



Analysis of Amended Bill

Author: De Leon, et al.

Sponsor:

Bill Number: SB 227

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Amended: June 4, 2018

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Related Bills: See Legislative
History

Subject: Refundable Local Schools and Colleges Voluntary Contribution Fund Tax Credit

Summary

This bill would, under the Personal Income Tax Law (PITL), allow a refundable tax credit for amounts contributed by a taxpayer to the Local Schools and Colleges Voluntary Contribution Fund.

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

Recommendation – No position.

Summary of Amendments

The June 4, 2018, amendments removed provisions that would have created the California Excellence Fund and replaced them with the provisions discussed in this analysis.

This analysis replaces the department's analysis of the bill as amended January 25, 2018.

Reason for the Bill

The reason for the bill is to encourage taxpayers to contribute to the Local Schools and Colleges Voluntary Contribution Fund by offering a tax credit equal to 85 percent of the amount contributed.

Effective/Operative Date

This bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2018.

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.

Current state tax law allows the College Access Tax Credit, in an amount equal to 50 percent of the amount contributed by a taxpayer to the College Access Tax Credit Fund, as allocated and certified by the California Educational Facilities Authority (Authority). The maximum aggregate amount of College Access Tax Credit that may be allocated and certified by the Authority is \$500 million.

Taxpayers are precluded from taking a deduction for amounts included in the calculation of the College Access Tax Credit. Any unused College Access Tax Credits may be carried forward for up to six years.

Except as specified, existing state law does not allow any tax credit to reduce regular tax below the tentative minimum tax (TMT) computed for purposes of the alternative minimum tax calculation.

The College Access Tax Credit may reduce tax below tentative minimum tax under both the PITL and the Corporation Tax Law.

Current federal law limits state and local tax deductions to the first \$10,000 of tax paid. However, the same limitation is not provided for charitable deductions.

Program Background

The Fiscal Crisis and Management Assistance Team (FCMAT) was established pursuant to Assembly Bill 1200, and the Kern County Superintendent of Schools is the county office of education selected to administer FCMAT and its operations. FCMAT assists and provides guidance to local educational agencies in the areas of business and financial management practices. Funding is appropriated each year in the Budget Act in support of FCMAT's activities and responsibilities, and the California Department of Education is then responsible for apportioning the funding to the Kern County Superintendent of Schools. This bill would expand FCMAT's authority to include allocating the Local Schools and Colleges Voluntary Contributions Fund Tax Credit created by this bill.

This Bill

This bill would create the Local Schools and Colleges Voluntary Contributions Fund¹ in the county treasury of the county in which the FCMAT has its principal office under the administration of the FCMAT.

Under the PITL, for taxable years beginning on or after January 1, 2018, this bill would allow a tax credit in an amount equal to the amount identified in the certification issued by the FCMAT. The aggregate amount of credits that may be allocated for a fiscal year by the FCMAT is

¹ Created by Section 42127.81 of the Education Code.

\$45 billion for the 2018-2019 fiscal year and each fiscal year thereafter, plus any unallocated credit amount, if any, for the preceding fiscal year. This cap would be allocated and administered by the FCMAT.

The FCMAT would be the administering agency for the credit under the Education Code and would be required to establish a procedure for individuals who contribute to the Local Schools and Colleges Voluntary Contributions Fund created by Section 42127.81 of the Education Code to obtain from the FCMAT a certification for the credit allowed by this section. The certification shall be issued in an amount equal to 85 percent of the amount contributed by the taxpayer to the Local Schools and Colleges Voluntary Contributions Fund. The procedure shall meet the following requirements:

- Beginning with the 2018-2019 fiscal year, certifications shall be issued for contributions in the order that the monetary contributions are received. The amount identified in a certification issued for the 2018-2019 fiscal year shall be allowed as a credit for taxable years beginning on or after January 1, 2018, but before January 1, 2019. The amount identified in a certification issued for every fiscal year thereafter shall be allowed as a credit for the taxable years on or after January 1, of the previous fiscal year, and before January 1, of the fiscal year.
- The FCMAT shall cease issuance of the certifications attributable to a fiscal year once the credit threshold amount is reached for the fiscal year. If the credit threshold amount is reached for a fiscal year before the fiscal year ends, the FCMAT shall begin issuing certifications for the following fiscal year.
- The FCMAT shall certify the contribution amount eligible for credit and the fiscal year to which the certification is attributable within 45 days following receipt of the contribution.
- Provide to the Franchise Tax Board (FTB) a copy of each credit certificate issued for the calendar year by January 31 of the calendar year immediately following the calendar year in which the credit certificate is issued.

The FCMAT would be required to adopt any regulations necessary or appropriate to implement the above stated requirements, and such regulations would be exempt from the Administrative Procedures Act.

If the amount allowable as a credit under exceeds the tax liability for the taxable year, the excess would be credited against other amounts due, if any, and the balance, if any, upon appropriation by the Legislature, would be paid from an unspecified Fund and refunded to the taxpayer.

