

**DEPARTMENT OF TAXATION
2013 Fiscal Impact Statement**

1. **Patron** James P. "Jimmie" Massie, III

2. **Bill Number** HB 1996

3. **Committee** House Finance

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

4. **Title** Tax Credits for Donations to Non-Profits
Providing Assistance to Low-Income
Families

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would make several changes to the Neighborhood Assistance Act and Education Improvement Scholarships Tax Credit. Specifically, this bill would increase the amount of Neighborhood Assistance Act Tax Credit and Education Improvement Scholarships Tax Credit that may be issued to an individual during the taxable year and would clarify that the existing \$500 minimum donation requirement would apply on an individual basis. This bill would also clarify what type of accounting reports must be provided by neighborhood organizations and scholarship foundations.

This bill would make several additional changes and technical amendments to the Education Improvement Scholarships Tax Credit. These changes include allowing tax credits for donations of marketable securities; clarifying the definition of "student" for purposes of qualifying to receive scholarships from scholarship foundations; altering the time frame during which scholarship foundations must disburse at least 90 percent of the value of donations for which tax credits were issued; and clarifying the deadlines for the annual reporting requirements for scholarship foundations, as well as specifying the information that must be reported. This bill would also make changes to the penalty provisions for the failure of a scholarship foundation to meet the requirements of this bill by the applicable deadlines.

This bill would extend the expiration dates for the Neighborhood Assistance Act Tax Credit and the Education Improvement Scholarships Tax Credit to July 1, 2028, and January 1, 2028, respectively.

This bill would be effective in due course, except that the provisions of this bill amending the minimum donation and establishing a maximum amount of donations made by individuals for which tax credits may be issued under the Neighborhood Assistance Act Tax Credit and Education Improvement Scholarships Tax Credit programs would be effective for taxable years beginning on or after January 1, 2013.

This is an Executive bill.

6. **Budget amendment necessary:** No.

7. No Fiscal Impact. (See Line 8.)

8. Fiscal implications:

Administrative Costs

The Department of Taxation (“the Department”), the Department of Social Services, and the Department of Education consider implementation of this bill as routine and are not requesting additional funding. If the Department of Education is required to collect the fines that would be imposed on scholarship foundations that fail to meet the disbursement or reporting requirements under this bill, it may incur additional costs. However, this would not require a budget amendment if the Department of Education is permitted to use the revenue to offset program costs.

Revenue Impact

This bill would have an unknown impact on General Fund revenues beginning in Fiscal Year 2015. The provisions of the bill making changes to the Neighborhood Assistance Act Tax Credit would have no revenue impact since the credit cap is currently being met. However, because this bill would increase the amount of Neighborhood Assistance Tax Credits that a particular taxpayer may receive, it could affect the distribution of credits among particular taxpayers.

The provisions of this bill making changes to the Education Improvement Scholarships Tax Credit could have a potential revenue impact. Because this tax credit program is not effective until 2013, it is still unknown whether credit applications will meet the credit cap. This bill would allow taxpayers to claim the credit for donations of marketable securities and would also increase the maximum amount of tax credits that individual taxpayers could receive. To the extent that these changes would increase the overall amount of credit claimed, there would be a negative revenue impact.

9. Specific agency or political subdivisions affected:

Department of Taxation
Department of Education
Department of Social Services

10. Technical amendment necessary: Yes.

To ensure that the Superintendent of Public Instruction has sufficient time to issue tax credit certificates, and to be consistent with language in the Senate companion bill, the Department of Education suggests the following technical amendment:

Line 201, after than
Strike: 20
Insert: 30

Because scholarship foundations may request tax credits on behalf of donors, but may not actually receive tax credits themselves, the following technical amendment is suggested:

Line 235, after funds
Insert: on a donor's behalf

Line 252, after funds
Insert: on a donor's behalf

To clarify which agency is responsible for collecting the fines that would be imposed under this bill, as well as where such funds would be deposited, the Department of Education suggests the following technical amendments:

Line 232, after disbursed.
Insert: Such fine shall be remitted by the scholarship foundation to the Department of Education within 30 days after the end of the one-year period and deposited to the General Fund.

