Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Hollingsworth	Analyst:	Darrine Distefano	Bill Number:	SB 1768
Related Bills:	See Legislative History	Telephone:	845-4142	Introduced Date:	February 24, 2006
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Contributions To School Tuition Organization Or Public School Credit

SUMMARY

This bill would provide an income tax credit for contributions made to a school tuition organization or a public school.

PURPOSE OF THE BILL

It appears that the purpose of this bill is to provide tax incentives for taxpayers to contribute more toward school programs.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective upon enactment and operative for taxable years beginning on or after January 1, 2006.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Individual taxpayers claim charitable contributions as an itemized deduction. Individual taxpayers are allowed to deduct the greater of the standard deduction or itemized deductions from their adjusted gross income when computing taxable income.

Deductions are allowed for monetary charitable contributions or gifts of property to qualified organizations formed for religious, charitable, educational, scientific, or literary purposes. A charitable contribution is defined as a contribution or gift made exclusively for public purposes. There are limitations on individual charitable contributions. The limitations vary from 20%, 30%, or 50%, depending on the individual's adjusted gross income (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.

Board Position:			Department Director	Date
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Corporate taxpayers are entitled to claim charitable contributions up to 10% of the corporation's taxable income, without regard to the charitable contribution. Any contributions in excess of the 10% limitation may be carried over for five years.

THIS BILL

Under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), this bill would provide a credit in an amount equal to any qualified contribution made by a taxpayer to a school tuition organization or public school. The credit amount would be capped at $5,000 under the PITL and $100,000 under the CTL per taxable year.

This bill would also cap the total amount of credits authorized under this section at $20 million each calendar year.

This bill defines the following terms:

- A "public school" means any kindergarten, elementary, or secondary school established by the Legislature or by municipal or district authority.
- "Qualified contribution" means any cash contribution that has been authorized as eligible for the credit in accordance with the requirements of the Superintendent of Public Instruction.
- "School tuition organization" means a charitable organization in this state exempt from federal taxation as defined in Internal Revenue Code section 501(c)(3), which generally includes only those entities organized and operated exclusively for religious, charitable, educational, scientific, or literary purposes. This charitable organization must allocate at least 90 percent of its annual revenue for educational scholarships or tuition grants to children that allow them to attend any qualified school of their parents' choice. The charitable organization would also provide educational scholarships or tuition grants to students without limiting availability to students of only one school.
- "Handicapped student" means a student that has any of the following conditions: hearing impairment, visual impairment, preschool delay, or speech or language impairment.
- "Qualified school" means a nongovernmental preschool, elementary or secondary school, or any combination of these, including a school for handicapped students located in this state that does not discriminate on the basis of race, color, handicap, family status, or national origin, and satisfies the requirements of the law for private schools in this state on January 1, 2001.

This bill requires each school tuition organization or public school that receives a contribution to provide the taxpayer with a receipt for the amount contributed.

This bill requires the taxpayer to do the following to be eligible for the credit:

- File an application for the tax credit with the Superintendent of Public Instruction.
- Provide the Superintendent with a copy of the receipt from the school tuition organization or public school.
- Provide the Superintendent his or her taxpayer identification number or, in the case of a partnership or S-Corporation, the taxpayer identification numbers of all partners or shareholders.

- Provide a copy of the certification issued by the Superintendent to the Franchise Tax Board (FTB). If the taxpayer fails to comply, the credit would be disallowed for any taxable year until the taxpayer subsequently complies.

This bill requires the Superintendent of Public Instruction to do the following:

- Certify that the taxpayer has made the contributions.
- Obtain the taxpayer's identification number and, in the case of a partnership or S-Corporation, the taxpayer identification numbers of all partners or shareholders.
- Process and approve or reject all applications on a first-come, first served basis.
- For approved applications, issue certificates for the tax credit that in total do not exceed the $20 million annual cap.
- Provide the taxpayer with a copy of the certification for their records.
- Provide an annual listing to FTB of qualified taxpayers that were issued certificates and the amount of contributions made by each taxpayer.

This bill would prevent the credit from being utilized if the taxpayer designates the use of their contribution as a direct benefit for a specific student or any dependent of a taxpayer.

