COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0341-03
Bill No.: HB 639
Subject: Charities; Economic Development Department; Education, Elementary and Secondary; Revenue Department; Taxation and Revenue.
Type: Original
Date: March 1, 2005

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2006	FY 2007	FY 2008
General Revenue	($40,000,000) to $523,000	($40,000,000) to $523,000	($40,000,000) to $523,000
Total Estimated Net Effect on General Revenue Fund	**($40,000,000) to $523,000**	**($40,000,000) to $523,000**	**($40,000,000) to $523,000**

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2006	FY 2007	FY 2008
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 10 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2006	FY 2007	FY 2008
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2006	FY 2007	FY 2008
Local Government	**$0 to ($40,523,000)**	**$0 to ($40,523,000)**	**$0 to ($40,523,000)**

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Secretary of State (SOS)** assume there would be costs due to additional publishing duties related to the Department of Economic Development and the Department of Elementary and Secondary Education's authority to promulgate rules, regulations, and forms. SOS estimates the departments could require approximately 20 new pages of regulations in the Code of State Regulations at a cost of $27.00 per page, and 30 new pages in the Missouri Register at a cost of $23.00 per page. Costs due to this proposal are estimated to be $1,230, however, the actual fiscal impact would be dependent upon the actual rule-making authority and may be more or less. Financial impact in subsequent fiscal years would depend entirely on the number, length, and frequency of the rules filed, amended, rescinded, or withdrawn. SOS does not anticipate the need for additional staff as a result of this proposal, however, the enactment of more than one similar proposal may, in the aggregate, necessitate additional staff.

Oversight assumes the SOS could absorb the costs of printing and distributing regulations related to this proposal. If multiple bills pass which require the printing and distribution of regulations at substantial costs, the SOS could request funding through the appropriation process. Any decisions to raise fees to defray costs would likely be made in subsequent fiscal years.

ASSUMPTION (continued)

Officials from the **Department of Revenue (DOR)** state the Personal Tax Division, to maintain the current processing time of returns, errors and correspondence, will have to reallocate from collection activities a Tax Processing Tech for every 4,000 credits claimed. Plus there is an additional add back if they were able to take a deduction on the federal return which will add a line in the modifications. Again, to maintain current processing times for returns, errors and correspondence, Personal Tax will have to reallocate from collection activities, 1 Tax Processing Tech for every 19,000 errors and 2,400 pieces of correspondence dealing with legislation.

Mainframe systems will need to be modified and tested for the implementation of this legislation. It is estimated that it will take 4 programmers 2 months to handle this implementation.

The Division of Taxation will have internal costs estimated to be $92,154 and 2 FTE associated with the implement of this legislation; however, the division believes it can manage these costs at current appropriation levels unless there is a material change in the division's other responsibilities

Oversight assumes DOR would incur the programming expenses as estimated; however, Oversight assumes DOR could administer the provisions of this proposal with existing resources or request additional staff through the budget process if the volume of tax credits warrants.

Officials from the **Department of Economic Development (DED)** state they would be required to administer the program or work with a designated administrator to review documentation and approve charities. DED or the administrator would allocate $40 million in credits to authorized charities. DED or the administrator would also answer questions as well as promote and oversee the program. Tax credits claimed would need to be tracked by DED. The Department of Revenue would have to be notified when $40 million in credits had been claimed in any one year. $40 million in credits issued plus carry forward of unused credits may mean that more than $40 million is requested each year when tax returns are filed. This might mean that some taxpayers may be denied use of the credit in any given year. DED or the designated administrator are authorized to receive 2% of contributed amounts to cover administrative costs. It is uncertain how the funds would get to DED or where DED would deposit the funds and expend them.

