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**FISCAL IMPACT STATEMENT**

**LS 7552**

**BILL NUMBER:** HB 1003

**NOTE PREPARED:** Mar 30, 2011

**BILL AMENDED:** Mar 29, 2011

**SUBJECT:** School Scholarships.

**FIRST AUTHOR:** Rep. Behning

**FIRST SPONSOR:** Sen. Kruse

**BILL STATUS:** As Passed House

**FUNDS AFFECTED:** X GENERAL  
DEDICATED  
FEDERAL

**IMPACT:** State & Local

**Summary of Legislation:** (Amended) *Tax Credits:* The bill increases the school scholarship tax credits that may be awarded for donations to a scholarship granting organization. It allows up to 25% of the credits to be awarded for donations to public school foundations. It allows scholarship granting organizations to grant scholarships to families with income that is not more than 250% of the amount required for the individual to qualify for the federal free or reduced price lunch program. It also prohibits a scholarship granting organization from limiting the availability of scholarships to students of only one participating school.

*School Scholarship Program:* The bill provides choice scholarships to students in families with income that is not more than 150% of the amount required for the individual to qualify for the federal free or reduced lunch program to pay the costs of tuition and fees at a public or private elementary school or high school that charges tuition. It provides for a supplemental distribution to public schools equal to the difference between the amount distributed as choice scholarships and the amount that would have been distributed to public schools to educate the children receiving choice scholarships. It requires fair admissions policies for schools eligible for choice scholarships. It limits the number of choice scholarships awarded per school year before June 30, 2013. It limits the choice scholarship granted to a student in grade 1 through 8 to \$4,500 per school year. It provides consequences for nonpublic schools who receive: (1) consecutive low category designations for school performance and improvement; and (2) a distribution of choice scholarships. It also provides for any savings from the choice scholarships to be used for tuition support for schools.

*Other:* The bill makes conforming changes.

**Effective Date:** July 1, 2011.

**Explanation of State Expenditures:** (Revised) *School Scholarship Program: Summary* - The bill provides that an eligible student in the 1<sup>st</sup> through the 12<sup>th</sup> grade is entitled to a state-funded scholarship to pay the cost of nonpublic school tuition or transfer tuition beginning in the 2011-2012 school year. The bill limits the number of scholarships provided to 7,500 during the 2011-2012 school year, and 15,000 per year beginning in the 2012-2013 school year. The estimated net impact reported in the table below is attributable to a cohort of 1,000 students from households with income not exceeding 250% of the amount required to qualify for the federal free or reduced price lunch program. Under the bill, 714 of the 1,000 students from this cohort would qualify for state scholarships. The table reports: (1) the tuition support used to pay the cost of scholarships; and (2) the tuition support remainder not used to pay scholarship costs that would be distributed to public schools and charter schools (except virtual charter schools) under the same formula used to distribute basic tuition support.

<b>Estimated Net Impact of Scholarship Program from 1,000 Student Cohort with Household Income Not Exceeding 250% of Free or Reduced Price Lunch Qualifying Income.</b>	
Qualifying Students at 150% or below	714
Tuition Support Used for Scholarship Cost	\$2.9 M
Tuition Support Remainder Distributed to Public & Charter Schools	\$1.0 M

The tuition support used to pay scholarship costs and the tuition support remainder distributed to public schools and charter schools would depend on the school formula. The current school formula expires December 30, 2011. The tuition support remainder distributed to public and charter schools would be altered if future school formulas include minimum guarantee or de-ghoster provisions.

*Department of State Revenue (DOR):* The DOR would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to reflect the changes proposed in this bill concerning the School Scholarship Tax Credit and to reflect the new Public School Foundation Tax Credit. The DOR's current level of resources should be sufficient to implement these changes.

*Department of Education:* The school scholarship program established under the bill will result in additional administrative responsibilities for the Department of Education. The fiscal impact that might arise from these new responsibilities is indeterminable and would depend on the scope of the scholarship program and the manner in which scholarships are distributed.

**Background Information - School Scholarship Program** - The bill establishes a program to provide scholarships to eligible students in the 1<sup>st</sup> through 12<sup>th</sup> grades to pay tuition at a nonpublic school or transfer tuition at an alternative public school that is not a charter school or a school in the school corporation where the student has legal settlement. The bill limits the number of scholarships provided to 7,500 during the 2011-2012 school year, and 15,000 per year beginning in the 2012-2013 school year. Among other eligibility requirements, the student must have: (1) been enrolled in a school corporation that did not charge the student transfer tuition for at least two semesters immediately preceding the first semester for which the student receives a scholarship; or (2) received a scholarship under the program or from a scholarship granting organization in a preceding school year.

A scholarship under the program is paid from state tuition support money that would otherwise go to the school corporation where the student attended before attending a nonpublic or alternative public school under

the program. The maximum scholarship is the least of the amounts described in (1), (2), or (3) below for an eligible student enrolled in Grade 1 to 8, or the least of the amounts described in (1) or (2) below for an eligible student enrolled in Grade 9 to 12.