Line 249, after fine.
Insert: Such fine shall be remitted by the scholarship foundation to the Department of Education by November 1 and deposited to the General Fund.

Finally, this bill would require a scholarship foundation to provide information as an appendix to its annual audit, review, or compilation, as applicable, regarding the total number and value of donations per locality received, the total number and dollar amount of qualified educational expenses scholarships disbursed, and the percentage of first-time recipients to whom qualified educational expenses scholarships were disbursed. Such information must be provided for the scholarship foundation's most recent year ended. The Department of Education suggests requiring that such information be included in the annual report that scholarship foundations are required to submit to the Department of Education, rather than as part of a scholarship foundation's accounting report. This would provide the Department of Education with additional information to use in evaluating the program. Additionally, requiring this information to be provided based on the state's fiscal year, rather than based on the scholarship foundation's most recent year ended, would allow this information to be used for comparison purposes.

11. Other comments:

Neighborhood Assistance Act Tax Credit

The Virginia Neighborhood Assistance Act provides an income tax credit to businesses and individuals that donate to neighborhood organizations for approved programs that benefit impoverished people. Under this Act, a neighborhood organization is allocated funding through the Neighborhood Assistance Act Program. The Department of Social Services and the Department of Education are responsible for approving the programs and allocating the tax credits to the neighborhood organizations. An individual or business that donates to an organization that qualifies as a neighborhood organization is then eligible to receive an income tax credit from that neighborhood organization.

A neighborhood organization is any local, regional or statewide organization whose primary function is providing neighborhood assistance for impoverished people and that is exempt from taxation under the provisions of IRC §§ 501(c)(3) and 501(c)(4), or any organization defined as a community action agency in the Economic Opportunity Act of 1964, or any housing authority as defined in *Va. Code* § 36-3. To qualify for this credit, at least 50 percent of the persons served by the organization must (1) be low-income persons with an annual family income not in excess of 300 percent of the current poverty guidelines or (2) eligible students with disabilities.

The Neighborhood Assistance Act Tax Credit is equal to 65 percent of the value of the money, property, professional services, and contracting services donated by a business firm, or 65 percent of the monetary donation or donation of marketable securities made by an individual. The minimum tax credit that may be issued to a business contribution is \$400. The minimum donation by an individual must be at least \$500, and the maximum tax credit for an individual or for married persons is \$50,000. Any unused tax credits may be carried over for the next five succeeding taxable years or until the total amount of credit has been taken, whichever is sooner.

No more than \$850,000 in tax credits may be approved to a neighborhood organization or grouping of neighborhood organization affiliates for all education proposals. Additionally, no more than an aggregate of \$500,000 in tax credits may be approved in a fiscal year to a neighborhood organization or grouping of neighborhood organization affiliates for all other proposals combined.

The total amount of credits that may be granted for each fiscal year is \$15 million. Out of this amount, \$8 million is allocated to education proposals, while the remaining \$7 million is allocated to all other proposals. If either the Department of Social Services or Department of Education has a balance of tax credits remaining after the initial allocation of tax credits to approved proposals, then the Commissioner of the Department of Social Services or the Superintendent of Public Instruction, as applicable, must reallocate the remaining balance of tax credits to such previously approved proposals to the extent that a neighborhood organization can use or allocate additional tax credits for the previously approved proposal. The \$500,000 and \$850,000 annual limitations for tax credits approved to a grouping of neighborhood organization affiliates are inapplicable to the extent of any such reallocation.

Educational Improvement Scholarships Tax Credit

Effective for the 2013 taxable year, taxpayers may earn an Educational Improvement Scholarships Tax Credit equal to 65 percent of the monetary donation made to a qualifying scholarship foundation. This credit may be claimed for the taxable year following the year of contribution, and may be applied against the individual income tax, corporate income tax, bank franchise tax, insurance premiums license tax, or tax on public service corporations. For taxpayers making estimated tax payments, the credit is prorated equally against estimated tax payments made in the third and fourth quarters of the taxable year in which the credit may be claimed, and the final tax payment.