Administrative and marketing costs paid to the educational assistance organizations are set on a sliding scale based on contributions. DED assumes that donations of $44,444,444.44 could be accepted to equate to $40 million in credits. Two percent of the donations, up to $888,888.89 could be used for administration. Of the remaining amount, the educational assistance organizations would be allowed to keep their marketing cost fee and the rest would be used as designated. The DED or designated administrator would have to insure compliance with the rest

ASSUMPTION (continued)

of the provisions of the bill, including designation of educational assistance organizations, reporting, coordination with DOR, etc. At this point, DED projects one FTE (at $44,508 annually) would be needed to administer and oversee the program. Costs for that person are projected to total roughly $90,000 annually. Other costs may be incurred as the bill is implemented and the costs projected are not definitive.

DED assumes the credits will go into effect 2005 based on the emergency clause and will be claimed in 2006. The cost of the credits will be $40 million in CY 2005. DED assumes some computer programming will be needed to adjust existing systems to track the credits claimed and keep a list of educational assistance organizations. This is an unknown amount. The cost for personnel, expense, and equipment will be needed in FY 2006. DED assumes the full $40 million in credits will be issued and claimed each year. DED assumes General Revenue funding will be appropriated and used for program costs and administrative funds will be collected and deposited into GR to offset expenditures.

Oversight has, for fiscal note purposes only, changed the starting salary for the Economic Development Incentive Coordinator to correspond to other such positions within DED. This decision reflects a study of actual starting salaries for new state employees for a six month period and the policy of the Oversight Subcommittee of the Joint Committee on Legislative Research. Oversight also assumes DED would not incur additional costs for office space for the additional FTE.

Officials from the **Department of Elementary and Secondary Education (DESE)** state the proposal authorizes a 90% state income tax credit for contributions to nonprofit educational assistance organizations. The cumulative amount of tax credits which may be claimed by all taxpayers contributing to a nonprofit educational assistance organization in any one fiscal year shall not exceed $40 million. The cumulative amount of tax credits shall be apportioned equally among all qualified nonprofit educational assistance organizations.

DESE assumes the Department of Revenue will likely experience an administrative burden, while the proposal has no impact to DESE. Tax credits will reduce income tax receipts flowing to the General Revenue fund. More tax credits mean less General Revenue available statewide for state use including education and fully funding the foundation formula.

DESE states the changes outlined in section 163.036 will not impact the state's burden in terms of school funding. A district's loss of state aid for a pupil who is no longer enrolled in the school district, does not equate to an equal savings in state funding. It merely makes such funding available to distribute to school districts statewide. In addition, costs to educate students differ

ASSUMPTION (continued)

from district to district. Therefore, there can be no assumption that the transfer of students between districts will have an equal impact on both districts' education costs.

DESE estimates a $40 million reduction in General Revenue receipts each year, starting with FY 2006 as a result of the proposal. DESE also assumes there may be a cost to a school district receiving a scholarship student because the scholarship may not be sufficient to pay the cost of education in that district.

Oversight assumes one of the intentions of the proposal is to realize an offsetting savings to the GR fund for monies the state would otherwise have paid to local school districts for the pupils that are now receiving scholarships to attend other schools. With this assumption, Oversight will show a possible savings to the General Revenue Fund for this reduction in payments to local school districts.

Officials from the **Office of Administration - Budget and Planning (BAP)** state there will be a reduction in General Revenue as a result of this proposal. There is an annual cumulative cap of $40 million to be adjusted for inflation in subsequent years. Since it is unknown how many credits will be claimed, BAP assumes that up to $40 million will be claimed in the first year.

In response to a similar proposal from last year (HB 1702), officials from the **St. Louis School District** stated there may be some reduction to their state revenue with any revisions to the components of the state foundation formula as implied in the legislation. The amount cannot be determined at this time.

In response to a similar proposal from last year (HB 1702), officials from the **School District of Kansas City, Missouri (KCMSD)** stated the proposed change in 163.036 would have a negative impact for KCMSD. The purpose of basing eligible pupil counts on the highest of three years is to shield school districts with declining enrollment from having to face sharp reductions in revenue. Imposing the proposed exception defeats the original purpose of allowing the highest of three years EP.

