Senate Fiscal Agency
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BILL ANALYSIS

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Senate Bill 544 (Substitute S-1 as reported)
Senate Bill 545 (Substitute S-1 as reported)
Senate Bill 546 (Substitute S-1 as reported)
Senate Bill 547 (as reported without amendment)
Senate Bill 548 (Substitute S-2 as reported)
Senate Bill 549 (as reported without amendment)
Sponsor: Senator Patrick J. Colbeck (S.B. 544, 547, & 548)
Senator Phil Pavlov (S.B. 545)
Senator Judy K. Emmons (S.B. 546)
Senator Mike Green (S.B. 549)
Committee: Education

CONTENT

Senate Bill 544 (S-1) would enact the "Enhanced Michigan Education Savings Program Act" as Part 2 of the Michigan Education Savings Program Act to do the following:

-- Create the Enhanced Michigan Education Savings Program.
-- Provide that the Program would consist of one or more saving plans that would allow account distributions for eligible services offered to students by public schools.
-- Create the "Enhanced Michigan Education Savings Program Fund".
-- Allow the State Treasurer, subject to appropriation, to use Program revenue in the Fund to maintain or enhance the State's education programs.
-- Require the Treasurer to enter into a contract with a Program Manager that would act as manager of one or more savings plans offered under the Program and perform specified responsibilities.

Senate Bill 545 (S-1) would enact provisions of the Enhanced Michigan Education Savings Program Act to do the following:

-- Require the Department of Education to determine which services offered by each public school would be eligible services that could be purchased using an account.
-- Provide that each public school that complied with Section 1210 of the Revised School Code (proposed by Senate Bill 548 (S-2)) would be eligible to receive payments from the Enhanced Michigan Education Savings Program.
-- Allow the Department of Education to designate other organizations as eligible to receive payments from the Program.
-- Require the Department to establish and maintain an internet website dedicated to the Program.

Senate Bill 546 (S-1) would enact provisions of the Enhanced Michigan Education Savings Program Act to prescribe the conditions under which an individual could open, contribute to, and distribute funds from an Enhanced Michigan Education Savings Account (ESA).

Senate Bill 547 would amend the Michigan Education Savings Program Act to designate the existing language as Part 1 of the Act.

Senate Bill 548 (S-2) would amend the Revised School Code to require a school district, intermediate school district, or public school academy, in order to be eligible to receive funds from the Enhanced Michigan Education Savings Program, to report to the Departments of Treasury and Education certain information about services to pupils and costs.

Senate Bill 549 would amend the Income Tax Act to allow a taxpayer to deduct from taxable income: 1) contributions, less qualified withdrawals, made pursuant to the proposed Enhanced Michigan Education Savings Program Act, subject to a limit of $5,000 for a single return and $10,000 for a joint return per tax year; 2) interest earned on the contributions; and 3) distributions that were qualified withdrawals from an Enhanced Michigan ESA. The bill also would require a taxpayer to add to taxable income the amount of a withdrawal from such an account that was not a qualified withdrawal.

Senate Bills 545 (S-1), 546 (S-1), 547, 548 (S-2), and 549 are tie-barred to Senate Bill 544. Senate Bill 548 also is tie-barred to Senate Bill 549.

Proposed MCL 390.1487 et al. (S.B. 544)
Proposed MCL 390.1491 & 390.1492 (S.B. 545)
Proposed MCL 390.1493 - 390.1495 (S.B. 546)
MCL 390.1471 et al. (S.B. 547)
Proposed MCL 380.1210 (S.B. 548)
MCL 206.30 & 206.30f (S.B. 549)

Legislative Analyst: Nathan Leaman

FISCAL IMPACT

Senate Bills 544 (S-1), 545 (S-1), 546 (S-1), 547, and 548 (S-2) would have a significant fiscal impact on the Department of Treasury, Department of Education, Center for Education Performance and Information (CEPI), and local school districts. The Department of Treasury would incur both one-time and ongoing costs. The administration, oversight, auditing, security, and data storage of the Enhanced Michigan Education Savings Program (E-MESP) would involve the student financial services, investments, and accounting divisions of the Department. At this time, the exact cost of creating an information technology system in one year is difficult to estimate as it would need an initial capacity of roughly 1.5 million accounts (approximately the number of K-12 students enrolled at present), and it would need to have the capacity to expand each year by the number of newly enrolled students (around 120,000 annually).

In addition, the system would need the ability to make payments to multiple providers and receive deposits from multiple providers, as well as the ability to add, remove, and adjust the cost for eligible services. Though an exact cost cannot be estimated at this time, based on the cost of the existing MESP, combined with the additional complexity, numbers of accounts, and time required to implement the Program, a rough estimate of the cost to create the system could range between $60.0 million and $100.0 million. This cost could be paid for in a variety of ways that would affect the Department either more directly or indirectly. If a vendor could provide this service, then the implementation costs could be spread out as an administrative fee and/or a transaction fee on account holders. Additionally, the system would have ongoing operational costs. Currently, the MESP pays for the $76.0 million cost of the Program through a three-year contract that charges a percentage of the investment earnings to pay for the cost of implementation and management of the Program. Those costs are related to the value of assets under management; as the Program grows, the costs increase. Furthermore, those costs exclude the Department of Treasury's expenses to oversee the MESP. If a vendor were not found for the E-MESP and the Department had to construct the system, then the Department would directly bear the costs.

