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**HOUSE OF REPRESENTATIVES
AS REVISED BY THE COMMITTEE ON
FISCAL POLICY & RESOURCES
ANALYSIS**

BILL #: HB 271
RELATING TO: Corporate Income Tax
SPONSOR(S): Representative(s) Negron, Melvin, and Diaz de la Portilla
TIED BILL(S): None

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

- (1) EDUCATION INNOVATION YEAS 10 NAYS 4
 - (2) FISCAL POLICY & RESOURCES
 - (3) EDUCATION APPROPRIATIONS
 - (4) COUNCIL FOR LIFELONG LEARNING
 - (5)
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I. SUMMARY:

HB 271 creates a corporate income tax credit for monetary donations to a nonprofit scholarship funding organization that is established to provide scholarships to students that qualify for the Federal Free or Reduced Price Lunch Program.

Corporate income taxpayers must receive a credit equal to 100% of the contribution, but the credit must not exceed 75% of the balance of taxes due after all other credits have been applied. Additionally, this tax credit is added to a corporation's taxable income for the purpose of determining its "adjusted federal income." The bill allows no carryover of credit to the next taxable year, nor may a taxpayer 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.

The bill directs an eligible nonprofit scholarship funding organization to provide scholarships to eligible students for tuition, textbook expenses, instructional expenses, and transportation expenses. The bill specifies that scholarship amounts must not exceed 1)\$4,000 to students enrolled in nonpublic primary or secondary schools located in Florida that offer general education to primary or secondary students and do not discriminate based on race, color, or national origin; 2)\$1,000 to students enrolled in eligible home education programs as defined in law; and 3)\$500 to students enrolled in Florida public schools that are located outside the district in which the students reside.

The bill requires nonprofit scholarship funding organizations to allocate, over a 5-year period, 100% of the annual eligible contributions received from a participating corporation. The organization must disburse at least 20% of the contributions each year. No portion of the contributions may be used for administrative expenses.

The bill specifies that funding for this credit must be established annually in the General Appropriations Act. The amount has not yet been determined, but will be appropriated from the General Revenue fund. However, every public school student who receives a scholarship and attends a nonpublic school or a home education program is likely to save local governments money due to the difference between the scholarship amounts and the average cost of providing public school education, which is primarily funded by ad valorem taxes.

II. SUBSTANTIVE ANALYSIS:

A. DOES THE BILL SUPPORT THE FOLLOWING PRINCIPLES:

- | | | | |
|-----------------------------------|---|-----------------------------|------------------------------|
| 1. <u>Less Government</u> | Yes <input checked="" type="checkbox"/> | No <input type="checkbox"/> | N/A <input type="checkbox"/> |
| 2. <u>Lower Taxes</u> | Yes <input checked="" type="checkbox"/> | No <input type="checkbox"/> | N/A <input type="checkbox"/> |
| 3. <u>Individual Freedom</u> | Yes <input checked="" type="checkbox"/> | No <input type="checkbox"/> | N/A <input type="checkbox"/> |
| 4. <u>Personal Responsibility</u> | Yes <input checked="" type="checkbox"/> | No <input type="checkbox"/> | N/A <input type="checkbox"/> |
| 5. <u>Family Empowerment</u> | Yes <input checked="" type="checkbox"/> | No <input type="checkbox"/> | N/A <input type="checkbox"/> |

For any principle that received a "no" above, please explain:

While this bill directs the Department of Revenue to adopt rules necessary to administer the corporate tax credit and the Department of Education to adopt rules necessary to determine the eligibility of nonprofit scholarship funding organizations, it does support the principle of less government because it provides students in government schools with the opportunity to attend non-government schools.