Further, in addition to the loss in foundation revenue due to the calculation of EP, this bill poses a serious burden on school districts to track information that it may not have access to. If an educational agency grants funds directly to a student, and the student uses the scholarship to transfer to another school the district may not be privy to the information. The proposal also creates a tremendous burden on the district to track who receives the education scholarship, and when it is received. And if the student leaves and returns within a school year, as occurs with

ASSUMPTION (continued)

charter students, the tracking becomes more complicated for purposes of this bill.

Oversight assumes that since the effective date of the program is for tax years beginning on or after January 1, 2005, that taxpayers would begin making contributions in calender year 2005 and utilize the credits against their returns filed in early calendar year 2006, or FY 2006. This would result in a possible loss to general revenue of up to $40 million in FY 2006. Oversight further assumes that scholarship charities would utilize the contributions by issuing scholarships for the school year 2005 - 2006.

Assuming that the $44 million in contributions ($40 million in tax credits / 90% credit rate) is divided by the maximum scholarship available ($3,800) to a qualified student, an estimated 11,578 students would be able to receive the scholarship. According to information on the Department of Elementary and Secondary's web page, the state averaged spending roughly $3,500 per student in the 2003 - 2004 school year for basic state aid, free and reduced lunch and for transportation costs for students in the sixteen provisionally accredited and unaccredited school districts (which includes the Kansas City and the St. Louis City school districts). If these same 11,578 students were to result in a savings to the state for not paying their current school districts these amounts, the state could realize a savings of up to $40,523,000 ($3,500 x 11,578 students). **Oversight's** calculations are based upon the anticipated state funding level for basic state aid, free and reduced lunch and for transportation costs in the 2003 - 2004 school year per student in the sixteen provisionally accredited and unaccredited school districts. The maximum potential savings of $40,523,000 assumes that the proposal would actually result in a reduced payment from the state to the local school districts and not just a change in the distribution of the same amount of funds. It also assumes that all of the students who receive a scholarship through this program had been enrolled in the public school system, and now will be attending a private institution.

The state, however, would not realize a possible savings or would realize a reduced savings in certain circumstances, such as children who are home-schooled, or children who are currently not attending any schools. The state had not paid $3,500 for these children in the previous fiscal year, therefore the savings would be reduced. There is not information available to determine how many of the scholarships would be utilized by the children who are receiving more or less than the average amount spent per pupil by the state. There also is not information regarding the number of children with disabilities that would receive a scholarship, with a maximum amount of $6,500.

The state would also not realize a savings if the nonprofit education assistance organization allocated some of the contributions to directly assist income eligible students who attend public

ASSUMPTION (continued)

school in defraying costs of supplies, private instructional assistance, or other programs (as allowed in 135.616.1(3), while remaining in the same public schools.

Oversight has ranged the fiscal impact of the scholarship (both the tax credit and the savings to the state) from $0 to the maximum amount calculated per year.

Oversight notes that this fiscal note does not include shifting between school districts from Proposition C funds, Fair Share funds and Free Textbook funds which would result in a zero net effect to the local school districts.

Oversight assumes the provisionally accredited and unaccredited school districts may realize some potential cost savings as a result of the reduction in students that are now attending their schools, but would attend other schools as a result of this proposal. According to DESE reports, the Kansas City School District spent roughly $10,221 per student in 2004, while St. Louis City School District spent nearly $10,782 per student. Oversight couldn't determine the fixed versus the variable costs associated with these amounts. Therefore, Oversight has reflected a $0 to Unknown potential savings resulting from reduced variable expenses to the two local school districts.

Officials from the **Wellston School District** and the **Normandy School District** did not respond to our request for fiscal impact.

The Missouri school districts that currently are provisionally accredited or unaccredited are;

Bunker R-III	Clarksburg C-2	Clever R-V	Craig R-III
Davis R-XII	Kansas City	McDonald Co R-I	Neelyville R-IV
Niangua R-V	Normandy	Raymondville R-VII	Spickard R-II
St. Louis City	Verona R-VII	Wheaton R-III	Wellston

This proposal could reduce Total State Revenues.

