LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 78TH LEGISLATIVE REGULAR SESSION
Revision 1

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TO: Honorable Ron Wilson, Chair, House Committee on Ways & Means

FROM: John Keel, Director, Legislative Budget Board

IN RE: **HB2563** by Paxton (Relating to a franchise or insurance premium tax credit for contributions made to certain nonprofit educational assistance organizations.), **As Introduced**

Estimated Two-year Net Impact to General Revenue Related Funds for HB2563, As Introduced: a positive impact of $23,600,000 through the biennium ending August 31, 2005.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2004	$3,600,000
2005	$20,000,000
2006	$20,000,000
2007	$20,000,000
2008	$20,000,000

All Funds, Five-Year Impact:

Fiscal Year	Probable Revenue (Loss) from *GENERAL REVENUE FUND* 1	Probable Revenue (Loss) from *FOUNDATION SCHOOL FUND* 193	Probable Savings/(Cost) from *FOUNDATION SCHOOL FUND* 193
2004	($25,000,000)	($5,000,000)	$33,600,000
2005	($17,500,000)	($2,500,000)	$40,000,000
2006	($17,500,000)	($2,500,000)	$40,000,000
2007	($17,500,000)	($2,500,000)	$40,000,000
2008	($17,500,000)	($2,500,000)	$40,000,000

Fiscal Analysis

The bill would amend Chapter 171 of the Tax Code and Chapter 4 of the Insurance Code to provide tax credits against the franchise tax and the insurance premium tax for contributions made to certain nonprofit, "educational assistance" organizations.

Under both taxes the credit would equal 50 percent of a corporation's or insurance carrier's contribution to the organization. The total amount of credit awarded to corporations for the franchise tax would be limited to $10 million per year. A similar limit would apply to the annual total amount of premium tax credit that could be awarded to insurance carriers. If the amount of credit claimed for either tax were to exceed $10 million in a year, the Comptroller would reduce the amount of credit awarded to each claimant proportionally. Corporations and insurance carriers would apply to the Comptroller for the credit on a form adopted by the Comptroller. The credit could not be carried forward or conveyed, assigned, or transferred to another entity.

"Educational assistance organization" would be defined as one that: (1) uses its annual revenue to award scholarships and pay educational expenses of public or nonpublic elementary or secondary schools located in this state, (2) is exempt from federal tax, (3) is not in violation of the federal Civil Rights Act, and (4) does not award scholarships only to students of a particular school or pay educational expenses incurred only at a particular school.

In addition, to qualify for the tax credit, a contribution would have to be to an educational assistance organization that (1) was located in this state, (2) allocated at least 90 percent of its annual revenue only for student scholarships, (3) allocated the remainder of its annual revenue only for marketing and administrative expenses, (4) allocated at least 50 percent of the contributions made that may receive a tax credit provided by the bill to students who are not counted toward a public school's average daily attendance and who were enrolled in a public school during the preceding year and were eligible for the national reduced price lunch program or who received a scholarship from the organization during a previous school year, (5) demonstrated a pattern of giving priority to awarding scholarships to students who demonstrate the greatest need, (6) gave the corporation or insurance carrier a receipt for the money contributed.

The amount of scholarship the educational assistance organization could award to a student would be limited and would depend on whether the student had a disability and on how the organization allocated certain portions of the contributions to the organization. A corporation or insurance carrier could not require that its contribution benefit a particular person. A contribution by a corporation or insurance carrier could not be used for the benefit of an employee, spouse, or dependent of an employee of the corporation or insurance carrier.

This bill would take effect immediately upon enactment, assuming that it received the requisite two-thirds majority votes in both houses of the Legislature. Otherwise, it would take effect September 1, 2003. A credit claimed under this bill could only be claimed for an expenditure made on or after the effective date of this bill.

Methodology

This fiscal note is based upon information provided by the Comptroller's Office and the Texas Education Agency.

