

Date of Hearing: August 27, 2018

ASSEMBLY COMMITTEE ON HIGHER EDUCATION

Jose Medina, Chair

SB 539 (De León) – As Amended August 20, 2018

SENATE VOTE: Not Relevant

SUBJECT: Cal Grants: taxes: credits: College Access Tax Credit.

SUMMARY: Expands the College Access Tax Credit (CATC) program in order to provide, upon appropriation by the Legislature, additional revenues from the CATC fund to the California Student Aid Commission (CSAC) to make annual disbursements for the Cal Grant Program. Specifically, **this bill:**

- 1) Increases, from 50% to 75%, the credit percentage for the CATC program.
- 2) Increases, from \$500 million to \$1 billion, the cap for the aggregate amount of credits that may be allocated and certified.
- 3) Requires, upon appropriation by the Legislature, any moneys allocated to CSAC from the CATC fund to be available for the purposes of making Cal Grant awards to eligible students.
- 4) Requires that if contributions to the CATC fund in the calendar year exceed \$10 million, the moneys allocated from the CATC fund shall be allocated to make annual Cal Grant disbursements as follows:
 - a) Eighty-five percent to make Cal Grant program awards, per existing law; and,
 - b) Fifteen percent to supplement awards for access costs, per existing law.
- 5) Requires that if, after making supplemental awards, moneys remain in the CATC fund, the moneys shall remain in the CATC fund for allocation for Cal Grant programs in future fiscal years.
- 6) Defines, “fund” as the CATC Fund created by Section 17053.87 of the Revenue and Taxation Code.

EXISTING LAW:

- 1) Establishes the CSAC for the purpose of administering specified student financial aid programs (Education Code (EC) Section 69510, et seq.).
- 2) Authorizes the Cal Grant program, administered by the CSAC, to provide grants to financially needy students to attend college. The program consists of the Cal Grant A, Cal Grant B, and Cal Grant C programs; eligibility is based upon financial need, grade point average, California residency, and other eligibility criteria, as specified (EC Sections 69430 – 69439).
- 3) Allows various tax credits under existing insurance tax (IT) law, the Personal Income Tax (PIT) Law, and the Corporation Tax (CT) Law. These credits are generally designed to

encourage socially beneficial behavior or to provide relief to taxpayers who incur specified expenses (Revenue and Taxation Code (RTC) Section 17001, et seq. and Section 23604, et seq.).

- 4) Creates the CATC Fund as a special fund in the State Treasury, with revenues allocated as follows:
 - a) First, to the General Fund (GF) in an amount equal to the aggregate amount of certified credits allowed, as specified;
 - b) Second, upon appropriation, to the Department of Insurance, the Franchise Tax Board (FTB), the California Educational Facilities Authority (CEFA), the State Controller, and CSAC for reimbursement of all administrative costs; and,
 - c) Third, the remaining revenue shall be continuously appropriated to the CSAC for purposes of awarding Cal Grants to students, as specified (RTC Section 17053.87).
- 5) Allows a CATC equal to 50% of the amount contributed by a taxpayer to the CATC Fund, as allocated and certified by the CEFA. The maximum aggregate amount of the CATC that may be allocated and certified by CEFA is \$500 million. Taxpayers are precluded from taking a deduction for amounts included in the calculation of the CATC. Any unused credits may be carried forward for up to six years. Finally, the CATC may reduce tax below the tentative minimum tax (TMT) under both the PIT Law and the CT Law (RTC Section 23687).

FISCAL EFFECT: According to the Assembly Appropriations Committee, revenue loss of \$2.4 million in 2018-19, \$2.1 million in 2019-20, and \$2.3 million in 2020-21 as a result of the additional credits allocated under the (PIT) Law and the (CT) Law. The GF is reimbursed from the CATC Fund for any revenue loss associated with the tax credit.

COMMENTS: *Assembly Rule 96.* This measure is being heard by this Committee pursuant to Assembly Rule 96.

Urgency clause and tax levy. This measure would take effect immediately as a tax levy.

The CATC program and fund. The CATC fund was created in 2014 by SB 174 (De León) Chapter 363, Statutes of 2014 and SB 798 (De León) Chapter 367, Statutes of 2014, and extended in 2017 by AB 490 (Quirk-Silva) Chapter 527, Statutes of 2017.

To note, SB 81 (Committee on Budget and Fiscal Review), Chapter 22, Statutes of 2015, subsequently recast some provisions of the CATC program and extended its operation to taxable years beginning on or after January 1, 2017, and before January 1, 2018. First, the credit was expanded to the IT law so insurers could apply the credit to their annual tax on gross premiums beginning in tax year 2017. Second, the credit was allowed to reduce tax below the TMT under the PIT Law and CT Law (credits generally only reduce tax down to, but not below, the TMT). Third, revenues would be continuously appropriated from the Fund to CSAC for purposes of awarding Cal Grants, rather than upon appropriation. Lastly, for tax year 2017, the amount of credit allowed was fixed at 50% of the amount contributed by the taxpayer, and the maximum aggregate amount of credit that could be allocated and certified by the Authority was set at \$500 million. The previous maximum aggregate amount of credit that could be allocated and certified

was \$500 million each calendar year, in addition to the amount of previously unallocated and uncertified credits.

The CATC program provides state and federal tax advantages for individuals and businesses that contribute to the CATC Fund that increases financial aid for low-income college students.

Specifically, the program provides a 50% state income tax credit for contributions to the fund. For example, a \$10,000 donation to the fund would allow a \$5,000 state income tax credit. Additionally, a contribution to the fund may be claimed as a charitable contribution deduction on federal income tax filings.