B. PRESENT SITUATION:

Chapter 220, F. S., currently does not provide a tax credit for corporate donations to nonprofit organizations that are established to provide scholarships to students. However, statutory provisions provide the following tax credits:

- Assessments against member HMO's income tax credit (s. 631.828, F.S.);
- Capital investment tax credit (s. 220.191, F.S.);
- Enterprise Zone jobs credit (s. 220.181, F.S.);
- Community contribution tax credit (s. 220.183, F.S.);
- Enterprise Zone property tax credit (s.220.182, F.S.);
- Rural job tax credit and urban high-crime area job tax credit (s. 220.1895, F.S.);
- Credit for emergency excise tax paid (s. 221.02, F.S.);
- Hazardous waste facility tax credit (s. 220.184, F.S.);
- Credit for Florida alternative minimum tax (s. 220.186, F. S.);
- Contaminated site rehabilitation tax credit (s. 220.1845, F.S.);
- Childcare tax credits (s. 220.19, F.S.); and
- State housing tax credit (s. 220.185, F.S.).

According to the Department of Revenue, Florida will collect \$1.5 billion in corporate income taxes for the current fiscal year.

Federal Tax Code

Section 501(c)(3), Internal Revenue Code, identifies several tax-exempt corporations. Among those listed are: corporations, and any community chest, fund or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes.

Arizona Income Tax Credit

Section 43-1089, Arizona Revised Statutes, creates a personal state income tax credit for donations to school tuition organizations that provide scholarships to students wishing to attend a nongovernmental school that does not discriminate on the basis of race, color, handicap, or national origin.

The maximum annual credit a single individual or a head of household can receive for contributions to school tuition organizations is \$500, while the maximum annual credit a couple filing jointly can receive for contributions to school tuition organizations is \$625.

This section of statute that provides a tax credit for monetary donations to a school tuition organization was challenged and ruled constitutional by the Arizona Supreme Court. The ruling was appealed to the United States Supreme Court and the Court denied certiorari, letting the decision of the Arizona Supreme Court stand.

Illinois Income Tax Credit

Beginning January 1, 2000, an Illinois resident who is the parent or legal guardian of one or more qualifying students is eligible to receive a credit against his or her state income tax liability for tuition and other qualified education expenses (tuition, book fees, or lab fees) paid to public schools, certain nonpublic elementary or secondary schools, and certain private schools providing educational instruction in the home. The maximum annual credit received may not exceed \$500. Two court cases were filed that challenged the tax credit, but both have been dismissed by Illinois courts.

Florida Nonprofit Scholarship Organizations

Florida, currently has a few nonprofit scholarship funding organizations that are established as charitable organizations that receive contributions for scholarships and are exempt from the federal income tax. In some instances, a nonprofit scholarship funding organization acts as a pass-through for contributions with all the revenue received immediately being utilized for scholarships. In other instances, nonprofit scholarship funding organizations invest the money, thus creating an endowment in order to create long-term scholarships. Three such Florida nonprofit scholarship funding organizations include: The Children First Central Florida Foundation, Miami Inner City Angels, and the Children's Scholarship Fund of Tampa Bay.

The Children First Central Florida Foundation was established in 1995 in order to award scholarships to students who qualify for federal free and reduced price lunch programs.

Miami Inner City Angels was established in the fall of 1998 in order to provide scholarships that are funded from individual and corporate donations.

The Children's Scholarship Fund of Tampa Bay was established in September of 1998 and provides scholarships to students who meet the requirements of Federal Free and Reduced Price Lunch Programs.

C. EFFECT OF PROPOSED CHANGES:

HB 271 provides a credit against the corporate income tax for eligible contributions made by corporations to eligible nonprofit scholarship funding organizations. Eligible contributions made to eligible nonprofit scholarship funding organizations are used to provide scholarships to students who qualify for the Federal Free or Reduced Price Lunch Program who enroll in eligible nonpublic schools, eligible home education programs, or Florida public schools that are outside the district in which the student resides.

