STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Tangipa

Sponsor:

Related Bills: See Legislative History

Bill Number: AB 386

Amended: April 28, 2025

SUBJECT

Student Loan Payments Tax Credit

SUMMARY

This bill, under the Personal Income Tax Law (PITL) and Corporate Tax Law (CTL), would for taxable years beginning on or after January 1, 2027, and before January 1, 2032, allow a tax credit for qualified taxpayers that make payments towards the repayment of a student loan on behalf of their full-time employees if they apply for and receive a credit reservation from the Franchise Tax Board (FTB).

This bill would also provide, under the PITL, a gross income exclusion to a full-time employee receiving a student loan payment made by a qualifying employer.

RECOMMENDATION

No position—The three-member Franchise Tax Board has not formally voted or taken a position on this bill.

SUMMARY OF AMENDMENTS

The April 28, 2025, amendments changed the operative date, modified the definitions of “qualified taxpayer,” “qualified expenditure,” and “qualified full-time employee,” added the definition for “student loan,” and made other technical changes.

The amendments resolved one of the three implementation considerations, several of the technical considerations, and the two policy considerations discussed in the FTB’s bill analysis as introduced on February 3, 2025, and created two new technical considerations and two new policy considerations.

REASON FOR THE BILL

The reason for this bill is to encourage employers to assist in reducing the burden of student loan payments on their employees.

ANALYSIS

Tax Credit

This bill would, under the PITL and CTL, for taxable years beginning on or after January 1, 2027, and before January 1, 2032, allow a tax credit for qualified taxpayers for an amount equal to the taxpayer's qualified expenditures during the taxable year.

This bill would define the following terms:

- A "qualified taxpayer" means a taxpayer whose employees do not perform public services jobs as described in Section 1087e(m)(3)(B) of Title 20 of the United States (U.S.) Code.
- A "qualified expenditure" means all payments made by a qualified taxpayer on behalf of a qualified full-time employee, not to exceed $3,000 per qualified full-time employee, towards repayment of a student loan.
- A "qualified full-time employee" means an individual employed by a qualified taxpayer for at least six months during the taxable year who is either:
  - o An employee of the qualified taxpayer who is paid wages for services not fewer than an average of 35 hours per week, or
  - o A salaried employee who was paid compensation during the taxable year for full-time employment, within the meaning of Section 515 of the Labor Code (LAB).
- A qualified full-time employee does not include those employees who receive more than $125,000 in wages or salary from the qualified taxpayer during the taxable year.
- "Student Loan" has the same meaning as the term defined under the Internal Revenue Code (IRC) section 108.

The total aggregate amount that would be allocated by credit reservation to all qualified taxpayers would not exceed $25,000,000 per calendar year.

A qualified taxpayer would be required to request a tentative credit reservation from the FTB during the month of July for each taxable year, or within 30 days of the start of their taxable year, if the taxpayer's taxable year begins after July. The qualified taxpayer would be required to request a credit reservation in the form and manner prescribed by the FTB and be required to provide all necessary information as determined by the FTB.

The FTB, in coordination with the Student Aid Commission, would be required to approve tentative credit reservations with respect to qualified expenditures incurred during the taxable year for qualified taxpayers, subject to the annual limitation established in this bill. In approving applications, the FTB would be required to give priority to applications submitted by qualified taxpayers that have at least one of the following criteria:

- Businesses owned by veterans,
- Employers that employ no more than 500 employees during the taxable year, or
- Businesses owned by disabled individuals.

The unused credit could be carried over for four years, until the credit is exhausted. Any deduction or credit otherwise allowed for a qualified expenditure made by the qualified taxpayer would be reduced by the amount of this credit.

In addition, the FTB may prescribe regulations necessary or appropriate to carry out the provisions of the bill.

For purposes of Section 41, the bill would require the FTB to submit a report to the Legislature, on or before December 1, 2028, and annually thereafter, including the number of qualified taxpayers allowed a credit and the total dollar amount of the credits allowed.

This credit would be repealed on December 1, 2032.

Gross Income Exclusion

This bill, under the PITL, for taxable years beginning on or after January 1, 2027, and before January 1, 2032, would provide a gross income exclusion for student loan payments made by a qualifying employer on behalf a qualified taxpayer that is a full-time employee of that qualifying employer.

This bill would define the following terms:

- A “full-time employee” is an employee of the qualified employer who is either paid wages for services not fewer than an average of 35 hours per week or is a salaried employee within the meaning of LAB section 515.
- A “qualified taxpayer” means an individual with adjusted gross income that does not exceed the following:
  - In cases of spouses filing a joint return, head of household, or a surviving spouse, $250,000, and
  - In the case of any other individual, $125,000.

