

MINNESOTA • REVENUE

INDIVIDUAL INCOME TAX Credit for Contributions to “School Tuition Organizations”

April 19, 2005

	Yes	No
Separate Official Fiscal Note Requested	X	
Fiscal Impact		
DOR Administrative Costs/Savings		X

Department of Revenue
Analysis of S.F. 584 (Olson) / H.F. 1858 (Sykora)

	<u>Fund Impact</u>			
	<u>F.Y. 2006</u>	<u>F.Y. 2007</u>	<u>F.Y. 2008</u>	<u>F.Y. 2009</u>
		(000's)		
General Fund	\$0	(\$5,500)	(\$11,100)	(\$13,600)

Assumed effective beginning with tax year 2006.

EXPLANATION OF THE BILL

The proposed law creates a nonrefundable income tax credit for individuals who make contributions to school tuition organizations (STOs) that in turn provide scholarships and grants to students attending kindergarten, elementary or secondary schools. The STO must allocate at least 85% of its annual revenue to scholarships or grants for children to allow them to attend any qualified school of their parents' choosing. It is assumed the credit is not available to corporations. Since a deduction for such a contribution already exists under IRC section 170, there will be an addition to federal taxable income on the Minnesota return for taxpayers who itemize their deductions. The students must come from families with incomes less than the statewide median family income. The credit would be equal to 75% of the contribution and has a maximum of \$1,000 per tax return.

Note: The proposal as introduced is effective beginning with tax year 2004. For purposes of this analysis, the proposal is assumed effective beginning with tax year 2006.

REVENUE ANALYSIS DETAIL

- It is not known how many STOs will be established to take advantage of this credit and how effective they will be at encouraging contributions.

REVENUE ANALYSIS DETAIL (Continued)

- The experience of the state of Arizona which has had a somewhat similar program since 1998 was used as a starting point for the analysis. The cost of their private school credit program has been as follows:
 - 1998 - \$ 1,816,299
 - 1999 - \$13,706,611
 - 2000 - \$17,542,662
 - 2001 - \$24,865,295
 - 2002 - \$26,169,177
 - 2003 - \$29,063,443
- The 2004 population estimates for Minnesota and Arizona are 5.10 million and 5.74 million respectively. The Minnesota to Arizona percentage of 88.9% was used as an adjustment.
- The Minnesota credit is 75% of the contribution. In Arizona the percentage is 100%. It was assumed that the lower Minnesota percentage would make it slightly less likely that contributions would be made. The percentage used was 90% of 75% or 67.5%.
- The maximum credit per taxpayer in Minnesota is \$1,000. The Arizona maximum credit per individual return is \$500 for a single filer and \$625 for a jointly filed return. The estimate was increased by 20% to reflect the higher maximums.
- In Minnesota, the income of the family of the recipient of the scholarship or grant must be below the statewide median income. In Arizona, there is no income limitation. The estimate was reduced by 10% because of the income limitation.
- The 2001-02 private school enrollment rates for Minnesota and Arizona are 10.6% and 4.6% respectively. The Minnesota to Arizona percentage is 230.4%. Because of the higher tendency to use private schools in Minnesota, the estimate was increased by 50%.
- It was assumed that the certification requirement for the STO and the requirement that no specific student could be designated as the recipient of the scholarship or grant could reduce the cost of the proposal by about 25%.
- The estimate was reduced because taxpayers who itemize will have an add-back on their Minnesota return. It was assumed that 50% of the credit would be taken by itemizers and that a marginal tax rate of 6% would apply.
- A 2% growth rate was assumed.
- In light of Arizona's experience, participation was phased in at 25% the first year, 50% the second year, and 60% the third year.

Number of Taxpayers Affected: Unknown.

Source: Minnesota Department of Revenue
Tax Research Division
http://www.taxes.state.mn.us/taxes/legal_policy