

**LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS**

Bill No: SB 355

49th Legislature, 1st Session, 2009

Short Title: Nonpublic School Scholarship Tax Credit

Sponsor(s): Senator Pete Campos

Analyst: Pamela Herman

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Bill Summary:

SB 355 adds a new section to the *Income Tax Act* and a new section to the *Corporate Income and Franchise Tax Act*, creating the “equal opportunity scholarship tax credit”:

- The credit may be taken against a New Mexico taxpayer’s income tax or corporate tax liability for contributions in the same amount made to a 501(c) (3) charitable organization that allocates at least 90 percent of its annual revenue for educational scholarships or tuition grants to “eligible” students to attend a “qualified” nonpublic elementary or secondary school in New Mexico.
- In any taxable year, the personal income tax credit may not exceed \$500 for an individual or \$1,000 for a married couple filing jointly; however, the corporate income tax deduction may be claimed “in an amount equal to the total contributions made.”
- The credit must be taken in lieu of a deduction from the taxpayer’s federal tax obligation.

SB 355 defines an eligible student as a student who:

- is a member of a household whose total annual income does not exceed an amount used to qualify for a reduced-price lunch through the federal school lunch program. Once a student receives a scholarship pursuant to the program, the student will remain eligible regardless of household income until the student graduates from high school or reaches 21 years of age; and
- resides in New Mexico while receiving a scholarship from a scholarship granting organization.

SB 355 defines a “qualified school” as an accredited nonpublic elementary or secondary school in New Mexico that:

- does not discriminate in admissions or treatment of students on the basis of a student’s race, national origin, or ethnicity;
- has been granted exemption from federal income tax as an organization qualified pursuant to Section 501(c) (3) of the Internal Revenue Code;
- requires students to take an annual academic test with individual scores provided to the parents of students;
- complies with all state laws that apply to nonpublic schools regarding criminal background checks for employees and that exclude from employment any person not permitted by state law to work in a nonpublic school; and

- fills available spaces by a random selection process, except that a qualifying school may give preference to siblings of enrolled students and previously enrolled scholarship students, if a qualifying school has more eligible students applying than spaces available.

Fiscal Impact:

The bill does not contain an appropriation.

To date, the Legislative Finance Committee has not issued a Fiscal Impact Report (FIR) nor has the Taxation and Revenue Department issued an agency analysis of SB 355. However, for similar legislation introduced during the 2008 legislative session, the FIR estimated a recurring general fund loss of approximately \$4.8 million beginning in the year,¹ following the first year to which the credit would apply, in this case FY 11.

Because of a “sunset clause,” the tax credit in SB 355 would apply to taxable years beginning on or after January 1, 2010, but not to taxable years beginning after January 1, 2014.

Fiscal Issues:

According to data available on the Public Education Department (PED) website, during school year 2008-2009 there were approximately 16,900 students enrolled in accredited nonpublic schools. However, there is no way of determining how many of those students have received a scholarship from a 501(c) (3) charitable organization, how many would qualify for a reduced-price lunch through the federal school lunch program, or how many attend nonpublic schools that fill available spaces using a random selection process.

One organization in New Mexico that would meet the criteria in SB 355 for a 501(c) (3) charitable organization is Educate New Mexico. Educate New Mexico describes itself as “an independent, nonprofit organization established by volunteers ... to assist low-income families with children entering grades K-12 [to] offset the cost of tuition at the school of their choice through a program of tuition assistance,” funding for which is provided “from private business and charitable and individual contributions.” According to information available on Educate New Mexico’s website, families qualify for assistance on the basis of income levels similar to those “used by the United States Department of Agriculture to determine if a family qualifies for the federally-funded school lunch program.”

Issues:

In its analysis of SB 355, PED notes that, because the bill allows a taxpayer to take a tax credit even if the taxpayer’s contribution is to a 501(c) (3) charitable organization that primarily supports private religious schools, “the state may find itself indirectly supporting private religious schools,” thus possibly coming into conflict with the Establishment Clause of the First Amendment to the federal constitution. The Establishment Clause states, “Congress shall make no law respecting an establishment of religion....”

For many years, the standard in deciding so-called “establishment” cases was *Lemon v. Kurtz*, 403 US 602 (1971). This Supreme Court nearly unanimous decision (with one justice not participating) established a three-part test for laws dealing with religious establishment. The Court found that, to be constitutional, a statute:

¹ Data were extrapolated from the Arizona Department of Revenue for a credit similar to the proposal in SB 355.

- must have a “secular legislative purpose”;
- must have principal effects that neither advance nor inhibit religion; and
- must not foster “an excessive entanglement with religion.”

