

Department of Legislative Services
Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 1259
Ways and Means

(Delegate Proctor, *et al.*)

**Building Opportunities for All Students and Teachers (BOAST) in Maryland
Tax Credit**

This bill creates an income tax credit for 75% of the contributions made by a business or nonprofit organization to an eligible nonprofit organization that either: (1) provides scholarships to eligible students or teachers at a nonpublic K-12 school; or (2) provides grants to (a) public schools to support innovative educational programs that are not part of the regular academic program in order to achieve the goals of the Bridge to Excellence in Public Schools Act of 2002; or (b) public school teachers to assist in the cost of graduate-level education or certification coursework. The amount of credits that the Maryland State Department of Education (MSDE) can award in each year cannot exceed the amount of money appropriated to a reserve fund established by the bill.

The bill takes effect July 1, 2009, and applies to tax year 2010 and beyond.

Fiscal Summary

State Effect: Potential significant general fund expenditure increase in FY 2010 and beyond. The amount of the expenditure increase depends on the amount of money, if any, appropriated to the reserve fund in each year. If the program is funded at a similar level to existing programs in other states, general fund expenditures will increase by \$50 million to \$75 million annually. Administrative costs increase by \$178,500 in FY 2010 and by \$219,400 in FY 2014.

Local Effect: Local highway user revenues distributed from the Transportation Trust Fund (TTF) will decrease as a result of credits claimed against the corporate income tax. Local expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill establishes a Building Opportunities for All Students and Teachers Reserve Fund. The total amount of initial credit certificates issued by the State Superintendent of Schools in each fiscal year cannot exceed the amount appropriated to the reserve fund in the State budget. The Governor may appropriate money to the reserve fund but the bill does not require or specify a recommended amount. The Governor may not reduce an appropriation to the reserve fund that is approved by the General Assembly. For each fiscal year, if funds are transferred from the reserve fund as a result of any law, the amount of total credits that can be approved by the Superintendent is reduced by the amount of money transferred. Any amount of money in the fund that is not expended in the fiscal year can be rolled over into the next fiscal year.

MSDE can approve a maximum of 60% of the total amount appropriated to the reserve fund for donations to education scholarship organizations (ESOs) and 40% to innovative educational organizations (IEOs). The value of the credit is equal to 75% of the eligible donation, not to exceed \$200,000. Any unused amount of the credit may not be carried forward to any other tax year. Organizations claiming the credit are required to add back the amount of credit claimed to Maryland adjusted gross income.

Organizations seeking the tax credit must apply to MSDE for each contribution it intends on making in the tax year; applications are approved on a first-come first-served basis until the total cap for the year is reached. In order for a contribution to qualify for the tax credit, the contribution must be made to an organization approved by MSDE. Upon receipt from MSDE that the business has been approved for the tax credit, the business must make its contribution within 90 days of the date of the notification letter, and provide proof within 60 days of the contribution to MSDE.

An eligible ESO must (1) be a 501(c)(3) charitable organization; (2) provide scholarship money to eligible students or teachers at a nonpublic K-12 school; (3) spend at least 85% of its annual contributions that qualify for the tax credit on scholarships; (4) contribute a maximum of 25% of its annual contributions that qualify for the tax credit to teacher scholarships at eligible nonpublic schools; (5) provide scholarships on a priority basis to students who qualify for a free- or reduced-price school lunch program under the National School Lunch Act and other students based on financial need; (6) apply to MSDE for approval in each year and submit other required information that verifies its eligibility for the program; and (7) provide scholarships to at least four different nonpublic schools annually.

An eligible IEO must (1) be a 501(c)(3) charitable organization; (2) provide grants to public schools to support innovative educational programs that are not part of the regular academic program in order to achieve the goals of the Bridge to Excellence in Public

Schools Act of 2002, or public school teachers to assist in the cost of graduate-level education or certification coursework; (3) spend at least 85% of contributions that qualify for the tax credit on grants, services, or programs for public schools and teachers in the year; (4) contribute a maximum of 25% of its annual contributions that qualify for the tax credit to teacher grants; (4) qualify as a State-aided education institution; and (5) apply to MSDE for approval and submit information that verifies its eligibility for the program.

Eligible nonpublic schools must (1) hold a certificate of approval from or be registered with the State Board of Education; (2) cannot charge tuition that is greater than the statewide average per pupil expenditure by the local education agency, as calculated by MSDE; and (3) comply with Title VI of the Civil Rights Act of 1964 as amended.

MSDE is required to (1) approve ESO and IEO and tax credit applications; (2) publish a list of eligible ESOs and IEOs; and (3) report specified information about the tax credit to the General Assembly by January 10 of each year.

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

Background: Similar tax credit programs exist in several other states, including Arizona, Florida, Georgia, Iowa, Pennsylvania, and Rhode Island. A brief discussion on the programs in Pennsylvania, Arizona, and Florida is provided below.

Pennsylvania Legislation

Act 4 of 2001 established Pennsylvania's Educational Improvement Tax Credit for businesses that contribute to eligible scholarship organizations at nonpublic schools or educational improvement organizations for "innovative programs" at public schools. Subsequent legislation has increased the annual amount of authorized credits from \$30 million to \$75 million. The credit is equal to 75% of the contribution made, not to exceed \$300,000 (\$150,000 for prekindergarten school contributions). The value of the credit can be increased to 90% of the contribution, if business agrees to provide same amount for two consecutive tax years. For contributions to prekindergarten scholarship organizations, a business may receive a tax credit equal to 100% of the first \$10,000 contributed and up to 90% of the remaining amount contributed – for a maximum credit of \$150,000 annually. During the 2007-2008 school year, organizations disbursed scholarships to 44,000 school children in addition to grants for public school programs.

