

INCOME TAX CREDIT: EDUCATIONAL FOUNDATIONS

House Bill 5043 (Substitute H-3) First Analysis (5-24-00)

**Sponsor: Rep. Michael Bishop
Committee: Tax Policy**

THE APPARENT PROBLEM:

One way that a community can support its public schools is through fundraising and private donations, either directly to a program or district, or to an educational foundation. In some areas of the state, educational foundations have become important in providing schools with resources that would otherwise not be available and enhancing educational opportunities for students and teachers alike. This kind of activity has become more important since the passage of Proposal A in 1994, which created the state's new school financing system. The new system restricts the ability of local taxpayers to increase their school taxes. In some districts that routinely raised their taxes to provide extra resources for schools, people are now instead promoting private fundraising and investment. Some people believe the state tax system should promote and reward this kind of private investment in the schools. Under the state's Income Tax Act, people who make contributions to colleges and universities, public libraries, public television, the state museum, and similar entities can claim a tax credit. Legislation has been introduced that would include educational foundations and some public school programs in the list of eligible institutions.

THE CONTENT OF THE BILL:

The bill would amend the Income Tax Act to provide a credit equal to 50 percent of the amount a taxpayer contributes during the tax year to an educational facility or organization, not to exceed \$100 or, for a husband and wife filing jointly, \$200. The term "educational facility or organization" would mean either 1) an educational foundation or 2) a continuing education, community education, or adult education program operated by a school district or a public school academy (charter school).

A resident estate or trust's credit could not exceed 10 percent of the year's tax liability or \$5,000, whichever was less, and the contribution could not have been deducted in arriving at federal taxable income.

The bill would amend Section 260 of the act and put contributions to an educational facility or organization in the same category as contributions to public libraries, public broadcast stations, institutions of higher learning, the Michigan Colleges Foundation, various public artwork donations, the state museum, and the state archives. The contribution limit applies to the aggregate amount given to all such organizations.

The bill specifies that a contribution to an entity listed under Section 261 could not be used to calculate a credit under the bill. Section 261 contains existing credits for contributions to community foundations and to shelters for homeless persons, food kitchens, food banks, and other entities in the state whose purpose is to provide overnight accommodation, food, or meals to the indigent. The credit limit in that section is separate from the credit limit in Section 260.

Educational Foundation. An education foundation would mean an organization that applied for certification on or before April 1 of the tax year for which the taxpayer was claiming a credit; that annually submitted documentation to the Department of Treasury demonstrating continued compliance with the requirements of the bill; and that the department certified for that tax year as meeting all of the following requirements:

- qualified for exemption from federal income taxation under Section 501(c)(3) of the Internal Revenue Code;
- maintained an ongoing program to attract new funds by seeking gifts and bequests from a wide range of potential donors in the community or area served;
- exclusively dedicated all funds, gifts, and bequests to a school district or public school academy or a foundation described in Sections 509(a)(1) or 509(a)(3) of the Internal Revenue Code that was located in the community or area served and located in the state;

- was publicly supported as defined by the regulations of the United States Department of Treasury;
- met the requirements for treatment as a single entity contained in federal treasury regulations;
- was incorporated or established as a trust at least six months before the beginning of the tax year for which the credit was being claimed;
- had an independent governing body representing the general public's interest and that was not appointed by a single outside entity; and
- was subject to an annual independent financial audit and provided a copy of the audit to the Department of Treasury not more than three months after the audit was completed.

MCL 206.260

FISCAL IMPLICATIONS:

The House Fiscal Agency estimates that the bill would lower income tax revenues by about \$15 million annually. The HFA points out that the current credit is claimed by about 270,000 filers and reduces income tax revenue by about \$22 million annually. About 25 percent of those claiming the credit reach the \$100/\$200 limit. (HFA fiscal note dated 5-23-00)

ARGUMENTS:

For:

The bill would treat contributions to educational foundations and certain school district programs in the same way that contributions to institutions of higher education and public libraries, public television stations, municipal art donations, and a number of other public organizations are treated under the state's Income Tax Act. Why shouldn't they be on an equal footing? This will encourage private investment in public education programs. In some school districts, private fundraising has replaced the voting of extra tax dollars for schools, because the school financing system prevents districts from increasing school taxes. Educational foundations in some areas are making substantial annual grants to enhance school programs, from technology to conflict management, from reading programs to cultural diversity training. They are providing programs and services that the districts cannot provide for themselves with limited funding. The bill, moreover, puts in place certain requirements on educational foundations similar to those found in the

Income Tax Act for community foundations to ensure that these are legitimate organizations.

Against:

The traditional criticisms of expansions of the income tax credit are 1) the cost to general fund revenues; and 2) the inequitable treatment of those organizations left out. Why should contributors to educational foundations, community education programs, and the like be eligible for a tax credit when contributions to other worthy organizations do not qualify? The groups the bill benefits are engaged in worthwhile endeavors. But so are the Girl Scouts, the Red Cross, the United Way, Habitat for Humanity, churches, and many other nonprofit charitable organizations. Perhaps the issue of tax credits for charitable giving should be re-evaluated and examined comprehensively.

Response:

Aren't groups engaged in efforts to support elementary and secondary education more like entities supporting higher education than like other nonprofit charities? Aren't educational foundations, particularly with the stiff requirements of this legislation, more like community foundations?

POSITIONS:

The Oakland Intermediate Schools have indicated support for the bill. (5-23-00)

The Michigan Education Association has indicated support for the bill. (5-23-00)

The Department of Treasury is opposed to the bill. (5-23-00)

Analyst: C. Couch

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.