Fiscal Note 2017 Biennium

GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Bill #	SB0410	**Title:**	Provide for tax credits for contributions to public and private schools
Primary Sponsor:	Jones, Llew	**Status:**	As Introduced

✓Significant Local Gov Impact ✓Needs to be included in HB 2 ✓Technical Concerns

☐Included in the Executive Budget ✓Significant Long-Term Impacts ✓Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2016 Difference	FY 2017 Difference	FY 2018 Difference	FY 2019 Difference
Expenditures:				
General Fund	$505,902	$83,798	$85,055	$86,331
State Special Revenue	$3,000,000	$3,300,000	$3,630,000	$3,993,000
Revenue:				
General Fund	($9,000,000)	($9,900,000)	($10,890,000)	($11,979,000)
State Special Revenue	$3,000,000	$3,300,000	$3,630,000	$3,993,000
Net Impact-General Fund Balance:	($9,505,902)	($9,983,798)	($10,975,055)	($12,065,331)

Description of fiscal impact: SB 410 would create two new tax credits, one for earmarking part of a taxpayer's individual or corporate income tax liability for a new educational improvement special revenue account for distribution to school districts for new innovative educational programs, and one for making donations to organizations that would give scholarships to students in private schools. This would divert $3.0 million to $4.0 million each year in general fund revenue to the new state special revenue account, and also reduce general fund revenue by an additional $6.0 million to $8.0 million.

FISCAL ANALYSIS

Assumptions:

Department of Revenue (DOR)

1. This bill would create two new tax credits, one for earmarking part of a taxpayer's individual or corporate income tax liability for a new educational improvement special revenue account for distribution to school districts for new innovative educational programs, and one for making donations to organizations that would give scholarships to students in private schools.
2. Both credits would first be available for tax year 2015, which is FY 2016, and would sunset after tax year 2021.

3. Both credits would be limited to $150 per taxpayer, and each would be subject to an aggregate limit of $3 million in credits for 2015, with the aggregate limit increasing 10% each year.

Educational Improvement Account

4. This bill would allow individuals and corporations to earmark up to $150 of individual or corporate income tax for the new educational improvement special revenue account rather than the general fund. (See Technical Note 1) Taxpayers who make this earmark would be allowed a tax credit equal to the amount of the earmark. Total credits would be limited to $3.0 million for tax year 2015, and would increase by 10% each year as long as the total was at least $3.0 million.
5. Credits would be claimed on tax returns filed in the spring following each tax year. The following table shows earmarks, credits, and the total reduction in general fund revenue for FY 2016 through FY 2019.

	FY 2016	**FY 2017**	**FY 2018**	**FY 2019**
Funds Diverted from General Fund to Educational Improvement Account	$3,000,000	$3,300,000	$3,630,000	$3,993,000
Tax Credits	$3,000,000	$3,300,000	$3,630,000	$3,993,000
General Fund Revenue Reduction	$6,000,000	$6,600,000	$7,260,000	$7,986,000

Student Scholarship Organizations

6. This bill would allow individuals and corporations to claim a credit of up to $150 for contributing to organizations that would grant scholarships to students in private schools. Total credits would be limited to $3.0 million for tax year 2015, and would increase by 10% each year as long as the total was at least $3.0 million. Based on experience in other states with similar credits, it is assumed that credits would be at the limit each year through at least 2018.
7. Credits would be claimed on tax returns filed in the spring following each tax year. The following table shows credits for FY 2016 through FY 2019.

	FY 2016	**FY 2017**	**FY 2018**	**FY 2019**
Tax Credits	$3,000,000	$3,300,000	$3,630,000	$3,993,000

