

Department of Legislative Services
 Maryland General Assembly
 2008 Session

FISCAL AND POLICY NOTE

House Bill 186 (Delegate Bates, *et al.*)
 Ways and Means

Great Schools Tax Credit Program

This bill creates an income tax credit for 50% of the contributions made by a business or individual to an eligible nonprofit organization that provides scholarships to lower-income students that attend an elementary or secondary school that is either (1) outside the district in which the student resides; or (2) a nonpublic school. The Comptroller’s Office is required to adopt regulations to implement the program and report specified information about the program to the Governor and the General Assembly by October 1 of each year.

The bill takes effect July 1, 2008 and applies to tax year 2008 and beyond.

Fiscal Summary

State Effect: Based on similar programs in other states, revenues would likely decrease by at least \$100 million annually beginning in FY 2009. Revenue losses could be substantially higher. The corporate income tax is projected to account for 60% of the tax credits. General fund expenditures could increase by \$34,000 in FY 2009 due to one-time tax form and computer programming expenditures at the Comptroller’s Office.

(\$ in millions)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
GF Revenue	(\$84.2)	(\$84.2)	(\$84.2)	(\$84.2)	(\$84.2)
SF Revenue	(15.8)	(15.8)	(15.8)	(15.8)	(15.8)
GF Expenditure	0	0	0	0	0
Net Effect	(\$100.0)	(\$100.0)	(\$100.0)	(\$100.0)	(\$100.0)

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

Local Effect: Local highway user revenues would decrease as a result of credits being claimed against the corporate income tax. Based on the assumptions above, local highway user revenues would decrease by \$3.7 million annually beginning in FY 2009. Expenditures would not be affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill creates a tax credit equal to 50% of the contributions made by a business or individual to an eligible nonprofit organization that provides scholarships to eligible lower-income students. In order to qualify, a student's household income must be less than 2.5 times the income standard used to qualify for a reduced-price lunch under the National Free or Reduced Price Lunch Program. The amount of the credit may not exceed the tax liability in the year, and any unused amount may be carried forward three tax years.

The Comptroller's Office is to maintain oversight of the program, including verifying that organizations are • distributing as scholarships a minimum of 90% of its total revenue; • eligible 501(c)(3) organizations; and • providing scholarships only to students who qualify.

Current Law: No similar tax credit exists, although businesses can deduct contributions for scholarships as charitable donations, which typically lowers federal and State income tax liability.

Background: Act 4 of 2001 established Pennsylvania's Educational Improvement Tax Credit for businesses that contribute to eligible scholarship organizations or educational improvement organizations. Subsequent legislation has increased the annual amount of authorized credits from \$30 million to \$75 million. In fiscal 2008, \$44.7 million was allocated to scholarship organizations, \$22.3 million to improvement organizations, and \$8.0 million to pre-K scholarship organizations. As of February 2008, all credit amounts were expended for improvement organizations, \$7.5 million remained for scholarship organizations, and \$1.1 million remained for pre-K organizations.

In 1997, Arizona enacted two education-related tax credits. The first is a tax credit for individuals who contribute to scholarship organizations that provide scholarships or grants to qualified students attending a nonpublic school. The maximum credit for individuals is \$1,000. The second is a credit for contributions or fees paid for public school extracurricular activities or character education programs. The maximum value of this credit is \$400. In tax year 2005, a total of \$42.2 million was claimed in public school

extracurricular fees credits and \$35.4 million was claimed in nonpublic school tuition credits.

In 2006, Arizona enacted a credit that allowed corporations to claim credits for contributions to qualifying scholarship organizations. In fiscal 2007, a total of \$10.0 million in credits could be awarded. The maximum amount that can be awarded will increase by 20% annually, totaling \$20.7 million in fiscal 2011, the last year of the program.

In 2001, Florida enacted a corporate tax credit for 75% of contributions to eligible scholarship organizations that grant scholarships to low-income students attending a nonpublic school or public school outside the student's district. Students can receive a maximum scholarship of \$3,750 annually, and up to \$500 of this amount can be used for travel expenses if the student attends a public school outside his/her district. The program was amended in 2006 to provide for greater fiscal accountability after a series of fiscal improprieties at several scholarship organizations. In the 2007-2008 school year, 20,099 students received scholarships under the program (to date); about 1% of total public school enrollment. Thirty-nine percent of students were African American, 24% were Hispanic, and 24% were White. A total of \$88 million in credits can be awarded annually.

Similar tax credit programs exist in several other states, including Iowa and Rhode Island.

Background: Under National Free or Reduced Price Lunch Program, children from families with incomes below specified thresholds are eligible for free or reduced-priced school meals. **Exhibit 1** lists the qualifying income for a reduced lunch in effect from July 1, 2007 to June 30, 2008, and the income threshold that cannot be exceeded in order to qualify for the tax credit for student expenses under HB 186.

Exhibit 1
Qualifying Income Threshold – National Free or Reduced Price Lunch Program

<u>Family Size</u>	<u>Reduced Lunch</u>	<u>HB 186 Income Threshold</u>
1	\$18,889	\$47,223
2	25,327	63,318
3	31,765	79,413
4	38,203	95,508
5	44,641	111,603

State Revenues: Tax credits could be claimed beginning in tax year 2008. Based on existing programs in other states and the value of the credit, State revenues would likely decrease by at least \$100 million annually. This estimate is based on the personal income tax credit in Arizona and corporate income tax programs in Florida and Pennsylvania, adjusted for factors that influence charitable giving and differences in population and economic activity in Maryland and these states.

The credit is limited by the taxpayer's tax liability, but unused amounts can be carried forward. As a result, revenue losses are likely to be greater beginning in fiscal 2010 as taxpayers claim credits carried forward from previous tax years.

The Comptroller's Office notes that there could be up to 661,000 eligible students under the program and, because individuals could also deduct contributions for federal tax purposes (which results in lower federal and State tax liability) and claim a 50% tax credit, the bill provides substantial incentive for contributions and revenue losses could be substantially higher than estimated.

State Expenditures: The Comptroller's Office reports that it would incur a one-time expenditure increase of \$34,000 in fiscal 2009 to add the credit to the personal income tax form. This amount includes data processing changes to the SMART income tax return processing and imaging systems and systems testing.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office, Department of Legislative Services

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