In fiscal 2009, \$44.7 million was allocated to scholarship organizations, \$22.3 million to improvement organizations, and \$8.0 million to prekindergarten scholarship organizations. As of February 2009, all credit amounts were expended for both education

improvement and prekindergarten organizations and \$6.0 million remained for scholarship organizations. According to the Pennsylvania Department of Community and Economic Development Center for Business Financing, all of the credits available in each year have been awarded and, despite the recession, it expects to award the remaining \$6.0 million in credits available in fiscal 2009.

Arizona Legislation

In 1997, Arizona enacted two education-related tax credits. An individual may claim a credit for making contributions or paying fees to a public school for support of extra curricular activities or character education programs. The maximum credit is \$200 for individuals (\$400 for joint filers). An individual may also claim a credit for making a donation to a qualified organization that provides scholarships for students attending nonpublic schools. The maximum credit for individuals is \$500 (\$1,000 for joint filers).

In tax year 2007, 204,000 taxpayers claimed a total of \$95 million in credits. Of this amount, 76,000 taxpayers donated a total of \$54.3 million to 55 private scholarship organizations in calendar 2007. The average donation was \$714. Scholarship organizations awarded 27,153 scholarships in calendar 2007 (the number of students could be less as multiple scholarships can be awarded to a student). Of the \$556 million in credits that have been awarded in the 10 years of the program, \$263 million (42%) has been claimed for donations to nonpublic schools. According to published news articles, education groups and some legislators are seeking to reduce the tax credit in order to avert a \$125 million cut in basic state education funding in the current fiscal year. Both of the credits are available for K-12 education only.

In 2006, Arizona enacted a credit that allowed corporations to claim credits for contributions to qualifying scholarship organizations. The maximum amount that can be awarded will increase by 20% annually, totaling \$20.7 million in fiscal 2011. In fiscal 2008, \$12 million in credits were awarded, the maximum amount under the cap.

Florida Legislation

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. Students can receive a maximum scholarship of \$3,950 annually. The program was amended in 2006 to provide for greater fiscal accountability after a series of fiscal improprieties at several scholarship organizations. In fiscal 2008, scholarships were awarded to 21,493 students attending 933 nonpublic schools. Two-thirds of students attended elementary school, one-fifth middle school, and the remaining attended high school. Forty percent of students were African American, 24% were Hispanic, and 23% were white. The Florida legislature has increased the total amount of credits that can be awarded in each fiscal year from \$50 million in fiscal 2004 to \$118 million in

fiscal 2009. In the last three fiscal years, approximately 96% of all credits available under the cap have been awarded. The tax credit program is limited to scholarships to students attending a qualifying K-12 education school.

State Fiscal Effect:

Appropriations to the Reserve Fund

The bill provides that the Governor may appropriate funds to the reserve fund, but does not require or suggest an amount that should be appropriated. The amount of credits available for corporate donations in states with similar programs is: Arizona (\$12 million, rising to \$20.7 million), Florida (\$118 million), and Pennsylvania (\$75 million). In addition, individuals in Arizona claimed a total of \$95 million in credits.

If the program proposed by the bill is funded at a similar level as these other states, general fund expenditures will increase by \$50 to \$75 million annually. The Governor is not required to provide a program appropriation or a minimum amount, however. To the extent that the Governor provides less or no money to the reserve fund in any year, general fund expenditures will be less.

Administrative Costs

The bill requires MSDE to implement and administer the tax credit program. MSDE indicates it would need two full-time budget specialists and one support staff position. General fund expenditures will increase by an estimated \$178,500 in fiscal 2010, which reflects a three-month implementation period before credits can be approved. This estimate includes salaries, fringe benefits, and ongoing operating expenses.

The Comptroller's Office reports that it would incur a one-time expenditure increase of \$37,400 in fiscal 2010 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.

Positions	3
Salaries and Fringe Benefits	\$127,489
Operating Expenses	<u>13,620</u>
MSDE Expenditures	\$141,109
Comptroller Expenditures	\$37,400
Total FY 2010 Expenditures	\$178,509

Future year expenditures reflect a full salary with 4.4% annual increases, 3% employee turnover, and 1% increases in ongoing operating expenses. Future year administration cost at MSDE total \$191,400 in fiscal 2011, \$200,300 in fiscal 2012, \$209,600 in fiscal 2013, and \$219,400 in fiscal 2014.

Additional Information

Prior Introductions: SB 373 of 2008 received a favorable with amendments report from the Senate Budget and Taxation Committee, passed the Senate and received a hearing in the House Ways and Means Committee, but no further action was taken. HB 812 of 2008 received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: SB 715 (Senator DeGrange, *et al.*) - Budget and Taxation.

Information Source(s): Arizona Department of Revenue, Florida Office of Program Policy Analysis and Government Accountability, Georgia Department of Education, Pennsylvania Department of Community and Economic Development Center for Business Financing, National Conference of State Legislatures, Comptroller's Office, Department of Legislative Services

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