STATE OF CALIFORNIA
Franchise Tax Board

Summary Analysis of Amended Bill

Author: De Leon, et al.	Sponsor:	Bill Number: SB 227
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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 (LSCVCF).

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

Recommendation – No position.

Summary of Amendments

The July 5, 2018, amendments added sunset and contingent operative dates. These amendments resolved one of the policy concerns discussed in the department's analysis of the bill as amended June 4, 2018, and an additional implementation consideration was identified.

Except for the "Effective/Operative Date," "This Bill," "Implementation Considerations," "Fiscal Impact," and "Policy Concerns" sections, the remainder of the department's analysis of the bill as amended on June 4, 2018, still applies. In addition, the "Economic Impact" section has been restated for convenience.

Effective/Operative Date

This bill would be effective January 1, 2019, if Senate Constitutional Amendment (SCA) 23 of the 2017–2018 Regular Session is submitted to, and approved by, the voters at the November 6, 2018, statewide general election. If so approved by the voters, this bill would be specifically operative for taxable years beginning on or after January 1, 2018, and before January 1, 2023.

This Bill

This bill would create the LSCVCF[1] in the county treasury of the county in which the Fiscal Crisis and Management Assistance Team (FCMAT) has its principal office under the administration of the FCMAT.

Under the PITL, for taxable years beginning on or after January 1, 2018, and before January 1, 2023, this bill would establish a tax credit, only if SCA 23 is approved by voters as specified, 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 $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 LSCVCF 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 would be issued in an amount equal to 85 percent of the amount contributed by the taxpayer to the LSCVCF. The procedure would be required to meet the following requirements:

- Beginning with the 2018-2019 fiscal year, and through the 2022-2023 fiscal year, certifications would 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 would 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 would 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 would 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 would begin issuing certifications for the following fiscal year.
- The FCMAT would 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.
- The FCMAT would 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.

[1] Created by Section 42127.81 of the Education Code.

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) would 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 tentative minimum tax for years that lack the appropriation required to trigger refunds and would be exempt from the provisions of Revenue and Taxation Code section 41.

This bill would be repealed by its own terms for taxable years beginning after January 1, 2023.

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.

This bill is contingent on voters at the November 6, 2018, statewide general election approving SCA 23 of the 2017–2018 Regular Session. If so approved by the voters, this bill would be operative for taxable years beginning on or after January 1, 2018, and before January 1, 2023. As such, taxpayers could make contributions through June 30, 2019, and claim the credit on the 2018 tax return. As such, there lacks sufficient time for the FTB to properly administer this bill as related to the 2018 tax returns.

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 may 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.

Fiscal Impact

Staff estimates a cost of approximately $2.3 million in fiscal year 2018-2019 and ongoing costs of $1.3 million annually to develop, program, and test revisions to existing systems for this bill.

Economic Impact

Revenue Estimate

This bill would allow taxpayers a refundable tax credit for contributions made to the LSCVCF. In the analysis of this proposal, the FTB noted several potential revenue impacts that could result.

First, because taxpayers would receive an 85 percent credit for their contribution to the LSCVCF, 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 LSCVCF near the end of the calendar year (fiscal year 2), receipts would be shifted from fiscal year 1 to fiscal year 2.

Unfortunately, the FTB is unable to predict the magnitude of any behavioral responses. If the majority of taxpayers that itemize choose to make contributions to the new LSCVCF 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.

Policy Concerns

This bill assumes that contributions deposited by the FCMAT to the LSCVCF 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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