This bill would preclude a taxpayer from claiming an otherwise allowable deduction for amounts included in the calculation of the credit. The FTB would be allowed to prescribe any regulations necessary or appropriate to carry out the purposes of this section. The Administrative Procedure Act (Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code) shall not apply to any rule, guideline, or procedure prescribed by the FTB pursuant to this section.

The credit would be allowed to reduce the tax liability below the TMT for years that lack the appropriation required to trigger refunds and would be exempt from the provisions of Revenue and Taxation Code section 41.

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.

A taxpayer that makes multiple contributions during a fiscal year would receive a certificate for each contribution. For ease of administration, the author may wish to consider requiring credit certificates to be issued on an annual basis and include identifying information for the taxpayer such as a social security number.

This bill would allow a credit for contributions made to an allocated fund that is tied to a fiscal year that will bridge two taxable and calendar years. Generally, deductions and credits are allowed for the taxable year when the expense is incurred or payment is made. To avoid confusion for the department and taxpayers, it is recommended to amend the bill to specify that the credit be allowed for the calendar year when the contribution is made, regardless of what fiscal year the credit is allocated from and that the corresponding certification be issued by January 31 of the following calendar year.

The bill would require any excess credit to be refunded to the taxpayer from an unspecified fund. For the FTB to be able to administer the refunds, the appropriate fund should be included in the language.

This bill would require regular annual appropriations by the Legislature to pay for the refundable portion of this credit. Refunds in excess of the appropriation would be denied. This concern could be alleviated by providing a continuous appropriation.

Legislative History

AB 1161 (Olson, 2015/2016) would have created an income tax credit for cash contributions made to the California Preschool Investment Fund. This bill was held in the Assembly Appropriations Committee.

AB 1261 and AB 2107 (Gorell, et al., 2013/2014) would have created an income tax credit for cash contributions made to the California Preschool Investment Fund. AB 1261 was held in the Senate Governance and Finance Committee and AB 2107 was held in the Assembly Appropriations Committee.

Other States' Information

Illinois, Massachusetts, Michigan, Minnesota, and New York laws were reviewed. The laws of these states were selected due to their similarities to California's economy, business entity types, and tax laws. *Illinois, Massachusetts, Michigan, and Minnesota* laws do not provide a credit comparable to the credit allowed by this bill.

New York recently enacted legislation to allow taxpayers to contribute to a charitable fund created for purposes of improving health care and education in New York. Taxpayers who donate to this fund, would receive a state tax credit equal to 85 percent of the donated amount for the tax year after the donation is made.

Fiscal Impact

The department's costs to implement this bill have yet to be determined, but are anticipated to be significant. As the bill moves through the legislative process, costs will be identified and an appropriation will be requested, if necessary.

Economic Impact

Revenue Estimate

This bill would allow taxpayers to make a charitable contribution to the Local Schools and Colleges Voluntary Contributions Fund (the Fund). In the analysis of this proposal, the FTB noted several potential revenue impacts that would result.

First, because taxpayers only receive an 85 percent credit for their contribution to the Fund, there would be a net gain to the State of 15 cents for every dollar contributed. The FTB cannot predict the level of participation, but if all \$45 billion is certified, there would be an approximate \$7 billion net gain to the State. To the extent that taxpayers are reluctant to participate in the program prior to receiving a definitive determination that these contributions would be deductible for federal purposes, the net gain could be significantly lower.

Second, if taxpayers reduce their withholding and estimated payments in the first half of the calendar year (fiscal year 1) then subsequently taxpayers make large contributions to the Fund near the end of the calendar year (fiscal year 2), receipts would be shifted from fiscal year 1 to fiscal year 2. Note, taxpayers would not owe an estimated tax penalty as long as their withholding and estimated payments are sufficient to cover their after credit liability.

Unfortunately, the FTB cannot predict the magnitude of any behavioral responses. If the majority of itemizing taxpayers choose to make contributions to the new Fund and shift the majority of their payments from the first half of the year to the end of the year the revenue transfer across fiscal years could be in the low tens of billions of dollars. The FTB expects the actual revenue transfer to be significantly less than that by an unknown amount.

Support/Opposition

Support: None provided.

Opposition: None provided.

Arguments

Proponents: Some may argue that this bill would encourage taxpayers to contribute to local schools and colleges thereby increasing the quality of education for Californians.

Opponents: Some may argue that a monetary contribution is too restrictive and contributions of appreciated capital gain property should be allowed.

Policy Concerns

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review of the effectiveness of the credit by the Legislature.

This bill assumes that contributions deposited by the FCMAT to the Local Schools and Colleges Voluntary Fund would be allowed as a charitable contribution deduction on the federal income tax return. If the Internal Revenue Service (IRS) or Department of the Treasury disagrees that the contributions qualify as charitable contributions, the author's intent may not be realized.

The department is concerned that another refundable credit could increase the trend in refund fraud and identity theft. Historically, both the IRS and the FTB have experienced fraud and improper claims with refundable credits. These concerns are heightened because if a refund is determined to be fraudulent; the refund commonly cannot be recovered.

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