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FISCAL IMPACT REPORT

ORIGINAL DATE 02/13/10

SPONSOR Campos, P. LAST UPDATED _____ HB _____

SHORT TITLE Scholarship Donation Tax Credit SB 198

ANALYST Gutierrez

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY10	FY11		
	\$6,200.0	Nonrecurring	General Fund

(Parenthesis () Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	FY11	FY12		
	(\$886.0)	(\$6,808.0)	Recurring	General Fund

(Parenthesis () Indicate Revenue Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From

Taxation and Revenue Department (TRD)

Public Education Department (PED)

Department of Finance and Administration (DFA)

SUMMARY

Synopsis of Bill

Senate Bill 198 provides an “equal opportunity scholarship tax credit” for contributions made to scholarship granting organizations against corporate or personal income tax obligations. The credit could only be claimed in the same taxable year in which the contribution was made. Credits would not be allowed for contributions included in a taxpayer’s itemized deductions. A scholarship granting organization must be a 501(c) (3) organization that devotes at least 90

percent of contributions it receives and all earnings from investment of these contributions on educational scholarships for students with family income (at the time of the initial scholarship grant) no higher than the qualifying income for a reduced-price lunch under the federal school lunch program. Educational scholarships could only be used by students who reside in New Mexico, and only to pay tuition and fees to qualified schools as defined in the Act. The credit would be for 100 percent of contributions, but not to exceed \$50,000 for contributions made by a corporation, \$500 for contributions made by a single taxpayer or \$1,000 for contributions made by married taxpayers filing a joint return.

The bill 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 the 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;
- operates in New Mexico;
- complies with all state laws that apply to nonpublic schools regarding criminal background checks for employees and 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.

The bill also appropriates \$1.2 million to the public education department (PED) for expenditure in fiscal year 2011 to make annual grants on a competitive basis for innovative efforts by educational providers to reduce the dropout rate for minority students. The balance shall revert to the general fund.

The bill also appropriates \$5 million to PED for expenditure in fiscal year 2011 to aid public schools to reflect the savings achieved through the equal opportunity scholarship tax credit program. The balance shall revert to the general fund.

The provisions of the Act are applicable to taxable years beginning on or after January 1, 2011, but before January 1, 2015.

Because no effective date is provided in the bill, its provisions will become effective ninety (90) days after the 2010 legislative session adjourns.

FISCAL IMPLICATIONS

TRD:

The revenue impact related to the personal income tax was based on the experiences of two states that analyzed similar tax credits, Ohio¹ and Arizona.² The 2002 revenue losses estimated in Ohio and Arizona were \$14.0 and \$14.2

¹ http://www.lbo.state.oh.us/fiscal/fiscalnotes/124ga/HB0202IN.htm#_ftn1

² <http://www.azleg.state.az.us/legtext/45leg/1r/fiscal/hb2146.htm>

million, respectively. Adjusting by population, the revenue loss for New Mexico would be \$2.6 million according to the Ohio experience, and \$4.4 if based on the Arizona experience. For the purposes of this estimate, a simple average of \$3.5 million in 2002 was used.

The revenue impact related to the corporate income tax was calculated using the amount of corporate giving in 2000 (\$10.9 billion)³ in the entire United States, of which 4.5% (\$490.5 million) was donated to schools. Adjusting this number to New Mexico using a population ratio of 0.65 yields an estimate of \$31.8 million, of which 5% flows to scholarships for low-income students. Hence the estimate for New Mexico in 2000 is \$1.6 million.

The individual and corporate income tax credit amounts (for 2002 and 2000, respectively) were assumed to grow at a 3% annual growth rate.

SIGNIFICANT ISSUES

TRD:

Arguments challenging the constitutionality of the Arizona credits have arisen on the grounds that credits essentially provide public funding for private schools. Similar arguments could be made with respect to the proposed equal opportunity scholarship tax credit in New Mexico. The credit may also violate the Anti-Donation Clause of the New Mexico Constitution.

PED:

Although categorized as an “Equal Opportunity Scholarship Credit” (Credit), the credit does not prohibit discrimination on the basis of religion. (See, e.g., pg 4 lines 12-14; pg 9 lines 6-85; pg 13 lines 3-5.)

Because the bill does not restrict the availability of the credit if the 501(c) \3 charitable organization primarily supports private religious schools, the state may find itself indirectly supporting private religious schools by permitting corporate and individual taxpayers to take the credit. This is more so of consequence since the bill does not prohibit discrimination on the basis of religion. The structure of this credit, therefore, implicates the Establishment Clause (1st Amendment) of the federal Constitution. It bears observation that SB 198 defines a qualified school as one that does not discriminate on the basis of a student’s race, national origin or ethnicity, noticeably omitting religion or gender, and that qualified schools may not have admissions standards, as many secular private schools do. The language in the bill does not reflect all three prongs of the test for determining Establishment Clause violations, which were laid down by the Supreme Court in *Lemon v. Kurtz*, 403 U.S. 602 (1971).

ADMINISTRATIVE IMPLICATIONS

PED:

The PED will incur substantial administrative duties if SB 198 is passed. The PED will be required to:

³ Matthew Sinclair. *The Non-profit Times* – June 1, 2001.

- 1) develop a committee or office and process to evaluate and administer the “competitive grants”.
- 2) investigate the “innovative efforts” of each school as a preliminary step in the grant evaluation.
- 3) administer the \$5 million set aside for public schools and will have to determine how much each school will receive based on their involvement with the tax credit program.

TECHNICAL ISSUES

TRD:

Ensuring that taxpayers have not included donations in itemized deductions will be difficult, as we do not collect itemized deduction information from the federal 1040 Form.

BLG/mew

The Legislative Finance Committee has adopted the following principles to guide responsible and effective tax policy decisions:

1. ***Adequacy:*** revenue should be adequate to fund government services.
2. ***Efficiency:*** tax base should be as broad as possible to minimize rates and the structure should minimize economic distortion and avoid excessive reliance on any single tax.
3. ***Equity:*** taxes should be fairly applied across similarly situated taxpayers and across taxpayers with different income levels.
4. ***Simplicity:*** taxes should be as simple as possible to encourage compliance and minimize administrative and audit costs.
5. ***Accountability/Transparency:*** Deductions, credits and exemptions should be easy to monitor and evaluate and be subject to periodic review.

More information about the LFC tax policy principles will soon be available on the LFC website at www.nmlegis.gov/lcs/lfc