(1) The sum of the tuition, transfer tuition, and fees required for the student to attend the nonpublic school or alternative public school.

(2) An amount equal to one of the following:

(A) 90% of the state tuition support amount per student of the school corporation where the student has legal settlement if the student is a member of a household with an annual income not exceeding 100% of the amount required to qualify for the federal free or reduced price lunch program; or

(B) 50% of the state tuition support amount per student of the school corporation where the student has legal settlement if the student is a member of a household with an annual income not exceeding 150% of the amount required to qualify for the federal free or reduced price lunch program.

(3) In the case of a student enrolled in Grade 1 to 8, \$4,500.

The potential number of students who might switch from their current public school to a nonpublic school, or to public school where the student does not have legal settlement, because of the scholarship program is indeterminable. Consequently, the impact on state tuition support expenses due to the scholarship program is indeterminable.

The scenario below is based on a cohort of 1,000 students from households with income not exceeding 250% of the qualifying income for the federal free or reduced price lunch program. The table reports the amount of tuition support used to pay for scholarships for this cohort and the tuition support remainder not used to pay scholarship costs that would be distributed to public schools and charter schools (except virtual charter schools) under the same formula used to distribute basic tuition support. The scholarship amounts are based on the CY 2011 average tuition support per student for regular programs (calculated at \$5,515). The scenario assumes that the tuition required at the nonpublic school or transfer tuition required by the alternative public school selected by the student exceeds the percentage of state tuition support that the bill allows. The distribution of students on the income parameters described above in (A)-(C) is based on the income distribution of state income taxpayers (single and joint filers) claiming the dependent child exemption for 1 to 10 children. The scenario also assumes that 67.5% of students are enrolled in Grade 1 to 8 and 32.5% are enrolled in Grade 9 to 12.

Household Income	Scholarship Levels	Scholarship Amount*	Students in Income Range	Tuition Support Used to Pay Scholarship Cost	Tuition Support Remainder Distributed to Public & Charter Schools
<b>Grade 1 to 8</b>					
Maximum <b>100%</b> free/reduced price lunch income level	90% of tuition support	\$4,500	341	\$1,534,500	\$346,115
Maximum <b>150%</b> free/reduced price lunch income level	50% of tuition support	\$2,758	141	\$388,808	\$388,808
Maximum <b>250%</b> free/reduced price lunch income level	Scholarships not awarded	\$0	193	\$0	\$0
<b>Grade 9 to 12</b>					
Maximum <b>100%</b> free/reduced price lunch income level	90% of tuition support	\$4,964	164	\$814,014	\$90,446
Maximum <b>150%</b> free/reduced price lunch income level	50% of tuition support	\$2,758	68	\$187,510	\$187,510
Maximum <b>250%</b> free/reduced price lunch income level	Scholarships not awarded	\$0	93	\$0	\$0
<b>Total</b>			<b>1,000</b>	<b>\$2,924,832</b>	<b>\$1,012,879</b>
*Assumes the CY 2011 average state tuition support per student for regular programs (=\$5,515).					

**Explanation of State Revenues: School Scholarship Tax Credit: Summary** - The bill increases the credit percentage and provides for a formula to increase the cap on credits awarded annually. Both changes will lead to a material increase in the revenue loss from this credit in future years. The magnitude and timing of the revenue loss is uncertain because of the low level of response to the credit in its initial 1.5 years.

The bill makes the following changes relative to the school scholarship tax credit for contributions to a certified scholarship granting organization (SGO).

(1) The bill increases the credit percentage from 50% to 60% of contributions to a certified SGO in 2012; to 70% of contributions in 2013; and to 80% of contributions beginning in 2014.

(2) The bill establishes a formula for increasing the cap on credits awarded in a year by \$10 M if the total credits awarded in the prior year totaled at least 90% of the prior year cap. The current annual credit cap is \$2.5 M, so under the bill, if awarded credits in a year totaled at least \$2.25 M, the credit cap would increase to \$12.5 M beginning in the following year.

Currently, only four SGOs have been certified by the Department of Education. The total amount of tax credits the Department of State Revenue awarded in FY 2010 (the first year tax credits could be awarded) was \$43,200. As of January 13, 2011, FY 2011 credits awarded by DOR total \$215,750. Annualizing this year-to-date total suggests that credits awarded in FY 2011 could come in at about \$430,000. This would leave about \$2 M in un-awarded credits for the fiscal year under the fiscal aggregate credit cap of \$2.5 M. This level of response and growth is well below that experienced in Arizona and Iowa where somewhat similar credits have been available, but initially only to individual taxpayers. The Indiana credit is available to both individual and corporate taxpayers.

