



Bill Analysis

Author: Committee on
Budget

Sponsor:

Bill Number: AB111

Related Bills: See Legislative
History

Introduced: January 9, 2023
Amended: February 1, 2023,
and April 28, 2023,

SUBJECT

Gross Income Exclusion – Student Loan Forgiveness, Discharged Fees, and Emergency Financial Aid Grants

SUMMARY

This bill would, under the Personal Income Tax Law (PITL), provide an exclusion from gross income for the following: amounts discharged for certain unpaid fees due or owed by a student attending a California community college and certain emergency financial aid grants received by a student in postsecondary education. Additionally, this bill would, under the PITL, conform to the provision under the federal American Rescue Plan Act of 2021 (ARPA) that provides a gross income exclusion for student loan forgiveness.

This analysis only addresses the provisions of the bill that would impact the Franchise Tax Board (FTB).

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The February 1, 2023, amendments added the Assembly Budget Committee as the author of the bill and made a technical change to the intent language relating to the Budget Act of 2023.

The April 28, 2023, amendments removed the intent language relating to the Budget Act of 2023 and replaced them with the provisions discussed in this analysis.

REASON FOR THE BILL

The reason for the bill is to provide financial relief to higher education students impacted by COVID-19 pandemic.

ANALYSIS

Community College Fees

This provision would, for taxable years beginning on or after January 1, 2022, and before January 1, 2027, exclude from gross income any amount of unpaid fees due or owed by a student to a community college that was discharged and expended as an allocation under the California Community College COVID-19 Recovery Block Grant. (Education Code section 32527 (a)(3)(G)).

This provision would be repealed on December 1, 2027.

Emergency Financial Aid Grants

This provision would, for taxable years beginning on or after January 1, 2020, and before January 1, 2028, exclude from gross income emergency financial aid grants received by a student in postsecondary education under the Coronavirus Aid, Relief, and Economic Security Act (CARES Act, Public Law 116-136), Consolidated Appropriations Act, 2021 (CAA, 2021, Public Law 116-260), and ARPA (Public Law 117-2).

This bill would be repealed on December 1, 2028.

ARPA student loan conformity

This provision would conform to the ARPA (Public Law 117-2) 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 any 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.

However, the exclusion would not apply to forgiveness of loans made by educational organizations which qualify as a charitable organization or made by private education lenders if the discharge is for services performed for such educational organizations or private education lenders.

This bill would appropriate \$20,000 to FTB to administer these provisions.

This bill contains a provision that the benefits authorized by this bill would not constitute a gift of public funds.

Effective/Operative Date

This bill, providing for appropriations relating to the Budget Bill, would be effective immediately upon enactment. The operative date for each provision varies as follows:

- The gross income exclusion for discharged community college fees would be retroactively operative for taxable years beginning on or after January 1, 2022, and before January 1, 2027.
- The gross income exclusion for emergency financial aid grants would be retroactively operative for taxable years beginning on or after January 1, 2020, and before January 1, 2028.
- The conformity to the gross income exclusion for discharges under ARPA would be retroactively operative for taxable years beginning on or after January 1, 2021, and before January 1, 2026.

Federal/State Law

Federal Law

Gross Income from the Discharge of Indebtedness

Existing federal and state laws provide that gross income generally includes the amount of any discharge of indebtedness of the taxpayer, subject to certain exceptions for debtors in Title 11 bankruptcy cases, insolvent debtors, certain student loans, certain farm indebtedness, certain real property business indebtedness, and qualified principal residence indebtedness (Internal Revenue Code (IRC) sections 61(a)(11) and 108).

Student Loan Forgiveness in General

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 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 (U.S.) (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 U.S., 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).)

For discharges of indebtedness after December 31, 2017, and before January 1, 2026, certain student loans that are discharged on account of death or total and permanent disability of the student are also excluded from gross income. 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).

Additionally, certain emergency financial aid grants provided under the CARES Act, CAA, 2021, and ARPA that provide relief during the coronavirus emergency are also excluded from the gross income of college and university students.