8. The credits allowed by this bill will reduce the net price of attending private school (tuition less discounts or scholarships and credits) for students whose families claim the credit. Some families who are not willing and able to send a child to a private school at current net prices would be willing with the lower net price. Recent research indicates that a 10% reduction in the net price of private school results in about a 2% increase in children whose families are willing and able to pay the net price to send them to a private school - (See, for example, Susan Dynarski, Jonathan Gruber and Danielle Li: Cheaper by the Dozen: Using Sibling Discounts at Catholic Schools to Estimate the Price Elasticity of Private School Attendance, Center for Economic Studies, U.S. Census Bureau paper CES 11-34, 2011, and Richard Blundell, Lorraine Dearden and Luke Sibieta: The Demand for Private Schooling in England: the Impact of Price and Quality, Institute for Fiscal Studies working paper 10/21, 2010).
9. Private schools would be willing to accept additional students only if they receive additional funding to pay the costs of serving them. On average, full tuition appears to cover about 60% of private school costs in Montana. Since many students receive some kind of discount, actual tuition payments cover less than 60% of costs. Spending per student is about $9,500, and non-tuition revenue per student is about $3,800. (Based on tuition and fees reported on private school websites, average cost per student in public schools from OPI and ratios of private school costs to public school costs estimated in Bruce Baker: Private Schooling in the U.S.: Expenditures, Supply, and Policy Implications, Boulder and Tempe: Education and the Public Interest Center, University of Colorado & Education Policy Research Unit, Arizona State University, 2009). The remaining expenses are paid from donations, subsidies from a supporting organization, such as a church,

and other non-tuition sources. Additional students attending private schools would pay tuition less than the cost of serving them. Private schools can accept these additional students and continue to meet all their expenses only if they raise tuition to capture part of the value of the tax credits and use these funds to subsidize the additional students.

10. The change in private school enrollment that could result if schools increased tuition to capture part of the credits was calculated using the following formulas describing the tuition-setting actions of affected private schools, and enrollment decisions of families of current and potential private school students:

$$tuition = \frac{total\ expenditures - nontuition\ revenue}{students}$$

$$\frac{additional\ students}{2014\ students} = -0.2\frac{change\ in\ net\ price}{2014\ tuition}$$

$$change\ in\ net\ price = tuition\ increase - average\ credits\ per\ student$$

11. The following table shows increases in private school enrollments that would occur if schools raise tuition to the point where the number of students wanting to attend with the higher tuition and average scholarship just equals the number of places that private schools are willing to provide. It is assumed that, on average, administrative costs of student scholarship organizations would be 5% of donations.

	2015	**2016**	**2017**	**2018**
Average Scholarship	$449	$495	$543	$596
Average Tuition Increase	$52	$57	$63	$69
Enrollment Increase	87	95	105	116

Department of Revenue (DOR) costs

12. This bill would require the DOR to develop and maintain a registry of student scholarship organizations and to compile and make public information from their annual reports. It also would require the department to maintain systems for taxpayers to apply to receive the two credits. One-time costs to develop new forms and add the new credits to the department's data processing systems would be $419,125 in FY 2016. Processing and verifying credit applications, credit claims, and annual reports from scholarship organizations would require an additional 1.00 FTE beginning in FY 2016.

Office of Public Instruction

13. SB 410 establishes an educational improvement account in the state special revenue fund. "Taxpayer-directed tax payments" must be paid into the account. The Office of Public Instruction (OPI) is required to distribute 95% of the revenue from the educational improvement account for supplemental funding to eligible public schools.
14. SB 410 defines student scholarship organizations as entities which provide scholarships to eligible students to attend instruction offered by a qualified education provider. The scholarship organization delivers scholarship funds directly to the qualified education provider selected by a parent or legal guardian. The organization may not provide a scholarship that exceeds 50% of the per-pupil average of total public school expenditures. Furthermore, the organization's average scholarship may not exceed 30% of the per-pupil average.

