee revenues by an estimated $13.3 million in fiscal 2005. This estimate assumes that proposed fiscal 2005 increases in tuition and fees for resident undergraduate students would take place without this legislation. The proposed increases range from 1.8% at University of Maryland University College to 9.9% at the University of Maryland, College Park.

For fiscal 2006 and 2007, annual tuition growth for resident undergraduates would be limited to 5% per year. USM advises that resident undergraduate tuition and fee rates will increase by approximately 6% annually after fiscal 2005 if the rates are not restricted. Tuition and fee revenues under the bill would be an estimated $24.6 million below planned tuition and fee revenues by fiscal 2007.

After tuition and fee limitations have been lifted, it is assumed that tuition and fees would increase by 6% annually. **Exhibit 3** shows the estimated annual impact of the tuition and fee limitations that would be imposed by the bill.

Exhibit 3
Impact of Resident Undergraduate Tuition and Fee Limitations
Fiscal 2005 to 2009
($ in millions)

	FY 2005	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**
USM Revenues					
HB 1188	$401.8	$429.3	$457.5	$492.8	$532.2
Current Estimates	413.8	446.3	480.0	516.9	558.1
Impact	($12.0)	($16.9)	($22.5)	($24.1)	($25.9)
MSU Revenues					
HB 1188	$27.4	$29.9	$31.9	$34.5	$36.9
Current Estimates	28.7	31.6	34.0	36.8	39.4
Impact	($1.3)	($1.7)	($2.1)	($2.3)	($2.4)
T&F Revenues	**($13.3)**	**($18.6)**	**($24.6)**	**($26.4)**	**($28.4)**

The bill requires USM institutions to establish a tuition level for out-of-state students that is equal to the cost of educating the student, unless the Board of Regents finds that there is a compelling reason to set the tuition at a lower rate. This could increase tuition for out-of-state students and increase USM tuition revenues. However, USM reports that it is in the process of making this change without legislation, so the bill would not materially impact out-of-state tuition levels.

State Expenditures: The bill provides supplementary fiscal 2005 appropriations for USM and MSU and mandates annual increases of at least 5% for USM and MSU for fiscal 2006 and 2007. The required annual appropriations, which would be paid with general funds and HEIF, are shown in **Exhibit 4**.

Exhibit 4
Required Annual Appropriations to USM and MSU
Fiscal 2005 to 2007
($ in millions)

	USM	**MSU**
Proposed Fiscal 2005 Appropriation	$747.3	$48.2
Supplementary Appropriation	25.4	1.6
Fiscal 2005 Total	$772.7	$49.8
Fiscal 2006 Total (+5%)	$811.3	$52.3
Fiscal 2007 Total (+5%)	$851.9	$54.9

Higher Education Investment Fund Expenditures

HEIF expenditures would increase by $27 million in fiscal 2005 to provide the supplementary appropriations specified in the bill. In future years, HEIF would support up to 60% of the cumulative required growth in State funding for USM and MSU from fiscal 2005 to 2007. HEIF expenditure estimates are shown in **Exhibit 5**, along with estimates of the annual revenues and the balance that would be carried forward each year.

Exhibit 5
The Higher Education Investment Fund
Fiscal 2004 to 2007
($ in millions)

	FY 2005	**FY 2006**	**FY 2007**
New Revenues	$59.5	$44.4	$24.5
Balance Carried Forward	0.0	32.5	35.4
Maximum Expenditures	$27.0	$41.5	$67.4
Actual Expenditures	27.0	41.5	59.9
Balance	$32.5	$35.4	$0.0

As shown in the exhibit, HEIF revenues are projected to expire before making the maximum allocation in fiscal 2007. It is assumed that general funds would support the estimated $7.5 million that would not be available from HEIF in fiscal 2007.

General Fund Appropriations

HEIF is limited to supporting 60% of the growth in State appropriations to USM and MSU from fiscal 2005 to 2007, and the remainder of the required increases must come from general funds. Assuming general fund appropriations would not increase beyond the level required by the bill, the estimated annual increases in general fund appropriations under the bill would be outpaced by current projections of increases in general fund appropriations. Current projections show increases in general fund appropriations for USM and MSU of approximately 4% per year. In effect, funding from HEIF would supplant a portion of projected general fund expenditures, resulting in an estimated general fund savings for fiscal 2006 and 2007.

In fiscal 2008 and 2009, it is assumed that general fund support for USM and MSU would increase off the higher base funding levels established from fiscal 2005 to 2007. The estimated general fund impact for fiscal 2006 to 2009 is shown in **Exhibit 6**.