A “qualifying employer” means a business whose employees do not perform public services jobs as described in Section 1087e(m)(3)(B) of the Title 20 of the U.S. Code.

This gross income exclusion would be repealed on December 1, 2032.

Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment and both the credit and income exclusion would be specifically operative for taxable years beginning on or after January 1, 2027, and before January 1, 2032.

Federal/State Law

Federal and state laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits, hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise be undertaken.

Federal and state laws also provide that gross income includes all income from whatever source derived, including compensation for services, business income, gains from property, interest, dividends, rents, and royalties, unless specifically excluded. Types of income currently excluded include amounts received as a gift or inheritance, certain compensation for injuries and sickness, educational assistance programs, foster care payments, interest received on certain state or federal obligations, and qualified scholarships.

Also, 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 certain employers. (IRC section 108(f).) The American Rescue Plan Act of 2021 (ARPA) (Public Law 117-2) also 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).) California conforms to this provision of the ARPA and additionally allows an exclusion from gross income for student loan debt that is repaid by the U.S. Department of Education or cancelled under the income-based repayment programs administered by the U.S. Department of Education.

Under existing state law, legislation that would create a new tax expenditure, which includes a credit, deduction, exemption, or any other tax benefit as provided for by the state, is required to include specific goals, purposes, objectives, detailed performance indicators, and data collection requirements to allow the Legislature to evaluate the effectiveness of the tax benefit. Legislation that would create an income exclusion would not require detailed performance indicators and data collection requirements performance measures if the Legislature determines there is no available data to collect and report.

Implementation Considerations

The FTB has identified the following considerations for purposes of a high-level discussion; additional considerations may be identified as the bill moves through the legislative process. FTB staff is available to work with the author's office to resolve these and other considerations that may be identified.

The bill uses the term "student loan payment" for purposes of the exclusion under Section 17139.4, but does not define the term, which could lead to taxpayer confusion. For clarify, the author may wish to amend the bill to define this term consistent with the credits under Sections 17053.83 and 23632.

The bill would require the FTB to approve credit applications and give priority to applicants whose business are either owned by veterans, disabled individuals, or businesses who employ no more than 500 employees. The FTB does not have expertise to determine if applicants meet the bill's requirements and taxpayers may challenge the FTB's determination on which applicants were given priority. Typically, credits involving areas for which the FTB does not have the expertise are certified by another agency that has the relevant expertise. The author may wish to amend the bill to include a certifying agency to verify applicant requirements and to add language that FTB's determination cannot be challenged in administrative or judicial proceedings.

Technical Considerations

For consistency and clarity, the following changes are recommended:

- In Section 17139.4(b)(2)(A) replace the term "heads of household" with "head of household."
- In Section 17139.4(a) add the phrase "during the taxable year" after "payments made by a qualifying employer."
- In Section 23632(a) replace "amount stated on the tentative credit reservation provided to the taxpayer pursuant to subdivision (d)" with "taxpayer's qualified expenditures during the taxable year."
- In Section 23632(e)(1) replace "Section 23632" with "Section 17053.83."
- In Section 23632(e)(3) remove "Issue tentative credit reservations to qualified taxpayers based on, and not in excess of, the taxpayer's expected qualified expenditures for the applicable taxable year." as Section 23632(a)(1) limits the tax credit to $3,000 per qualified full-time employee.
- For consistency with Section 17053.83, in Section 23632(e)(2), replace "Approve applications, giving" with "In approving applications, the Franchise Tax Board shall give…"

This bill uses the terms “tentative credit reservation” and “credit reservation” interchangeably. For clarity, the author should amend the bill to use exclusively “tentative credit reservation.”

Policy Considerations

The exclusion in Section 17139.4 could apply to student loan payments made by a qualifying employer that is not eligible for, or does not receive a tentative credit reservation for, a credit allowed under Section 17053.83 or 23632. If this is contrary to the author’s intent, the author may wish to revise the bill.

If a qualified taxpayer, as defined under Sections 17053.83 and 23632, applies for a credit reservation on November 1, 2031, the first day of their 2031 taxable year, is approved for the tentative credit reservation, and then pays the employee’s student loan payment on February 1, 2032, the qualified taxpayer would be eligible for the credit under Section 17053.83 or 23632 because the payment was made during the qualified taxpayer’s 2031 taxable year. However, the employee would not be eligible for the exclusion under Section 17139.4 because the student loan payment would be made within the qualified employee’s 2032 taxable year. If this is contrary to the author’s intent, the author may wish to amend the bill.

