Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Pescetti	Analyst:	Kristina E. North	Bill Number:	AB 1625
Related Bills:	None	Telephone:	845-6978	Introduced Date:	February 23, 2001
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Donation to Charitable Organization that Provides Private School Scholarships to Low-Income Children Credit

SUMMARY

This bill would create a 100% credit for donations to a nonprofit charitable organization that provides private school scholarships to low-income children.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to give low-income children an opportunity to attend private schools by encouraging taxpayers to make donations to nonprofit charitable organizations that provide private school scholarships.

EFFECTIVE/OPERATIVE DATE

This bill is a tax levy and would be effective immediately upon enactment. The credit would apply to taxable years beginning on or after January 1, 2001.

POSITION

Pending.

Summary of Suggested Amendments

Department staff is available to assist the author in resolving the implementation and policy considerations discussed below.

ANALYSIS

FEDERAL/STATE LAW

Current federal and state tax laws provide various tax credits designed to provide tax relief for taxpayers that incur certain expenses (e.g., child and dependent care credits) or to influence business practices and decisions or achieve social goals.

Current federal and state tax laws allow a taxpayer to claim charitable contributions as an itemized deduction. Deductions are allowed for monetary charitable contributions or gifts of property to qualified federal, state, or local governments, or to organizations formed for religious, charitable, educational, scientific, or literary purposes or for the prevention of cruelty to children or animals.

Board Position:			Department Director	Date
______ S	______ NA	______ NP		
______ SA	______ O	______ NAR	Gerald H. Goldberg	05/30/01
______ N	______ OUA	__X__ PENDING		

A charitable contribution is defined as a contribution or gift made exclusively for public purposes. A taxpayer is allowed to subtract the greater of the standard deduction or itemized deductions from adjusted gross income (AGI) to calculate taxable income.

Under **federal and state laws**, the deductible amount of any charitable contribution may be reduced depending on the type of contributed property, the organization to which the property is contributed, and the income of the taxpayer. Generally, the amount of any deduction for contributed property that would have resulted in ordinary income being recognized had the property been sold is limited to the property's basis. The charitable contribution deduction for corporations is generally limited to 10% of its taxable income (computed without regard to the contributions) for the taxable year.

Current federal and state tax laws place limitations on charitable contributions. The limitations vary from 20%, 30%, or 50%, depending on the individual's AGI and the amount of contributions made, the types of organizations that receive the donations, and the type of property donated. If an individual's charitable contributions are limited, the excess may be carried over for five years.

<u>THIS BILL</u>

This bill would create a 100% credit for amounts donated by taxpayers to a nonprofit charitable organization that provides scholarships for low-income children to attend a private school in California.

Any excess credit may be carried over indefinitely.

<u>IMPLEMENTATION CONSIDERATIONS</u>

This bill does not define "amounts" donated, thus, a taxpayer could donate property instead of cash. Also, for contributions other than cash, no method of determining the donation amount, such as by the contribution's adjusted basis or its fair market value.

This bill does not define "nonprofit charitable organization." The author may wish to clarify whether this term means only organizations that are exempt from tax under the Revenue and Taxation Code (R&TC §23701d) and the Internal Revenue Code (IRC §501(c)(3)), or other types of nonprofit organizations.

Additionally, the charitable organization is not required to be organized primarily to provide private school scholarships to low-income students, and the donation is not tied to the scholarship. For example, a taxpayer could make a donation to the charitable organization and receive a credit for $10,000, even if the organization provides only $1,000 in private school scholarships that year. No requirement exists that the remaining $9,000 be maintained in a fund exclusively for providing private school scholarships to low-income children. The organization is not prohibited from using the donation for purposes other than providing the private school scholarships.

This bill uses the undefined term "low-income children." The author may wish to consider using the term "low-income" to define the *parents* of the children who would be provided scholarships to private schools. Generally, low-income persons have been defined as people whose annual household income does not exceed 80% of the median for all households in the metropolitan area in which they reside, or for all persons residing outside metropolitan areas in the state, as determined by the United States Department of Housing and Urban Development. Additionally, the term "children" is not defined. It is unclear if children would include adult children.

The term "private school" is undefined and could be interpreted to include private colleges and other organizations. It is unclear if the author intended to limit this credit for contributions given to organizations that provide private scholarships to children attending K-12.

OTHER STATES' INFORMATION

Review of *Florida, Illinois, Massachusetts, Michigan, Minnesota*, and *New York* laws found no comparable tax credits. These states were reviewed because of the similarities to California income tax laws.

FISCAL IMPACT

Once the implementation concerns are resolved, this bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Tax Revenue Estimate

Revenue losses from this bill are projected to be in the following orders of magnitude:

Estimated Revenue Impact of AB 1625 (*) As Introduced February 23, 2001 Enactment Assumed After June 30, 2001 (In $Millions)			
Fiscal Years	2001/2002	2002/2003	2003/2004
T O T A L (Rounded)	-$400	-$680	-$700

(*) As written, this bill would cover any private school in California.

Any possible changes in employment, personal income, or gross state product that might result from this proposal are not taken into account.

Tax Revenue Discussion

Revenue losses would depend on the amount of contributions made by taxpayers in any year to nonprofit charitable organizations that provide private school scholarships to low-income children in this state.

This bill would permit taxpayers to reduce or eliminate their state tax liability dollar-for-dollar on contributions made to provide scholarships. Many taxpayers will redirect cash contributions normally made to take advantage of this tax benefit. Other taxpayers will start making contributions.

According to departmental data, the total number of cash contributors (individuals and businesses) was over 4.3 million for tax year 1998.

Assuming that the number of taxpayers claiming this credit is equal to 5% of existing contributors during the first taxable year and 10% thereafter and they contribute $1,500 on average, the revenue impact of this 100% tax credit would be as indicated above.

POLICY CONCERNS

This bill does not specify a repeal date or limit the number of years for the carryover period. Credits typically are enacted with a repeal date to allow the Legislature to review their effectiveness. However, even if a repeal date were added, the department would be required to retain the carryover on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover period limitation since experience shows credits typically are exhausted within eight years of being earned.

Credits generally are provided as a percentage of actual amounts paid. This bill would allow a 100% credit, which is unprecedented.

Conflicting tax policies would come into play since this credit is allowed for an item that may already be deductible as a charitable contribution. Providing both a credit and a deduction would have the effect of providing a double benefit for that contribution. On the other hand, disallowing the deduction to eliminate the double benefit creates a difference between state and federal taxable income, which is contrary to the state's general conformity policy.

LEGISLATIVE STAFF CONTACT

Kristina E. North	Brian Putler
Franchise Tax Board	Franchise Tax Board
845-6978	845-6333