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## FISCAL IMPACT REPORT

ORIGINAL DATE 02/15/11

SPONSOR Ortiz y Pino LAST UPDATED \_\_\_\_\_ HB \_\_\_\_\_

SHORT TITLE Enact "Special Needs Student Scholarship Act" SB 398

ANALYST \_\_\_\_\_

### REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	FY12	FY13		
	(\$312.0)	(\$357.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

### ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
<b>Total</b>		\$27.0	\$27.0	\$200.0	Recurring	PED (General Fund)

(Parenthesis ( ) Indicate Expenditure Decreases)

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Public Education Department (PED)

Richard Komer, Institute for Justice

### SUMMARY

#### Synopsis of Bill

Senate Bill 398 enacts the "Special Needs Student Scholarship Act," and creates an income tax and corporate tax credit for contributions to a tuition scholarship organization that will provide educational scholarships for special needs students to attend public or private schools of the parents' choice. The bill outlines the process for certifying tuition scholarship organizations, the duties of the scholarship organization, along with the duties of the PED in regards to the administration of the Special Needs Student Scholarship Act.

The amount of scholarship is limited to 80% of the "three-year rolling average of the state equalization guarantee distribution for the respective level of an eligible student as calculated for the associated program units." While the scholarship amount is limited, the amount of the

income tax or corporate income tax credit is 90% of the amount donated, limited to 50% of the taxpayers liability. Amounts donated in excess of the 50% limit may be rolled over for three years (with apparently no restriction on stacking rollovers or limiting refundability in the rollover year).

The bill also amends the membership projections and budget requests under 22-8-12.1 NMSA 1978 in case any parents of special needs students parents choose to have their children attend public schools and receive a scholarship through a TSO payable to the public school. SB 398 would provide additional choices to parents of children attending private schools since the cost of attending private schools could be partially covered by the scholarships awarded to their child.

## **FISCAL IMPLICATIONS**

According to PED, there have been an average of roughly 130 students (aged 3 – 21) with disabilities enrolled in private or parochial schools in NM over the previous three years. (See table below.) Assuming that the average tuition payment, net of current scholarships is \$4,000 (approximately 80% of “three-year rolling average of the state equalization guarantee distribution for the respective level of an eligible student as calculated for the associated program units;”) Further assume that half of the parents have sufficient liability to cover the full amount of the credit and the other half can cover 20% of the tuition paid amount with personal income tax liability. The general fund impact will be  $65 * \$4000 + 65 * 4000 * .2 = \$312K$ . This implicitly assumes that the private and parochial schools will adjust regular needs-based scholarships to take advantage of this proposal.

The fiscal analysis assumes that the scholarship organizations would receive donations to cover operating costs from PACs, or other out-of-state, not-for-profit entities. Funds donated by a national donor organization would not reduce general fund revenues, since the credit is not only not refundable, but is limited to 50% of the taxpayers liability after other credits are applied. Non-profits would have no personal or corporate income tax liability, hence no tax credit.

Note also that unlike donations to not-for-profit organizations under the federal IRS code, the state tax credit does not prohibit the donor of the funds from receiving any services or goods in exchange for the donation. The bill prohibits claiming a credit for donations claimed on an IRS Form 1040 or a corporate income tax return and claiming a credit on the same donation. For genuine deductions from third parties, the state tax credit is worth substantially more than a combined federal and state tax deduction. For the state tax credit granted to parents and related individuals of the student, IRS would not allow a deduction because of the educational services received. For this class of donation, the value of the state credit far exceeds the zero value of the (disallowed) deduction.

Since Individuals with Disabilities Education Act (IDEA) guarantees specialized and highly qualified teachers for students with Individual Educational Plans (IEP), the pool of applicants for these vouchers is quite limited. There is no particular benefit of these vouchers conferred on parents enrolling their special needs children in public school. There is no compelling reason for these parents to make donations to the TSO in exchange for a special needs scholarship. The major participation in this scholarship plan would be from parents with special needs students enrolled in private or parochial schools. There would be some growth in out-years in parents taking up these vouchers for use in private and parochial schools, but growth might be in the 10% to 15% per year. Note the comment, however, under significant issues regarding future fiscal consequences of this voucher program.

