SCS Agency
Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author: Alquist | Analyst: Jeani Brent | Bill Number: AB 1662

Related Bills: AB 1149 (1997) AB 3399 (1996) | Telephone: 845-3410 | Amended Date: 03/12/98

Attorney: Doug Bramhall | Sponsor: ______

SUBJECT: Community College Property, Facility, and Maintenance Donation Credits

_____ DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _________.

X AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

_____ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended _________.

X FURTHER AMENDMENTS NECESSARY.

X DEPARTMENT POSITION CHANGED TO Support.

_____ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED/AMENDED ____________ STILL APPLIES.

X OTHER - See comments below.

SUMMARY OF BILL

Under the Revenue and Taxation Code, this bill would allow three separate tax credits for donations to community colleges in California. The credits would be allowed for: (1) the cost of donated qualified property, (2) the cost of modifications to a qualified facility that is donated to a community college, or (3) monetary donations to maintain the qualified facility.

Under the Education Code, this bill also would provide legislative intent and rules regarding a public-private partnership between community colleges and California businesses as this partnership. This analysis does not address these provisions because they would not impact the department's programs and operations.

SUMMARY OF AMENDMENT

The March 12, 1998, amendments removed all the bill's provisions, which related to the Single Parent Protection Act of 1998, and replaced them with the provisions discussed in this analysis.

DEPARTMENTS THAT MAY BE AFFECTED:

____ STATE MANDATE ____ GOVERNOR'S APPOINTMENT

Board Position:	Agency Secretary Position:	GOVERNOR'S OFFICE USE
_X_ S ____ O	____ S ____ O	Position Approved ____
____ SA ____ OUA	____ SA ____ OUA	Position Disapproved ____
____ N ____ NP	____ N ____ NP	Position Noted ____
____ NA ____ NAR	____ NA ____ NAR	
________ PENDING	DEFER TO ____________	
Department/Legislative Director Date	Agency Secretary Date	By: Date:
G. Alan Hunter 3/30/98		

EFFECTIVE DATE

This bill would be effective January 1, 1999; however, the bill specifies that the Revenue and Taxation Code provisions would apply to taxable or income years beginning on or after January 1, 1998, and before January 1, 2002.

SPECIFIC FINDINGS

Existing federal and state laws allow a taxpayer to claim a deduction for a charitable contribution made to a qualified organization under certain circumstances. "Qualified organizations" include:

- the United States, any state, or any political subdivision;
- organizations operated for charitable, religious, educational, scientific, or literary purposes, for the prevention of cruelty to children or animals, or to foster national and international amateur sports competitions;
- war veterans' organizations;
- domestic fraternal societies; and
- certain nonprofit cemetery companies.

A charitable contribution is a gift to, or for the use of, a qualified organization. It may be in the form of money or property given to a qualified organization or specific costs or unreimbursed out-of-pocket expenses incurred by the taxpayer relating to services performed by the taxpayer for the qualified organization.

Existing federal and state laws impose general rules on determining the allowable charitable contribution deduction. Federal and state laws also impose limitations on the amount of the deduction depending on the type of property contributed, the type of organization receiving the contribution and the adjusted gross income of the individual donor or the net income of the corporate donor. **State law** also requires an alternative minimum tax adjustment for the fair market value of charitable contributions of appreciated property.

Federal law, under Section 263A of the Internal Revenue Code, provides rules on the capitalization of all direct costs and certain indirect costs of (1) real property and tangible personal property produced by the taxpayer and (2) specified real property and personal property which is acquired for resale. Direct costs are generally (1) material costs that become an integral part of the produced property or which are consumed during production, (2) labor costs that can be identified with the particular property produced, and (3) acquisition costs of property acquired for resale. Indirect costs include all costs that are not direct costs but that directly benefit or are incurred for production or resale activities, including indirect labor costs (labor that cannot be identified with the particular property), officers' compensation, pension and other employee benefit expenses, purchasing costs, handling and storage costs, rent, taxes, insurance, utilities, repairs and maintenance, quality control, bidding costs, etc.

