ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author:	Nestande and Allen	Analyst:	Diane Deatherage	Bill Number:	AB 2421
Related Bills:	See Legislative History	Telephone:	845-4783	Amended Dates:	April 1& April 22, 2014
		Attorney:	Bruce Langston	Sponsor:	

SUBJECT: Contributions to Nonprofit Education Scholarship Organization Credit

SUMMARY

This bill would create the Nonprofit Education Scholarship Organization tax credit under the Corporation Tax Law (CTL).

RECOMMENDATION

No position.

Summary of Amendments

The April 1, 2014, amendments added a coauthor, removed the legislative intent language from the bill as introduced February 21, 2014, and added provisions that would create a corporate tax credit for contributions to fund scholarships for foster care youth as discussed in this analysis.

The April 22, 2014, amendments added several coauthors and modified the corporate tax credit provisions as discussed in this analysis.

This is the department's first analysis of the bill. This analysis only addresses the provisions of this bill that impact the department's programs and operations.

REASON FOR THE BILL

The reason for this bill is to encourage contributions to support scholarships relating to education for foster care and homeless youth by offering an income tax credit.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2015, and before January 1, 2020.

ANALYSIS

FEDERAL/STATE LAW

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

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Current state and federal laws generally allow taxpayers engaged in a trade or business to deduct all expenses that are considered ordinary and necessary in conducting that trade or business.

Existing state and federal laws allow deductions from income for charitable contributions. The charitable contribution deduction for a corporation is limited to the adjusted basis of the property being contributed. In addition, the amount a corporation can deduct for a charitable contribution in a given year is limited to 10 percent of the corporation's net income. A contribution made by either an individual or a business in excess of the percentage limitations may be carried over and deducted in future years.

THIS BILL

For taxable years beginning on or after January 1, 2015, and before January 1, 2020, this bill would establish, under the CTL, the Nonprofit Education Scholarship Organization credit, with a sunset date of December 1, 2020.

This bill would create a tax credit equal to 50 percent of the monetary contribution made by a taxpayer to a qualified education scholarship organization (ESO) to fund qualified college or K-12 education scholarships for a specified pupil to attend private school or to fund partial or full payments of fees associated with the general costs of transportation to attend a private, public, or charter school or to attend school-related activities and other educationally beneficial programs.

The following requirements would apply to the credit:

- The tax credit could not exceed $200,000 per taxpayer per taxable year.
- The ESO would submit, to the FTB, financial and compliance audit reports performed by a certified public accountant.
- The ESO would be required to apply for and receive certification from the State Department of Education.
- Any unused tax credit could be carried forward up to six years, until the credit is exhausted.
- The tax credit would be in lieu of any other credit or deduction claimed by a taxpayer for contributions made to a nonprofit ESO.
- The tax credit would be required to be filed on a timely filed original return.

The aggregate amount of credits allowed would be limited to a maximum of $50 million for each calendar year and the allocation of credits would be on a first-come, first-serve basis. The Legislature would be authorized to increase the aggregate amount of the credits allowed.

This bill would authorize the Franchise Tax Board (FTB) and the State Department of Education to administer this tax credit.

The FTB would be required to do the following:

- Adopt rules and regulations as necessary or appropriate in implementing the credit.
- Track credits claimed.
- Post aggregate totals of the credits claimed on the department's Internet Web site.
- Determine when the aggregate total of credits reaches $50 million for a calendar year.

The rules, guidelines, and procedures established would be exempt from the regulatory requirements of the Administrative Procedures Act.[1]

The State Department of Education would be required to do the following:

- Adopt rules and regulations necessary to determine whether education scholarship organization and contribution requirements are met.
- Submit a list of eligible ESOs annually to the FTB, by March 15.
- Establish application forms and procedures.
- Certify that the contributions meet the requirements.

The bill would define various phrases including “qualified education scholarship organization,” “qualified college or K-12 education scholarship,” “specified pupil,” and “private school.”

