JOINT LEGISLATIVE AUDIT AND REVIEW COMMISSION
Fiscal Impact Review
2004 Session

Bill Number: HB1036 as Introduced
Review Requested By: Delegate Parrish

JLARC Staff Fiscal Estimates

Fund Source	FY 2005	FY 2006
Dollars		
General Fund	$230,400	$97,160
Non-General Fund	$0	$0
Positions		
General Fund	0	0
Non-General Fund	0	0

JLARC staff concur with the Department of Taxation's Fiscal Impact Statement (FIS) for HB 1036. Revenue loss to the general fund would be capped at $2 million. The Department of Taxation estimates that HB 1036 would cost them $230,400 in FY 2005, $97,160 in FY 2006, and approximately $10,000 annually thereafter. These estimates are comprised primarily of costs associated with system development and testing, and forms revisions. The Department expects that existing staff could absorb the additional administrative responsibilities created by the implementation of this tax credit.

As the program is capped at $2 million, JLARC staff concur with the Department of Taxation's assessment of the revenue impact of HB 1036.

It should be noted that the implementation of HB 1036 could lead to a decrease in State and local public school expenditures and, consequently, present a partial offset to the cost of the proposed tax credit and its implementation. The award of tuition scholarships resulting from this bill may cause some Virginia public school students to enter a private school based on the experience of other states such as Arizona, which implemented similar legislation in recent years. However, limited data is available to quantify the magnitude of this impact.

An explanation of the JLARC staff review is included on the following pages.

Authorized for Release: Philip A. Leone

JLARC offers Fiscal Impact Reviews in accordance with Item 21D of Chapter 1042 (2003 Acts of Assembly). JLARC Fiscal Impact Reviews do not comment on the merits of the bill under review.

Background

Bill Summary: HB 1036 would create a tax credit to promote educational opportunities for children who are at risk of educational failure. Tax credits would be awarded to business entities for eligible contributions made to eligible nonprofit scholarship-funding organizations (NSFO). The amount of the credit would equal 25 percent of the eligible contribution, but could not exceed 75 percent of the tax liability of the business entity. The contributions to NSFOs could be awarded for students' tuition in public and nonpublic schools and their tutoring expenses. The credit would be effective for taxable years beginning on and after January 1, 2005 and would be capped at $2 million annually.

Discussion of Fiscal Implications: The Department of Taxation estimates administrative costs of $230,400 in FY 2005, $97,160 in FY 2006, and approximately $10,000 annually thereafter for the implementation of HB 1036. Administrative costs would include system modifications and testing, and forms redesign. Modifications would be made to the taxpayer accounting system, "Advantage Revenue", as well as to the Department's auditing and tracking applications. All system changes would need to be tested after final development. Finally, tax credit schedules used by individuals and businesses would need to be modified. The Department plans on utilizing existing staff to absorb the increased administrative responsibilities associated with reviewing the applications of businesses and scholarship-funding organizations that wish to participate in the program.

<u>Department of Taxation</u>
JLARC staff concur with the Department of Taxation's estimates for system development, testing, and forms redesign. The Department of Taxation's cost estimates related to systems and forms modifications appear reasonable and are consistent with the estimates provided for the implementation of other tax credit legislation introduced during this session. These costs tend to be fairly standard because the work required to implement a new tax credit does not vary materially with the specific features or magnitude of the credit, unless it is very complex to administer as in the case of a refundable credit.

JLARC staff also concur that existing Department of Taxation staff will be able to carry out the administrative responsibilities stemming from the implementation of HB 1036. The Department believes that existing staff could handle approximately 250-300 such applications. Based on the experience of other states that implemented similar tax credits in recent years, the volume of business and nonprofit applications to be expected in Virginia is likely to fall within or near this range. The average Pennsylvania business contribution was approximately $28,000 in 2002. Using this number as a benchmark, 285 businesses could participate in the Virginia program and claim 25 percent of their combined $8 million contribution before reaching the $2 million tax credit ceiling. The Department would not have to evaluate business applications submitted after the $2 million ceiling has been reached because of the "first-come, first-serve" specification in this legislation, and would likely spend minimal effort on sending standard denial letters. The Department would also be responsible for assessing the eligibility of nonprofit scholarship-funding organizations every three years. Other states that offer similar tax credits have a relatively small number of NSFOs, ranging between 6 in Florida to 60 in Pennsylvania.

<u>Department of Agriculture and Consumer Affairs</u>
JLARC does not believe that the Department of Agriculture and Consumer Affairs will incur additional costs due to the implementation of HB 1036. HB 1036 instructs participating NSFOs to file an annual compliance and financial audit with the Office of Consumer Affairs. Per discussions with staff in that

office, existing personnel can handle filings by the relatively low number of NSFOs expected to participate given the previously described experience of other states.

Public Education Expenditures

The State and localities may experience some savings resulting from the payment of this tax credit if the credit prompts parents to take their children out of public schools and enroll them in private institutions. The State and localities would no longer have to pay for the public education of this pupil, realizing a reduction in expenditures. Limited data exists as to the number of students who may be expected to switch from public to private school, making it difficult to estimate a reliable fiscal impact.

Budget Amendment Necessary: Yes. Items 284 and 285, Department of Taxation.

Agencies Affected

Department of Taxation
Office of the Commissioner of Agriculture and Consumer Services

Date Released, Prepared By: 02/03/2004; Nathalie Molliet-Ribet