However, PED indicates that the language in SB 355 “does not reflect all three prongs” of the test in *Lemon v. Kurtz*.

Since the *Lemon* decision, the Supreme Court has announced a string of other opinions regarding the constitutionality of state assistance to nonpublic schools, leaving the law in this area less settled.

US Supreme Court Decisions

- PED notes that, on November 27, 2006, the US Supreme Court refused to hear a challenge to an April 2006 decision of the Maine Supreme Judicial Court that upheld a Maine law prohibiting the use of public funds to send students to private religious schools.
- In *Hibbs v. Winn*, 542 U.S. 88 (2004), despite a provision in the federal *Tax Injunction Act* prohibiting federal courts from restraining the implementation of state tax laws, the Supreme Court asserted the jurisdiction of the federal courts in such cases. At issue was a claim of violation of the Establishment Clause in a suit seeking to enjoin the operation of an Arizona tax law that authorizes an income tax credit for payments to nonprofit “state tuition organizations” that award scholarships to students in private elementary/secondary schools, including those attending religious-based schools. The case did not resolve the main question regarding the constitutionality of the tax credit.
- In *Zelman v. Simmons-Harris*, 536 U.S. 639 (2002), the Supreme Court held that an Ohio pilot scholarship program did *not* violate the Establishment Clause in giving aid primarily to families below the poverty line with children at a failing school district so they could choose to attend either another public school or private school, receive tutorial assistance, enroll in a magnet school, or receive a scholarship.
- In *Mueller v. Allen*, 463 U.S. 388 (1983), on a five-to-four vote, the Supreme Court *upheld* a Minnesota law, challenged on the basis that it violated the Establishment Clause, that allowed state taxpayers, in computing their state income tax, to deduct expenses incurred in providing “tuition, textbooks and transportation” for their children attending a private elementary or secondary school.
- Earlier, in *Byrne v. Public Funds for Public Schools of New Jersey*, 442 U.S. 907 (1979), the Supreme Court summarily affirmed a lower federal court holding that a state tax deduction for taxpayers with children attending nonpublic school *violated* the Establishment Clause.
- In *Franchise Tax Board of California v. United Americans for Public Schools*, 419 U.S. 890 (1974), the Court summarily affirmed a lower federal court judgment that *struck down* a state statute providing income-tax reduction for taxpayers sending children to nonpublic schools.
- In *Committee for Public Education & Religious Liberty v. Nyquist*, 413 U.S. 756 (1973), the court stated, “The system of providing income tax benefits to parents of children attending New York’s nonpublic schools also *violates* the Establishment Clause because, like the

tuition reimbursement program, it is not sufficiently restricted to assure that it will not have the impermissible effect of advancing the sectarian activities of religious schools.”

New Mexico Constitution

Article 12, Section 3 of the New Mexico Constitution states in part, “. . .no part of the proceeds arising from the sale or disposal of any land granted to the state by congress, or any other funds appropriated, levied or collected for educational purposes, shall be used for the support of any sectarian, denominational or private school, college or university.” Proceeds from state income taxes are the second largest source (after gross receipts taxes) of General Fund dollars, and General Fund dollars are the source of an average of 90 percent of funding for public schools in New Mexico.

The New Mexico Constitution’s so-called “Anti-Donation Clause” (Article 9, Section 14) is often interpreted as a prohibition against public support of private interests. It states in part, “Neither the state nor any county, school district or municipality . . . shall directly or indirectly lend or pledge its credit or make any donation to or in aid of any person, association or public or private corporation”

The New Mexico Attorney General has considered the question of the constitutionality of state assistance to private school students on several occasions, most recently in an opinion dated January 29, 1999.

- Citing the federal decisions in *Nyquist* and *Mueller*, above, the opinion stated that the prohibition in Article 12, Section 3 is not limited to direct payments from the state to private schools, but prohibited payments provided to private school students or their parents.
- In addition, the opinion stated that the anti-donation clause in Article 9, Section 14 appears to prohibit the state from providing tuition assistance in the form of vouchers to private school students, stating, “Whether the beneficiary of the assistance is the parents or the schools, the use of public money to subsidize the education of private school students, without more, is a donation to private persons or entities in violation of the state Constitution.”
- The opinion also suggested that a voucher program might run afoul of Article 12, Section 1, which states that a “uniform system of free public schools sufficient for the education of, and open to, all the children of school age in the state shall be established and maintained.” If it diverted funds from the public schools to the extent that it compromised the state’s ability to meet its obligation to establish and maintain a public school system sufficient to educate all school-age children in the state, such a program might be found to be unconstitutional.

Related Bills:

SB 575a *Instructional Material Purchases*

SB 603 *Private School Tuition Tax Deduction*