15. A qualified education provider may not be a public school nor a home school. If the provider is not accredited, has not applied for accreditation, or is not provisionally accredited by a state, regional, or national accreditation organization, the provider or tutor must inform the child's parents or legal guardian in writing at the time of enrollment that the provider is not accredited and is not seeking accreditation.
16. The OPI is responsible for:
    a. Making recommendations to adjust the geographic regions and large districts over time as necessary to preserve equity and fairness;
    b. Determining the ratio of a school's quality educators to the total number of quality educators in the school's geographic region or large district;
    c. Obligating at least 95% of its annual revenue from the educational improvement account for supplemental funding to eligible public schools for innovative educational programs and technology deficiencies; and
    d. Calculating the statewide average per-pupil spending as defined in Section 22.
17. SB 410 allows the agency to use 5% of the funding in the educational improvement account for administrative expenses which is assumed to cover all such costs. The additional workload for OPI will be associated with allocating individual donations among eleven geographic regions or seven large districts based on the taxpayer's residential address. The DOR will need to provide taxpayer addresses to OPI. It is likely that OPI will need to contract for GIS services to assist with this effort.
18. Using the calculation required by SB 410, Section 22, the per-pupil average of total public school expenditures was $10,418 for the FY 2013-14 school year. The average was $9,551 for elementary programs and $11,272 for high school programs. The funds that must be included in the calculation of the per-pupil average include general fund; transportation; bus depreciation; food services; tuition; retirement; miscellaneous programs; traffic education; non-operating; lease rental agreement; compensated absence fund; metal mines tax reserve; state mining impact; impact aid; litigation reserve; technology acquisition; flexibility fund; debt service; building reserve; and inter-local agreement.
19. School districts will deposit the supplemental funding received under SB 410 in the school flexibility fund. No additional reporting is required of the school district as to how the district spends the funding on innovative educational programs. There is also no deadline for a school district to expend the donated monies.
20. SB 410 does not provide a timeline for when OPI will distribute funds to districts. OPI will determine the timeline through the rulemaking process.

	FY 2016 Difference	FY 2017 Difference	FY 2018 Difference	FY 2019 Difference
Fiscal Impact:				
FTE	1.00	1.00	1.00	1.00
Expenditures:				
Personal Services (DOR)	$77,094	$77,094	$78,250	$79,424
Operating Expenses (DOR)	$428,808	$6,704	$6,805	$6,907
Personal Services (OPI)	$49,345	$49,345	$50,085	$50,836
Operating Expenses (OPI)	$100,655	$115,655	$131,415	$148,814
Grants to Schools (OPI)	$2,850,000	$3,135,000	$3,448,500	$3,793,350
TOTAL Expenditures	$3,505,902	$3,383,798	$3,715,055	$4,079,331
Funding of Expenditures:				
General Fund (01)	$505,902	$83,798	$85,055	$86,331
State Special Revenue (02)	$3,000,000	$3,300,000	$3,630,000	$3,993,000
TOTAL Funding of Exp.	$3,505,902	$3,383,798	$3,715,055	$4,079,331
Revenues:				
General Fund (01)	($9,000,000)	($9,900,000)	($10,890,000)	($11,979,000)
State Special Revenue (02)	$3,000,000	$3,300,000	$3,630,000	$3,993,000
TOTAL Revenues	($6,000,000)	($6,600,000)	($7,260,000)	($7,986,000)
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	($9,505,902)	($9,983,798)	($10,975,055)	($12,065,331)
State Special Revenue (02)	$0	$0	$0	$0

Effect on County or Other Local Revenues or Expenditures:

Office of Public Instruction (OPI)

1. SB 410 creates a new state-sanctioned revenue source that generates funding for some districts that is not available to other districts.

Long-Term Impacts:

Department of Revenue (DOR)

1. This bill would sunset December 31, 2021. Credits for tax years 2019 through 2021 would be claimed in FY 2020 through FY 2022. The following table shows revenue effects for these fiscal years.

	FY 2020	FY 2021	FY 2022
Funds Diverted from General Fund to Educational Improvement Account	$4,392,300	$4,831,530	$5,314,683
EIA Tax Credits	$4,392,300	$4,831,530	$5,314,683
SSO credits	$4,392,300	$4,831,530	$5,314,683
Total General Fund Revenue Reduction	$13,176,900	$14,494,590	$15,944,049

Technical Notes:

Department of Revenue (DOR)

