Department of Finance and Administration

Legislative Impact Statement

Bill: SB740
Bill Subtitle: TO PROVIDE K-12 SCHOLARSHIPS TO ECONOMICALLY DISADVANTAGED STUDENTS BY PROVIDING A TAX CREDIT FOR CONTRIBUTIONS TO NONPROFIT SCHOLARSHIP-FUNDING ORGANIZATIONS; AND TO DECLARE AN EMERGENCY.

Basic Change :
Senator J. English

The bill would create a tax credit equal to 100% of a contribution to an eligible scholarship funding organization. The scholarship funding organization must meet certain criteria and would fund scholarships to private schools for grades K-12 for children of families making 250% or less than the federal poverty level. The credit may offset 100% of the tax liability and unused credits may be carried forward three years. A taxpayer may not claim a deduction under the income tax law or premium tax law for the same contribution. A taxpayer may not convey, assign, or transfer the income tax credit to another entity unless all of the assets of the eligible taxpayer are conveyed, assigned, or transferred in the same transaction. An eligible taxpayer may rescind all or part of the taxpayer's allocated income tax credit. The rescinded amounts shall become available for purposes of the cap for the state fiscal year. The rescinded amounts shall become available on a first-come, first-served basis after the date of rescission.

Eligible students must reside in a school district that exceeds 1,000 students. Scholarships are limited to the lesser of $4,000 per year or the amount of tuition. Scholarship funding organizations must submit quarterly reports to DFA of the number of students receiving scholarships, the eligible private schools at which students are enrolled and other rules deemed necessary by DFA. Eligible private schools must inform the Department of Education of its planned participation in the program. Eligible scholarship funding organizations must have owners and operators undergo background checks every 5 years and must submit audited financial and compliance statements to DFA. The credit would be limited to $10,000,000 per year, but could increase by 35% if at least 90% of the credit is used in the previous year.

The DFA and DOE shall develop a cooperative agreement to assist in the administration of the credit. The DFA shall adopt rules to administer the credit including rules establishing application forms and procedures governing the allocation and carry forward of the credits. The bill is effective July 1, 2013.

Revenue Impact :
FY2014 - $10.0 m loss
FY2015 - $13.5 m loss

Taxpayer Impact :

A taxpayer will be allowed to claim a credit for 100% of a contribution to an eligible nonprofit scholarship-funding organization. Taxpayer would have to complete the appropriate forms to claim or carry forward the credit.

Resources Required :
Forms, instructions and computer updates will be required - $2,000
Two additional DFA Service Reps - $65,000 per year

Time Required :

Adequate time is provided.

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Procedural Changes :
Income tax employees would need to be trained to administer the credits claimed on returns. Forms will need to be developed and instructions will need to be updated. The tax community will need to be informed. Tax Credit staff would need to be added to administer the tax credits and monitor the credit limits. DFA and DOE will need to develop a cooperative agreement.

Other Comments :
The bill does not provide how the $10M annual cap is to be enforced. There is no mechanism whereby those making contributions will be assured that they will actually receive the credit. Taxpayers will make contributions not knowing whether their tax credit claim will be allowed or denied because they will not know whether the $10M cap has been exceeded. This problem could be overcome by establishing the credit through a State agency before the contribution is made. The state agency could then enforce the $10M cap by discontinuing the issuance of additional credits once the total of $10M in credits has been issued. As written, taxpayers will not know when they file their tax returns claiming the credit whether the $10M limit has been reached or not. DFA would process returns and allow the credits until the $10M threshold has been reached. Persons filing returns claiming the credit after that point would be denied the credit.

DFA will require additional employees to comply with its duties under this bill. The bill requires DFA to annually list and verify the eligibility of each nonprofit scholarship funding organization. DFA is also required to annually verify the eligibility of expenditure records of these organizations. DFA is also required to notify these scholarship organizations if any student is receiving corporate income tax scholarships from other similar organizations. Finally, DFA is to make quarterly reports concerning participation in this scholarship program and to work with the Department of Education to administer the scholarship program. At least two additional employees with accounting degrees will be needed.

Legal Analysis :

SB740 provides a credit against state income tax or insurance premium tax of 100% of eligible contributions made during the year to an eligible nonprofit scholarship funding organization (NSFO). The credit may not exceed 100% of the tax. Additionally, the credit is subject to a reduction by an amount to be determined by calculating the difference in the tax due with and without the credit. Unused credits may be carried forward up to three years. A taxpayer may not convey, assign, or transfer the credit to another entity unless all of the assets of the taxpayer are conveyed, assigned, or transferred in the same transaction.

There is a $10 million cap on income tax credits and carry forward of income tax credits for the fiscal year beginning July 1, 2013. The limitation for fiscal years after July 1, 2014 is the amount of the credits for the preceding year. An eligible taxpayer is allowed to rescind all or part of the credit , which amount becomes available for purposes of the cap under conditions stated in the bill.

An NSFO is required to provide DFA with annual financial and compliance audits of its accounts and records as well as certain quarterly reports. DFA is required to: 1) provide an annual list of NFSOs, 2) annually verify the eligibility of NFSOs, 3) annually verify the eligibility of expenditures of NSFOs, 4) notify NSFOs of any identified students receiving corporate income tax credit scholarships from other NSFOs, 4) require quarterly reports from NSFOs regarding the number of

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students participating in the scholarship program, as well as the eligible private schools at which the students are enrolled and any other information deemed necessary by DFA, 6) adopt necessary rules, 7) cooperate with the Department with Education to develop a cooperative agreement to assist in the administration of the requirement of the act, and 8) approve transfers of funds to other NSFOs in the event the funds are required to meet scholarship demand at the receiving NSFO. The bill does not identify what is to be done with the information received and retained by DFA.

If an NSFO intends to either deny, suspend or revoke an eligible private school's participation in a scholarship program or suspend payment of scholarship funds, these decisions are appealable to DFA. Such an appeal would not fall under the provisions of the Tax Procedure Act and any such hearings would fall under the requirements of the Administrative Procedure Act at Ark. Code Ann. §25-15-201 et seq.

The bill states that a taxpayer that claims an income tax credit cannot take a deduction under the income tax law or the premium tax law for the same contribution.

The bill contains an emergency clause with an effective date of July 1, 2013.