CORPORATE INCOME TAX CREDIT

Corporate income taxpayers must receive a credit equal to one dollar for every one dollar contributed to an eligible nonprofit scholarship funding organization provided that the total credit does not exceed 75% of the balance of taxes due after all other credits have been applied. The following tax credits must be applied in the following order before the tax credit provided by this bill can be applied:

- Assessments against member HMO's income tax credit (s. 631.828, F.S.);
- Capital investment tax credit (s. 220.191, F.S.);
- Enterprise Zone jobs credit (s. 220.181, F.S.);
- Community contribution tax credit (s. 220.183, F.S.);
- Enterprise Zone property tax credit (s. 220.182, F.S.);
- Rural job tax credit and urban high-crime area job tax credit (s. 220.1895, F.S.);
- Credit for emergency excise tax paid (s. 221.02, F.S.);
- Hazardous waste facility tax credit (s. 220.184, F.S.);
- Credit for Florida alternative minimum tax (s. 220.186, F. S.);
- Contaminated site rehabilitation tax credit (s. 220.1845, F.S.);
- Childcare tax credits (s. 220.19, F.S.);
- State housing tax credit (s. 220.185, F.S.); and
- Contributions to nonprofit scholarship funding organizations (s. 220.187, F.S.).

The bill specifies that unused credit may not be carried forward to subsequent years and may not be transferred to another entity unless all of the taxpayer's assets are transferred in the same transaction.

Additionally, the tax credit established by the bill is added back to a corporation's taxable income for the purpose of determining its "adjusted federal income."

APPLICABLE DEFINITIONS

The bills defines:

- "eligible contribution" as a monetary contribution from a Florida corporation that is provided to an eligible nonprofit scholarship funding organization if the taxpayer does not designate a specific child as the beneficiary of the contribution;
- "eligible nonpublic school" as a nonpublic primary or secondary school located in Florida that offers a general education to primary or secondary students and does not discriminate based on race, color, or national origin; and
- "eligible nonprofit scholarship funding organization" as a charitable organization that is exempt from federal income tax as specified in s. 501(c)(3) of the Internal Revenue Code.

STUDENT ELIGIBILITY CRITERIA

The bill directs an eligible nonprofit scholarship funding organization to provide scholarships to students who qualify for the Federal Free or Reduced Price Lunch Program. Students enrolled in an eligible nonpublic school can use the scholarships.

- in order to cover tuition, textbook expenses, or transportation expenses;
- students participating in a home education program as defined in s. 232.0201, F. S., can use the scholarships in order to cover instructional expenses; and
- students enrolled in a Florida public school that is located outside the district in which the student resides can use the scholarships in order to cover transportation expenses.

AWARD AMOUNT

The bill specifies scholarship amounts must not exceed the following:

- \$4,000 to a student enrolled in an eligible nonpublic school;
- \$1,000 to a student enrolled in a home education program (as defined in s. 232.0201, F.S.); and
- \$500 to a student enrolled in a Florida public school that is located outside the district in which the student resides.

It should be noted that during the current fiscal year, the State of Florida provides an average of \$5,000 per public school student.

NONPROFIT FUNDING ORGANIZATIONS REQUIREMENTS

The bill requires nonprofit scholarship funding organizations to allocate, over a 5-year period, 100% of the annual eligible contributions received from participating corporations. The nonprofit scholarship funding organization must disburse at least 20% of the contributions each year. No portion of the contributions may be used for administrative expenses.

FUNDING PROVISIONS

The bill specifies that appropriations for funding of this credit be established annually in the General Appropriations Act (GAA). Credit will be allocated on a first come, first served basis. If applications exceed available funding on a given day, the bill requires the Department of Revenue to prorate credit among applications received on that day, based on postmark, and notify each corporation of the credit amount approved.

D. SECTION-BY-SECTION ANALYSIS:

Section 1: Creates s. 220.187, F.S., in order to

- (1) provide a credit against the corporate income tax for eligible contributions, made by corporations, to eligible nonprofit scholarship funding organizations;
- (2) define "eligible contribution," "eligible nonpublic school," and "eligible nonprofit scholarship funding organization;"
- (3) specify the amount of credit that corporations must receive;
- (4) specify student eligibility;
- (5) provide for use of contributions made to eligible nonprofit scholarship funding organizations for scholarships to certain children and provide requirements and limitations;
- (6) specify the amount of scholarships, requirements, and limitations;
- (7) provide for the annual funding through the General Appropriations Act;
- (8) provide for the allocation of the credit;
- (9) direct the Department of Revenue to adopt rules, establish application forms and procedures to administer this section;
- (10) direct the Department of Revenue and the Department Education to develop a cooperative agreement to assist in the administration of this section; and

(11) require the Department of Education to provide the Department of Revenue with a list of eligible nonprofit scholarship funding organizations each year.