Existing state law provides general rules that apply to the division of credits when multiple taxpayers, including partnerships, share in the costs used as the basis of the credit. These rules apply unless an individual credit specifies different rules.

Existing state law limits the low-income housing credit and the research credit to the tax attributable to the taxpayer's passive activities. (Two expired credits, the jobs credit and the orphan drug credit, also were subject to this limitation.) The purpose of the passive activity loss (PAL) limitation is to prevent taxpayers from using a credit from a passive activity to offset tax attributable to other income. Credit amounts in excess of the PAL limitation may be carried over to offset tax attributable to passive income in subsequent years.

Except as specified, **existing state law** does not allow any tax credit to reduce regular tax below the tentative minimum tax for purposes of the AMT calculation.

This bill would allow three separate tax credits for donations to community colleges in California. The credits would be allowed for: (1) the cost of donated qualified property, (2) the cost of modifications to a qualified facility that is donated to a community college, or (3) monetary donations to maintain the qualified facility. Each credit will be discussed separately, and then the general rules for all three credits will be discussed.

<u>Property Credit</u>

The property credit would be allowed for donations of tangible personal property that is "state-of-the-art" equipment (as defined). "Qualified costs" would be defined as the purchase price of property purchased for donation or an aggregate of cost of materials, direct labor, and certain indirect costs (as defined in federal law) if the taxpayer self-constructs the property. The credit amount would be 10% of qualified costs up to $100,000 and 20% of qualified costs over $100,000, not to exceed $1,000,000 of costs.

The property credit must be claimed on the tax return for the year in which the qualified property is donated to the community college. The community college would be required to provide documentation to the taxpayer that the donation has been accepted and that the property qualifies as "state-of-the-art."

<u>Facility Credit</u>

The facility credit would be allowed for a portion of the qualified costs paid or incurred for the modification of a qualified facility that the taxpayer donates to a community college. "Qualified costs" would be defined as any costs directly related to the modification of the facility that meets the "qualified purpose" of the facility. The credit amount would be 10% of qualified costs up to $500,000 and 20% of qualified costs over $500,000, not to exceed $2 million of costs per facility for each taxpayer.

The facility credit must be claimed on the tax return for the year in which the qualified facility is placed in service by the community college.

To be qualified, the facility must be used for the "qualified purpose" of furthering the students' education and preparing the students to be productive in the work environment. Also, the facility must (1) be approved by the designated representatives of the community college throughout modification; (2) be located on the grounds of the community college or on land in California owned by the community college; and (3) meet certain standards regarding its use.

Maintenance Credit

The maintenance credit would be allowed for amounts donated to pay for the maintenance and upkeep of a qualified facility. The credit amount would be 10% of amounts up to $50,000 and 20% of amounts over $50,000, not to exceed $200,000 of the amount contributed during the year. The maintenance credit must be claimed on the tax return for the year in which the contribution is made to the community college.

A "qualified facility" would be any facility for which the taxpayer has claimed the facility credit and that is used during the year by community college students for the qualified purpose expressed in the facility credit.

Maintenance and upkeep of a facility would include amounts donated so that the facility continues to satisfy its qualified purpose and any fees paid to service technicians for necessary repairs of specialized equipment in the facility.

General Rules For All Three Credits

All three credits share the following requirements:

1. Taxpayers would be required to reduce any deduction for the qualified costs by the amount of this credit.

2. The credit would be in lieu of any other credit for the qualified costs.

3. Any portion of the credit not used in the year of donation could be carried forward for up to seven years.

The general rules regarding the division of credits would apply, and these credits could not reduce regular tax below the tentative minimum tax for AMT purposes. These credits are not included in the list of passive activity credits; therefore, taxpayers who generate these credits from passive activities would be allowed to use the credits to offset tax attributable to non-passive income.