Tax credits are awarded to taxpayers on a first-come, first-served basis. The total amount of credits available in any given fiscal year is capped at \$25 million. No tax credit is allowed if the monetary donation is less than \$500. No more than \$50,000 in tax credits may be issued to an individual or to married persons in a taxable year. The \$50,000 limitation does not apply to credits issued to any business entity, including a sole proprietorship. Any unused tax credits may be carried over for the next five succeeding taxable years or until the total amount of credit has been taken, whichever is sooner.

Taxpayers are required to request and receive preauthorization for a specified tax credit amount from the Superintendent of Public Instruction. The preauthorization notice must accompany the donation from the taxpayer to the scholarship foundation. The scholarship foundation is then required to return the notice to the Department of Education within 20 days certifying the amount of the donation and date received. A taxpayer is required to make the preauthorized contribution within 60 days of issuance of the notice. In addition to being preauthorized, taxpayers claiming credit for a contribution are required to submit verification from each scholarship foundation to which monetary donations have been made.

For purposes of this credit, a "scholarship foundation" is defined as a nonstock, nonprofit corporation that is exempt from taxation under IRC § 501(c)(3), that has been approved by the Department of Education, and that is established to provide financial aid for the education of students residing in the Commonwealth. In order to be approved to receive and administer tax credit-approved funds, scholarship foundations are required to apply to the Department of Education. The Department of Education is required to issue a notice of approval or denial, including reasons for denial to the applicant within 60 days after the application is submitted.

A scholarship foundation is required to disburse at least 90 percent of the amount of each donation for which a tax credit may be received within one year of such donation for "qualified educational expenses" through scholarships. Tax credit-derived funds not used for such scholarships may be used only for the administrative expenses of the scholarship foundation. "Qualified educational expenses" would mean school-related tuition and instructional fees and materials, including textbooks, workbooks, and supplies used solely for school-related work. Scholarship foundations must provide receipts to individual taxpayers for their contributions.

By September 30 of each year, each scholarship foundation is required to provide the following information to the Department of Education:

- The total number and dollar amount of contributions received between September 1 of the prior calendar year and September 1 of the current calendar year,
- The dates when such contributions were received, and
- The total number and dollar amount of qualified educational expenses scholarships awarded for the school year that began during the current calendar year

In awarding scholarships from tax credit-derived funds, the scholarship foundation is required to (i) provide scholarships for qualified educational expenses only to students whose family's annual household income is not in excess of 300 percent of the current poverty guidelines or any eligible student with a disability; (ii) not limit scholarships to

students of one school; and (iii) comply with Title VI of the Civil Rights Act of 1964. Scholarship foundations are also be required to ensure that schools selected by students to which tax credit-derived funds may be paid (i) are in compliance with the Commonwealth's and locality's health and safety laws and codes; (ii) hold a valid occupancy permit as required by the locality; (iii) comply with Title VI of the Civil Rights Act of 1964; and (iv) comply with nonpublic school accreditation requirements administered by the Virginia Council for Private Education or maintain an assessment system that annually measures scholarship students' progress in reading and math using a national norm-referenced achievement test.

For purposes of this credit, a "student" is defined as a child who is a resident of Virginia and meets one of the following criteria:

- Is enrolled in Virginia's public schools for the year prior to receiving a scholarship foundation scholarship,
- Is a prior recipient of a scholarship foundation scholarship,
- Is eligible to enter kindergarten or first grade, or
- Was not a resident of Virginia during the preceding school year.

Any scholarship foundation that fails to disburse at least 90 percent of any donated amount within one year or that fails to provide the required report by September 30 is removed from the annual list published by the Department of Education and is not entitled to request preauthorization for additional tax credits, nor is it entitled to receive and administer additional tax credit-derived funds.