IMPLEMENTATION CONSIDERATIONS

Department staff has identified the following implementation considerations for purposes of a high-level discussion; additional concerns may be identified as the bill moves through the legislative process. Department staff is available to work with the author’s office to resolve these and other concerns that may be identified.

The amendments modifying the roles of the FTB and State Department of Education appear to be incomplete. For example, it is unclear why the FTB would remain as the agency receiving financial and compliance audit reports from the ESOs, and the agency responsible for administering the allocation of the annual aggregate credit amount. It is recommended that this bill be amended to clearly express the author’s intent.

Although the bill would require the State Department of Education to certify the credit, the bill fails to limit credit eligibility to taxpayers that receive certification from the State Department of Education. If this is contrary to the author’s intent, this bill should be amended.

Additionally, the bill lacks administrative details necessary to implement the bill and determine its impacts on the department's systems, forms, and processes. For example, this bill is silent on the following:

- When, how often, and what information from the certificate would the State Department of Education report to the FTB?
- Would the first-come, first-served basis of allocating the credit be based on contribution date? Date the return claiming the credit was filed?
- How and when would a taxpayer request, and receive notification of an allocation?
- Would a reallocation of any unallocated amount or unused allocated amount for a fiscal year be allowed?
- Would the department be required to provide information on the cumulative annual calendar year allocation on its Web site?

[1] Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code.

Lack of clarity on the administration of the credit could result in disputes between the State Department of Education, the FTB, and taxpayers. If it is the author's intent that the FTB's responsibility would be limited to confirming that reported tax credits "matched" to a tax credit certificate as to taxpayer, tax credit amount, and taxable year, this bill should be amended.

LEGISLATIVE HISTORY

AB 2422 (Nestande, 2013/2014), a similar bill, would create a tax credit for monetary contributions to nonprofit organizations that support innovative programs for K-12 students attending public and private schools. AB 2422 has been referred to the Assembly Revenue and Taxation Committee.

AB 943 (Nestande, 2013/2014), a similar bill, would have created credits for monetary contributions to a nonprofit organization that either provides grants to schools to support qualified K-12 innovative programs or that gives scholarships for foster youth or disabled children to attend public or private schools. AB 943 failed to pass out of the Assembly Revenue and Taxation Committee.

AB 2582 (Nestande, 2011/2012), a similar bill, would have created two credits for contributions to a public school for support of cocurricular activities or to an educational improvement organization that supports innovative programs in public schools. AB 2582 failed to pass out of the Assembly Revenue and Taxation Committee.

AB 1542 (Negrete-McLeod, 2011/2012) would have created an income tax credit for contributions made to a local educational advancement program (LEAP) organization. AB 1542 failed to pass out of the Assembly Revenue and Taxation Committee.

AB 279 (Duvall, 2009/2010) would have created an income tax credit for contributions to a scholarship granting organization. AB 279 failed to pass out of the Assembly Revenue and Taxation Committee.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota,* and *New York.* These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida has a corporate tax credit scholarship program known as the Step Up for Students. The tax credit allows corporations to receive a dollar-for-dollar tax credit of up to 75 percent of their state income tax liability for donations made to Scholarship Funding Organizations. *Florida* does not have a personal income tax.

Illinois, Massachusetts, Michigan, Minnesota, and *New York* do not provide a credit comparable to the credit allowed by this bill.

FISCAL IMPACT

The department's costs to administer this bill have yet to be determined. As the bill continues to move through the legislative process and implementation concerns are resolved, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 2421 As Amended on April 22, 2014 Assumed Enactment After June 30, 2014 ($ in Millions)		
2014-15	2015-16	2016-17
- $9	- $30	- $50

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Proponents: Some could argue that these credits would provide funding to support enhanced educational opportunities for grades kindergarten through college, as well as provide new opportunities for foster care and homeless individuals.

Opponents: Opponents may argue that these credits could constitute an indirect subsidy of public funds to religious schools.

POLICY CONCERNS

This bill would provide a tax benefit for corporations that would not be provided to other business entities. Thus, this bill would provide differing treatment based solely on business organization.

LEGISLATIVE STAFF CONTACT

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