This bill would require that any qualified contributions are to supplement, not replace, existing government funding for scholarships.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

The allocation of funds provision is similar to the Low-Income Housing Credit and the Farmworker Housing Credit. Both of these credits are allocated a specific amount during the calendar year that also includes any returned or unused credits from the previous year. For this bill, it is suggested that the author clarify if returned or unused credits would increase the $20 million allocation each calendar year or would simply be lost if not allocated.

The California Tax Credit Allocation Committee (CTAC) is responsible for allocating the credit for both of those other programs. CTAC is located within the California State Treasurer's Office. In conjunction with CTAC, the department is able to administer these credits with ease. To ease administration of this credit, the author and the Superintendent may wish to consult with CTAC to determine how to administer the allocation of this credit.

The author may wish to clarify if the $5,000 would be allocated for each partner in a partnership or for the entire partnership.

TECHNICAL CONSIDERATIONS

The term "Superintendant" is spelled incorrectly on page 3, lines 2, 3, 4, 7, 11, and 16, and on page 5, lines 10, 11, 12, 15, 20, and 25. The correct spelling is "Superintend<u>e</u>nt."

Also, the author may wish to use the term “State Superintendent of Public Instruction” since that is the title of the office within the California Department of Education.

The bill identifies partnerships under the PITL and S-corporations under CTL. S-Corporations shareholders file tax returns under the PITL and partnerships can be corporations under the CTL. Department staff is available to work with the author’s office to identify the type of entities that are required to provide information under this bill.

LEGISLATIVE HISTORY

AB 1262 (Haynes, 2005/06) would have created a 75% credit for donations to a nonprofit organization that provides scholarships to elementary and secondary school students. This bill remained in the Assembly Revenue & Taxation Committee.

SB 1273 (Haynes, 2001/02) contained similar provisions to AB 1262. SB 1273 failed passage out of the Senate Revenue and Taxation Committee.

AB 1358 (Pringle, 1997/98) would have allowed a credit equal to 100% of the unreimbursed qualifying educational expenses paid or incurred by a parent or legal guardian for his or her child. This bill failed to pass out of the house of origin by January 31 of the second year of the session.

AB 2110 (Kaloogian & Baldwin, 1997/98) would have allowed a credit equal to any voluntary cash contributions made to a school tuition organization in this state, not to exceed $500 per taxable year. This bill failed passage in the Assembly Revenue & Taxation Committee.

FISCAL IMPACT

This bill would not significantly impact the department’s costs.

ECONOMIC IMPACT

<u>Revenue Estimate</u>

Based on data and assumptions discussed below, this provision would result in the following revenue losses.

Estimated Revenue Impact of SB 1768 Effective for Tax Years Beginning On or After 1/1/2006 Assumed Enactment Date After 6/30/06 (in Millions)		
2006/07	2007/08	2008/09
-$18	-$16	-$16

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Revenue Discussion

Based on departmental data and donation trends identified by the National Center for Charitable Statistics (NCCS), it is anticipated that qualifying contributions could generate $157 million in credits for both PITL and CTL taxpayers.

Because potential credit losses of $157 million clearly exceed the $20 million annual limit, the estimate assumes $20 million will be allocated annually. It is estimated that 80%, or $16 million, of the credits generated each year would actually be able to be used because for some taxpayers the full amount of this credit will be in excess of net tax. The revenue loss of $18 million for fiscal year 2006/07 includes credits generated in 2006 and anticipated 2007 tax year withholding adjustments. Thereafter, the annual revenue loss would total $16 million.

ARGUMENTS/POLICY CONCERNS

Credits generally are provided as a percentage of amounts paid or incurred. This bill would allow a 100% credit for qualified contributions up to $5,000 per taxable year, which is unprecedented.

Most credits contain a sunset date. Sunset dates generally are provided to allow periodic review by the Legislature.

In addition, most credits contain a limit on the number of years for the carryover period of excess credits. Without a time limit the department would be required to retain the carryover on the tax forms indefinitely because presently the bill would allow an unlimited credit carryover period. Recent credits have been enacted with a carryover limitation because experience shows credits are typically used within eight years of being earned.

LEGISLATIVE STAFF CONTACT

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