Proposed Legislation

Neighborhood Assistance Act Tax Credit

This bill would increase the amount of Neighborhood Assistance Act Tax Credits that may be issued to an individual during the taxable year. Under current law, no more than \$50,000 in tax credits may be issued to an individual or to married persons in a taxable year. This bill would allow credits to be issued for the first \$125,000 in donations made by the individual during the taxable year. Donations of \$125,000 would equate to a 65 percent tax credit of \$81,250. This provision would apply on an individual basis, thereby allowing a married couple to receive credits for donations of up to \$250,000 (a credit of \$162,500).

This bill would clarify that the existing \$500 minimum donation requirement would apply on an individual basis.

This bill would also clarify what information must be provided by neighborhood organizations prior to approval for allocating tax credits. Current law requires that regulations or guidelines adopted by the Department of Social Services or the Department of Education contain a requirement that neighborhood organizations provide an annual audit, review, or compilation as required under federal standards. This bill would clarify this requirement by stating that neighborhood organizations with total revenues in excess of \$100,000 for the organization's most recent year must provide an audit or review for the year performed by an independent certified public accountant.

Neighborhood organizations with revenues of \$100,000 or less for the organization's most recent year would be required to provide a compilation for the year performed by an independent certified public accountant.

This bill would extend the expiration date for the Education Improvement Scholarships Tax Credit to January 1, 2028, notwithstanding the requirement that any bill renewing an existing tax credit have an expiration date of not longer than five years from the effective date of the renewed tax credit.

Education Improvement Scholarships Tax Credit

This bill would increase the amount of Education Improvement Scholarships Tax Credits that may be issued to an individual during the taxable year. Under current law, no more than \$50,000 in tax credits may be issued to an individual or to married persons in a taxable year. This bill would allow credits to be issued for the first \$125,000 in donations made by the individual during the taxable year. Donations of \$125,000 would equate to a tax credit of \$81,250. This provision would apply on an individual basis, thereby allowing a married couple to receive credits for donations of up to \$250,000 (a credit of \$162,500).

This bill would also clarify that the existing \$500 minimum donation requirement would apply on an individual basis.

This bill would clarify the definition of "student" for purposes of qualifying to receive scholarships from scholarship foundations. Under this bill, a qualifying student would include a child who is a resident of Virginia and meets one of the following criteria:

- Has enrolled and attended a public school in Virginia for at least one-half of the current year, or
- Has enrolled and attended a public school in Virginia for at least one-half of the school year that immediately preceded his receipt of a scholarship foundation scholarship.

This bill would also clarify that a child who did not attend a nonpublic school in Virginia for more than one-half of the school year would be a qualifying student if he is a resident of Virginia and was domiciled in a state other than Virginia for the school year that immediately preceded his receipt of a scholarship foundation scholarship. A child who is a resident of Virginia and either a prior recipient of a scholarship foundation scholarship or who is eligible to enter kindergarten or first grade would continue to qualify as students eligible to receive scholarship foundation scholarships.

This bill would expand the Education Improvement Scholarships Tax Credit by allowing tax credits for donations of marketable securities.

This bill would also alter the time frame during which scholarship foundations must disburse at least 90 percent of the value of donations for which tax credits were issued. Current law requires scholarship foundations to disburse 90 percent of the amount of each donation for which a tax credit may be received within one year of such donation. This bill would amend the existing requirement to require scholarship foundations to disburse 90 percent of the value of donations for which tax credits were issued during the 12-month period ending on June 30 by the immediately following June 30. Required

disbursements would begin with donations received for the period January 1, 2013 through June 30, 2014.

