Bill Analysis

SUBJECT
Conformity to Gross Income Exclusion for Student Loan Forgiveness

SUMMARY
This bill would, under the Personal Income Tax Law, conform to the student loan forgiveness provisions under the federal American Rescue Plan Act of 2021 (ARPA).

RECOMMENDATION
No position.

SUMMARY OF AMENDMENTS
The March 25, 2021, amendments removed the property tax provisions and added conforming provisions to the ARPA change for student loan forgiveness.

REASON FOR THE BILL
The reason for the bill is to alleviate the burden that student loan debt forgiveness places on Californians, by excluding certain student loan discharge of indebtedness from gross income.

ANALYSIS
This bill would conform to the ARPA student loan provision that excludes from gross income certain student loan debt that is fully or partially discharged on or after January 1, 2021, and before January 1, 2026. The exclusion is available for the following student loans:

- Any loan provided expressly for post-secondary educational expenses if the loan was made, insured, or guaranteed by a federal, state, or local governmental entity, or an eligible educational institution (under the Higher Education Act of 1965),
- Any private education loan,
• Any loan made by an educational organization which qualifies as a charitable organization under Internal Revenue Code (IRC) section 170(b)(1)(A)(ii), if the loan is made under an agreement with any governmental entity or any private education lender that provided the loan to the educational organization, or under a program of the educational institution that is designed to encourage its students to serve in occupations with unmet needs or in areas with unmet needs and under which the services provided by the students (or former students) are for or under the direction of a governmental unit or a tax-exempt charitable organization.

• Any loan made by an educational organization which qualifies as a charitable organization under IRC section 170(b)(1)(A)(ii), or by a tax-exempt organization to refinance a loan to an individual to assist the individual in attending an educational organization but only if the refinancing loan is under certain programs of the refinancing organization.

However, the exclusion would not apply to educational organizations described above or made by private education lenders if the discharge is for services performed for such educational organizations or private education lenders.

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, 2021, and before January 1, 2026.

Federal/State Law

Federal Law

Student Loan Forgiveness in General

Under federal and state law, gross income generally includes the amount of any discharge of indebtedness of the taxpayer. Under an exception to this general rule, gross income does not include any amount from the forgiveness (in whole or in part) of certain student loans, provided that the forgiveness is contingent on the student’s working for a certain period of time in certain professions for any of a broad class of employers (IRC section 108(f)).

Student loans eligible for this exception to the general rule must be made to an individual to assist the individual in attending an educational organization that normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of students in attendance at the place where its education activities are regularly carried on. Loan proceeds may be used not only for tuition and required fees, but also to cover room and board expenses. The loan must be made by: (1) the United States (or an instrumentality or agency thereof), (2) a state (or any political
subdivision thereof), (3) certain tax-exempt public benefit corporations that control a state, county, or municipal hospital and whose employees have been deemed to be public employees under state law, or (4) an educational organization that originally received the funds from which the loan was made from the United States, a state, or a tax-exempt public benefit corporation (IRC section 108(f)(2)).

In addition, an individual’s gross income does not include amounts from the cancellation of loans made by educational organizations (and certain tax-exempt organizations in the case of refinancing loans) out of private, nongovernmental funds if the proceeds of such loans are used to pay costs of attendance at an educational institution or to refinance any outstanding student loans (not just loans made by educational organizations) and the student is not employed by the lender organization (IRC section 108(f)(3)). In the case of such loans made or refinanced by educational organizations (or refinancing loans made by certain tax-exempt organizations), cancellation of the student loan must be contingent upon the student working in an occupation or area with unmet needs and such work must be performed for, or under the direction of, a tax-exempt charitable organization or a governmental entity.

Finally, an individual’s gross income does not include any loan repayment amount received under the National Health Service Corps loan repayment program or certain state loan repayment programs (IRC section 108(f)(4)).

The ARPA expanded the types of student loan discharges that are excluded from gross income for tax years beginning after December 31, 2020, and before January 1, 2026, as described above (IRC Section 108(f)(5)).

State Law

California allows an exclusion from gross income for student loan debt that is cancelled or repaid under the income-based repayment programs administered by the U.S. Department of Education. This exclusion applies to discharges of indebtedness occurring on or after January 1, 2014 (Revenue and Taxation Code (RTC) section 17132.11(a)).