State Law

California generally conforms to the federal definition of gross income, including income from the discharge of indebtedness as of January 1, 2015, except as otherwise provided.

Community College fees

California does not allow an exclusion from gross income for unpaid fees, relating to the COVID-19 pandemic, owed by students to a California Community College that were discharged by the Chancellor's Office of California Community Colleges.

Emergency Financial Aid Grants

California does not conform to the federal exclusion from gross income of emergency financial aid grants under the CARES Act, CAA, 2021, or ARPA.

ARPA student loan conformity

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).)

State law also excluded 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 applied 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 because of the closure of Corinthian Colleges and similar closures. (RTC section 17144.7.) This provision was repealed on December 1, 2020.

Existing state law excludes from gross income a student loan that is discharged due to the death or total and permanent disability of the student. This exclusion applies to loan discharges after December 31, 2018. (RTC section 17144.8.)

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

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 26 (Fong, 2023-2024) would have provided a gross income exclusion for student loan debt forgiven under the U.S. Department of Education and Biden-Harris Administration's student loan debt relief plan. AB 26 did not pass out of the Assembly by the constitutional deadline.

AB 35 (Ting, 2023-2024) would have, under the PITL, conformed to the student loan forgiveness provisions under the federal ARPA. AB 35 did not pass out of the Assembly by the constitutional deadline.

SB 1 (Glazer, 2023-2024) and SB 220 (Committee on Budget and Fiscal Review, 2023-2024) are identical to AB 35. SB 1 is in the Senate Appropriations Committee and SB 220 is in the Senate Committee on Budget and Fiscal Review.

SB 111 (Committee on Budget and Fiscal Review, 2023-2024) is identical to this bill. SB 111 did not pass out of the Assembly by the constitutional deadline.

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.

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 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 668 (Petrie-Norris, 2021-2022), would have conformed to the student loan forgiveness provisions under the ARPA for taxable years beginning on or after January 1, 2021, and before January 1, 2026. AB 668 was held in Assembly Revenue and Taxation Committee.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

The changes proposed in this bill could result in amended returns being filed by impacted taxpayers that have already filed a tax return prior to bill enactment. The sum of \$20,000 has been appropriated from the General Fund to the FTB for administration of these provisions.

ECONOMIC IMPACT

Community College fees

Using data from the California Community College Chancellor's Office, as well as fee data from various California Community College Districts, approximately 1 million community college students will have been charged roughly \$175 million dollars in fees during the 2022 taxable year. Should all the fees for every student be waived and excluded from income, and applying an average tax rate of 1.5 percent, the revenue loss will be approximately \$2.5 million dollars.

However, it is unlikely that every student will have every fee waived as a result of this program. Assuming that approximately 35% of the students have their fees completely waived, roughly \$30 million in fees will be excluded. Applying an average tax rate of 1.5% will result in an estimated revenue loss of \$450,000.

Additionally, according to fee data, the amount of fees that would be waived for each taxpayer will not reach the threshold for a taxpayer to receive a 1099-C. As a result, most taxpayers will be unaware of the requirement to include the waived fees in income. Also, it is anticipated that many of these students will have very little income and thus have no filing requirement. Therefore, the actual revenue loss could be much lower than estimated.

Emergency Financial Aid Grants

This provision does not change the way income or franchise tax is calculated under the RTC.

ARPA student loan conformity

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 111 as amended on April 28, 2023
Assumed Enactment before June 30, 2023

(\$ in Millions)

Fiscal Year	Revenue
2022-2023	-\$0.30
2023-2024	-\$0.50
2024-2025	-\$0.60
2025-2026	-\$0.40

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 of 2021 for Modification of Treatment of Student Loan Forgiveness. The JCT estimated the federal revenue loss from the exclusion would be \$1 million for the 2021 taxable year. It is estimated the corresponding revenue loss to California would be to be \$170,000 for the 2021 taxable year.

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

None on file.

ARGUMENTS

None noted.

LEGISLATIVE CONTACT

FTBLegislativeServices@ftb.ca.gov