Any scholarship foundation that fails to disburse at least 90 percent of the value of donations within the specified time period would be subject to a fine for the first offense. Such fine would be equal to 200 percent of the difference between 90 percent of the donated amount and the amount that was actually disbursed. The bill does not specify which state agency would collect any such fines, nor does it specify where these funds would be deposited. For the second offense within a five-year period, a scholarship foundation would be removed from the annual list and would not be permitted to receive and administer tax credit-derived funds for two years. After two years, the scholarship foundation would be permitted to reapply to be included on the annual list. If the scholarship foundation is reauthorized, the next subsequent offense would be treated as a first offense.

This bill would make several changes to the reporting requirement for scholarship foundations. Under this bill, scholarship foundations would be required to report the following information:

- The total number and value of contributions received by the scholarship foundation in its most recent fiscal year ended for which tax credits were issued;
- The dates when such contributions were received, and
- The total number and dollar amount of educational expenses, scholarships disbursed by the scholarship foundation during its most recent fiscal year.

Such information would be reported by September 30 of each year, beginning with September 30, 2014. Any scholarship foundation that fails to meet this reporting requirement by the deadline would be required to pay a \$1,000 fine for the first offense. The bill does not specify which state agency would collect any such fines, nor does it specify where these funds would be deposited. For the second offense within a five-year period, a scholarship foundation would be removed from the annual list and would not be permitted to receive and administer tax credit-derived funds for two years. After two years, the scholarship foundation would be permitted to reapply to be included on the annual list. If the scholarship foundation is reauthorized, the next subsequent offense would be treated as a first offense.

This bill would also clarify the reporting standards for scholarship foundations' tax credit-derived funds. Current law requires that an annual audit, review, or compilation, as required by federal standards, be conducted on a scholarship foundation's tax credit-derived funds. This bill would require that scholarship foundations with total revenues in excess of \$100,000 for the foundation's most recent year have an audit or review of the foundation's donations received for each year performed by an independent certified public accountant. Scholarship foundations with revenues of \$100,000 or less for the foundation's most recent year would be required to provide a compilation of the foundation's donations for the year performed by an independent certified public accountant. The scholarship foundation's board of directors would be required to certify the statutorily required information as an appendix to the applicable report.

Upon receipt and approval by the Department of Education of the preauthorization notice with required supporting documentation and certification of the value and type of donation by the scholarship foundation, the Superintendent of Public Instruction would be required to issue tax credit certificates to eligible taxpayers within 20 days. Taxpayers would be required to attach the tax credit certification to the applicable tax return. The Department of Education would be required to provide a copy of the tax credit certification to the scholarship foundation.

This bill would extend the expiration date for the Education Improvement Scholarships Tax Credit to January 1, 2028, notwithstanding the requirement that any bill renewing an existing tax credit have an expiration date of not longer than five years from the effective date of the renewed tax credit.

This bill would be effective in due course, except that the provisions of this bill amending the minimum donation and establishing a maximum amount of donations made by individuals for which tax credits may be issued under the Neighborhood Assistance Act Tax Credit and Education Improvement Scholarships Tax Credit programs would be effective for taxable years beginning on or after January 1, 2013.

Similar Legislation – Executive Bills

Senate Bill 1227 is similar to this bill, except that it would impose different penalties on scholarship foundations that fail to meet certain requirements.

Senate Bill 1206 would amend several of the requirements imposed on schools and scholarship foundations for purposes of the Education Improvement Scholarships Tax Credit.

Similar Legislation – Other Bills

House Bill 1512 would create an income tax subtraction for income from the lease of a building to a local public school division.

House Bill 1767 would create an income tax credit for donations of machinery and equipment to a community college or vocational school that would be principally used in Virginia in teaching or training students.

Senate Bill 749 would create an income tax credit for contributions to STEM organizations for use in science, technology, engineering, and math (STEM) programs at qualified public schools.

Senate Bill 848 would create a tax credit for scholarships to students attending Virginia two-year colleges.

Senate Bill 1000 would repeal the Education Improvement Scholarships Tax Credit.

Senate Bill 1009 would make several changes to the Neighborhood Assistance Act Tax Credit.

cc : Secretary of Finance

Date: 1/21/2013 KLC
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