LEGISLATIVE HISTORY

AB 509 (Fong, 2023/2024) would have, under the PITL, created a gross income exclusion for qualified education loan payments made by an employer on an employee’s behalf. AB 509 did not pass out of the Assembly by the constitutional deadline.

AB 1729 (Voepel, et al., 2021/2022) would have, under the PITL, allowed a gross income exclusion for education loan payments made by an employer on an employee’s behalf. AB 1729 did not pass out of the Assembly by the constitutional deadline.

SB 424 (Durazo, et al., 2021/2022) would have, under the PITL and CTL, created the California Homeless Hiring Credit available to a qualified taxpayer that employs a person who is homeless or someone who is receiving supportive services from a homeless services provider. SB 424 did not pass out of the Senate by the constitutional deadline.

AB 1169 (Frazier, 2019/2020) would have, under the PITL, allowed a credit to a qualified employer for wages paid to qualified employees. AB 1169 did not pass out of the Assembly by the constitutional deadline.

AB 1726 (Arambula, 2019/2020) would have, under the PITL and the CTL, provided a tax credit to certain employers that hire employees who are members of a targeted group. AB 1726 did not pass out of the Assembly by the constitutional deadline.

AB 2041 (Dahle, 2019/2020) would have, under the PITL and the CTL, established a credit for qualified wages paid to a qualified employee that is a former foster youth or ex-offender that is age 18 to 25 by a qualified taxpayer. AB 2041 did not pass out of the Assembly by the constitutional deadline.

SB 1333 (Durazo, et al., 2019/2020), would have, under the CTL, created the California Homeless Hiring Tax Credit available to a qualified taxpayer that employs a homeless individual. SB 1333 did not pass out of the Senate by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 386 as amended on April 28, 2025
Assumed Enactment after June 30, 2025

($ in Millions)

Fiscal Year	Revenue
2025-2026	-$34
2026-2027	-$43
2027-2028	-$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 uses data from the U.S. Department of Education, estimates prepared by the Joint Committee on Taxation, and other publicly available data on student loan repayment programs. It is estimated that the revenue loss from allowing a business tax credit and PITL gross income exclusion would be approximately $29 million in the 2027 taxable year.

It is assumed the maximum credit allocation of $25 million would be made each calendar year. It is estimated that approximately 90 percent, or $22 million would be generated by taxpayers with sufficient tax liability to offset with the credit. Of that amount, about 55 percent, or $12 million, would be claimed in the year generated and the remaining credit would be used over the subsequent four years.

To arrive at the offsetting tax effect of expense deduction that would otherwise be allowed under current law, it is estimated that qualified taxpayers would be able to deduct approximately $25 million in qualified expenses in taxable year 2027. Applying an average tax rate of 7.5 percent results in an offsetting revenue gain of $1.8 million.

Accounting for the exclusion proposed in this bill and the phase out of the existing federal program currently offered by California employer’s it is estimated that the revenue loss from allowing a gross income exclusion for qualified student loan payments would be approximately $18 million in the 2027 taxable year. The resulting net revenue loss from the credit and the gross income exclusion for the taxable year 2027 would be approximately $29 million.

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.

EQUITY IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

Assembly Committee on Revenue and Taxation, dated May 5, 2025.

Support

Society of Human Resources Management

Opposition

California Tax Reform Association
CFT – a Union of Educators and Classified Professionals, AFT, AFTL-CIO

ARGUMENTS

Assembly Committee on Revenue and Taxation, dated May 5, 2025.

Proponents

None of file.

Opponents

Writing in opposition to this bill, the California Tax Reform Association notes, in part:

> While student debt relief is often considered appropriate and necessary, we oppose this bill because it provides relief in an arbitrary manner, not based on need but based on the interest and application to the FTB of an employer. This relief could very well be for a well-compensated or professional employees and could become part of a pay package rather than necessary relief. While we appreciate that this credit is not open-ended because of the $25 million limitation, there are no criteria for allocation, just whichever employer qualifies on a first-come basis and is willing to pay this debt. Some student debts such as those for proprietary colleges which have useless degrees, or those in public service—are more appropriately discharged than others. This bill generates general fund and education revenue losses, without any criteria for determining whether discharge of student debt is appropriate in a particular case. And such determinations would be beyond the scope of the FTB.

LEGISLATIVE CONTACT

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