Exhibit 6
General Fund Impact
Fiscal 2006 to 2009
($ in millions)

	FY 2006	**FY 2007**	**FY 2008**	**FY 2009**
HB 1188	$822.1	$846.9	$945.6	$985.9
Current Estimates	830.1	865.4	902.4	940.8
Impact	($8.0)	($18.4)	$43.2	$45.0

The combined impact of increased HEIF funding and general fund support, as compared to projected current law general fund appropriations for USM and MSU, is shown in **Exhibit 7**.

Exhibit 7
Estimated State Funding Increases
Fiscal 2005 to 2009
($ in millions)

	FY 2005	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**
USM Appropriations					
HB 1188 Funding (GF+HEIF)	$772.7	$811.3	$851.9	$887.7	$925.1
Current Estimates (GF)	747.3	779.1	810.9	844.9	880.5
Increase	$25.4	$32.3	$41.1	$42.8	$44.6
MSU Appropriation					
HB 1188 Funding (GF+HEIF)	$49.8	$52.3	$54.9	$57.9	$60.8
Current Estimates (GF)	48.2	51.0	54.5	57.5	60.4
Increase	$1.6	$1.3	$0.4	$0.4	$0.4
State Funding Increase	**$27.0**	**$33.5**	**$41.4**	**$43.2**	**$45.0**

Impact on Sellinger, Cade, and BCCC formulas

Formulas supporting private colleges and universities and community colleges would be based on State general fund and HEIF support for the public four-year institutions of higher education. If State support increases as proposed in this bill, funding for the Sellinger formula (for private colleges and universities), the Senator John A. Cade funding formula (for locally-operated community colleges), and BCCC (which is operated by the State) would also increase. The formulas are based on State support in the prior fiscal year, so there would be no impact on the formulas until fiscal 2006. **Exhibit 8** shows the estimated increases for each of the formulas.

Exhibit 8
Impact on Sellinger, Cade, and BCCC Formulas
Fiscal 2006 to 2009
($ in millions)

	FY 2006	FY 2007	FY 2008	FY 2009
Sellinger				
HB 1188	$46.9	$47.8	$50.3	$52.7
Current Law	44.1	46.0	48.2	50.5
Impact	$2.8	$1.7	$2.1	$2.2
Cade				
HB 1188	$155.5	$160.7	$172.4	$182.1
Current Law	148.7	155.2	162.6	170.2
Impact	$6.8	$5.4	$9.9	$11.9
BCCC				
HB 1188	$35.1	$36.2	$38.9	$40.8
Current Law	32.2	33.7	35.3	36.9
Impact	$2.8	$2.5	$3.6	$3.9
GF Exp Increase	**$12.5**	**$9.7**	**$15.6**	**$18.1**

Commission Expenses

General fund expenditures would increase by an estimated $50,000 to contract with ECS for a study of current and future higher education funding needs. A similar study conducted by ECS six years ago cost approximately $44,000. It is assumed that the $50,000 expense would be incurred at $25,000 per year in the two fiscal years, 2005 and 2006, that the commission would meet.

Aggregate Fiscal Effect on USM and MSU: Overall revenues for USM, including the tuition and fee revenue reduction and the State funding increase, would increase by an estimated $13.4 million in fiscal 2005 and an estimated $18.6 million in fiscal 2009. For MSU, overall fiscal 2005 revenues would increase by an estimated $336,000. However, from fiscal 2006 to 2009 the effect of the 5% tuition limitation on MSU relative to a projected 6% increase would more than offset the additional State funding mandated under the legislation. The estimated combined net impacts on USM and MSU are shown in **Exhibit 9**.

Exhibit 9
Net Impact of Increased State Funding and Decreased Tuition Revenues
Fiscal 2005 to 2009
($ in millions)

	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
USM					
State Funding Increase	$25.4	$32.3	$41.1	$42.8	$44.6
Tuition and Fees Decrease	(12.0)	(16.9)	(22.5)	(24.1)	(25.9)
Net Impact	$13.4	$15.3	$18.6	$18.7	$18.6
MSU					
State Funding Increase	$1.6	$1.3	$0.4	$0.4	$0.4
Tuition and Fees Decrease	(1.3)	(1.7)	(2.1)	(2.3)	(2.4)
Net Impact	$0.3	($0.4)	($1.7)	($1.9)	($2.0)
Total Net Impact	**$13.7**	**$14.9**	**$16.9**	**$16.8**	**$16.6**

Additional Information

Prior Introductions: None.

Cross File: SB 770 (Senator Pinsky) – Budget and Taxation.

Information Source(s): Comptroller's Office, Maryland Higher Education Commission, University System of Maryland, Department of Legislative Services

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