

**LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS**

Bill Number: SB 113

50th Legislature, 1st Session, 2011

Tracking Number: .183420.2

Short Title: Tax Credit for Certain Scholarship Donations

Sponsor(s): Senator Mark Boitano

Analyst: Pamela Herman

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Bill Summary:

SB 113 amends the *Income Tax Act* to provide for a personal income tax credit of up to \$500 per taxable year for a contribution to a “school tuition organization” for educational scholarships or tuition grants for one or more children.

Among its provisions, SB 113 states that:

- the purpose of the credit is to encourage individuals and businesses to contribute to school tuition organizations that provide scholarships for students to attend “nongovernmental schools” chosen by the students’ parents;
- the credit shall not be allowed for a contribution in a taxpayer’s itemized deductions, and may only be claimed for the tax year in which the contribution was made;
- a husband and wife who file separately for a tax year in which they could have filed jointly may each only claim one-half of the credit they could have claimed on a joint return;
- the Taxation and Revenue Department (TRD) shall:
 - compile an annual report for the Revenue Stabilization and Tax Policy Committee (RSTPC) showing how many taxpayers are approved for the credit and the aggregate and median amounts of credits approved; and
 - determine every four years, beginning in 2015, if the credit is achieving its purpose;
- certain terms are defined as follows:
 - “nongovernmental school” means a nonprofit or for-profit elementary, middle or secondary school;
 - “qualified school” to mean an accredited nongovernmental elementary, middle or secondary school in New Mexico; and
 - school tuition organization” means an organization that:

- ✓ has 501(c)(3) tax exempt status under federal law;
- ✓ provides scholarships to students to attend any qualified school of their parents' choice; and
- ✓ expends 100 percent of its tax-credit-qualifying revenue for scholarships for children enrolled in qualified schools.

Fiscal Impact:

SB 113 does not contain an appropriation.

Fiscal Issues:

According to the TRD bill analysis, the fiscal impacts of SB 113 are uncertain but likely to be substantial. Based on New Mexico personal income tax data, TRD estimates that:

- 7,500 tax returns for 2011 would claim the full amount of the credit;
- 6,000 returns would claim half the credit;
- the total fiscal impact for FY 12 would be approximately \$5.0 million; and
- the amount is assumed to grow significantly over time, to as much as approximately \$11.0 million by FY 15.

Technical Issues:

The substance of the bill speaks to scholarship for “nongovernmental schools.” In its definitions, however, SB 113 limits the applicability of the tax credit to contributions made to organizations that fund scholarships at “*accredited* nongovernmental schools.”

Since the limitation to accredited schools appears to be a matter of substance, the sponsor may wish to propose an amendment that modifies “nongovernmental” on page 2, line 10, and the phrase “elementary, middle or secondary school” on page 3, line 21 by the term “accredited,” and that deletes the term “qualified school” and “qualified” from the subsection of the bill containing definitions, on page 3, lines 22-24 and page 4, lines 9 and 12.¹

Substantive Issues:

The TRD bill analysis notes that provisions of the proposed measure allowing credits to private schools may be subject to legal challenge on the basis of the federal constitutional requirement for the separation of church and state. TRD states that a provision similar to that in SB 113 was challenged in Arizona and found constitutional.

In 2009, the Public Education Department (PED) bill analysis for SB 355, *Nonpublic School Scholarship Tax Credit* (a bill very similar to SB 113) raised concerns about potential conflicts between its provisions and the Establishment Clause of the federal Constitution and the Anti-donation Clauses of the New Mexico Constitution. In its analysis of SB 355, PED noted that,

¹ According to the Legislative Council Service *Legislative Drafting Manual*, substantive law should not be put in a definition section, since to do so can cause unnecessary problems with amendments as well as enforcement of the law.

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 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). The Supreme Court's nearly unanimous decision established a three-part test for laws dealing with religious establishment; to be constitutional, a statute must:

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

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

US Supreme Court Decisions

- 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 April 2009, in *Winn v. Arizona Christian School Tuition Organization*, the 9th Circuit Court of Appeals ruled that a group of taxpayers had stated a valid legal claim that an Arizona tuition tax credit law similar to that proposed in SB 113 violates the US Constitution's Establishment Clause. In that case, the statute allowed for contributions to "state tuition organizations (STOs)" that "allow them to attend *any* [emphasis supplied] qualified school of their parents' choice"—language identical to that in SB 113.
- 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.” According to the Legislative Finance Committee, proceeds from state income taxes are the second largest source (after gross receipts taxes) of General Fund revenues, 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 118 *Optional Contribution to School Fund*

SB 398 *Enact “Special Needs Student Scholarship Act”*

SB 433 *Equal Opportunity Scholarship Act*