

Fiscal Note

BILL # SB 1243

TITLE: STOs; individual income tax credits

SPONSOR: Mesnard

STATUS: As Introduced

PREPARED BY: Patrick Moran

Description

The bill would eliminate the School Tuition Organization (STO) "switcher" individual income tax credit. The bill would offset the loss of the switcher credit by increasing the statutory cap on donations eligible for the "original" STO credit.

Estimated Impact

The bill's higher caps for the original program would allow taxpayers to increase their credit usage, which would reduce state General Fund revenues. The magnitude of this impact is difficult to predict with certainty. We assume that donations to the consolidated original individual STO credit program under the bill would increase by 1%, which would decrease General Fund revenues by \$(1.2) million annually beginning in FY 2025. The Arizona Department of Revenue has not yet provided an estimate of the bill's impact.

Analysis

The bill would consolidate the 2 existing individual income tax credits for donations to School Tuition Organizations (STOs) that provide tuition scholarships to students attending private schools. Currently, the original credit is capped at \$655 for individuals (\$1,308 for married filing jointly), while the switcher credit provides an additional credit of \$652 for single filers (\$1,301 for married filers) for individuals who have already received the maximum credit from the original program. The original STO credit had a cost of \$73.8 million in FY 2022 while the switcher credit had an impact of \$46.9 million, for a total impact of \$120.7 million. These credit caps are adjusted annually for inflation.

A.R.S. § 43-1603 stipulates that donations associated with the switcher credit may only be used to provide private school tuition scholarships for private school pupils that meet at least one of the following criteria:

- Attended a governmental school as a full-time student in the prior fiscal year for at least 90 days.
- Is enrolled in a private kindergarten or preschool program for students with disabilities.
- Is a dependent of the armed forces that is stationed in Arizona.
- Is homeschooled before enrolling in a private school.
- Moved from out-of-state before attending a private school.
- Previously participated in the Empowerment Scholarship Account (ESA) Program and did not renew their ESA account in order to participate in the STO program.

Under the bill, the switcher credit would no longer be available, but the original credit cap would be increased by an amount that mostly offsets the elimination of the switcher credit. We estimate that under current law both the switcher and original credit would be subject to an 11.51% adjustment in TY 2024 based on the estimate change in the Phoenix-Mesa Consumer Price Index (CPI) from CY 2022. After this adjustment, we estimate that the increases specified in the bill

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for the original credit would reduce the total available credits by \$(3) for single filers and \$(8) for married individuals filing jointly (see Table 1 below). As a result, we do not anticipate that the change in the cap would itself have a material fiscal impact relative to current law.

The bill may, however, increase STO donations for 2 groups of taxpayers and thereby reduce General Fund revenues:

- Taxpayers who currently receive the maximum original credit under current law, but not the full switcher credit. Under the bill, such individuals would be able to increase their donations under the original program to receive at least the amount of credits they were previously receiving under the switcher program and more if they choose to make additional donations and have sufficient tax liability. According to DOR, there were 58,209 taxpayers who participated in the switcher program in FY 2022 who received an average credit of \$805. We lack data, however, to determine the share of those taxpayers that claimed the maximum switcher credit.
- Individuals who currently receive the maximum original credit under current law, but choose not to participate in the switcher program. Under the bill, taxpayers who are receiving the maximum original credit but not participating in the switcher program would be eligible to receive additional credits under the higher original program caps if they make additional donations and have sufficient tax liability. According to DOR, there were 91,921 taxpayers who claimed the original individual credit in FY 2022, of which 58,209 participated in the switcher program, meaning that there are 33,712 taxpayers who participated in the original program who did not to participate in the switcher program (91,921 – 58,209 = 33,712). We lack data, however, on how many of the 33,712 claim the maximum original credit.

The magnitude of the increase in STO donations under the bill is uncertain. Some taxpayers may prefer to donate to the original program compared with the switcher program given that the original program does not require scholarship recipients to have attended a public school in the prior year for 90 days, but we cannot determine the relative preference between the original and switcher STO program with precision. As noted above, we also do not know how many individuals are currently under the cap in the switcher program or at the cap in the original program and not participating in the switcher program. The Universal Empowerment Scholarship Account (ESA) program may also serve to limit donation increases that could occur under the bill (private school students may not simultaneously participate in the ESA program and receive a STO scholarship).

Table 1			
SB 1243 Impact on Individual STO Tax Credit Caps			
	<u>TY 2024 (Current Law Est.)</u>	<u>Tax Year 2024 (SB 1243)</u>	<u>Change</u>
Original Single	\$731	\$1,456	\$725
Original Married	\$1,459	\$2,902	\$1,443
Switcher Single	\$728	0	\$(728)
Switcher Married	\$1,451	0	\$(1,451)
<i>Total Single</i>	<i>\$1,459</i>	<i>\$1,456</i>	<i>\$(3)</i>
<i>Total Married</i>	<i>\$2,910</i>	<i>\$2,902</i>	<i>\$(8)</i>

Given the data limitations outlined above, we assume that the overall increase in individual STO donations would be limited to 1% beginning in Tax Year 2024 (FY 2025). The resulting state fiscal impact would be a General Fund revenue decrease of \$(1.2) million (\$120.7 million X 1% = \$1.2 million)

Local Government Impact

Beginning in FY 2024, incorporated cities and towns receive 18% of individual and corporate income tax collections from 2 years prior from the Urban Revenue Sharing (URS) Fund established by A.R.S. § 43-206. Therefore, under the bill, URS distributions to cities and towns would decrease by \$(216,000) annually beginning in FY 2027.