Section 2: Amends s. 220.02(8), F.S., to provide the order that credits for contributions to nonprofit scholarship funding organizations are to be claimed relative to other credits authorized under Chapter 220, F.S.

Section 3: Amends s. 220.13(1)(a), F.S., to add tax credit amounts claimed under s. 220.187, F.S., back to taxable income for the purpose of determining a taxpayer's "adjusted federal income."

Section 4: Provides an effective date of January 1, 2002.

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

See fiscal comments.

2. Expenditures:

See fiscal comments.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Through a corporate tax credit, the bill provides an incentive for Florida corporations to provide contributions to nonprofit scholarship funding organizations for the purpose of awarding scholarships.

Students and parents are allowed to attend the schools of their choice. The bill may increase the accessibility of private schools for students that are not able to afford going to private schools by the provision of scholarships.

D. FISCAL COMMENTS:

The total statewide amount of the tax credit will be established in the General Appropriations Act. However, every public school student who receives a scholarship and attends a nonpublic school or a home education program is likely to save local governments money due to the difference between the scholarship amounts (up to \$4,000 to attend a nonpublic school and up to \$1,000 to enroll in a home education program) and the average cost of providing public school education (approximately

\$5,000, which includes basic student FEFP funding, transportation, textbooks, and supplies), which is primarily funded by ad valorem taxes.

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

The bill does not require counties or municipalities to spend funds or take action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

The bill does not reduce the authority that counties or municipalities have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

The bill does not reduce the authority that counties or municipalities have to raise revenues in the aggregate.

V. COMMENTS:

A. CONSTITUTIONAL ISSUES:

In 1997, Arizona enacted a statute that allowed a state tax credit for persons who donated to a school tuition organization. This statute was challenged in court and found to be constitutional by the Arizona Supreme Court. The U.S. Supreme Court declined to review this decision.

The Arizona court engaged in an extensive analysis of the statute as it relates to the Establishment Clause of the First Amendment to the U.S. Constitution. Were HB 271 to become law and be challenged in the Florida courts, a similar Establishment Clause analysis would apply. The Arizona decision is not binding in Florida courts, but could be cited as persuasive authority.

The Arizona court applied the three pronged test established by the U.S. Supreme Court in *Lemon v. Kurtzman*, 403 U.S. 602, 612-13, 91 S.Ct. 2105, 2111, 29 L.Ed.2d 745 (1971), to determine whether their statute complied with the Establishment Clause. Simply stated, a statute does not violate the First Amendment if (1) it serves a secular purpose; (2) its principal or primary effect neither advances nor inhibits religion; and (3) it does not "foster an excessive government entanglement with religion." *Id.*

In finding that its statute met the first prong of the *Lemon* test, the Arizona court relied heavily on the U.S. Supreme Court case of *Mueller v. Allen*, 463 U.S. 388, 103 S.Ct. 3062, 77 L.Ed.2d 721 (1983). The Minnesota statute at issue in *Mueller* allowed a tax deduction for certain educational and transportation expenses for children attending any elementary or secondary schools (public, private sectarian, or nonsectarian private). The *Mueller* court found that this deduction served a secular purpose and stated:

A state's decision to defray the cost of educational expenses incurred by parents – regardless of the types of schools their children attend – evidences a purpose that is both secular and understandable. An educated populace is essential to the political and economic health of any community, and a state's efforts to assist parents in meeting the rising cost of educational

expenses plainly serves this secular purpose of ensuring that the state's citizenry is well-educated.

Id. at 395, 103 S.Ct. at 3067.