It appears that this bill creates a very limited voucher program intended to strategically establish the constitutionality and legality of the concept. If a voucher program were made general and expanded, parents could donate money to a scholarship organization and receive a tax credit for 90% of the amount donated. The donation would be a legal fiction really intended to allow parents to receive almost dollar-for-dollar credit against the cost of their children's private or parochial education. If the program became general, then the fiscal impact on state revenues could be very large. However, the impact on enrollment would probably not be nearly as great as the impact on revenue. The marginal elasticity of the tax credit on enrollment would be somewhere in the range of -.4 to -.6 based on tuition payments net of current scholarships. The revenue cost would come from "buying the base," that is, if the program became general, the parents of every student enrolled in private or parochial schools would be eligible for a credit equal to 90% of the amount they currently pay for tuition. To reiterate, this warning is not applicable to this bill, but to the extent that this bill creates a precedent, policy makers should understand the larger consequences of this proposal.

PED notes that administration of this program would require certification of each tuition scholarship organization (TSO), calculating associated program units for eligible students receiving scholarships while attending public schools and monitoring and auditing TSO compliance. Total cost of carrying out PED responsibilities associated with passage of this bill would be about \$27, assuming fewer than 50 TSO's were established. However, PED notes that this estimate depends on the numbers of TSOs certified, the number to be monitored, and the number of scholarships awarded. If the number of TSOs is high (such as 50 or more), the estimated costs provided here would be low, and the cost to PED could increase substantially. If the positions identified were required to be full-time, the total cost would increase to \$212.5. These estimates are speculative as there is no way to accurately predict what the numbers would be.

There is a remote possibility that the provisions of this bill could be used by taxpayers to earmark a portion of their tax payments for specific purposes and deny that revenue to priorities of the legislature and governor. This remote possibility is not quantified in the fiscal table. See "Significant Issue" below for more discussion of this point.

### **SIGNIFICANT LEGAL ISSUES**

The AGO has not weighed in on the legal issues involved in this form of vouchers. However, Richard Komer, Senior Litigator for the Institute for Justice, has written several rebuttal letters to the sponsors and PED concerning legal contentions expressed in previous bill reviews on bills proposing vouchers. Counselor Komer's conclusion is that vouchers funded by state personal income tax and corporate income tax credits are constitutional and do not violate anti-donation provisions of the state constitution. The state grants a number of tax credits to private individuals and companies without those tax credits violating anti-donation doctrine. Article XII, Section 3 reads as follows:

Sec. 3. [Control of constitutional educational institutions; use of state land proceeds and other educational funds.]

The schools, colleges, universities and other educational institutions provided for by this constitution shall forever remain under the exclusive control of the state, and no part of the proceeds arising from the sale or disposal of any lands 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.

Funding special needs scholarships with donations and allowing a personal or corporate income tax credit for 90% of the value of the donation, even if the donor is receiving educational services in exchange for the donation is likely to conform to both the anti-donation provisions and the prohibition on using state funds for private or parochial education.

The remainder of this bill review assumes that there is no constitutional or statutory defect in the bill's proposal.

### SIGNIFICANT ISSUES

One important policy issue is implicit in this bill. While it is not likely to happen in amounts that would devastate state revenues, the provisions of the bill give individuals the ability to direct their tax payments based on their own wishes and not the wishes of the legislature and the governor. An individual who wanted to support special needs education and not, for example, general assistance or Medicaid, could give their tax money to a TSO and get a tax credit for 90% of the amount donated. The amount of the credit would be limited to 50% of the taxpayer's net liability, but the credit amount would not be available to the legislature for appropriation. This possibility is not included in the fiscal analysis above.