The estimated fiscal impact addresses only the impact of the franchise and premium tax credits. The estimate is based on programs in Arizona, Pennsylvania, and Florida with similar credit provisions for donations to scholarship organizations.

Because insurance companies are allowed to base their two semiannual prepayments for their following year premium tax liability on either their previous tax year tax liability or their estimated current year tax liability, the fiscal impact for fiscal 2004 reflects the assumption that insurers would take a full $10 million credit on their 2004 report (for tax year 2003) and make two $5 million reductions in their March and August 2004 prepayments for their report due March 2005 (for tax year 2004).

The general revenue losses shown in the table reflect the credits for the franchise and the insurance taxes. The Foundation School Fund revenue loss is for insurance taxes that would now be credited rather than deposited in the Foundation School Fund.

The bill would potentially impact the funding needed for the Foundation School Program. For each student that leaves the public education system, there would be savings to the program. Because public school students must be qualified for the free or reduced-price lunch program, their departure would also affect funding for the compensatory education allotment, but not until the year after they are no longer present, since the compensatory education allotment uses a prior year count of students as its funding basis. Their departure may also affect other allotments depending on program participation.

In the initial year (2004), the state would save an average of about $4,200 for each student that leaves public education, assuming the student does not participate in special program services that would generate higher funding (special education, career and technology courses, gifted/talented programs, bilingual or ESL programs). The departure of students that would be expected to participate in the special program areas could save the state even more funding. In the second and subsequent years after a student's departure, the savings would be higher because of the change to the compensatory education funding count, and would likely be about $5,000.

Based on the expected credit amount for donations to educational assistance organizations, there could be as much as $60 million available in 2004 and $40 million in 2005 available for scholarships. The bill may require annual distribution of the contributions as scholarships, but it is unclear whether the scholarship must be paid in the same year as the donation is received, or could be paid in a subsequent year. The amount of the funds available for scholarships would be sufficient to fund 16,216 scholarships in 2004 and 10,811 scholarships in subsequent years at the $3,700 rate.

The law would require that at least 50% of the contributions be used for scholarships for students that might be departing public education. At the 50% level, scholarships could number as few as 8,108 in 2004 and 5,406 in subsequent years. The bill also allows the same 50% share of contributions to benefit students who received scholarships in the previous year from the educational assistance organization. There are entities in existence and operation today that may meet the definition of an educational assistance organization as it appears in this bill. A review of web sites for various local affiliates of CEO America and other local foundations operating in Texas and offering private school scholarships found reports of more than 2,200 scholarships offered by those organizations. It is likely that there are other foundations in operation that do not have an Internet presence and could not immediately be found.

The bill also would allow any low income kindergarten student that would otherwise attend a private school to receive a scholarship. The estimated private school enrollment statewide is about 350,000 students, based on 2000 U.S. Census data. The kindergarten grade enrollment is estimated to be about 27,000 (one thirteenth of the total). Because about half the students in Texas are low income, it is reasonable to expect that up to 13,500 private school kindergarten students are eligible to receive a scholarship and satisfy the bill's requirement to spend 50% of contributions on the specified populations. The number of potential kindergarten students that could be funded, when combined with known numbers of students already receiving scholarships from organizations that appear to meet the requirements of the bill for being "educational assistance organizations", likely totals to nearly 16,000, or about double the number of students that would need to be funded from the maximum 2004 contributions in order to satisfy the primary spending requirement in the bill.

If scholarships were offered to 8,000 current public school students, the estimated savings to the Foundation School Fund would be $33,600,000 in 2004 and $40,000,000 each year thereafter. State savings would be less to the extent that educational assistance organizations targeted their efforts on eligible non-public school students.

Local Government Impact

To the extent that students are diverted from public school enrollment, school districts would lose revenue from the Foundation School Program. Under the assumptions stated above, public school districts would lose state funding of $33.6 million in 2004 and $40 million each year thereafter.

Source Agencies: 304 Comptroller of Public Accounts, 307 Secretary of State, 454 Department of Insurance, 701 Central Education Agency

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