The Mueller court went on to note that private schools frequently serve to stimulate public schools by relieving tax burdens and producing healthy competition. Id. This same analysis applies to this bill. Corporations choosing to use this tax credit will be providing funds, administered through an eligible nonprofit scholarship funding organization, to help defray educational expenses of children and thereby help ensure a well-educated citizenry.

The second prong of the Lemon test is whether the principal effect of the law is to further sectarian aims of the nonpublic schools. The Arizona court found that the "aid was provided on a neutral basis with any financial benefit to private schools sufficiently attenuated." Id. at 279, 972 P.2d at 612. The tax credit was one of many allowed by the state in an extensive assortment of tax saving mechanisms, and the credit could also be used for public school extracurricular activity fees.

Furthermore, the Arizona taxpayers could not restrict the gift to benefit a particular child. Taxpayers give gifts to school tuition organizations (STO) and students then apply to the STO for a scholarship to attend the school of their choice. The court found that this arrangement made schools "no more than indirect recipients of taxpayer contributions, with the final destination of these funds being determined by individual parents." Id. at 281, 972 P.2d at 614. The Arizona court also found that this process prevents "excessive government entanglement with religion" Lemon, 403 U.S. 613, 91 S.Ct. 2105, and therefore satisfies the third prong of the Lemon test.

HB 271 follows the same structure as the one used in Arizona. Corporations must give their gifts to an "eligible nonprofit scholarship funding organization" that then grants scholarships to children to attend the school of their choice. The bill also allows scholarships to be awarded to public school students for transportation expenses when students attend a public school outside the district in which they reside.

In addition to the Establishment Clause, Florida's Constitution also has a provision which states that "[n]o revenue of the state or any political subdivision or agency thereof shall ever be taken from the public treasury directly or indirectly in aid of any church, sect or religious denomination or in aid of any sectarian institution." Some may argue that this tax credit is a way of indirectly giving "revenue . . . from the public treasury" to aid sectarian educational institutions. The Arizona court addressed a similar issue in its case, and its analysis is useful in addressing this provision in the Florida Constitution.

The Arizona court rejected the argument that the tax credit diverts to private schools money that would otherwise be state revenue. "It does not follow, however, that reducing a taxpayer's liability is the equivalent of spending a certain sum of money." Kotterman, 193 Ariz. at 286, 972 P.2d at 619.

This analysis would also apply to the provisions of this bill. Although it is not possible to predict how the Florida courts would interpret this provision, it would seem that this tax credit does not appropriate revenue from the public treasury. Rather, it allows corporations to reduce their taxes before the money is required to be paid in to the public treasury.

B. RULE-MAKING AUTHORITY:

The bill grants the Department of Revenue rulemaking authority to administer the tax credit and to establish application forms and procedures. In addition, the bill grants the Department of Education rulemaking authority to determine eligibility of nonprofit scholarship funding organizations.

C. OTHER COMMENTS:

None.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

On February 6, 2001, the Committee on Education Innovation adopted three amendments without objection. The amendments are currently traveling with the bill. The amended bill differs from the original bill in the following ways:

- Amendment number one clarifies that students in kindergarten are also eligible to receive a scholarship.
- Amendment number two clarifies that children from families that meet income eligibility guidelines for free and reduced price lunch meals pursuant to the National School Lunch Act are eligible to receive a scholarship. Additionally, this amendment clarifies that children attending nonpublic schools can use a scholarship to cover tuition, textbook, and transportation expenses. This amendment also clarifies that regardless of the number of scholarships a student receives that the total award can not exceed the limits established in the bill.
- Amendment number three directs the Department of Education to adopt rules that confirm compliance, rather than determine eligibility, of nonprofit scholarship funding organizations.

VII. SIGNATURES:

COMMITTEE ON EDUCATION INNOVATION:

Prepared by:

Elsie J. Rogers

Staff Director:

Daniel Furman

AS REVISED BY THE COMMITTEE ON FISCAL POLICY & RESOURCES:

Prepared by:

Carol Dickson-Carr

Staff Director:

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