The program is designed to supplement the Cal Grant B Access Award, which provides stipends to qualifying low-income California college students to help cover living expenses such as books, housing, and food.

To note, the per-student amount of the Cal Grant B Access Award is set annually in the Budget Act, and is \$1,648 in the 2018 Budget Act. Almost 260,000 students are expected to receive the award in the 2018-19 fiscal year.

The CATC Fund adds to the Access Award's per-student amount. During the past three years, the fund has generated between \$5.1 and \$5.6 million, adding \$22 to \$24 per student to the Cal Grant B Access Award. This is significantly lower than anticipated, as statute limits the aggregated amount of tax credits at \$500 million, and the per-student amount to \$5,000.

Need for this measure. According to the author, "California is a so-called donor state, only receiving around 78-cents on every dollar state taxpayers sent to Washington."

The author states, "Educational attainment levels predict the overall economic performance of states and nations. However, most students are spending too much time at part-time and full-time jobs to pay for school and living costs when they should be and want to be focused on their studies. Those who don't drop out due to costs are graduating with crippling debt. Allowing students to focus on their studies instead will help them stay enrolled and graduate and allow graduates to contribute to our local economies rather than focusing on loan – repayment."

The author contends that, "It's time to leverage federal dollars to help offset skyrocketing college costs. To further help our neediest students complete college, we need to be creative."

This measure seeks to modify the CATC by increasing the credit percentage from 50% to 75% of the amount contributed by the taxpayer in each taxable year and increasing the total aggregated credit amount that may be allocated from \$500 million to \$1 billion; thus making donations to the Cal Grant program potentially even more generous for taxpayers.

Federal deductibility of donations to a state agency. While the Internal Revenue Service's (IRS) view has generally been that donations to state agencies are recognized as a charitable contribution eligible for a deduction, the IRS recently issued a notice informing taxpayers that it intends to propose regulations addressing this issue.

The proposed changes would limit the type of charitable contributions that Americans are allowed to deduct on their federal taxes. The rule would effectively exclude donations that are rewarded with state tax credits and render said credits effectively useless for taxpayers.

To note, with this proposal, an individual who makes a \$10,000 charitable contribution to the state and receives an \$8,500 tax credit could only deduct \$1,500 from federal taxes – which is the difference between the value of the credit and the contribution. Prior to the federal rule changes, Americans were able to deduct the entire value of a charitable contribution associated to a state tax credit.

Arguments in support. Campaign for College Opportunity (Campaign) argues that the Cal Grant is a critical lever for college affordability in the state, but its purchasing power has not kept pace with the increasing non-tuition expenses faced by today's students. The Campaign contends that by incentivizing use of the CATC, the state will generate greater revenue to support one of the most important investments in California's future. The Campaign states, "Each additional dollar of revenue provided to funding for Cal Grants by the CATC is of benefit to the hundreds and thousands of eligible applicants we currently allow to go without aid."

Arguments in opposition. The California Teachers Association (CTA) argues that funding for public education is a necessity and opposes any reduction in revenue to the state's GF which CTA believes would reduce Proposition 98 funding. Additionally, CTA contends that, "The granting of tax credits, reduces revenue to the state's GF, which in turn reduces Proposition 98 funding." Further, CTA affirms that it consistently opposes tax credits for a variety of corporations, individuals, and causes due to what CTA believes would have a negative effect on the GF and Proposition 98.

Committee comments.

- 1) As discussed in the "federal deductibility of donations to a state agency" section of this analysis, with the IRS indicating that it will crack down on states that have created state and local tax workarounds, *the Committee may wish to determine if it is prudent to vote on legislation that may cause the state to be sued.*
- 2) The measure requires the first \$10 million of the CATC program to go to the base of Cal Grant programs; however, it is presently unclear under this measure whether the vast majority of CATC funds will now supplement or supplant existing GF dollars for these Cal Grant programs. To note, the original intent of the CATC program was to raise additional funds to offset the Cal Grant B Access Award (which provides funds to eligible students to be used for non-tuition college expenses). This measure appears to broaden the scope of the CATC program.

The Committee may wish to examine if the CATC program should supplement additional Cal Grant programs.

Committee Staff understands from some stakeholders, that assuming the CATC fund largely supplant existing state funds for Cal Grant, college students more than likely will see no benefit from the CATC program. However, assuming the CATC fund serves to supplement, the value to college students remains unclear since the measure currently does not specify how the vast majority of funds will be used. The one exception being that the measure

stipulates that 15% of any funds above an initial \$10 million threshold be earmarked for supplemental awards.

To note, the state already covers the full cost of tuition at the University of California and California State University, so unless program utilization exceeds \$10 million, over 200,000 Cal Grant B access award recipients stand to lose the supplemental access award that they would have received. As noted in the "the CATC program and fund" section of this analysis, the value of this supplement has varied from year to year. For 2017-18, the CATC program increased the base amount by \$24. While that is not a large amount, college students who are Cal Grant B recipients would still experience this as a net loss to their state financial aid.

The Committee may wish to examine if it is prudent to potentially create unknown cost pressures to the GF.

- 3) Committee Staff understands that the CATC program is already underutilized. This measure does not provide for marketing of CATC or its changes. *The author may wish to work with the State Treasurer's Office in order to come up with a marketing plan.*

REGISTERED SUPPORT / OPPOSITION:

Support

Campaign for College Opportunity

Opposition

California Federation of Teachers
California Teachers Association

Analysis Prepared by: Jeanice Warden / HIGHER ED. / (916) 319-3960