For public schools, the cost of providing special education is already covered by state funds from the State Equalization Guarantee (SEG) and supplemented by Individuals with Disabilities Education Act (IDEA) sub-grants that require special education to be provided to public school students at no cost to the parents.

The number of children with disabilities parentally placed in private schools is a small percentage compared to all children with disabilities in New Mexico. PED has provided the table below, which highlights the number of children with disabilities parentally placed in New Mexico's private schools.

School Year	Number of children parentally placed in private schools	Total number students (aged 3 – 21) with disabilities in NM
2007/2008	145	46,384
2008/2009	104	45,957
2009/2010	161	45,782

PED has also provided the chart below, which displays the percentage of Parentally Placed Private School Students in the U.S. compared to New Mexico. New Mexico is significantly below the national average.

School Year	NM %	US %
2008/2009	0.53%	2.27%
2007/2008	0.73%	2.31%

Note: 2009/2010 data not yet available on IDEAdata.org

PED notes the following regarding the parental placement of special needs students in private or parochial schools.

The bill provides for the educational scholarships for special needs students to attend public or private schools of the student's parents' choice. The IDEA includes federal regulations regarding students with disabilities parentally placed in the private schools. Under 34 CFR § 300.130 a parentally placed private school child with a disability means a child with a disability enrolled by his/her parent in private, including religious, schools or facilities.

The provision of special education services in private schools differs from the services provided in the public schools. In the public schools, students identified as having disabilities under the IDEA or Subsection B(4) and B(18)(b) of 6.31.2.7 NMAC are required to have an Individualized Education Program (IEP) developed and implemented in accordance with 34 CFR §§ 300.320 through 300.324.

Children enrolled by their parents in private schools or facilities are not entitled to an IEP. It is important to note that 34 CFR § 300.137(a) states that no parentally placed private school child with a disability has an individual right to receive some or all of the special education and related services that the child would receive in a public school. Children with disabilities enrolled by their parents in private schools are not entitled to Free Appropriate Public Education (FAPE) under 34 CFR § 300.101. The school district is responsible for making the final decisions with respect to the services to be provided to the parentally placed private school student.

34 CFR § 300.132(b) requires a service plan to be developed and implemented for each private school child with a disability who has been designated by the local education agency (LEA) in which the private school is located to receive special education and related services. Guidance on the development of service plans can be found at <http://www.ped.state.nm.us/SEB/law/Private%20School%20Q%20and%20A.pdf>.

The provision of special education and related services, meaning the how, where, and by whom services will be provided, are determined through consultation between the private school and the school district where the private school is located. This includes discussions about the types of services, including direct services and alternate service delivery mechanisms and how special education and related services will be apportioned if funds are insufficient to serve all parentally placed private school children. Children with disabilities enrolled by their parents in private schools are counted in the enrollment of the school district where the private school is located. The school district uses the enrollment count to determine the proportionate amount of IDEA funds to be utilized to provide services for students in the private schools.

It is important to point out that limited procedural safeguards under the IDEA are available to parents and their students, who are parentally placed in private schools. A parent cannot file for due process relating to the identification, evaluation, or the educational placement of a child with a disability or the provision of FAPE, except in regards to child find. The reasons to file state-level complaints are also limited to include only service plans, expenditures, consultation with the school district, proportionate share of IDEA funds, and equitable services. Parents and their children with disabilities are entitled to the full procedural safeguards under the IDEA in accordance with 34 CFR § 300.504, if enrolled in the public schools.

Students enrolled in the public schools are entitled to be taught by highly qualified teachers under the Elementary and Secondary Education Act (ESEA) and highly qualified special education teachers under the IDEA. However, in accordance with 34 CFR § 300.18(h), highly qualified requirements do not apply to teachers hired by private elementary and secondary schools including private school teachers hired or contracted by school districts to provide equitable services to parentally placed private school children with disabilities.

## **ADMINISTRATIVE IMPLICATIONS**

PED notes, "...the PED would have to certify and monitor TSOs and administer the Act which (unless the number of TSOs and scholarships awarded were very low) would require additional staff or FTE. At this point, there is no way to predict what those numbers would be and as a result, the administrative costs identified in the Fiscal Implications section assumes a low to moderate number of TSOs and scholarships awarded."

