Department of Finance and Administration

Legislative Impact Statement

Bill: SB539
Bill Subtitle: TO CREATE THE ARKANSAS TAX CREDIT SCHOLARSHIP ACT.

Basic Change :

Sponsor: Senators B. Johnson and J. Hendren; Representative Bragg

SB539 creates the Arkansas Tax Credit Scholarship Act and provides an income tax credit to individuals or businesses equal to 100% of contributions to eligible student support organizations. The credit may not exceed an eligible taxpayer's tax due after the application of any other allowable income tax credits and unused credits may be carried forward for five years. Spouses who file separate returns may each only claim one-half of the credit. Contributions made before the fifteenth day of the fourth month of the tax year may be applied as a credit to either the current or previous year. Eligible taxpayers may rescind any credit available and the rescinded credit is eligible to be reissued on a priority basis after the rescission is accepted. Scholarships would enable students to attend private schools if the family meets income requirements. The bill is effective for tax years beginning on or after January 1, 2019.

Revenue Impact :

FY2020 - $3 Million Reduction in State General Revenue

Taxpayer Impact :

All eligible taxpayers (individual and business) that make an eligible contribution to an eligible student support organization will receive a 100% credit to reduce their income tax. Taxpayers would be required to document qualifying contributions. Taxpayers would also be able to deduct eligible contributions as charitable deductions.

Resources Required :

DFA would be required to promulgate rules. Computer programs, tax forms and instructions will need to be updated.

Time Required :

Adequate time is provided for implementation.

Procedural Changes :

Computer programs, tax forms and instructions as well as training manuals will need to be updated. Department employees will need to be educated as well as the tax community.

Other Comments :

The bill encourages more students to attend private schools by providing a means by which low income students may have their tuition costs covered all or in part by scholarships. The bill limits the amount of state income tax credits and the amount of credits that can be carried forward to $3 million, but it is unclear if that is for the entire program or per taxpayer. The bill is equal to 100% of the

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contribution and there is no provision disallowing a charitable contribution deduction. The bill does not contain any provision for allowing credits on a first come-first served basis, only that applications must be made to DFA. Any unused income tax credit can be carried forward for five years following the tax year in which the credit was earned. The credit is not transferrable or sellable unless all the assets of the eligible taxpayer are conveyed, assigned, or transferred in the same transaction. This would apparently allow the credit to transfer if a business is acquired or merged with another business.

Legal Analysis :

SB539 provides that an eligible student support organization (SSO) may establish scholarships for use in paying the nonpublic school education expenses for a student. The SSO must satisfy various criteria outlined in the bill and must file an application with the Office of the Treasurer by May 1 before the academic year for which the SSO intends to fund scholarships. Within sixty (60) days after receipt of the application, the Treasurer must certify the eligible SSO if it meets all necessary requirements. The SSO must conduct annual audits of all student scholarship accounts.

Parents may apply to an SSO to establish a scholarship account for an eligible student. The parent must use the funds from the account for educational expenses at a nonpublic school. Eligible education expenses are outlined in the bill. The SSO must approve applications by order of receipt. The organization must maintain separate accounts for student scholarship funds and operating funds of the organization. The SSO may fund for each eligible student an equivalent amount of the foundation funding amount as provided in state law for each academic year. For the 2018-2019 school year, that amount was $6,781.

The SSO must disburse amounts to the student's parents in quarterly installments. The SSO must develop a system for direct payment at a parent's direction to education service providers or other entities by electronic funds transfer, automatic clearing house transfer, or other payment method. Scholarship funds will not be taxable income of a parent or eligible student.

Taxpayers who make eligible contributions will receive a state income tax credit equal to 100% of the contribution amount. The tax credit may be used to offset up to 100% of the income tax due for the tax year. Unused credits may be carried forward for five consecutive tax years following the tax year in which the credit was earned. The act is effective for tax year 2019 and following. The bill limits the available tax credit beginning in 2019 to $3 million, including tax credits carried forward from previous years. The DFA Director must adopt rules necessary to allocate the tax credits on a first-come, first-served basis.

This bill does not account for the fact that some taxpayers file returns early, some file on the due date, and some file with an extension. Individual income tax returns are filed from January through October of the filing year, and all of those returns are timely under state law. Those taxpayers making contributions under this bill who do not file until later will expect to receive the tax credit and may file too late to benefit from the bill because the $3 million limit has been reached. In addition, corporate income tax returns are due throughout the year based on whether the corporation is a calendar year or fiscal year filer. Corporations with a later due date may be denied the tax credit.

This bill does not provide a mechanism for the DFA Director to preauthorize taxpayer contributions to an SSO for eligibility for the tax credit. In the event that a taxpayer makes a contribution that is not eligible for the tax credit because the $3 million limit has been reached or for some other reason, the

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DFA Director will have to assess the taxpayer and collect the additional tax owed. As a result, this bill may result in the issuance of tax assessments and reduced income tax refunds for taxpayers.

Lines 22-25, page 5 require the Office of the Treasurer to certify an SSO "if the organization meets the requirements under subsection (b) of this section [6-18-2004]." Subsection (b) contains a list of required application materials that an SSO must provide to the Office of the Treasurer, but it does not specify the requirements of the organization. Therefore, the language likely should be amended to read "if the organization meets the requirements under this subchapter."

In line 14, page 14, "§ 6-15-2008(b)" likely should read "§ 6-18-2008(c)."

In line 6, page 17, "§ 6-18-2008(a)" likely should read "§ 6-18-2008(b)."

Beginning on line 30, page 14, § 6-18-2010 requires the SSO to obtain an annual audit of its financial accounts. Additional language may be necessary to clarify that an audit under this section does not preclude an audit by the DFA Director under § 26-18-401.

In line 32, page 19, the phrase "an eligible taxpayer tax due" likely should read "an eligible taxpayer's tax due."

This bill would create significant additional certification and recordkeeping duties for the DFA Director. Issues regarding the use of the Treasurer's Office to certify certain entities but having DFA be required to prioritize issuance for the credits in different systems will require additional administrative responsibilities for DFA.

This bill does not contain an emergency clause. The bill will become effective for tax years beginning on or after January 1, 2019.