Existing state law also excludes from gross income student loan debt that is cancelled or repaid under the Income Contingent Repayment plan, the Pay As You Earn Repayment plan, and the Revised Pay As You Earn Repayment plan as administered by the U.S. Department of Education (Title 20, U.S.C. section 1087e(e)). This exclusion applies to cancellation or repayments, beginning on or after January 1, 2017, and before January 1, 2022 (RTC 17132.11(b)).
For discharges of indebtedness occurring on or after January 1, 2015, and before January 1, 2020, existing state law excluded from an eligible individual's gross income amounts that would otherwise result from a student loan forgiven as a result of the closure of Corinthian Colleges and similar closures (RTC section 17144.7). This provision was repealed on December 1, 2020.

For taxable years beginning on and after January 1, 2019, and before January 1, 2024, California provides an exclusion from gross income for the discharge of a student loan of an eligible individual (RTC section 17144.6). An individual would be eligible for the exclusion if any of the following apply:

- Is granted a discharge of any student loan because the individual successfully asserts that the school did something wrong or failed to do something that it should have done or because the individual could not complete a program of study due to the school closing.
- Attended a Brightwood College school on or before December 5, 2018, and is granted a discharge of any student loan made in connection with attending that school.
- Attended a location of The Art Institute of California and is granted a discharge of any student loan made in connection with attending that school.

Implementation Considerations

None noted.

Technical Considerations

For consistency of conformity terminology and clarity, the following changes are recommended:

- Strike subdivision (c) from RTC section 17132.11,
- Modify RTC section 17144.8(b) by striking “January 1, 2026” and inserting in its place “January 1, 2021.”

Add the following text after subdivision (b) of RTC section 17144.8: “(c) Notwithstanding subdivisions (a) and (b), Section 108(f)(5) of the IRC, relating to special rule for discharges in 2021 through 2025, as stricken and inserted by Section 9675(a) of the federal American Rescue Plan Act of 2021 (Public Law 117-2), shall apply for taxable years beginning on or after January 1, 2021, and before January 1, 2026.”
Policy Considerations

Under RTC section 41, legislation that would create a new tax expenditure, which includes a credit, deduction, exclusion, exemption, or any other tax benefit as provided for by the state, is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the tax benefit. The author may want to amend this bill to satisfy the RTC section 41 requirements.

LEGISLATIVE HISTORY

AB 91, (Burke, Chapter 39, Statutes of 2019) for taxable years beginning after December 31, 2018, provides that for discharges of indebtedness, certain student loans that are discharged on account of death or total and permanent disability of the student are also excluded from gross income.

SB 63 (Hertzberg, Chapter 468, Statutes of 2019) for taxable years beginning on and after January 1, 2019, and before January 1, 2024, provides an exclusion from gross income for income that would otherwise result from the discharge of a student loan of an eligible individual.

AB 461(Muratsuchi, Chapter 525, Statutes of 2017) for taxable years beginning on or after January 1, 2017, and before January 1, 2022, excludes from gross income student loan debt that is cancelled or repaid under the Income Contingent Repayment plan, the Pay As You Earn Repayment plan, and the Revised Pay As You Earn Repayment plan as administered by the U.S. Department of Education.

SB 150 (Nguyen, et al., Chapter 650, Statutes of 2015) excluded from gross income several types of student loan debt discharged on or after January 1, 2015, and before January 1, 2020, including debt that is discharged, pursuant to discharge agreements between certain schools that closed, or other situations in which a student was unable to complete a program of study due to a school closing or doing something wrong.

SB 1271 (Evans & Leno, Chapter 841, Statutes of 2014) excludes from gross income student loan debt that is forgiven or repaid under the income-based repayment programs administered by the U.S. Department of Education.

SB 1003 (Evans, 2013/2014), was identical to SB 1271. SB 1003 was held in the Assembly Rules Committee.

PROGRAM BACKGROUND

None noted.
FISCAL IMPACT

This bill would not impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 668 as Amended March 25, 2021
Assumed Enactment after June 30, 2021

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Revenue</th>
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<tr>
<td>2021-2022</td>
<td>-$400,000</td>
</tr>
<tr>
<td>2022-2023</td>
<td>-$400,000</td>
</tr>
<tr>
<td>2023-2024</td>
<td>-$400,000</td>
</tr>
</tbody>
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This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

Revenue Discussion

This estimate is based upon the proration of the Joint Committee on Taxation (JCT) federal tax estimate on the ARPA for Modification of Treatment of Student Loan Forgiveness. The JCT estimated the federal revenue loss from the exclusion would be $3.6 million in the 2021 taxable year and $8 million in the 2022 taxable year. It is estimated the corresponding revenue loss to California would be $170,000 in the 2021 taxable year and $400,000 in the 2022 taxable year and each year thereafter.

The tax year estimates are converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table.

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.
SUPPORT/OPPOSITION
To be determined.

ARGUMENTS
None noted.

LEGISLATIVE CONTACT
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