

BILL # HB 2465

TITLE: charitable organization; tax credit
S/E re: same subject on charitable tax credit

SPONSOR: Anderson

STATUS: As Amended by House Ways and Means

REQUESTED BY: House

PREPARED BY: Stefan Shepherd

FISCAL YEAR

| | 2000 | 2001 | 2002 |
|--------------------------------------|-------------|-------------|---------------|
| REVENUES | | | |
| General Fund - Individual Income Tax | \$-0- | \$-0- | \$5,746,000 * |

* The bill would have a cost of \$26.3 million once fully implemented in FY 2004

FISCAL ANALYSIS

Description

The strike-everything amendment would create a new \$200 “charitable” individual income tax credit for persons who do not itemize charitable deductions on their individual income tax returns, starting in tax years from and after December 31, 2000.

Estimated Impact

The JLBC Staff estimates that the strike-everything amendment would reduce General Fund revenues by \$5,746,000 in FY 2002, \$14,628,000 in FY 2003, and \$26,301,000 in FY 2004.

Assumptions

Under current law, Arizona taxpayers may receive a non-refundable credit of up to \$200 against their individual income tax obligation each year for contributions to qualifying charitable organizations (QCOs). QCOs are 501(c)(3) charitable organizations that spend at least 50% of their budget on services to Temporary Assistance for Needy Families (TANF) recipients or Arizona residents below 150% of the federal poverty level (FPL). The credit is available only for contributions to QCOs exceeding the total amount of charitable contributions deducted in the taxpayer’s “baseline year.” A taxpayer’s “baseline year” is tax year 1996 if the taxpayer deducted charitable contributions that year, or the first tax year after 1996 in which the taxpayer deducted charitable contributions. The \$200 limitation applies to taxpayers filing jointly; married couples filing separately may each claim only half of the credit that would have been allowed for a joint return.

The strike-everything amendment would extend the \$200 “charitable” individual income tax credit to persons who do not itemize charitable deductions on their individual income tax returns. The proposed credit for non-itemizers is similar to the current credit for itemizers, except that non-itemizers do not need to have a “baseline year.” The proposed credit would take effect in tax years from and after December 31, 2000. The current credit for itemizers is unchanged by the amendment.

To calculate the fiscal impact of this credit, we started with the total amount of charitable deductions claimed by Arizona taxpayers on their federal tax returns in tax year (TY) 1997, or \$1,434,121,000. Although these deductions grew by 35% over the two-year period from TY 1995 to TY 1997, we assumed just 40% growth (about 9% annually) from TY 1997 to TY 2001. We estimated 9% annual growth in charitable deductions we believe the 17% growth from TY 1995 to TY 1997 cannot be sustained in the long run. The 9% yearly growth over 4 years results in total estimated deductions of just over \$2.0 billion in TY 2001 (FY 2002). Data from the nonprofit group Independent Sector (IS) indicates that only about 69% of all contributions were deducted on tax forms, which means that the total amount of all charitable contributions estimated for TY 2001 is about \$2.9 billion.

(Continued)

Assumptions (Continued)

Since the bill affects non-itemizers only, we must now estimate the portion of all charitable contributions made by non-itemizers. The IS data also indicates that about 8.7% of total contributions are made by non-itemizers in amounts of \$200 or less. In addition to these contributions, the IS data also indicates that approximately 1.8% of total contributions are made by persons who itemize but do not deduct those contributions of less than \$200. We assume that one-third of these contributions, or 0.6% of total contributions, would potentially be claimed for the credit. Combining the 8.7% figure representing non-itemizers and the other 0.6% yields a total 9.3% of total contributions \$200 or less potentially eligible to be claimed under the new provision. Applying that figure to the \$2.9 billion estimate of total charitable contributions yields an estimate of more than \$270 million of Arizona charitable contributions \$200 or less made by persons who do not itemize charitable deductions.

According to two different studies, the percent of charitable contributions for "human services" organizations is about 9.1%. We estimate, therefore, that about \$24.6 million, or 9.1% of \$270 million, would be donated in amounts of \$200 or less to human services organizations in TY 2001 by non-itemizers. We assume that in the first year of the credit, two-thirds (67%) of these organizations would be self-certified as Qualifying Charitable Organizations (QCOs), which reduces the amount of potentially claimed deductions to \$16.4 million. We also estimate that in the first year of the credit, 50% of people eligible to take the credit would do so, further reducing the amount to be claimed to \$8.2 million.

Finally, we had to make an adjustment for married filers. In tax year 1997, joint filers filed approximately 41% of all tax returns. In addition to these filers, married couples filing separately file approximately 2% of returns. Data from the IS nonprofit group indicates that the average donation exceeds \$200. Placing a \$200 limit on married couples, therefore, will limit usage. If married couples file 43% of all tax returns, then the amount to be claimed must be reduced by 30%. For example, if a group of 10 people includes 3 joint returns and 4 individual returns, the percentage of joint returns as a total of all returns is 43%, but if they each make \$200 contributions, the amount of monies that could be claimed under the proposed credit would be \$1,400. This amount represents a 30% reduction from the total contributions of \$2,000, if each of 10 individuals claimed \$200 apiece. With this adjustment for married filers, we estimate the total reduction in revenues of the proposed individual income tax credit to be \$5,746,000 in FY 2002.

For FY 2003, we expect the following changes in the credit:

- 1) The amount of total contributions will increase by 10%
- 2) Human services donations as a percentage of total contributions will increase from 9.1% to 12%
- 3) The percentage of human services organizations self-certifying as QCOs will increase from 67% to 90%
- 4) The percentage of eligible persons claiming the credit will increase from 50% to 65%.

These changes increase the total impact of the credit from \$5,746,000 in FY 2002 to about \$14,628,000 in FY 2003. In FY 2004, we expect human services donations as a percentage of total contributions to increase from 12% to 15% and the percentage of eligible persons claiming the credit to increase from 65% to 85%. These changes make the estimated cost of the credit in FY 2004 approximately \$26,301,000.

Local Government Impact

Because it reduces income tax revenues, the amended bill would reduce the amount of Urban Revenue Sharing revenues passed on to local municipalities. State law provides that local municipalities are to receive 15.0% of state income tax revenues from 2 years prior to the current year. Any changes affecting FY 2002 revenues, therefore, would affect Urban Revenue Sharing in FY 2004. JLBC Staff estimates that the bill as amended would reduce Urban Revenue Sharing distributions to municipalities by \$(861,900) in FY 2004, by \$(2,194,200) in FY 2005, and by \$(3,945,200) in FY 2006.

Amendments

Because the amendment analyzed here is a strike-everything amendment, the JLBC Staff has not estimated the fiscal impact of the underlying bill.