FISCAL IMPACT - State Government	FY 2006 (10 Mo.)	FY 2007	FY 2008
GENERAL REVENUE			
Savings - Education costs the state would not pay to the local school districts for students receiving the scholarship set up through this proposal (Section 163.036) *	$0 to $40,523,000	$0 to $40,523,000	$0 to $40,523,000
Savings - up to 2% of contributions may be used to offset expenses incurred by DED or the designated nonprofit oversight organization (Section 135.624.2 **	$0 to $81,186	$0 to $78,536	$0 to $80,587
Costs - Department of Economic Development (DED)			
Personal Service (1 FTE)	($41,734)	($42,777)	($43,847)
Fringe Benefits	($17,804)	($18,249)	($18,705)
Expense and Equipment	($21,648)	($17,510)	($18,035)
Total Costs - DED	($81,186)	($78,536)	($80,587)
Loss - Tax Credits for Contributions to educational assistance organizations *	$0 to ($40,000,000)	$0 to ($40,000,000)	$0 to ($40,000,000)
ESTIMATED NET EFFECT TO THE GENERAL REVENUE FUND	**($40,000,000) to $523,000**	**($40,000,000) to $523,000**	**($40,000,000) to $523,000**

*** The net effect to the General Revenue Fund from the Scholarship Charity Tax Credit Program assumes the maximum amount of tax credits are being utilized by taxpayers and that the average anticipated savings per pupil are being realized by the state.**

**** Administrative costs for DED (or possible designated nonprofit oversight organization) shall be no more than 2% of contributions.**

FISCAL IMPACT - Local Government	FY 2006 (10 Mo.)	FY 2007	FY 2008
LOCAL SCHOOL DISTRICTS			
Savings - of educational expenses of not educating students who receive scholarships to attend other schools	$0 to Unknown	$0 to Unknown	$0 to Unknown
Loss - of state funding for students who receive scholarships from program to attend other schools	$0 to ($40,523,000)	$0 to ($40,523,000)	$0 to ($40,523,000)
ESTIMATED NET EFFECT TO LOCAL SCHOOL DISTRICTS	**UNKNOWN TO ($40,523,000)**	**UNKNOWN TO ($40,523,000)**	**UNKNOWN TO ($40,523,000)**

FISCAL IMPACT - Small Business

Small businesses may choose to participate in this tax credit program.

DESCRIPTION

This proposal authorizes an individual income tax credit for contributions made to a Missouri nonprofit educational assistance organization. Contributions for the educational expenses of a taxpayer's dependent do not qualify. The amount of the tax credit will be equal to 90% of the contribution.

The amount of the tax credit cannot exceed the tax liability of the taxpayer in any one year. Any unused credit can be carried forward for four years.

The cumulative amount of tax credits cannot exceed $40 million per fiscal year. The Director of the Department of Economic Development will establish a procedure to apportion the tax credits among all nonprofit educational assistance organizations.

The director will annually determine which organizations may be classified as nonprofit educational assistance organizations. The proposal lists the conditions for qualification.

DESCRIPTION (continued)

The proposal allows the director to contract with a nonprofit educational assistance organization to be a designated nonprofit oversight organization to administer the program. Contributions are to be distributed to the educational assistance organization for student scholarships less up to 2% for administrative and marketing costs.

The proposal requires the eligible pupil count to be adjusted if a pupil no longer is enrolled or transfers to another school because of using the proceeds of an educational scholarship.

The tax credit will apply to all tax years beginning on or after January 1, 2005.

The proposal has an emergency clause

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Department of Economic Development
Department of Elementary and Secondary Education
Department of Revenue
Office of Administration - Budget and Planning
Office of the Secretary of State
St. Louis School District
Kansas City School District

NOT RESPONDING: Wellston School District, Normandy School District

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Director
March 1, 2005