## **TECHNICAL ISSUES**

It is not clear that any rollover tax credit in excess of 50% of the current year's PIT or CIT liability would be limited in the rollover year to 50% of that year's liability. A case could certainly be made that the entire amount of excess could be used up in the first subsequent year.

Similarly, it is not clear that a rollover credit in excess of 50% of the current year's PIT or CIT liability would not be fully refundable in the rollover year, even in excess of the rollover year's total liability.

It is unclear from the phrase "shall not exceed eighty percent of the three-year rolling average of the state equalization guarantee distribution for the respective level of an eligible student as calculated for the associated program units" includes or excludes the adjustment in the school equalization guarantee (SEG) for special needs students. See "Questions" below.

PED notes that, "...SB 398 may conflict with the provisions of the Open Enrollment Statute, Paragraph (3) of Subsection E of Section 22-1-4 NMSA 1978 which establishes priorities for enrollment for students, in the public schools, as follows: (a) first, students residing within the school district or attendance area; and (b) second, students enrolled in a school ranked as a school that needs improvement or a school subject to corrective action; (c) third, students who previously attended the public school; and (d) fourth, all other applicants. Subsection G of Section 22-1-4 NMSA 1978 states that as long as the maximum allowable class size established by law or by rule of a local school board, whichever is lower, is not met or exceeded in a public school by enrollment of first and second priority persons, the public school shall enroll other persons applying in the priorities stated. If the parents of a student awarded a scholarship desired to enroll their child in a district outside of their attendance area, the award of the scholarship would not change the priorities established by the Open Enrollment Act."

PED also notes that Page 3, line 8 and page 15, line 10 uses the term "individualized education plan." The IDEA uses the term "individualized education program." Using the word "program" instead of "plan" would align with the federal law.

## **OTHER SUBSTANTIVE ISSUES**

PED, in an attempt to quantify to exposure to parental placement of special needs students in New Mexico’s private parochial schools conducted the following research:

Ten New Mexico private schools were randomly selected and researched regarding student admission process and tuition costs. The majority of these schools have a lengthy admission process beginning with an application; some schools require letters of recommendation, school visits and an interview. Through this research, it was found that the smaller private schools referenced having very limited resources, and therefore, students with “special needs” would most likely not be admitted because the school would not be able to provide the services required. The larger schools accept students with “special needs” but every application is reviewed carefully to make a decision based on the best interest of the student and the school. Tuition costs for one year range from \$2,500 at a small day-school in a mid-sized district to \$19,000 at a large school in a large school district. \$10,000 was the average of the ten schools’ tuition costs. The rigorous process, letters of recommendations, and interviews, may be difficult for students with “special needs”. It is unclear if some of these requirements would be waived because of the scholarship process.

It is also uncertain whether tuition at private and parochial schools would adjust to conform to any scholarship provided by a TSO.

## **WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL?**

PED notes the consequences of not enacting this bill. Students with disabilities would continue to receive services in the public schools and/or transfer to another public school in the district in accordance with the ESEA or apply for open enrollment in another school district in accordance with Paragraph (3) of Subsection E of Section 22–1–4 NMSA 1978. Parents wishing to enroll their children in a private school will have to pay the tuition or seek out other scholarships.

## **AMENDMENTS**

On page 3, line 8 and page 15, line 10, change “plan” to “program.”

Page 7, lines 10 – 12 requires schools to certify to the tuition scholarship organization that the school does not discriminate on the basis of race, color, or national origin. Discrimination based upon a disability, type of disability, or on level of special education service should be added.

## **POSSIBLE QUESTIONS**

Does the phrase “shall not exceed eighty percent of the three-year rolling average of the state equalization guarantee distribution for the respective level of an eligible student as calculated for the associated program units” include or exclude the adjustment in the school equalization guarantee (SEG) for special needs students?