(Revised) *School Foundation Tax Credit*: The bill establishes an AGI tax credit for individuals and corporations for contributions made by an individual or corporate taxpayer to nonprofit public school foundations. The income tax credit is effective beginning in tax year 2012. The potential revenue loss from this new tax credit is indeterminable but could be significant. While data is unavailable regarding contributions specifically to “public school foundations” annual contributions to public schools is significant. Annual contributions to public schools is reported in the table below.

<b>Fiscal Year</b>	<b>Total Contributions</b>
FY 2005	\$19.9 M
FY 2006	\$27.3 M
FY 2007	\$19.8 M
FY 2008	\$31.7 M
FY 2009	\$36.0 M
FY 2010	\$37.9 M

The public school foundation tax credit is equal to 60% of contributions to a public school foundation in 2012, 70% of contributions in 2013, and 80% of contributions beginning in 2014. Under the bill, the tax credit is included under the aggregate annual cap currently applicable only to the school scholarship tax credit. The bill limits credits awarded in a year to no more than 25% of the amount of school scholarship tax credits awarded during that year. The tax credit is nonrefundable and unused credits may not be carried forward or carried back. The tax credit may be applied to individual or corporate AGI Tax, Financial Institutions Tax, or Insurance Premiums Tax liabilities.

*Background Information -School Scholarship Tax Credit* - Under current statute, the tax credit is equal to 50% of the contributions made by an individual or corporate taxpayer to nonprofit K-12 school scholarship-generating organizations. The tax credit was first effective for tax year 2010. The tax credit is nonrefundable and unused credits may not be carried forward or carried back. Total credits allowed may not exceed \$2.5 M for all taxpayers per fiscal year. The tax credit may be applied to individual or corporate AGI Tax, Financial Institutions Tax, or Insurance Premiums Tax liabilities. Revenue from these taxes is distributed to the state General Fund.

*Arizona Tax Credit*: Arizona offers a tax credit to individual and corporate taxpayers for contributions to school tuition organizations. Individuals may receive tax credits of up to \$500 for single filers and \$1,000 for joint filers, and corporations may receive tax credits equal to the amount of their contributions. There is no aggregate cap on tax credits for individuals, but tax credits for corporations are capped at \$14.4 M annually. In 1999, the second year of the credit for individual taxpayers, there were 33 school tuition organizations in Arizona and creditable donations totaled \$13.8 M, even though the joint return credit maximum was \$500 (the same as the single return maximum). In 2009, there were 53 school tuition organizations in Arizona and creditable donations by individual taxpayers totaled \$50.9 M. In FY 2009, corporate credits totaled \$10.5 M. This was the third year of the corporate credit.

Iowa Tax Credit: Iowa offers a tax credit to individual and corporate taxpayers for contributions to school tuition organizations. The credit for individual and corporate taxpayers is equal to 65% of the contribution to a school tuition organization. The individual credit started in 2006, and the corporate credit began in 2009. The credit is subject to an aggregate cap of \$7.5 M annually; however, the credit cap was \$2.5 M in 2006, \$5 M in 2007, and increased to the current \$7.5 M beginning in 2008. In 2006, \$2.4 M in credits were awarded, and \$4.7 M in credits were awarded in 2007. As of 2009, there were 11 school tuition organizations in Iowa.

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:** (Revised) *School Scholarship Program*: The program could have two impacts depending on whether or not a school corporation or charter school is losing students due to the scholarship program.

(1) School corporations or charter schools that lose students due to the scholarship program would experience a loss in state tuition support due to the reduction in the number of students attending school and being counted in their ADM for future school formula calculations. The loss in revenue could be offset by reductions in expenditures depending on the number of students that participate in the scholarship program and the supplemental tuition support distribution. Under the scenario outlined above (see *Explanation of State Expenditures*) the tuition support reduction to such schools would total about \$2.9 M for 714 scholarship-eligible students before the supplemental distribution.

(2) School corporations or charter schools that do not lose students due to the scholarship program would receive additional tuition support since the tuition support remainder not used to pay scholarship costs is to be distributed to all school corporations and charter schools (except virtual charter schools) as a supplemental tuition support payment under the same formula used to distribute basic tuition support. (See *Explanation of State Expenditures* for discussion of the scholarship funding and tuition support remainder.)

**State Agencies Affected:** Department of State Revenue; Department of Education.

**Local Agencies Affected:** School corporations.

**Information Sources:** Arizona Department of Revenue, *Individual Income Tax Credit for Donations to Private School Tuition Organizations: Report for 2009 - Executive Summary*; Corporate Income and Insurance Premium Tax Credits for Contributions to School Tuition Organizations: Reporting for 2009, [www.azdor.gov](http://www.azdor.gov). Iowa Department of Revenue, *Iowa's 2006 Tax Credit Claims - Tax Credits Program Report*, February 2009; *Iowa's 2007 Tax Credit Claims - Tax Credits Program Report*, April 2010, <http://www.iowa.gov/tax/taxlaw/>. The Foundation for Educational Choice, *Iowa - Tax Credits for School Tuition Organizations*, <http://www.edchoice.org>. OFMA Income Tax databases, 2008.

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