After the initial one-time cost, the ongoing administration by the Department of Treasury (in addition to establishing and maintaining an internet website dedicated to the E-MESP) would result in additional costs. At this time, it is unknown whether the amount Treasury would be allowed to charge as annual administrative fees (up to 2.0% of the average daily net assets of an account) would be sufficient to pay for managing account contracts and the ongoing administration and marketing of the Program. Arizona's scholarship account program uses 4.0% of the scholarship value toward administration of the program and Nevada uses 3.0% of scholarship value toward administration of the program. This would place Michigan's 2.0% administrative fee cap lower than the fee in other states that have individual education scholarship account programs.

The Department of Education likely would incur additional costs associated with determining which services offered by public schools and other organizations would be eligible services that could be purchased using an E-MESP account. At this time, the exact cost to the Department is unknown. Since the Department of Education would not have explicit access to the administrative fee, it is unclear whether any additional costs could be covered by the fee or would require additional appropriations.

The CEPI would incur additional costs in order to ensure that student records could keep track of education services gained outside of the student's primary district, such as work study programs.

Local school districts would likely incur annual costs associated with estimating the "direct costs and fully burdened costs" for eligible services, and processing the enrollment of students in those various services. Since schools do not typically calculate costs for each individual education service, outside consultation and training could be necessary for initial implementation. The cost of these duties is difficult to estimate given the difference in school types and the amount of eligible services that districts would seek to provide. Local school districts could see increased revenue to the extent parents would choose to purchase additional district services (beyond those provided to the students funded from "traditional" State school aid dollars), using funds deposited by the family or other private sources into an E-MESP account.

Senate Bill 549 would reduce General Fund and School Aid Fund revenue by an unknown, and potentially significant amount, depending on the number and characteristics of taxpayers affected by the bills. The proposed legislation would affect a wider array of taxpayers, and cover a broader array of expenses, than current education saving account provisions, which are estimated to reduce State revenue in fiscal year 2016-17 by approximately $13.7 million. As a result, Senate Bill 549 would likely reduce State revenue by more, and possibly significantly more, than $13.7 million.

Several provisions in the bills exhibit unclear language that could affect the fiscal impact. For example, Senate Bill 544 (S-1) would define "qualified withdrawal" but the definition would not include withdrawals to pay education expenses that were not for postsecondary costs, meaning that withdrawals to pay for services offered by school districts, intermediate school districts, and public school academies under the other bills would not represent qualified withdrawals. However, Senate Bill 544 (S-1) also indicates that withdrawals, not just qualified withdrawals, would be exempt from taxation as provided in Section 30 of the Income Tax Act--although the changes to Section 30 proposed by Senate Bill 549 generally would retain the limitation under which only qualified withdrawals could be deducted. (The bill contains an exception that would allow a taxpayer to forgo adding a withdrawal to income if the withdrawals were less than amounts contributed.) However, contributions would be deductible regardless of whether the withdrawals were qualified. Similarly, Senate Bill 548 (S-2) refers to "fully burdened costs", a term not defined by the bills, and it is unclear whether such costs would represent expenses that would be considered qualified withdrawals.

Participation could be affected by provisions that would require, upon the death of student, money in the account to return to the Michigan Education Savings Program Fund. When a beneficiary dies under existing education savings program contracts, the taxpayer may withdraw funds from the account and all taxpayer withdrawals associated with the student are qualified withdrawals. Similarly, some taxpayers could reduce their contributions to existing ESAs and direct money to the accounts created by the bills, thereby reducing the fiscal impact--although if the taxpayers contributed more to the new accounts, because a wider array of expenses would be covered, such a shift could still increase the revenue loss.

The bills would appear to allow taxpayers to exempt income spent on a variety of current expenses. For example, approximately half of Michigan's public high schools require participants in a variety of athletic or academic programs to pay a fee to participate in the activity, and almost 80.0% do or are considering assessing the fee annually. Fees range from $20 to $425 per student, with a median fee of $150. It is unknown what other costs, for example costs associated with school lunches, instrument rental, or damage to textbooks or school-issued computers, would represent eligible expenses under the bills. However, the bills would appear to allow parents to direct money used to pay many of these fees or expenses through accounts created under the bills, thereby exempting the income used to pay such costs from taxation. As a result, schools would have an incentive to levy fees for more activities or purposes and/or increase existing fees.

Approximately 80.0% of public school students participate in some form of extracurricular activity, and although the percentage of those activities that are offered via the school is unknown, other data suggest the figure could be significant. For example, approximately 300,000 students each year participate in a sport offered by a public high school (although this figure counts students in multiple sports as more than one student). There are approximately 1.5 million Michigan public school students, and these students may participate in other activities beyond athletics that are associated with a fee, such as theatre, debate/forensics, quiz bowl, social clubs, community service groups, Science Olympiad, and robotics. (Approximately one-third of Michigan public schools levy participation fees for nonathletic activities.) If accounts were created for 25.0% of public school students, and an average $1,000 per student were deposited each year, the bills would reduce revenue by approximately $15.9 million per year. Greater participation and/or greater average contribution amounts would increase the loss of revenue; similarly, less participation and/or lower average contributions would reduce the loss of revenue. For example, if accounts were created for 35.0% of students, and the average deduction were $2,500, the bills would reduce revenue by $55.8 million. (The bills would allow a maximum of $5,000 for a single filer or $10,000 for a joint return to be deducted, and contributions could be used to pay more expenses than participation fees.)

Date Completed: 9-27-17

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