Policy Considerations

Although the property credit would require taxpayers to reduce by the amount of credit claimed any deduction otherwise allowed for the donated property, this provision would only apply to deductions allowed in the year the credit was claimed. If a taxpayer purchased property prior to the year it was donated, the taxpayer may receive a deduction under the appropriate depreciation or expensing rules in the year(s) prior to the donation.

This bill would allow a credit for modifications to a facility that began in a year prior to the bill, but completed after January 1, 1998.

Implementation Considerations

Implementing this bill would occur during the department's normal annual system update.

Technical Considerations

The bill requires the facility credit to be claimed on the tax return for the year in which the qualified facility is **placed in service** by the community college. “Placed in service” is the appropriate term for a facility built or acquired, but not for one modified. Amendments 1 and 5 would change the requirement to reference the year in which the modification of the facility is complete.

For the definition of "qualified taxpayer" and "qualified facility," the maintenance credit references the property credit. The property credit does not contain a definition for either term. Amendments 2, 3, 4, 6, 7, and 8 would change the reference to the facility credit section.

FISCAL IMPACT

Departmental Costs

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

Tax Revenue Estimate

This proposal is estimated to impact PIT and BC&T revenues as shown in the following table. It was assumed that both costs incurred for donated property and actual contributions occur in taxable/income years beginning after December 31, 1997, and before January 1, 2002.

Fiscal Year Cash Flow Taxable Years Beginning After December 31, 1997 Enactment Assumed After June 30, 1998 $ Millions		
1998-9	1999-0	2000-01
($8)	($8)	($9)

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

Revenue Discussion

The revenue impact for this bill would be determined by the amount of donations and the amount of credits applied against available tax liabilities. This analysis follows the analysis completed for AB 1149 (as amended May 5, 1997), but with a one year lag.

The cost of modifying and maintaining these buildings was estimated to be $12 million annually. The value of qualifying donations of equipment was estimated to be $160 million over four years, including $35 million in 1998.

This bill would provide credits for the modification or renovation, maintenance, and equipping of high-technology educational facilities in Community Colleges. It is assumed that no qualifying buildings would be modified and completed during 1998. This estimate assumes that $12 million a year would be donated for building modifications. The amount and average cost of equipment donations qualifying under this bill was developed through discussions with the California Postsecondary Education Commission Office, California Community College Chancellor’s Office, and the Foundation Office at American River College.

This estimate is based on a statewide total of $160 million in qualifying equipment donations over four years. Taken together, the donations for modifications, maintenance, and equipment generate approximately $35 million in credits over four years. The fiscal revenue loss pattern presented in the table above incorporates information received from the sources described above concerning the timing of donations. It was assumed that 75% of allowable credits would be applied in any given year and the remaining would be carried over and exhausted by the third year.

BOARD POSITION

At its March 26, 1998, meeting, the Franchise Tax Board voted 2-0 to support this bill, with Robin J. Dezember, on behalf of Member Craig L. Brown, abstaining.

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Attorney Doug Bramhall

FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 1662
As Amended March 12, 1998

AMENDMENT 1

On page 5, modify lines 36 through 38 as follows:

(4) The credit allowed by this section shall be claimed on the return for the taxable year in which the ~~qualified facility is placed in service by the community college~~ modification of the facility is complete.

AMENDMENT 2

On page 7, line 38, strikeout "17059.2" and insert:

17059.4

AMENDMENT 3

On page 8, line 5, strikeout "17059.2" and insert:

17059.4

AMENDMENT 4

On page 8, line 8, strikeout "17059.2" and insert:

17059.4

AMENDMENT 5

On page 11, modify lines 1 through 3 as follows:

(4) The credit allowed by this section shall be claimed on the return for the income year in which the ~~qualified facility is placed in service by the community college~~ modification of the facility is complete.

AMENDMENT 6

On page 13, line 5, strikeout "23659.2" and insert:

23659.4

AMENDMENT 7

On page 13, line 10, strikeout "23659.2" and insert:

23659.4

AMENDMENT 8

On page 13, line 13, strikeout "23659.2" and insert:

23659.4