

Department of Legislative Services  
2010 Session

FISCAL AND POLICY NOTE

Senate Bill 385

(Senator DeGrange, *et al.*)

Budget and Taxation

Ways and Means

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

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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 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, 2010, and applies to tax year 2011 and beyond.

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**Fiscal Summary**

**State Effect:** Potential significant general fund expenditure increase beginning in FY 2011. 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 \$50.0 million annually. Administrative costs increase by \$183,000 in FY 2011 and by \$208,400 in FY 2015.

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

**Small Business Effect:** Minimal.

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## 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. Any amount of money in the fund that is not expended in the fiscal year must 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 educational 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 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.

An eligible ESO must (1) be a 501(c)(3) charitable organization; (2) provide scholarships 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 meals 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 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; (5) qualify as a State-aided education institution; and (6) apply to MSDE for approval and submit information that verifies its eligibility for the program.

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 Governor and 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 Program*

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.

In fiscal 2008 and 2009, a total of \$75 million in credits were available under the program: \$44.7 million was allocated to scholarship organizations; \$22.3 million to improvement organizations; and \$8.0 million to prekindergarten scholarship organizations. The total amount of credits was reduced to \$60.0 million in fiscal 2010 and \$50.0 million in fiscal 2011. All of the credits are typically awarded in each fiscal year.

#### *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. 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. A maximum amount of \$10 million in credits may be awarded in fiscal 2007. This limit will increase by 20% annually, totaling \$20.7 million in fiscal 2011. In fiscal 2009, \$10.8 million in credits were awarded.

### *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. Of the students receiving scholarships, 40% 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.

### **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. If the program proposed by the bill is funded at a similar level as these other states, general fund expenditures will increase by \$50.0 million annually. To the extent that the Governor provides less or no money to the reserve fund in any year, the increase in general fund expenditures will be less. Although the tax credit can be claimed beginning in tax year 2011, appropriations to the reserve fund may be made beginning in fiscal 2011.

### *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 \$145,600 in fiscal 2011, 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 2011 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.

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Salaries and Fringe Benefits	\$128,836
Operating Expenses	<u>\$16,723</u>
<b>MSDE Expenditures</b>	<b>\$145,559</b>
<b>Comptroller Expenditures</b>	<b>\$37,400</b>
<b>Total FY 2011 Expenditures</b>	<b>\$182,959</b>

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 \$180,600 in fiscal 2012, \$189,400 in fiscal 2013, \$198,600 in fiscal 2014, and \$208,400 in fiscal 2015.

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### **Additional Information**

**Prior Introductions:** SB 715 and HB 1259 of 2009 were not reported from the Senate Budget and Taxation Committee and the House Ways and Means Committee, respectively. 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:** HB 946 (Delegate Proctor, *et al.*) - Ways and Means.

**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, Maryland State Department of Education, Comptroller's Office, Department of Legislative Services

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