STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Ward	Sponsor:	Bill Number: AB 2524
	Related Bills: See Legislative History	Introduced: February 13, 2024 Amended: April 1, 2024

SUBJECT

Long-Term Qualified Tuition Plan Gross Income Exclusion

SUMMARY

This bill would exclude from gross income a distribution from a qualified tuition program (QTP) to a Roth Individual Retirement Account (IRA).

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The April 1, 2024, amendments added a sunset date and made nonsubstantive changes to Section 41 reporting requirements.

This is Franchise Tax Board's (FTB) first analysis of the bill.

REASON FOR THE BILL

The reason for the bill is to provide conformity to the federal law which brings tax relief and ease of return preparation for taxpayers who transfer funds from a QTP to a Roth IRA.

ANALYSIS

For distributions made during taxable years beginning on or after January 1, 2024, and before January 1, 2029, this bill, under the Personal Income Tax Law (PITL), would conform to provisions of the Consolidated Appropriations Act (CAA), 2023 (P.L. 117-328) related to rollover distributions from certain QTP accounts to Roth IRAs. Specifically, this bill would allow a taxpayer to exclude from gross income a rollover distribution, up to $35,000 in the aggregate for all taxable years, from a QTP that was maintained for 15 years to a Roth IRA.

This bill would require the officer or employee of the QTP to provide to the trustee of the Roth IRA that the distribution was made with a copy of the report that includes information about the contributions, distributions, and earnings of the QTP. The report would be required to be filed at the time and manner prescribed by the Franchise Tax Board (FTB).

These rules would apply under both the Golden State Scholarshare Trust provision and the general QTP provision.

Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment and specifically operative with respect to distributions made during taxable years beginning on or after January 1, 2024, and before January 1, 2029.

Federal/State Law

Federal Law

Internal Revenue Code (IRC) section 529 (Section 529 Plan) provides tax-exempt status to qualified tuition programs.

Contributions to a qualified tuition program must be made in cash. The Section 529 Plan does not impose a specific dollar limit on the amount of contributions, account balances, or prepaid tuition benefits relating to a qualified tuition account; however, the program is required to have adequate safeguards to prevent contributions in excess of amounts necessary to provide for the beneficiary’s qualified higher education expenses. Contributions are not tax deductible for federal income tax purposes, but amounts earned in the account (i.e. interest) accumulate on a tax-free basis.

Distributions from a qualified tuition program are excludable from federal tax if used for the beneficiary's qualified higher education expenses. If a distribution from a qualified tuition program exceeds the qualified higher education expenses incurred for the beneficiary, the portion of the excess that is treated as earnings generally is subject to income tax and an additional 10-percent tax. Amounts in a qualified tuition program may be rolled over to another qualified tuition program.

For purposes of receiving a distribution from a QTP that qualifies for favorable tax treatment under the IRC, expenses mean qualified higher education expenses, qualified elementary and secondary education expenses, and expenses for special needs services in the case of a special needs beneficiary that are incurred in connection with such enrollment or attendance.

Pursuant to CAA, 2023, beginning in 2024, a rollover from QTPs that have been maintained for 15 years can be distributed to a Roth IRA without a tax or penalty. The transfer must be trustee to trustee, cannot exceed the aggregate amount contributed and earnings to the QTP more than five years before the distribution, and is limited to an aggregate of $35,000 in the current and prior taxable years. An amount distributed from a QTP to a Roth IRA would be treated in the same manner as the earnings and contributions of a Roth IRA.

State Law

California's QTP is the Golden State ScholarShare College Savings Trust. The trust was created in 1997 and is administered by the ScholarShare Investment Board.

Under the PITL, California automatically conforms to IRC 408A, relating to Roth IRAs. California generally conforms by reference to the federal rules related to QTPs under IRC section 529 as of the specified date of January 1, 2015. As a result, the IRC Section 529 amendments made by CAA 2023, do not automatically apply under California law. The distribution from the Golden State Scholarshare Trust 529 plan or QTPs to a Roth IRA would be includable in California taxable income and subject to 2.5 percent premature distribution penalty.

Implementation Considerations

None noted.

Technical Considerations

For clarity, in Sections 17140(g)(2) and 17140.3(e)(2), it is recommended that "except that "Franchise Tax Board" shall be substituted for "Secretary"" be removed. Revenue and Taxation Code sections 17024.5(h)(7) and 23051.5(h)(7) provide for the substitution when applying any section of the Internal Revenue Code.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 629 (Wallis, 2023/2024) was identical to AB 2524. AB 629 did not pass out of the Assembly by the constitutional deadline.

AB 1026 (Ta, 2023/2024) would have allowed a qualified taxpayer a deduction from gross income for contributions made to a California qualified tuition program. AB 1026 did not pass out of the Assembly by the constitutional deadline.

AB 340 (Ward, Chapter 557, Statutes of 2021) conforms the existing Golden State Scholarshare Trust for college savings to the federal QTP definition of qualified higher education expenses by adding apprenticeship program expenses, and principal and interest of qualified education loan expenses.

SB 1374 (Borgeas, 2021/2022), substantially similar to AB 211, would have allowed a qualified taxpayer a deduction from gross income for contributions made to a California qualified tuition program. SB 1374 was vetoed by the governor whose veto message stated in part: "While I appreciate the intent to incentivize Californians to save for higher education expenses, ScholarShare already has significant tax advantages. An additional tax deduction would largely benefit higher-income families that have tax liability and enough disposable income to contribute."

AB 211 (Calderon, et al., 2019/2020) would have allowed an above-the-line deduction for monetary contributions made by a qualified taxpayer during the taxable year to one or more accounts established pursuant to the California qualified tuition program on behalf of a beneficiary. AB 211 was vetoed by the governor whose veto message stated in part:" While I appreciate the Legislature's intent, a careful balancing of the benefits of the proposed tax deduction in relation to the revenue losses, approximately $13 million, would be better addressed through the annual budget process."

AB 350 (Choi, 2019/2020) would have allowed a deduction, under the PITL, for amounts contributed by a qualified taxpayer to a qualified tuition program. AB 350 did not pass out of the Assembly Revenue & Taxation Committee by the constitutional deadline.

SB 1218 (Gaines, 2017/2018), substantially similar to AB 350, would have allowed a deduction for contributions made to a qualified tuition program. SB 1218 did not pass out of the Senate by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be identified.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 2524 as Amended April 1, 2024
For Distributions Made Beginning on or after January 1, 2024
Assumed Enactment after June 30, 2024

($ in Millions)

Fiscal Year	**Revenue**
2024-2025	-$9.5
2025-2026	-$7.8
2026-2027	-$8.7

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 on a proration of the Joint Committee on Taxation (JCT) federal estimate for the inclusion of special distribution rules from long-term qualified tuition programs to Roth IRAs. In December 2022, the JCT estimated the federal revenue impact of the exclusion to be a loss of $85 million in federal fiscal year 2023-2024. The corresponding loss to California is estimated to be $5 million in calendar year 2024.

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

Per the Assembly Revenue & Taxation Committee analysis of AB 2524, dated April 8, 2024, the following individual and organization are in support on of this bill.

Support

Fiona Ma, California State Treasurer (Sponsor)
Securities Industry and Financial Markets Association

Opposition

None on file.

ARGUMENTS

To be determined.

LEGISLATIVE CONTACT

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