Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author:	Bonilla, et al.	Analyst:	Jane Raboy	Bill Number:	AB 17
Related Bills:	See Prior Analysis	Telephone:	845-5718	Amended Date:	May 21, 2015
		Attorney:	Bruce Langston	Sponsor	

SUBJECT:	Contributions to Qualified Tuition Program Account Credit

SUMMARY

This bill would create a credit for contributions to a qualified tuition program under the Personal Income Tax Law.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The May 21, 2015, amendments modified the federal adjusted gross income for a qualified taxpayer and replaced the refundable credit and appropriation language with intent language. These amendments resolved one of the implementation concerns and the policy concern discussed in the department's analysis of the bill as amended April 21, 2015, and created an additional policy concern.

Except for the "This Bill," "Program Background," "Implementation Considerations," "Fiscal Impact," "Economic Impact," and "Policy Concerns" sections, the remainder of the department's analysis of the bill as amended April 21, 2015, still applies. The "Support/Opposition" section has been updated and provided below for convenience.

THIS BILL

For each taxable year beginning on or after January 1, 2016, and before January 1, 2021, this bill would allow a credit equal to the lesser of 20 percent of the monetary contributions made by a qualified taxpayer to one or more qualified tuition programs during the taxable year; or $500.

This bill would define the following phrases:

- "Qualified taxpayer" means an individual who, on behalf of a beneficiary, contributes money to a qualified tuition program for which the individual is the account owner and has one of the following annual adjusted gross incomes:
  - o In the case of a single individual or married individual filing a separate return, $75,000 or less.
  - o In the case of a head of household or surviving spouse, as defined in Section 17046, or a married couple filing a joint return, $150,000 or less.
- "Qualified tuition program" means a qualified tuition program, as defined in Internal Revenue Code (IRC) Section 529.

Board Position:						Legislative Director	Date
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An additional tax would be imposed on a qualified taxpayer who receives a nonqualified withdrawal in an amount that is the lesser of:

- 10 percent of that nonqualified withdrawal, or
- The total credit amount allowed for the current taxable year and all prior taxable years that the qualified taxpayer was allowed a credit.

"Nonqualified withdrawal" means a payment or distribution from a qualified tuition program that is subject to additional tax pursuant to IRC Section 529(c)(6), relating to additional tax.[1]

This bill would authorize the Franchise Tax Board (FTB) to prescribe rules, guidelines, or procedures necessary or appropriate to administer the credit.

Any standard, criterion, procedure, determination, rule, notice, or guidelines established or issued by the FTB would be exempt from the Administrative Procedures Act.[2]

This credit would remain in effect only until December 1, 2021, and would be repealed as of that date.

IMPLEMENTATION CONSIDERATIONS

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

With the exception of contributions to the California ScholarShare program, it is unclear how the department could verify that the contributions were made to an out-of-state qualified tuition program.

FISCAL IMPACT

Costs to implement this bill have yet to be determined. As the bill continues to move through the legislative process and the implementation concern is resolved, costs will be identified and an appropriation will be requested, if necessary.

[1] If a distribution is not used to pay qualified higher education expenses, the distribution is included in gross income. The income tax is increased by 10 percent of the amount of earnings which are so included, unless otherwise specified.
[2] Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 17 As Amended on May 21, 2015 Assumed Enactment After June 30, 2015 ($ in Millions)		
2015-16	2016-17	2017-18
- $24	- $48	- $55

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

Revenue Discussion

This bill allows a qualified taxpayer to file for a tax credit based on contributions to a Section 529 Plan. Once fully implemented, the revenue loss is estimated at $55 million per year.

The Investment Company Institute (ICI), reports there were 11.9 million open Section 529 Plan accounts nationwide as of June 2014. If the percentage of these accounts held by Californians is proportional to California's share of the population (about 12 percent), California residents have approximately 1.4 million accounts. In addition, California nonresidents have an additional 85,000 accounts, bringing the total accounts to 1.5 million. Scholarshare data reports approximately 1.65 accounts per account owner which would imply that approximately 920,000 California taxpayers have Section 529 Plan accounts.

Using 2012 Federal adjusted gross income (AGI) data, approximately 60 percent or 520,000 of the estimated California resident owners meet the income requirements specified in the bill. After applying the 4.5 percent average annual historical growth rate to the 2014 and 2015 account volumes, there would be an estimated 575,000 qualified taxpayers in 2016.

There is some survey evidence (such as by Hart Research Associates) suggesting that the proportion of Californians with Section 529 Plan accounts is below the national average. The incentives in this proposal should increase participation, bringing California's proportion closer to the national average. This estimate assumes that after implementation, participation in California would be about 10 percent below the national average. Thus, about 520,000 California taxpayers would qualify for this credit.

Based on TIAA-CREF Financial Services data, approximately 50 percent of account holders make regular annual contributions. This percentage rises to 58 percent in states with deductions or nonrefundable tax credits for contributions. This estimate assumes 60 percent in regular contributions or 310,000 account holders.

It was assumed single taxpayers with AGI less than $25,000 and married filing joint taxpayers with AGI less than $40,000 would not contribute to a Section 529 Plan. For taxpayers with AGI higher than $25,000 or $40,000, depending on the filing status, it was assumed contribution amounts would increase relative to the increase in AGI. After multiplying the assumed contribution amount by the number of taxpayers in each assumed contribution tier, it is estimated that qualified contributions for residents would be $250 million in taxable year 2016.

The total estimated contribution per taxable year, based on the lesser of 20 percent of qualified contributions or $500, was multiplied by 20 percent, arriving at a potential tax credit of $50 million in taxable year 2016.

The estimate assumes 80 percent of eligible taxpayers would take advantage of the credit in the first year and 100 percent thereafter. The taxable year estimates were reduced by one percent for taxpayers taking nonqualified withdrawals for taxable year 2016. The total credit for resident taxpayers was offset by the additional tax amount to calculate the total credit per taxable year, or $40 million for taxable year 2016.

The revenue impact for nonresident taxpayers was estimated using the same methodology as for resident taxpayers. Additionally, because Revenue and Taxation Code section 17055 requires the credit for nonresidents and part-year residents be limited to the “credit percentage” (the ratio of California taxable income to total taxable income), an 81.6 percent reduction was made (based on analysis of taxable year 2012 data), arriving at an estimated credit of $300,000 in taxable year 2016.

The combined results for the resident and nonresident taxpayers were then converted to fiscal years and rounded.

SUPPORT/OPPOSITION[3]

Support: Treasurer, State of California (Sponsor), California Association of Private School Organizations, California Catholic Charities, California Communities United Institute, Contra Costa County Office of Education, Early Edge California, Financial Services Institute, Greenlining Institute, National Association of Insurance and Financial Advisors – California, Parent Institute for Quality Education, Pleasanton Unified School District, President, John F. Kennedy University, Securities Industry and Financial Markets Association, State Farm Mutual Automobile Insurance Company's, United Way California Capital Region, and Urban League of San Diego County

Opposition: California Taxpayers Association and California Tax Reform Association.

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[3] As noted in the Assembly Committee on Revenue and Taxation bill analysis dated May 15, 2015.

POLICY CONCERNS

This bill lacks carryover language. As a result, any unused credit would be lost if the taxpayer is unable to use the entire credit amount in the year claimed. The author may wish to add language allowing a limited carryover period.

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