STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Glazer, et al.	Sponsor:	Bill Number: SB 1
	Related Bills: See Legislative History	Introduced: December 5, 2022

SUBJECT

Gross Income Exclusion for Federal Student Loan Debt Relief Plan

SUMMARY

This bill would, under the Personal Income Tax Law (PITL), exclude from gross income amounts discharged under the federal student loan debt relief plan.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

Not applicable.

REASON FOR THE BILL

The reason for the bill is to exclude certain student loan discharge of indebtedness from gross income.

ANALYSIS

This bill would, for taxable years beginning on or after January 1, 2022, and before January 1, 2026, exclude from gross income any student loan amount that is waived, canceled, or otherwise forgiven by the United States (U.S.) Department of Education pursuant to the student debt relief plan announced by the President of the United States on August 24, 2022.

This bill would require the Franchise Tax Board (FTB) to collect and report to the Legislature by July 1, 2027, the following:

- The number of taxpayers that received student loan debt forgiveness.
- The total dollar amount total dollar amount of debt forgiveness excluded.

This reporting would be treated as an exception to the general prohibition against disclosure of confidential taxpayer information.

This exclusion would be repealed on December 1, 2027.

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, 2022, and before January 1, 2026.

Federal/State Law

Federal Law

Biden-Harris Administration's Plan for Student Debt Relief

President Biden and Vice-President Harris created a student loan debt relief plan, also known as the Biden-Harris Administration's Plan for Student Debt Relief, that would provide loan forgiveness up to $20,000 to Pell Grant recipients and up to $10,000 to non-Pell Grant recipients whose adjusted gross income is less than $125,000 ($250,000 for individuals filing jointly or as a Head of Household, or as a qualifying widow(er)). On October 12, 2022, the federal Office of Postsecondary Education within the Department of Education "updated waivers and modifications of statutory and regulatory provisions governing the federal student financial aid programs under the authority of the Higher Education Relief Opportunities for Students Act of 2003," (Summary of Federal Register 87FR 61512) to include the debt discharges under this student loan debt relief plan.

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 in certain professions for any of a broad class of employers. (Internal Revenue Code (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 American Rescue Plan Act of 2021 (ARPA) (Public Law 117-2) 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. (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 section 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

The department has identified the following implementation considerations and is available to work with the author's office to resolve these and other considerations that may be identified.

This bill requires the FTB to collect data and report to the Legislature on the number of taxpayers who excluded the discharged debt from gross income, the total dollar amount excluded, and total number of taxpayers in each tax bracket who excluded the discharge debt from gross income. FTB does not collect information for items that are excluded from income.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 26 (Mike Fong, 2023-2024) is related to this bill and is held in the Assembly pending referral.

AB 35 (Ting, 2023-2024) and SB 25 (Skinner, 2023-2024) are companion bills that would, under the PITL, 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. AB 35 is in the Assembly Revenue and Taxation Committee and SB 25 is in the Senate Governance and Finance Committee.

AB 91, (Burke, Chapter 39, Statutes of 2019) for taxable years beginning after December 31, 2018, under the PITL, 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, under the PITL, 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, under the PITL, 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.

AB 668 (Petrie-Norris, 2021-2022), under the PITL, 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

This bill would not significantly impact the department’s costs.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 1 as Introduced on December 5, 2022
Assumed Enactment before June 30, 2023

($ in Millions)

Fiscal Year	Revenue
2022-2023	$0
2023-2024	-$850
2024-2025	-$450

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

Based on data from the U.S. Department of Education's Federal Student Aid program, approximately 4 million Californians had $150 billion dollars in federal student loans as of September 30, 2022. It is assumed that approximately 85 percent or 3.5 million taxpayers would earn income below the maximum allowed ($125,000 for single or $250,000 for married filing joint and head of household). Of these individuals, it is estimated that 65 percent would be Pell Grant recipients and qualify for up to $20,000 in debt relief. Furthermore, it is assumed that if the remaining loan amounts were less than the maximum amounts allowed ($20,000 or $10,000), the taxpayer would only exclude the remaining loan balance from income. Based on Department of Education's loan data, approximately 55 percent of Pell Grant recipients owe less than $20,000 and approximately 30 percent of all others owe less than $10,000. It is estimated that these individuals would qualify for approximately $40 billion in student debt forgiveness. Applying an estimated average tax rate of 3.3 percent results in an estimated revenue loss of $1.3 billion.

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

To be determined.

LEGISLATIVE CONTACT

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