1. The bill uses the terms "taxpayer-directed tax payment," "contribution," and "donation" to refer to funds to be deposited into the educational improvement special revenue account and uses the terms "taxpayer" and "donor" to refer to persons who direct funds to the account. It is not clear whether the program is to allow taxpayers to earmark part of their tax for the new account or is to allow taxpayers to make donations in a manner similar to the existing income tax check-off programs. This needs to be clarified and the wording needs to be made consistent. The bill should include either check-off language similar to the language in 15-30-2387, 2389, 2390, or 2392 or clear language stating that a taxpayer may designate up to $150 of tax payable under Title 15, chapters 30 or 31 for deposit into the educational improvement special revenue account.
2. Sections 13(5)(c) and 14(5)(c) contain detailed requirements for credit claim forms. The specifics in section 13(5)(c) do not coordinate well with the rest of the bill, and it is likely that following the requirements in these sections may complicate implementation of this bill. In general, it is better to give the department authority to develop necessary forms rather than to put this level of administrative detail in law.

Office of Public Instruction (OPI)

3. The Office of Public Instruction is responsible for administering the newly created educational improvement state special revenue account, into which the "taxpayer-directed tax payments" are paid. It is unclear what the mechanism is for deposit of these tax payments into the account.
4. Section 4 requires the superintendent of public instruction to distribute funding from the educational improvement account to schools within a geographic area or large district. The maximum receivable amount for each school is based on a ratio of a school's number of quality educators to the total number of quality educators in the school's geographic region or large district. It appears that the maximum is a limit on the proportion that any given school can receive, not a limit on the amount that a school can receive.
5. It is unclear whether a large school district will receive an allocation when a donation is made to a geographic region. SB 410 does not preclude a large district from receiving a share of the funding designated for a geographic region.
6. If a donor resides in an area served by an independent elementary and a large high school district, OPI must allocate the supplemental funding between the two districts based on the number of grades served. There is inequity in this as the large high school may have many more students than the independent elementary school, but the K-8 elementary district serves nine grades while the high school district serves four grades.
7. Quality educator FTE are counted at the school district level, not at the school level. Teachers may be assigned to more than one school. Administrators and program coordinators are not assigned to specific schools within a district. If the intention is to distribute funding to specific schools (as opposed to districts), the FTE related to a district's central office will not be included in the calculation.
8. The Office of Public Instruction makes payments to districts and receives district-level expenditure reports. SB 410 does not require districts to report on the expenditure of supplemental funding to specific schools.
9. No appropriation exists in SB 410 for the new state special revenue account created in Section 5.

Sponsor's Initials	Date	Budget Director's Initials	Date

GOVERNOR'S OFFICE OF BUDGET AND PROGRAM PLANNING

Dedication of Revenue 2017 Biennium

17-1-507-509, MCA.

a) **Are there persons or entities that benefit from this dedicated revenue that do not pay? (please explain)**

Yes, taxpayers contribute and school districts receive the funds for innovative programs. It also provides taxpayer relief of paying the expenses.

b) **What special information or other advantages exist as a result of using a state special revenue fund that could not be obtained if the revenue were allocated to the general fund?**
It is easier to track the funding both revenue and expenditures when not included in the general fund.

c) **Is the source of revenue relevant to current use of the funds and adequate to fund the program activity that is intended? Yes / No (if no, explain)**
Yes, there are no current funds being used for this purpose and the amount of funds are limited for both revenue and thus expenditure.

d) **Does the need for this state special revenue provision still exist? ___Yes ___No (Explain)**
If SB 410 passes this fund will be necessary.

e) **Does the dedicated revenue affect the legislature's ability to scrutinize budgets, control expenditures, or establish priorities for state spending? (Please Explain)**
The restricted state special revenue fund allows the legislature to clearly see revenue, expenditures, and fund usage.

f) **Does the dedicated revenue fulfill a continuing, legislatively recognized need? (Please Explain)**
If SB 410 passes, the legislature has recognized a need for a state special revenue fund. This fund allows OPI to appropriately account for the funds.

g) **How does the dedicated revenue provision result in accounting/auditing efficiencies or inefficiencies in your agency? (Please Explain. Also, if the program/activity were general funded, could you adequately account for the program/activity?)**
The dedicated revenue provision ensures OPI will utilize the dedicated revenue as the legislature intended with the passage of SB 410.