HB 769

Department of Legislative Services

2011 Session

FISCAL AND POLICY NOTE

House Bill 769 (Delegate Bates, *et al.*)
Ways and Means

Great Preschools Tax Credit Program

This bill creates an income tax credit for contributions made by a business or individual to an eligible nonprofit organization that provides scholarships to students (1) whose family income is below specified income thresholds; and (2) who attend either a qualifying nonpublic school approved by the Maryland State Department of Education (MSDE) to provide prekindergarten program services, or a nationally accredited child care center. The tax credit may not exceed 50% of the State income tax for that year. 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, 2011, and applies to tax year 2011 and beyond.

Fiscal Summary

State Effect: Based on similar programs in other states, general fund revenues may decrease by at least $9.3 million beginning in FY 2012. Transportation Trust Fund revenues may decrease by $2.0 million annually and Higher Education Investment Fund revenues may decrease by $0.7 million annually beginning in FY 2012. Revenue losses may be substantially higher. General fund expenditures increase by $0.1 million in FY 2012 due to implementation expenses at the Comptroller's Office.

($ in millions)	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
GF Revenue	($9.3)	($9.3)	($9.3)	($9.3)	($9.3)
SF Revenue	($2.7)	($2.7)	($2.7)	($2.7)	($2.7)
GF Expenditure	$.1	$.1	$.1	$.1	$.1
Net Effect	($12.1)	($12.1)	($12.1)	($12.1)	($12.1)

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

Local Effect: Local highway user revenues will decrease as a result of credits being claimed against the corporate income tax. Based on the assumptions above, local highway user revenues will decrease by an average of $197,900 annually beginning in FY 2012. Local expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill creates a tax credit equal to the contributions made by a business or individual to an eligible nonprofit organization that provides scholarships to eligible students from lower-income households. The amount of the credit may not exceed 50% of the income tax liability, and any unused amount of the credit may be carried forward three tax years.

In order to qualify, the student's household income may not exceed an amount equal to 2.5 times the income standard used to qualify for a reduced price lunch under the National Free or Reduced Price Lunch Program.

A qualifying school is a State or nationally accredited child care center or nonpublic school approved by MSDE to provide prekindergarten program services. A qualifying school must (1) comply with all health and safety laws or codes that apply to nonpublic preschools; (2) hold a valid occupancy permit if required by the county or municipal corporation where the school is located; (3) certify that it will not discriminate in admissions; and (4) provide academic accountability to parents of the students.

The Comptroller's Office must maintain oversight of the program, including verifying that organizations are (1) distributing as scholarships a minimum of 90% of its total revenue from donations; (2) eligible 501(c)(3) organizations; and (3) 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: According to the Foundation for School Choice, several states offer similar tax credit programs that grant tax credits for contributions to organizations that provide scholarships for children to attend private school; these include Arizona, Florida, Georgia, Indiana, Iowa, and Pennsylvania. Other states, including Minnesota and Illinois, offer tax credits or deductions for the eligible costs of attending a private school. A brief discussion of the programs in Pennsylvania and Florida is provided below.

Pennsylvania

In 2001, Pennsylvania enacted an Educational Improvement Tax Credit for businesses that contribute to eligible scholarship organizations for nonpublic schools or educational improvement organizations for “innovative programs” at public schools. The credit is equal to 75% of the contribution made, not to exceed $300,000. The value of the credit can be increased to 90% of the contribution, if a business agrees to provide the 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 annual credit of $150,000.

In fiscal 2011, a total of $60.0 million in credits were available under the program: $40.2 million was allocated to scholarship organizations; $13.4 million to educational improvement organizations; and $6.4 million to prekindergarten scholarship organizations. All of the credits for contributions to educational improvement organizations and prekindergarten scholarship organizations were awarded on the first day in which credits could be awarded. All program funds were exhausted within a week of the beginning of the application period.

Florida

In 2001, Florida enacted a corporate tax credit for eligible scholarship organizations that grant scholarships to low-income students attending a nonpublic school. A corporation can claim a dollar-for-dollar credit for the amount of contributions made, up to 75% of its state income tax liability. The program was amended in 2006 to provide for greater fiscal accountability after a series of fiscal improprieties at several scholarship organizations. In fiscal 2011, a total of $140.0 million in credits can be awarded. Recent legislation expanded the tax credit to other business taxes and provided that the maximum amount of credits that can be awarded could be increased by 25% if at least 90% of the maximum amount of credits were awarded.

During the 2009-2010 school year, a total of $106 million in scholarships were awarded to a total of 28,927 students enrolled in 1,033 private schools, a little less than double the amount of students receiving scholarships in the 2005-2006 school year. The average scholarship granted was $3,950.

Income Threshold for Qualifying Students

Under the National Free or Reduced Price Lunch Program, children from families with incomes below specified thresholds are eligible for free or reduced price school meals. **Exhibit 1** lists the qualifying income for a reduced price lunch in effect from July 1, 2009 to June 30, 2010, and the income threshold that cannot be exceeded in order for a family to qualify for the tax credit under the bill.

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

Family Size	Reduced Lunch	Income Threshold under the Bill
1	$20,036	$50,090
2	26,955	67,388
3	33,874	84,685
4	40,793	101,983
5	47,712	119,280

State Revenues: Tax credits can be claimed beginning in tax year 2011. Based on existing programs in other states and the value of the credit, State revenues may decrease by at least $12.0 million annually beginning in fiscal 2012. This estimate is based on similar programs in other states, adjusted for differences between existing programs and the program proposed by the bill, 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 for up to three years. As a result, revenue losses are likely to be greater beginning in fiscal 2013 as taxpayers claim credits carried forward from previous tax years. In addition, the bill provides a substantial incentive to make a qualifying contribution and claim a tax credit. As a result of this incentive, revenue losses may be significantly higher than estimated.

It is also assumed that it is the intent of the bill to limit scholarships and tax credits to students in prekindergarten or child care programs. To the extent that under the bill tax credits are claimed on behalf of scholarships to students enrolled in grades K-12 at a school that offers prekindergarten programs, the revenue loss will be significantly higher than estimated.

State Expenditures: The bill requires the Comptroller's Office to administer the tax credit program. The Comptroller's Office indicates it will need one revenue specialist. General fund expenditures will increase by an estimated $122,000 in fiscal 2012, which reflects the bill's July 1, 2011 effective date. This estimate includes salaries, fringe benefits, and ongoing operating expenses.

The Comptroller's Office also reports that it will incur a one-time expenditure increase of $40,000 in fiscal 2012 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	1
Salary and Fringe Benefits	$75,177
Operating Expenses	6,775
Computer Programming Expenses	40,000
Total FY 2012 Expenditures	**$121,952**

Future year expenditures reflect a full salary with 4.4% annual increases and 3% employee turnover, as well as 1% annual increases in ongoing operating expenses.

Additional Information

Prior Introductions: HB 952 of 2010 and HB 603 of 2009 received a hearing in the House Ways and Means Committee, but no further action was taken. HB 186 of 2008 received an unfavorable report from the House Ways and Means Committee.

Cross File: None.

Information Source(s): Maryland State Department of Education, Comptroller's Office, Foundation for School Choice, Department of Legislative Services

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